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Case No
COMP/M.3653 -
Siemens/VA Tech

Only the German text is authentic.

REGULATION (EC) No 139/2004
MERGER PROCEDURE

Article 8 (2)

Date: 13/07/2005



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 13 July 2005

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PUBLIC VERSION

COMMISSION DECISION

of 13 July 2005

**declaring a concentration compatible with the common market and the
EEA Agreement**

(Case No COMP/M.3653 - Siemens/VA Tech)

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Commission Decision

of 13 July 2005

**declaring a concentration compatible with the common market and the
EEA Agreement**

(Case No COMP/M.3653 - Siemens/VA Tech)

(Only the German text is authentic)

(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings,¹ and in particular Article 8(2) thereof,

Having regard to the Commission decision of 14 February 2005 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations,²

Whereas:

¹ OJ L 24, 29.1.2004, p. 1.

² OJ C [...], [...] 2003, p. [...].

- (1) On 10 January 2005 the Commission received notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004 ("the Merger Regulation").³ According to the notification, the following is proposed: the company Siemens Österreich AG ("Siemens Österreich", Austria), which is controlled by Siemens AG ("Siemens", Germany), is to gain control, within the meaning of Article 3(1)(b) of the Merger Regulation, of the company VA Tech AG ("VA Tech", Austria) by a public takeover bid made on 10 December 2004.
- (2) The Commission concluded that the notified concentration fell within the scope of the Merger Regulation and took the preliminary view that it raised serious doubts as to its compatibility with the common market and the European Economic Area. It therefore adopted on 14 February 2005 a decision pursuant to Article 6(1)(c) of the Merger Regulation initiating Phase II proceedings for examination of the notified proposal.
- (3) On 22 April 2005 the Commission sent a statement of objections to the notifying parties in which it found that, as a preliminary assessment and on the basis of the information so far available to the Commission, the notified proposal was incompatible with the common market
- (4) Siemens replied to the statement of objections in a written statement submitted on 6 May 2005. In a written statement submitted on 25 May 2005, Siemens offered commitments designed to remove any existing competition concerns.
- (5) The Commission has now come to the conclusion that, in its notified form, the proposal is liable to significantly impede effective competition in a substantial part of the common market, in particular as a result of the creation of a dominant position. However, the commitments given by the parties allow the competition concerns regarding the concentration to be dispelled. This Decision is issued pursuant to Article 8(2) of the Merger Regulation.

I. THE PARTIES

- (6) Siemens supplies products and services worldwide in various areas of industry and electrical engineering. Its areas of activity include plants for power generation, transmission and distribution, automation and traction technology, plant engineering and construction, technical services, traffic engineering, building services engineering and information technology.
- (7) In the area of equipping hydroelectric power stations, Siemens is working on a joint venture ("JV") with the company J.M. Voith AG (Heidenheim, Germany), in which Siemens holds 35% of the shares and has joint control. [...] * The Commission's competition assessment rests on the same basis, but it would not change fundamentally if, hypothetically, the concentration were only to lead to Siemens acquiring a majority holding in VA Tech and continuing the JV separately with

³ OJ L 24, 29.1.2004, p. 1.

* Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

Voith. Only the extent, but not the existence, of the effects to be expected from the concentration might possibly change as a result.

- (8) Through various subsidiaries, VA Tech is active in the areas of power generation (hydroelectric power stations and fossil fuel power stations), power transmission and distribution, metallurgy engineering, infrastructure (in particular building infrastructure), rail traffic technology and electrical plant engineering.

II. THE PROPOSAL

- (9) The object of the notification is the proposal by Siemens, through a public bid by its subsidiary Siemens Österreich, to increase an existing holding in VA Tech from 16.45% of the voting rights to at least 50% plus one share and so to acquire sole control. [...] ⁴

III. CONCENTRATION

- (10) The proposal is a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

IV. COMMUNITY DIMENSION

- (11) The companies involved achieve a combined aggregate worldwide turnover of more than EUR 5 billion.⁵ (Siemens: EUR 74 billion in the financial year from 1 October 2002 to 30 September 2003; VA Tech: EUR 3.9 billion in the financial year 2003). Siemens and VA Tech each have an aggregate Community-wide turnover of more than EUR 250 million [...]. Neither of the companies achieved more than two thirds of its aggregate Community-wide turnover within one and the same Member State. The notified concentration therefore has a Community dimension within the meaning of Article 1(2) of the Merger Regulation. The proposal constitutes a case of cooperation with the EFTA Surveillance Authority under Article 57 of the EEA Agreement.

V. COMPETITION ASSESSMENT

- (12) The proposed concentration leads to numerous horizontal overlaps and vertical links, in particular in the following areas: A. Power generation (equipping hydroelectric power stations and gas-and-steam power stations); B. Power transmission and distribution; C. Rail; D. Frequency Inverters; E. Metallurgy and Other Industrial Plant Building; F. Low Voltage Switchgear; G. Building technology; and H. Infrastructure Facilities and Cable Ropeway Electrics, I. Other IT-Services

⁴ [...]

⁵ The turnover calculation is made on the basis of Article 5(1) of the Merger Regulation and the Commission notice on calculation of turnover (OJ C 66, 2 March 1998, p. 25).

A. POWER GENERATION

AI. EQUIPMENT FOR HYDROELECTRIC POWER STATIONS

1. Relevant product market

- (13) Siemens says that the equipping of hydroelectric power stations is a product market in its own right and that further segmentation, e.g. into electrical and mechanical engineering, is not necessary. The product market proposed by Siemens accordingly comprises all the mechanical and electrical components of a power station, such as water turbines, generators, instrumentation and controls, hydraulic control systems, pump turbines, valves, etc. The construction work (e.g. the dam), on the other hand, would belong to a separate product market, in which neither Siemens nor VA Tech is active.
- (14) According to Siemens, the fact that, on the supplier side, most competitors can offer both mechanical and electrical engineering, as well as a trend also evident in Europe towards joint tenders for both groups of components, indicate such a broad product market definition. In this connection, the notifying party refers to several concentrations between manufacturers of mechanical equipment and electrical manufacturers in recent years, including Alstom/ABB, GE Hydro/Kvaerner and VA Tech/Sulzer as well as the joint venture between Siemens and the mechanical manufacturer J.M. Voith AG. To this extent, in Siemens' opinion, the market conditions since the Commission Decision in Voith/Siemens/JV (M.1793) have changed.
- (15) The Commission's market investigation confirmed that the main suppliers of hydroelectric power stations in the EEA, including Voith Siemens, VA Tech, Alstom, and GE Hydro, can supply both mechanical and electrical components, even if market presence and reputation with customers are not the same for both areas in each case. The companies' product range includes in particular water turbines and hydrogenerators as well as other mechanical and electrical components, the "mechanical balance of plant" ("MboP") and the "electrical balance of plant" ("EboP"). It is not possible to confirm whether the Asian suppliers (from China, India and Japan) are also active in the various areas because, at present, they are not perceived as credible suppliers in the EEA by the customers questioned in the market investigation. Nor have they so far taken part in any tenders in the EEA (see Part VI).
- (16) The market investigation also shows that the scale of the product packages jointly sought in tenders for hydroelectric power stations varies enormously. There are both tenders for total equipment (mechanical and electrical) and tenders for individual components. The latter is particularly the case in modernisation projects, which account for a large share of demand in the EEA. Here tenders often relate to only

parts of the mechanical or electrical equipment.⁶ From the point of view of demand, the various hydroelectric power station components are not substitutable.⁷

- (17) On the other hand, the supply-side substitutability cited by the parties leads to the conclusion that the relevant product market covers the equipping of hydroelectric power stations (without any distinction as between mechanical and electrical equipment) since the main competitors listed by Siemens, in so far as they are active in the EEA, have confirmed that they are active in both mechanical engineering and in electrical engineering as well as in MBoP/EBoP.⁸
- (18) Furthermore, hydroelectric power stations vary considerably in size. For example, water turbines are supplied with an output ranging from less than one megawatt up to an output of approximately 700 MW. A number of smaller local suppliers are active mainly in the area of small hydroelectric power stations ("compact hydro" or "small hydro").⁹ Some of these companies only have an annual turnover of less than €10 million. The hydroelectric power station components in the compact hydro sector are much more standardised and, from the point of view of demand, cannot be substituted with larger components. However, hydroelectric power station equipment is offered in a continuum of output levels, without there being any obvious dividing line. For organisational purposes, VA Tech Hydro¹⁰ classes installations up to 15 MW as belonging to the compact hydro area of the business.¹¹ The reason given for this classification is, among other things, that some national tax incentive programmes are limited to installations under 15 MW. Furthermore, these are standardised and modularised products which can be used on the market for smaller installations.¹² Other market participants have suggested lower output levels for a delimitation of the small hydro segment. The German law on renewable energies (in contrast to other national programmes) currently limits the tax incentive to 5 MW installations.¹³
- (19) Together with the lack of a clearly definable dividing line for a possible distinction between size classes, the following additional characteristics of the hydroelectric power market in the EEA lead to the conclusion that subdivision into different product markets on this basis would not be appropriate. The dividing line is further blurred by the fact that in the EEA most tenders relate to the replacement, modernisation or refurbishment of power station components. Smaller competitors sometimes offer refurbishment work on larger installations, whereas larger suppliers also offer their services for very small tenders for projects of less than EUR 1 million.¹⁴ Given these supply-side factors, a subdivision of the market for the

⁶ See, for example, the comments of Norsk Hydro (a Norwegian customer) on possible tendering strategies (#1973).

⁷ For example, turbine versus generator, piping versus electrical components. The fact that these products cannot be substituted for each other but are at most complementary products, should not need any further explanation.

⁸ See competitors' replies to the Commission's market survey and customers' replies, described in further detail in Section 3.

⁹ Including Andino, Kössler, Wasserkraft Volk, Gugler, Gilkes and Andritz.

¹⁰ In VA Tech Hydro GmbH, VA Tech's hydroelectric and "combined cycle" activities are combined.

¹¹ 2003 Annual Report of VA Tech Hydro, p. 4.

¹² See VA Tech's reply to question 3 of the request for information "Questions to VA Tech, 17.3.2005".

¹³ See HydroWorld Alert, 1.12.2003, p. 7, submitted by Siemens in document #6661.

¹⁴ See Siemens' bidding lists.

equipping of hydroelectric power stations into different size classes is not necessary in this case.

- (20) As suggested by Siemens, the relevant product market therefore covers the equipping of hydroelectric power stations. As explained in paragraphs 16 to 19, the products in this market are characterised by considerable product differentiation.

2. Relevant geographic market

- (21) Siemens is of the opinion that the market in hydroelectric power station equipment is a worldwide market as all the main suppliers are active worldwide and "only rarely" do national preferences still exist. Even suppliers which had so far only been active regionally (including the Chinese suppliers Dongfang and Harbin, the Indian BHEL or Japanese firms) had in the meantime been making advances worldwide. For example, among other things, the Chinese supplier Sichuan Electricity had been awarded a project in Georgia. Furthermore, Siemens says in the notification (pp. 27/28) that price formation for hydroelectric power equipment takes place worldwide, that worldwide price competition is "enormous", that "regional price differences are hardly noticeable" and that there are no "major cost-related trade barriers". It also points out that its own hydroelectric power business (Voith Siemens) alone has production capacities outside the EEA, in China and Brazil. The market data submitted by Siemens indicate that some [5-10]*% of the worldwide turnover in hydroelectric power equipment comes from the EEA.
- (22) So far the Commission has examined the market in equipping hydroelectric power stations only for the purpose of clearance decisions pursuant to Article 6(1)(b) of the Merger Regulation. In case COMP/M.1793 - Voith/Siemens, the parties argued that the market was worldwide or at least EEA-wide, but that for maintenance work it was only EEA-wide. In that case, however, the relevant geographic markets did not need to be delineated further because in all alternative geographic markets examined effective competition would not have been significantly impeded in either the EEA or in a substantial part thereof.
- (23) The concentration in the case COMP/M.1484 - Alstom/ABB related to different types of power generation equipment, in particular for gas and gas-and-steam power stations. Hydroelectric power components played a subordinate role. The parties had argued in favour of a worldwide market, using the following arguments: "According to the parties the relevant geographic market for all affected product markets is the world for the following reasons: the major players in the power generation equipment industry (i.e. GE (US), Mitsubishi ("MHI") (Japan), Siemens (D)/Westinghouse (US) and ABB and ALSTOM), bid for all the major contracts in the world regardless of the location of the customer and do win bids in all of these areas. This worldwide tendering has resulted in worldwide price convergence for steam turbines and a substantial degree of worldwide price convergence for gas turbines."¹⁵ In this case too, the Commission ultimately left the geographic market definition open as there were no concerns about competition regardless of whether an EEA-wide or a worldwide market definition was applied. The hypothesis put forward by the parties in the Alstom/ABB case that in a world market all major

¹⁵ COMP/M.1484 - Alstom/ABB, paragraph 32.

competitors take part in tenders worldwide and also win them, as well as the question of price convergence will, however, also be examined below.

- (24) In the present case, the Commission's market investigation confirms that the leading suppliers in the market in hydroelectric power station equipment in the EEA (Voith Siemens, VA Tech, Alstom and GE Hydro) are active worldwide, even if they focus on certain main geographical areas. Siemens, Alstom and GE in particular have considerable production capacities outside the EEA. [...] ^{16 17}
- (25) The competitor analysis contained in the internal documents submitted by Voith Siemens also confirms the Commission's observation¹⁸ that the main geographical areas in which Siemens, VA Tech, Alstom and GE Hydro are active are supported by a local presence with service offices or even production plants. [...] ¹⁹ GE Hydro is similarly successful particularly in the regions (e.g. North America and Scandinavia) where it is represented by production plants and/or service offices. Alstom has production facilities in France and in China and Brazil.²⁰
- (26) Therefore, even if the main competitors listed by Siemens with a base in Europe are active to varying degrees on the world market, the EEA market differs from other parts of the world in that the Asian suppliers named by Siemens have so far not entered the EEA as credible bidders and so far have not won any projects here either. Similarly, the Asian competitors cited by the parties are not perceived as being potential suppliers by the customers questioned in the market investigation.²¹ The argument put forward by the parties that there are worldwide tendering procedures in the hydroelectric power market does not alter this. The fact that firms from other geographical areas which are less highly regarded by or unknown to customers could theoretically take part in tenders does not in itself alter the fact that a small but significant non-temporary price rise by a hypothetical monopoly-holder in the EEA would be profitable. In addition to this, the competitors would also have to be in a position to offer sufficiently close substitutes quickly, without significant sunk costs arising. Particular importance also attaches to being able to cite references from successfully completed projects, such references being necessary to allow firms to position themselves as credible suppliers. The absence from the EEA of the competitors listed by the parties as well as the clearly lower regard in which they are held by customers in the EEA²² indicates that there is not a uniform world market in hydroelectric power station equipment.
- (27) Accordingly, the observed market shares of European companies in Europe do not, as argued by the parties in response to the decision pursuant to Article 6(1)(c) of the Merger Regulation, result only from past history, but also from the customers' structure of preferences (see also Part VI) and from the ability of the suppliers to supply products tailored to the needs of the customer and, where necessary, to provide rapid support through customer service.

16 [...]*

17 [...]*

18 For example, on the basis of the bidding lists (see also section 3 below).

19 [...]*

20 According to notification (p. 28).

21 See evaluation of customers' responses to the Commission's market investigation in section 3 below.

22 Ditto.

- (28) In response to the Commission's enquiry as to any activities of new non-European competitors in the EEA,²³ Siemens was unable to provide any relevant evidence. In the analysis, a distinction must in any case be made between belonging to a *relevant market* and *potential competition* through market entry. In terms of content, the parties' arguments seem to be geared more to market entry but, even against this background, appear speculative as they are neither substantiated by the parties nor confirmed by the market investigation.
- (29) As for the argument put forward in the reply to the Commission's decision pursuant to Article 6(1)(c) of the Merger Regulation that, in the case of hydroelectric power station equipment, "worldwide homogeneous pricing or the presence of a correlation of price changes" was evident, Siemens put it down to demand. [...] ²⁴*
- (30) [...] ^{25 26 27}* If a single world market did in fact exist, it would be expected that Chinese suppliers would have endeavoured in 2001 and 2002 to win orders from European customers in order to take advantage of the - from their point of view - attractive price levels in the EEA. In fact, however, nothing points to any participation of Chinese companies in tenders for hydroelectric power station equipment in the EEA. The same applies to companies from other regions of the world (including other Asian countries), in so far as they are not already active in the EEA. Nor is the reference by the parties to two fairly large hydroelectric power projects by Dongfang in Albania in the 1960s and 1970s convincing in this respect.²⁸
- (31) [...] ^{29 30 31}*
- (32) Both from the examination of the current market structure and from the replies of competitors and customers to the Commission's market survey (outlined in section 3) [...] ^{*}, it therefore transpires that customers for hydroelectric power station equipment in the EEA see themselves faced with a different supplier structure than customers in other parts of the world and that potential market power in the EEA would in particular not be eliminated by the presence of suppliers in China, India or other parts of the world.³² The relevant geographic market does not therefore extend beyond the EEA.

3. Competition assessment

(a) Market shares

- (33) In the notification, Siemens estimated its own market share as well as those of VA Tech and the other competitors (see the following table). It suggested here that the market shares should be considered cumulatively over a period of five years (2000 to

²³ See question 1 of the request for information of 10.3.2005.

²⁴ [...] ^{*}

²⁵ [...] ^{*}

²⁶ [...] ^{*}

²⁷ [...] ^{*}

²⁸ See reply to the request for information of 10.3.2005, Annex 1b.

²⁹ [...] ^{*}

³⁰ [...] ^{*}

³¹ [...] ^{*}

³² See also paragraph 9 of the Commission's notice on the definition of the relevant market.

2004) as they vary widely from year to year. For a number of years, according to its own information, Voith Siemens made no sales in the EEA.

Equipment for hydro power stations: data provided by Siemens in the notification

EEA market shares (%) 2000-04	Equipment total
	Value (EUR)
	1999-2004
Voith Siemens	[20-30]*
VA Tech	[20-30]*
Total	[40-50]*
Alstom	[10-15]*
GE Hydro	[10-15]*
Ansaldo/Franco Tosi	[<2]*
Andritz	[<2]*
Others	[30-40]*

Source: Siemens in the notification.

- (34) VA Tech, by contrast, puts Siemens' and VA Tech's joint share of the market at [40-50]*% (Voith Siemens [10-15]*%, VA Tech [30-40]*%, Alstom [15-20]*%, GE Hydro [15-20]*%, Others [20-30]*%).³³ Alstom estimates that Siemens/VA Tech would jointly account for 61% of EEA sales of hydroturbines. In the case of electrical equipment, it estimates Siemens'/VA Tech's share of EEA-wide sales as being 43%.³⁴ The market share estimates of the other competitors and customers are generally within the same range, even if the estimates of smaller competitors in particular show fluctuations in both directions. For example, Andino estimates Siemens' and VA Tech's joint market share at 70%,³⁵ while Andritz puts it at only 41%.³⁶
- (35) On the basis of turnover figures for the competitors listed by Siemens, the Commission has carried out its own market share calculations. If one accepts here the volume of the turnover not attributed by Siemens to any competitor ("Others"), the market shares are as follows:

EEA 2000-04	€ million	Market share(%)
Siemens	[...]*	[10-20]*%
VA Tech	(*)	[30-40]*%
Combined	(*)	[...]*%
Alstom	(*)	[20-30]*%
GE Hydro	(*)]	[0-10]*%
Ansaldo	(*)	[<1]*%
Andritz	(*)	[<1]*%
Others	[...]*	[20-30]*%
Sum	(*)	100%

Source: Calculations by the Commission.

(*)These turnover figures are business secrets of the individual firms.

³³ See VA Tech's reply to question 35 of the "Questionnaire to Competitors - Power Generation".

³⁴ See Alstom's reply to question 35 of the "Questionnaire to Competitors - Power Generation" (#3680).

³⁵ See Andino's reply to question 35 of the "Questionnaire to Competitors - Power Generation" (#1310).

³⁶ See Andritz's reply to question 35 of the "Questionnaire to Competitors - Power Generation" (#1324).

- (36) From the turnover figures for competitors compiled by the Commission, just as in the case of the VA Tech estimate, it can be seen that Siemens has overestimated its own market share but underestimated that of VA Tech. Alstom achieves much higher market shares, while GE's market share is lower than that estimated by Siemens.
- (37) The notified concentration would therefore bring together two of the leading suppliers of hydroelectric power plant equipment. Voith Siemens/VA Tech would increase their market leadership considerably over the remaining competitors Alstom and GE. [20-30]*% of the market is not attributed to any competitor or is accounted for by very small suppliers or suppliers which supply only certain EboP components or services but are not active in the core areas of hydroelectric power.³⁷
- (38) Siemens argues³⁸ that, in the case of hydroelectric power plant equipment a competitive bidding market is involved and that market shares therefore "tell us very little". It quotes here from the Commission's decisions in Framatome/Siemens³⁹ and Siemens/Alstom Gas⁴⁰ as well as from the US Horizontal Merger Guidelines. The passages quoted indicate that (in view of the market strength given) market shares in competitive bidding markets must be treated with caution where orders are only rarely awarded. Furthermore, reference is also made to the number of credible suppliers for competition in a competitive bidding market. The passage quoted from the US Merger Guidelines is as follows: "Where all firms have, on a forward-looking basis, an equal likelihood of securing sales, the Agency will assign equal market shares." In the present case, however, it is neither a question of orders rarely being awarded, nor does anything indicate that there is an equally great probability of all the competitors named by the parties being awarded future tenders.
- (39) It should be noted that the fact that there is bidding on a market does not in itself allow any conclusion to be drawn as to the intensity of competition to be expected or as to the significance of market shares as an indicator of possible market power. The key factor is rather the bidding pattern in individual cases. For example, even where there is a small number of credible bidders, particularly intensive competition is to be expected if, in a bidding market, a large proportion of tenders is awarded in a few, large transactions and the products of the various competitors and their cost structure are largely homogeneous. In this and similar cases, market shares would, in practice, provide very little information on the possible market power of a bidder. The following remarks show, however, that the sources cited by the parties for the market for hydroelectric power plant equipment are not relevant.
- (40) Even if, in the market for hydroelectric power plant equipment there is a bidding market, various factors lead to the conclusion that the market shares of the various competitors in the current case do nevertheless say a great deal about their market strength. In particular, there are frequent tenders, often of a very small size. Only [...] of the [...] tenders submitted by Siemens had an order size of more than EUR [...]. As described in the notification (see *inter alia* p. 66), what is involved in

³⁷ These also include in particular ABB, which, according to Siemens' bidding data, regularly takes part in tenders in the EboP area but otherwise does not produce either hydroturbines or generators.

³⁸ In its reply to the Commission's Article 6(1)(c) decision.

³⁹ COMP/M.1940.

⁴⁰ COMP/M.3148.

the case of hydroelectric power plant equipment are individual components which are customised to suit the order in question. The heterogeneity of the products supplied by different manufacturers, the large variety of different components and the varying esteem in which the competitors are held by different customers (see below) show that the market is characterised by clear product differentiation.

- (41) For larger projects there is also *ex ante* uncertainty about the actual profitability of a project for the winner of an invitation to tender as the exact costs are subject to certain technical and legal imponderables.⁴¹ In a tender, therefore, the expected value of the lowest bid rises if the number of credible bidders goes down.
- (42) The market shares of Siemens, VA Tech and their competitors are consequently the result of over [...] real purchasing decisions by many customers over the five-year period in question. They also reflect the decisions of competitors to make a bid for a certain tender. Assuming maximisation of profit, the decision of whether to make a bid or not is based on a weighing-up of the costs which would be incurred and the probability of having a real chance with a given customer.⁴² In view of the large number of tenders, it must be assumed that the market structure observed did not come about by chance but is the result of the product portfolios offered by the different manufacturers, their installed base, their cost structure and similar differentiation features, as well as customer preferences. The market shares therefore contain considerable information about the market strength of the different suppliers, i.e. their ability to take part successfully in future tenders as credible bidders.
- (43) Consequently, the high joint market shares of Voith Siemens and VA Tech, as well as the wide gap between them and the only significant remaining competitors, Alstom and GE, already suggest that the notified concentration is likely to lead to a considerable lessening of effective competition in the common market (dominant position of Siemens/VA Tech). The number of credible suppliers would be reduced from four to three. This assessment is not weakened but, on the contrary, reinforced by the concerns voiced by numerous customers and competitors that the concentration would lead to a lessening of competition, as well as well as by the analysis of the tendering data submitted by Siemens, VA Tech, Alstom and GE Hydro.

(b) Market investigation and internal documents

- (44) The following were contacted for the market investigation: the customers in the EEA named by Siemens in the notification, the competitors named by Siemens, the customers named by VA Tech and the 50 largest hydroelectric power station operators in the EEA, this list also being compiled by Siemens. Of the latter, however, several said that they did not operate any hydroelectric power stations. Of the competitors outside Europe, only [...] replied. Both among those customers who replied and among the competitors a large number (and numerically a clear majority) expressed concerns that the notified concentration would lead either to "anti-competitive effects" or to higher prices. A number of customers and competitors said that they could not foresee the effects on competition or were not

⁴¹ See *inter alia* Alstom's reply to question 7 of the "Questionnaire to Competitors - Hydro Power".

⁴² [...]*

active in the hydroelectric power market. On the other hand, there were hardly any positive reactions.

- (45) It is clear from the market investigation and from the internal documents of Voith Siemens and other competitors that Siemens, VA Tech, Alstom and GE Hydro are together perceived in the market as a group of competitors who clearly stand out from the other suppliers as regards product portfolio and market penetration. In the respective competitor analyses the other suppliers in the EEA are totally ignored. [...]*⁴³
- (46) It was already clear from the answers to the Commission's questionnaires in Phase I that Siemens, VA Tech, Alstom and GE Hydro were viewed in the question on strengths and weaknesses⁴⁴ as being suppliers with the strongest product ranges while mainly attributes such as a lack of flexibility, high price and similar factors were deemed to be weaknesses. It was clear already from these replies that the other competitors were viewed as being much weaker or the relevant boxes were not filled in.
- (47) The Phase II questionnaires were intended to quantify the market position of the individual competitors more accurately. The question to customers was:

"How would you rate the following suppliers of hydro power equipment, in terms of know-how and market penetration **relative to VA Tech**? Please use the following grading system:

⁴³ [...]*.

⁴⁴ Question 37 of the "Questionnaire to Customers - Power Generation" and question 42 of the relevant competitor questionnaire.

- +2 - This competitor is significantly stronger than VA Tech in this area.
- +1 - This competitor is somewhat stronger than VA Tech in this area.
- 0 - This company is comparable to VA Tech in terms of know-how and market penetration.
- 1 - This competitor is somewhat less strong than VA Tech in this area.
- 2 - This competitor is significantly weaker than VA Tech in this area.

Competitor	Hydro power equipment generally	Hydro turbines	Hydro generators	Mechanical balance of plant (e.g. valves, gates, pipes etc.)	Electrical balance of plant (e.g. pumps, transformers etc.)	Services
Alstom						
Voith Siemens						
VA Tech						
GE Hydro						
Ansaldo						
Franco Tosi						
Andritz						
Andino						
Toshiba						
Hitachi						
Dongfang						
Harbin						
BHEL						
Any others:						

"

(48) The evaluation of the replies of the 25 customers who filled out the table produced the following result for "hydro equipment generally" (9 = do not know the competitor, no business relationship, no reply or something similar):

Customer assessment of competitors

Competitors	Hydro power equipment generally					
	2	1	0	-1	-2	9
Alstom	4%	8%	56%	28%	0%	4%
Voith Siemens	8%	16%	52%	16%	0%	8%
VA Tech	0%	0%	100%	0%	0%	0%
GE Hydro	4%	12%	40%	20%	0%	24%
Ansaldo	0%	0%	4%	20%	4%	72%
Franco Tosi	0%	0%	0%	24%	4%	72%
Andritz	0%	0%	12%	16%	12%	60%
Andino	0%	4%	0%	12%	12%	72%
Toshiba	0%	0%	8%	8%	4%	80%
Hitachi	0%	0%	8%	8%	4%	80%
Dongfang	0%	0%	0%	4%	8%	88%
Harbin	0%	0%	0%	4%	8%	88%

BHEL	0%	0%	0%	4%	4%	92%
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The evaluation of the table above shows first of all that all the respondents, as asked, gave their assessment relative to VA Tech (100% grade "0"). The assessment of Siemens, Alstom and GE Hydro is symmetrical to VA Tech, which means that approximately the same number of customers rate this competitor as being as strong or stronger/less strong. On average, Voith Siemens is rated slightly more highly than Alstom and GE Hydro. All other competitors are rated either very much lower or are unknown to the customers surveyed. The latter applies in particular to all non-European suppliers.

- (49) An even more detailed evaluation of the data further reveals that, in the area of hydrogenerators, Alstom is considered to be the strongest supplier among the four market leaders, while Voith Siemens, followed by VA Tech, is given the highest ratings for turbines.⁴⁵ This customer assessment would be in line with Alstom's reply to the Commission's questionnaires, according to which Siemens and VA Tech had the leading hydroturbine technology. This result is obtained by aggregating the customer assessments. Although the evaluation also stands up to a sensitivity analysis regarding the method of aggregation,⁴⁶ because of the small number of customers on which it is based it can provide only indications. The one reliable result of the evaluation of the Phase II questionnaires remains the finding that Siemens, VA Tech, Alstom and GE Hydro form a leading group, from the point of view of customers, as regards know-how and market penetration and, as such, clearly stand out from all the other competitors. [...]*
- (50) The competitors' replies to the relevant question of the Phase II questionnaire come to the same result. However, a quantitative aggregation is not a straightforward matter here, as the assessments are in each case carried out in relation to the respondent's own company.⁴⁷ Reference is therefore made to the competitors' individual replies. However, the division between Voith Siemens, VA Tech, Alstom and GE Hydro, on the one hand, and the other competitors, on the other, is clear here too.

(c) Tendering data

- (51) In a subsequent step the Commission analysed bidding lists submitted by Siemens, VA Tech, Alstom and GE Hydro in order to obtain further information about the closeness of the competitive relationship between Siemens, VA Tech and the other competitors. An examination of the market shares suggests that Siemens and VA Tech are frequently in competition with each other in tenders. If this were not the case, it might be that the two companies did not supply close substitutes, e.g. because they covered different segments of the market. This could lead to the conclusion that the market share addition observed exaggerates the actual effect on competition. The analysis is based on the assumption that companies take part in particular in those tenders which they think they have a chance of winning, e.g. because they are able to meet the tender specifications.

⁴⁵ See Excel tables prepared by the Commission "Siemens_Ranking by Customers".

⁴⁶ Ditto: cf. working papers "Results, generators" and "Results, turbines".

⁴⁷ The question put was: "How would you rate the following suppliers of hydro power equipment, in terms of know-how and market penetration **relative to your own company?**".

As participation in tenders involves costs, this hypothesis is consistent with the assumption of profit maximisation. [...] ⁴⁸

- (52) Ideally, the bidding data should be evaluated on the basis of an aggregated list of all competitors. However, this was not possible for two reasons. In the first place, both VA Tech and also Alstom and GE Hydro class their bidding lists as being confidential. Secondly, it is not possible to assign the four bidders to a single bidding list in many cases. This is because the respective tenders appear in the various lists under different descriptions. Even the tendering date varies in most cases. Even when there are similar project names, it is often not clear whether the same tender is involved or different lots within the same project.
- (53) The Commission therefore first analysed separately the bidding data submitted by Siemens. The Siemens data include [...] * tenders, of which only [...] * have a value of more than EUR [...] * . Of these, participating competitors are named in [...] * cases. This reveals the following:

Participation in tenders in the EEA (Siemens data)

Voith Siemens	VA Tech	Alstom	GE Hydro	Andritz	Kössler	F. Tosi	ABB	Others	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*
[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*	[...]*

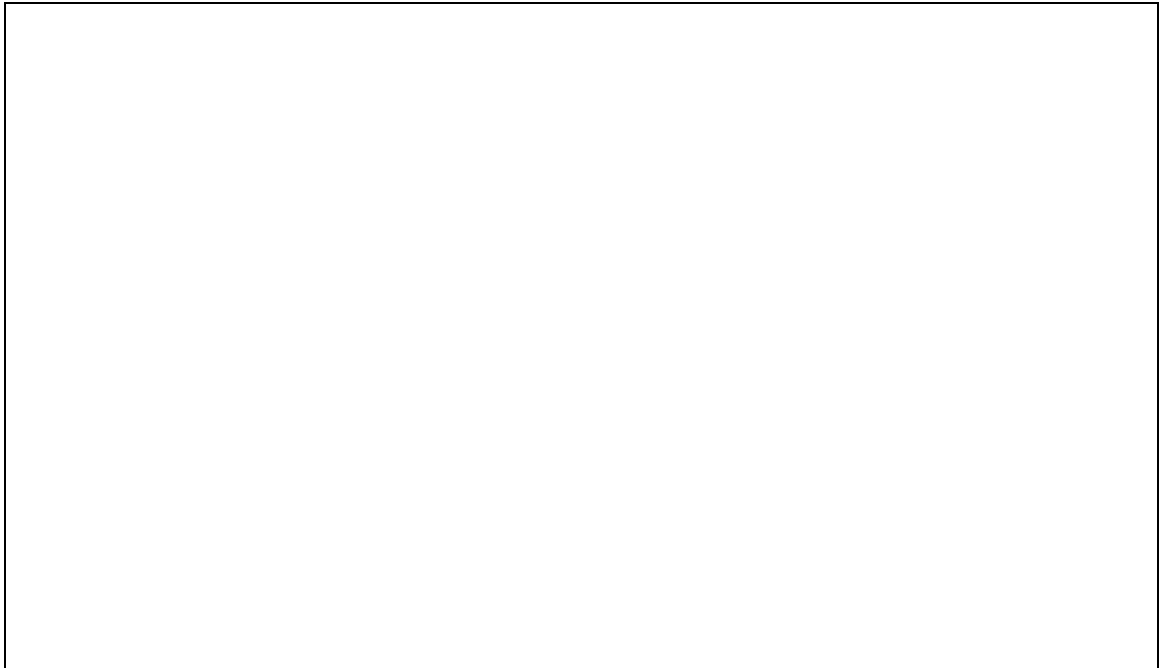
[...]*

- (54) [...] * The following chart compares the geographical profile of the four companies, with the names of the countries on the x-axis being removed for reasons of confidentiality. The y-axis shows the percentage of bids accounted for by each country.

Geographical profile of participation in tenders

[...]*

⁴⁸ [...] *.



- (55) The bidding data examined show that Siemens and VA Tech are the bidding companies which most frequently come into direct competition with each other. [...] *GE Hydro is currently tending to reduce its presence in Europe.⁴⁹ With the notified concentration, Siemens would therefore take over its most direct competitor in the EEA.
- (56) The evaluation of the replies to the Commission's requests for information and of the tender documents consequently confirms that the proposal would result in a significant impediment to competition, in particular as a result of the creation of a dominant position for Siemens.

(d) The parties' arguments (dynamic effects/potential competition)

- (57) During the in-depth market investigation the Commission informed Siemens of the results of its findings, including at two discussions in Brussels on 23 March and 15 April 2005. In response to the first of these meetings, the parties submitted on 8 April 2005 a written pleading⁵⁰ in which they argued on the basis of dynamic aspects that, although the notified concentration did reveal a need for adjustment on the part of customers for equipment for hydroelectric power stations, the concentration would not result in a significant impediment to effective competition. Although the "dynamic process of worldwide consolidation" which was taking place meant inconvenience for customers since long-established supplier relationships would be affected, there were alternative suppliers which the customers could turn to at a reasonable cost. The written pleading was followed by the other documents of 12 April⁵¹ (received by DG COMP on

⁴⁹ See e-mail from Scottish Southern of 11 April 2005 referring to the relocation of GE's hydro management centre from Oslo to Quebec, Canada, and the downgrade of its Doncaster (UK) site.

⁵⁰ #6661.

⁵¹ #7020.

14 April) and of 13 April 2005⁵² and, finally, by the parties' reply to the statement of objections, in all of which a similar line of argument is pursued.

- (58) The alternative suppliers cited by the parties are mainly small suppliers from the small-hydro segment, service firms, manufacturers of small components (e.g. fittings or electrical parts) which can also be used in hydroelectric power stations, and smaller companies outside Europe. The firms listed in the written pleading of 12 April 2005 extend far beyond the companies identified as "competitors" in the notification. Siemens argues "that the majority of the orders awarded in Europe may involve a great many individual aspects of work from the area of modernisation and maintenance, for which, in turn, a great many suppliers are available." Siemens also says that: "Small specialised suppliers too are a competitive force in the market. As the procurement of equipment for hydroelectric power stations and also the awarding of maintenance and modernisation contracts take place as part of a tendering procedure, the very existence of the suppliers referred to here constitutes a 'credible threat' for companies such as Voith Siemens, Alstom, GE Hydro and VA Tech." The individual aspects of work are also specified in the written pleading. These include hydroelectric power station components such as turbine and generator parts as well as maintenance work such as checking for cracks, cleaning, replacing seals, total overhauls and similar activities.⁵³
- (59) [...]*
- (60) The documents submitted by the parties confirm the Commission's findings that in the market for hydroelectric power station equipment in the EEA, in addition to the four market leaders, there is also a fairly large number of small companies which provide the small-hydro segment with relatively standard products, as well as maintenance and service companies and small component manufacturers which are entrusted with the small projects described by the parties. The company Andino Hydropower, highlighted by the parties, is an example of this category of company. Andino's reply to the Commission's market survey in Phase I does not contain any business secrets and is therefore fully accessible to the parties.⁵⁴ The reply to the Phase II questionnaire is also partly accessible.⁵⁵ In 2004 the company had an annual turnover of EUR [...]*. In the period 2000-04 the EEA market share was [less than 1]*%. True, there is nothing to suggest that Andino is not a successful supplier of hydroelectric power products, in particular in the small-hydro segment. Andino itself says that its proximity to the customer and flexibility ("to travel with lighter baggage") is an advantage compared with VA Tech. But at the same time the company states: "Andino is simply a too small company for being considered as a competitor to the leading suppliers."
- (61) The same applies to the other companies listed by Siemens as credible bidders, whose size in terms of turnover amounts to significantly less than 1% of Siemens/VA Tech. They would have to increase their turnover by a factor of 50-100 to match the order of magnitude of VA Tech. In order to do this, they would have to develop further the relevant product portfolio with references outside the small-hydro area.

⁵² #6955.

⁵³ #7020.

⁵⁴ See Andino's reply to the questionnaire "Questionnaire to Customers - Power Generation", #1310.

⁵⁵ See Andino's reply to the questionnaire "Questionnaire to Customers - Hydro Power", #4733.

- (62) Nor, finally, is there any credibility in the argument put forward by the parties at various points that the notified concentration is part of a "dynamic process of the worldwide consolidation of manufacturers"⁵⁶ in which the European market (with a 10% share of the world market) is of negligible importance.⁵⁷ Apart from the fact that the relevance of this argument for the analysis of competition remains unclear, the concentration with VA Tech would eliminate a competitor which is mainly active in Europe and has a leading market position there. With the notified transaction Siemens would take over its most important competitor in the EEA.

(e) Conclusion

- (63) To summarise, the high joint market shares of Siemens and VA Tech, the wide gap between them and the rest of the competitors, the elimination of a leading credible bidder in the market for hydroelectric power station equipment, the fact that the concentration would bring together two close, probably indeed the closest, competitors and the absence of credible potential competitors all point to the conclusion that the notified proposal would result in a significant impediment to effective competition in the common market through the creation of a dominant position for Siemens/VA Tech. These conclusions are based on the market information submitted by numerous customers and competitors as well as on the competition concerns voiced by them, the analysis of the tender data submitted by Voith Siemens, VA Tech, Alstom and GE Hydro, and internal documents of Voith Siemens.⁵⁸

A2. EQUIPMENT FOR GAS-AND-STEAM POWER STATIONS

1. Relevant product markets

- (64) In the area of equipment for fossil-fuel power stations, the activities of Siemens and VA Tech overlap only in the case of certain components for gas-and-steam power stations. VA Tech's product range here is much narrower than that of Siemens. VA Tech essentially supplies turnkey gas-and-steam power stations using mainly components supplied by third parties. VA Tech's turnkey supply is based on turbines supplied by GE as key components, which are combined with turbo generators from its own in-house production. As part of the cooperative arrangement, VA Tech also supplies generators to GE for projects being carried out by GE. Nor does VA Tech itself manufacture steam turbines and other power station components.
- (65) Siemens therefore argues that the only market affected by the notified concentration is the market for turnkey gas-and-steam power plants. This involves integration and engineering services through which the numerous components of a power station are integrated to form a turnkey plant.
- (66) The notifying party does not attribute any significant market shares to VA Tech for the GE turbines distributed by it (since the demand relates to GE turbines and not to supply by VA Tech), nor does VA Tech appear in Siemens' presentation as a market participant for generators (since these are supplied solely as part of turnkey projects

⁵⁶ Siemens' letter to the Commission of 8 April 2005, #6661.

⁵⁷ See *inter alia* p. 26 of the notification.

⁵⁸ These are supplemented by the confidential internal documents of other market participants, which are therefore not available to Siemens.

or through GE). Nevertheless, an objective market definition is proposed in the case of turbines on the basis of the Commission Decision in Siemens/Alstom Gas & Steam Turbines (M.3148). According to that decision, a separate market exists for large gas turbines with an output of over 60 MW. According to Siemens, all the turbines affected by the concentration belong to this market.

- (67) The Commission's market investigation essentially confirmed Siemens' proposed market definition for turnkey gas-and-steam power plants.
- (68) Siemens' proposed market definition for large gas turbines was also confirmed (although, in some cases, 50 MW was proposed as the lower limit). The basis for the subdivision is the observation that gas turbines with an output of under 60 MW (50 MW) derive from aircraft turbines. The question of whether the precise lower limit for large gas turbines should be 50 MW, 60 MW or another output level can be left open here since it does not affect the assessment of competition.
- (69) Siemens does not give any more detailed definition of the generator market since it disputes that VA Tech is a market participant here. The market investigation indicates that, on the demand side at least, it might be necessary to draw a distinction between turbo generators for gas-and-steam power plants and other generators and possibly, in addition, to establish a subdivision by size category. Gas and steam turbo generators differ from other types of generator through their high turning speed, which requires a particular design. However, the market definition can be left open here since it does not affect the assessment of competition.

2. Relevant geographic markets

- (70) For the definition of the relevant geographic markets, Siemens refers to the Commission Decision in Siemens/Alstom Gas & Steam Turbines (M.3148). In that case, the notifying party (Siemens) argued that the relevant geographic market was at least EEA-wide and indeed probably worldwide. The Commission did not have to examine the market definition any further in Siemens/Alstom and therefore left it open. In the present case, the definition of the relevant geographic markets can also be left open since it has no impact on the assessment of competition.

3. Competition assessment

- (71) In the market for turnkey gas-and-steam power plants, the joint annual market share of Siemens and VA Tech in the EEA between 1999 and 2003 amounted, according to Siemens, to between [5-10]*% and [15-20]*%. Taking the period 1999-2003, the average combined market share was [10-15]*%, of which only [2-5]*% was accounted for by VA Tech. In the turnkey market, a number of suppliers would remain even after the notified merger. These include the turbine manufacturers Siemens (or Siemens/VA Tech), Alstom and Mitsubishi, but also engineering firms such as Bechtel and others, as well as the boiler manufacturer Foster & Wheeler. In the market for turnkey steam-and-gas power plants, the merger would not therefore, at horizontal level, give rise to any competition concerns.
- (72) The Commission's market investigation confirmed that VA Tech operates as a turnkey supplier of gas-and-steam power plants on the basis of turbines made by GE and turbo generators from its own in-house production. It seems to be customary and technically necessary for gas turbines and turbo generators to be matched technically

to one another and supplied as a package. The market investigation also confirmed that VA Tech does not fundamentally operate separately as a supplier of generators but supplies them for turnkey projects, together with turbines made by GE. Horizontally, therefore, there is no addition of market shares in the case of generators.

- (73) VA Tech does not manufacture gas turbines. Horizontally, therefore, there would be no overlaps here. The merger as notified would deprive GE, the world market leader for gas turbines, of a sales channel for these products in the form of VA Tech. GE (like Siemens, Alstom and Mitsubishi) also has its own generator production capacities. Given the role of gas turbines as key components in gas-and-steam power plants and given GE's leading market position in that area, it appears unlikely that GE would, as a result of the notified concentration, be deprived of access to the gas turbine market, nor did GE itself express any concerns in this respect in the market investigation.
- (74) Accordingly, the notified transaction does not, in the area of equipment for gas-and-steam power plants, result either horizontally or vertically in a significant impediment to effective competition in the common market or in a substantial part thereof.

B. POWER TRANSMISSION AND DISTRIBUTION ("T&D")

1. Relevant product markets

- (75) Like power generation equipment, the T&D market comprises a wide range of different components that are supplied individually or integrated into a system. Customers are mainly national grid operators and local/regional electricity distributors. In the T&D area too, Siemens has a wider range of component manufacture than VA Tech, which, in the case of turnkey projects, relies more heavily on external suppliers.
- (76) On the basis of the horizontal overlaps in the product range, Siemens proposes that relevant product markets be defined on the basis of the product groups listed under (a) to (e) below. According to Siemens, the area of energy automation and information systems forms an exception, with power system management and protective relays each constituting a separate market.

(a) High-voltage products (for transmission networks operating at voltages between 52 kV and 800 kV)

- (i) air-insulated switchgear
- (ii) gas-insulated switchgear
- (iii) circuit breakers
- (iv) disconnectors
- (v) instrument transformers
- (vi) coils

(b) Transformers

- (i) power transformers
- (ii) distribution transformers

(c) Energy automation and information systems

- (i) power station management
- (ii) protective relays

(d) Turnkey projects

- (i) high-voltage projects
- (ii) medium-voltage projects

(e) T&D services

- (i) asset services
- (ii) network planning

- (77) The market investigation largely confirmed the structuring of T&D markets proposed by Siemens (on the basis of the Commission Decision in Areva/Alstom (M.3296)). However, the market investigation also showed that T&D products are not only demanded as turnkey projects but that in the case of many customers there is also a demand for individual components. Purchasing policy is essentially customer-specific. Large national grid operators in particular have their own project management skills and undertake the integration of individual components themselves. Other companies have shed such activities and their demand relates mainly to turnkey projects. Market transactions therefore exist both for turnkey projects and for individual components (as regards the latter, both between component manufacturers and customers and between component manufacturers and turnkey integrators).
- (78) Since the structure of suppliers differs distinctly as between the individual components and since the various components are not substitutable, relevant product markets could exist both in the turnkey area and also at the level of the individual components. The product groups identified in paragraph (76) under (a) to (e) as (i) to (vi) would thus represent possible separate relevant product markets. This analysis was only partly confirmed by the market participants surveyed. Some customers and competitors stated in their answer to the relevant question that a market definition in terms of the general product groups was sufficient. This assessment seemed, however, to be not always based on a competition-law analysis, but frequently on a technical classification. The precise product market definition can, however, be left open in this case since it does not affect the competition assessment.
- (79) According to the Commission's enquiries, VA Tech, like Siemens, also operates in air-insulated and gas-insulated switchgear in the medium-voltage area, through its subsidiary Elin EBG. The question of whether each of these products constitutes a separate relevant product market or forms part of a wider market for MV products as a whole (similar to the overall market for HV products proposed by Siemens) can also be left open here. Whatever the relevant product market definition, the merger does not give rise to any competition concerns in this area too, which as a much less concentrated market structure than the HV sector.

2. Relevant geographic markets

- (80) Siemens argues that the relevant geographic markets in the T&D area are to be defined "after the liberalisation of energy markets as at least EEA-wide and in part possibly even worldwide". It states that there are international tenders for T&D projects in which "the traditional 'home advantage' of domestic suppliers scarcely plays any role". Furthermore, it argues, transport costs are small, international trade

is intensive, there are globally active suppliers and technical standards, and customers' internal certification procedures no longer represent significant trade barriers.

- (81) The market investigation indicates that national grid operators have indeed increasingly opened up to supplies from outside their traditional group of suppliers. Technical standards seem no longer to pose any significant trade barrier, and internal certification procedures too are ultimately in the hands of the customer. This applies in particular to the high-voltage area, which is the area in which the parties' activities mainly overlap and in which projects are, in any case, significantly customised. However, a local presence in the country of the relevant customer seems to continue to play a role in the case of national grid operators when awarding contracts. Suppliers that do not have any production capacity in the EEA (e.g. those from Japan) seem not so far to have bid to any significant extent for T&D projects in the EEA, even in cases in which they were encouraged to do so.
- (82) In so far as national differences continue to exist in the structure of supply and demand in the T&D markets, they are attributable essentially to the purchasing policy of a few large customers. In France in particular, EDF seems in some product markets to continue to be inclined to purchase from national suppliers. The main producers of T&D products are, however, all active throughout the EEA, a fact reflected both in participation in tenders and in successful bids. Consequently, the T&D markets are EEA-wide.

3. Competition assessment

(a) Market structure

- (83) In the T&D area, according to the information provided by the notifying party, the activities of Siemens and VA Tech overlap in the areas set out in the following table. On the basis of the data contained in the notification, the market shares are as follows:

EEA market shares 2003 (% , value)

Product	Siemens	VA Tech	Combined	Main competitors
a. High-voltage products	[15-20]*	[5-10]*	[20-30]*	Areva [15-20]*, ABB [15-20]*
(i) Air-insulated switchgear	[5-10]*	[5-10]*	[15-20]*	Areva [10-15]*; ABB [5-10]*; Cegelec [5-10]*, EFACEC [5-10]*
(ii) gas-insulated switchgear	[30-40]*	[10-15]*	[40-50]*	ABB [30-40]*, Areva [20-30]*
(iii) circuit breakers	[30-40]*	[5-10]*	[40-50]*	Areva [30-40]*, ABB [20-30]*
(iv) disconnectors	[30-40]*	[20-30]*(*)	[30-40]*/ [50-60]*	Areva [20-30]*, HAPAM [10-15]*
(v) instrument transformers	[10-15]*	[5-10]*	[15-20]*	Areva [20-25]*, ABB [10-15]*, Ritz [10-15]*, Artech [10-15]*, Pfiffner [0-10]*
(vi) coils	[20-30]*	[10-15]*	[30-40]*	Areva [20-30]*, ABB [15-25]*, Trafomec [5-10]*
b. Transformers	[10-15]*	[5-10]*	[20-30]*	ABB [15-25]*, Areva [15-20]*, RWE Solutions

				[5-15]*, Schneider [0-10]*, Pauwels [0-10]*, others
(i) power transformers	[10-15]*	[10-15]*	[20-30]*	ABB [20-25]*, Areva [15-25]*, RWE Solutions [5-15]*, Pauwels [2-5]*, EFACEC [2-5]*, others
(ii) distribution transformers	[10-15]*	[2-5]*	[10-15]*	ABB[10-20]*, Schneider [5-15]*, RWE Solutions [5-15]*, Areva [5-15]*, Pauwels [5-10]*, others
c. Energy automation and information systems				
(i) power system management	[10-15]*	[10-15]*	[20-30]*	ABB [10-15]*, Areva [5-10]*, others (including various software companies)
(ii) protective relays	[20-30]*	[<2]*	[20-30]*	Areva [20-30]*, ABB [10-20]*, Schneider [0-10]*
d. Turnkey projects				
(i) high-voltage projects	[50-60]*	[10-15]*	[60-70]*	ABB [15-20]*, Areva [10-15]*, Cegelec [5-10]*
(ii) medium-voltage projects	[10-15]*	[<2]*	[10-15]*	ABB [15-20]*, Areva [15-20]*, Cegelec [10-15]*
e. T&D services				
No affected markets on EEA or national basis				

[...]*(*)

- (84) The market investigation confirmed that there are essentially four competitors (Siemens, VA Tech, ABB and Areva) which produce a comparably wide range of T&D components and operate as turnkey suppliers in high-voltage projects. [...]*
- (85) Several other competitors, including Cegelec, EFACEC, Ansaldo, HAPAM, Pauwels and others, cover only individual tentative product markets. They supply individual components either direct to final customers or as subcontractors to turnkey suppliers.
- (86) On the basis of the product market definition proposed by Siemens and of the market share figures contained in the notification, the combined market share in high-voltage products, transformers, power system management and protective relays is always [20-30]*% or less. In the market for turnkey projects, the combined market share would be [20-30]*%. In each of these markets, even after the merger, four or more credible competitors would remain. The same applies to medium-voltage switchgear, where, in addition to Siemens, VA Tech, ABB and Areva, a number of other suppliers exist.
- (87) On the basis of the tentative smaller product markets identified above (see section 1 on relevant markets), market shares are sometimes significantly higher. In the case of high-voltage turnkey projects, the combined EEA market share of Siemens and VA Tech in 2003 amounted to [60-70]*% (Siemens [50-60]*%, VA Tech [10-15]*%).
- (88) The merger also leads to high market shares in a number of (tentative) component markets, particularly in the case of gas-insulated switchgear ([40-50]*% market

share), circuit breakers ([40-50]*%) and coils ([30-40]*%), with VA Tech in each case having a much smaller market share than Siemens. In the case of a separate market for disconnectors, Siemens would acquire the 40% (non-controlling) shareholding which VA Tech still holds in the business area otherwise sold to Southern Company.

- (89) The customers and competitors surveyed in the market investigation confirmed the identity of the competitors listed by Siemens in the various product areas and their market shares, albeit with some differences in estimates of market shares. In particular, no other market participant estimated the market share of Siemens and VA Tech in the high-voltage turnkey area as high as Siemens itself [...]*. This might be because the allocation of turnover to turnkey business (in contrast to the supply of the underlying components) is difficult at individual level and is handled differently by the market participants. As explained in paragraphs (93) to (95), however, market shares in the high-voltage turnkey market are of only minor importance for the competition assessment.

(b) Non-coordinated effects

- (90) As in the hydro market, Siemens argues that market shares in the T&D markets do not provide any direct information on suppliers' market power because orders are awarded through tenders. It also argues that, in the wake of deregulation and privatisation in recent years, energy supply companies have developed a strong awareness of costs which is reflected in the demand that suppliers provide "massive" discounts.
- (91) The Commission examined in particular the effects of the notified merger in the possible product markets for high-voltage turnkey projects, gas-insulated switchgear and circuit breakers as part of the more detailed market investigation. It should be borne in mind here that the horizontal overlaps between Siemens and VA Tech in the high-voltage turnkey market are, to a substantial extent, attributable to GIS-based turnkey substations. Circuit breakers are used as components *inter alia* in gas-insulated switchgear. The same applies to disconnectors, although these are comparatively less technology-intensive. These (tentative) product markets are therefore, to a significant extent, vertically linked, with Siemens, VA Tech, Areva and Alstom each being active at all three levels.
- (92) Some of the customers and competitors surveyed in the market investigation expressed concern at the notified merger, although the proportion of negative reactions was much lower than, for example, in the case of hydropower (see Section A). Competition concerns expressed by the customers surveyed were based in particular on the observation that the transaction would eliminate a further credible competitor in an already highly consolidated market. The market investigation therefore focused on determining whether the high combined market shares of Siemens/VA Tech and the reduction in the number of credible bidders from four to three in some tentative product markets would result in a significant impediment to effective competition, in particular through the creation of a dominant position.
- (93) In the (tentative) market for high-voltage turnkey projects in the EEA, Siemens already had a market share of [50-60]*% in 2003 alone. Together with VA Tech ([10-15]*%), the combined market share would have been [60-70]*%. The rest of

the market was divided between ABB ([20-30]*%) and Areva ([5-10]*%). However, the high-voltage turnkey market is heavily project-driven, and the bulk of turnover in a given year may be generated by a small number of large projects. Accordingly, the market shares of Siemens, VA Tech, ABB and Areva fluctuate widely over time. In the five-year period from 1999 to 2003, Siemens' market share fluctuated between [5-10]*% (2000) and [50-60]*% (2003). VA Tech's market share in the same period ranged between [<2]*% (1999) and [15-20]*% (2002). ABB and Areva accounted for the remaining market shares in each year. [...] It may be concluded from the wide fluctuations from year to year in market shares and the importance attaching to individual projects that the market for high-voltage turnkey projects is indeed a project-driven market in which the market shares of the individual competitors, in so far as they regularly take part credibly and successfully in tenders, cannot automatically be used to draw conclusions regarding their market power. Customers and competitors seem to perceive Siemens, ABB, Areva and VA Tech consistently as credible competitors who largely offer comparable products.

- (94) Other competitors did not achieve any significant turnover in the EEA between 1999 and 2003. The Japanese suppliers Toshiba-Mitsubishi and JAEPS participated only in tenders in Iceland and Cyprus, although they were rated as competitive suppliers by several customers at product level. However, they do not seem to have participated in tenders in the EEA apart from Iceland and Cyprus even though there was customer encouragement.
- (95) As an interim conclusion it may thus be said that the (tentative) market for high-voltage turnkey projects in the EEA is a highly project-driven market and that the notified merger would reduce the number of credible competitors in that market from four to three. Against this background, the merger could result in a significant impediment to effective competition especially if Siemens and VA Tech were rated by a substantial number of customers as first and second choice in their product preference or if the two companies were, because of their cost structure, particularly keen competitors against one another in tenders. The answers given by customers and competitors to the Commission's market survey did not provide any initial indications of any such scenario. Other indications might be provided by the bidding behaviour of Siemens and VA Tech.
- (96) If, from the customers' point of view, Siemens and VA Tech supplied close substitutes compared with other competitors, the expectation would be that they would take part in a substantial number of tenders as competitors. [...] In nearly all of these tenders, ABB and/or Areva also submitted bids. ABB and then Areva are the companies which by far bid most frequently in direct competition with Siemens. [...]
- (97) The same bidding analysis as for high-voltage turnkey projects was also carried out for gas-insulated switchgear and for circuit breakers. All the tenders identified by Siemens and, as far as possible, aligned with competitors' data for the period from 1999 to the beginning of 2005 were examined. [...] As previously, ABB and/or Areva also submitted bids in the case of gas-insulated switchgear and circuit breakers in almost every tender in which Siemens and VA Tech participated. ABB and then Areva are here once again and by a wide margin the companies bidding most frequently in direct competition with Siemens. As mentioned above, gas-insulated switchgear products form the basis of a substantial proportion of high-voltage turnkey projects.

- (98) The Commission then went on to analyse the bids by Siemens, VA Tech, ABB and Areva in the [...] tenders for the period from 1999 to 2003 for gas-insulated switchgear and turnkey gas-insulated switchgear,⁵⁹ in which, according to their information, all four competitors participated. The aim was to ascertain whether Siemens and VA Tech possibly were the lowest and second-lowest bidders in a significant number of bidding situations and thus, being in competition, had a particularly marked influence on the transaction price. However, this hypothesis too could not be confirmed on the basis of the data.
- (99) In the case of disconnectors and coils, the market investigation reached the same conclusion on the basis of more limited bidding data. In both (tentative) markets, compared with GIS and HV turnkey projects, there remains one other competitor. In the case of coils, this is Trafomec. In the case of disconnectors, the horizontal overlaps are confined to VA Tech's (non-controlling) [...] shareholding in the business. In addition, compared with GIS and HV turnkey projects, the products are much more standardised.
- (100) The Hungarian company Ganz-Transelektro has submitted several bids for GIS in the EEA since the country joined the European Union in May 2004 and has since won its first contract [...]. According to its own data, it is already active in other parts of the world, particularly the Middle East. By contrast, Japanese competitors still seem not to be engaging in competition in the EEA to any significant extent (with the exception of offshore islands such as Iceland and Cyprus).
- (101) To summarise, the situation is as follows: because of their structure, the (tentative) markets for HV turnkey projects, GIS and circuit breakers could produce competitive market results in principle even with only three credible bidders offering close substitutes (and one possible potential competitor). Neither the market survey nor the bidding analysis allows the conclusion to be drawn that the notified merger would result in a significant impediment to effective competition, notably through the creation of a dominant position. This analysis relates to possible non-coordinated effects of the notified merger.

(c) Coordinated effects

- (102) In addition, the elimination of a competitor from a market which, with only four suppliers, is already highly concentrated could allow the remaining firms to coordinate their competitive behaviour and thus, at the expense of their customers, achieve higher prices in tenders for HV turnkey projects, GIS and circuit breakers than in an independent submission of bids. Siemens/VA Tech, ABB and Areva would have to manage to find a coordination mechanism through which bids could be effectively coordinated. Deviations from the coordinated price would have to be evident to the other oligopolists and a credible deterrence mechanism would have to make any deviation unprofitable.⁶⁰

⁵⁹ As mentioned earlier, gas-insulated switchgear products form the basis of a large proportion of high-voltage turnkey projects. In the case of GIS projects, it is difficult in the case of some projects to allocate an individual price since the suppliers in some cases show the various components, services and options differently and separately. Other HV turnkey projects for which the various bids tended to be even more difficult to compare were therefore not included.

⁶⁰ See judgment of the Court of First Instance in Case T-342/99 *Airtours v Commission* 2002 ECR II-2585.

- (103) Any tacit coordination of bid prices in the various tenders involves considerable difficulties. In particular, individual HV turnkey projects, GIS and circuit breakers differ widely in their technical complexity and hence also in their price since each project is customised to meet the relevant customer's requirements. The products are therefore characterised by considerable non-homogeneity, and the market is thus not very transparent.
- (104) Nor is it possible from the market data and bidding data examined during the merger control procedure to identify any evidence of possible coordination mechanisms for behaviour in tenders. All four companies (Siemens, VA Tech, ABB and Areva) take part successfully in tenders practically throughout the entire EEA. The very complex coordination mechanism that would be necessary for coordinating competitive behaviour given the bidding pattern observed in this case would be difficult to maintain. There is no convincing evidence based on the data available of any coordination that already exists or would be brought about by the merger in the (tentative) markets for HV turnkey projects, GIS and circuit breakers.

(d) Conclusion

- (105) It follows that, whatever the product market definition applied, the notified merger would not, in the T&D area, lead to the creation or reinforcement of a dominant position or result in any significant impediment to effective competition.

C. RAIL

CI. ROLLING STOCK

- (106) The takeover of VA Tech by Siemens leads to overlaps in electrical traction systems for trams, underground trains, regional trains and electrical locomotives. In addition, vertically affected markets arise for trams, underground trains and electrical regional trains.

1. Relevant product markets

(a) Electrical traction systems for rail vehicles

- (107) Hitherto the Commission has examined the market in electrical traction systems for rail vehicles only for the purpose of an authorisation decision under Article 6(1)(b) of the Merger Regulation. In the Alstom/Fiat Ferroviaria Decision,⁶¹ a separate market was assumed for electrical traction, which was not, however, subdivided further. The drive train of an electrical rail vehicle essentially consists of four elements: the power converter, the traction engine, the transformer and the control system.
- (108) Either the manufacturer of a rail vehicle can buy these components individually and integrate them into the train itself, i.e. it possesses system-integration skills; for the individual components, in particular the traction motor, there are several independent suppliers. Or the manufacturer can acquire the complete drive train

⁶¹ See paragraph 31 of Commission Decision COMP/M.2069 Alstom/Fiat Ferroviaria of 18 September 2000.

from an electrical system integrator. Both Siemens and VA Tech's subsidiary Elin EBG Traction ("ETR") offer the construction and delivery of the complete drive train for the following four product groups: trams, underground trains, regional trains and locomotives. Suppliers of electrical traction also operate, as members of a consortium, under their own name in contacts with the customer, as in the case of the "Talgo 22" regional-train project.⁶²

- (109) Trams and underground trains obtain their power from a direct current network generally with 600 V to 750 V. Actual trains such as regional trains run on an alternating current network with higher voltages of up to 25 kV. From the point of view of customers, i.e. the non-integrated suppliers of rail vehicles, which manufacture only the mechanical part of a rail vehicle because of the different construction needed for the electrical traction of the various product groups such as trams, underground trains and regional trains, the tractions are not exchangeable.
- (110) In its reply to the statement of objections, however, Siemens argued that all the main suppliers, in particular the large integrated suppliers, have a portfolio that covers all areas of traction from trams to high-speed trains. Furthermore, according to Siemens, the electrical systems for the individual product groups do not differ technologically. The independent suppliers such as ETR and Vossloh-Kiepe ("Kiepe"), by contrast, specialise in specific areas and are not in a position to extend their production within a brief period of time to traction for high-speed trains. For the purposes of this Decision, therefore, electrical traction systems for rail vehicles are subdivided by product group into separate markets.

(b) Rail rolling stock

- (111) The market for electrical rail vehicles is downstream from the market for the electrical traction of rail vehicles. In the ABB/Daimler-Benz Decision,⁶³ the Commission subdivided the market for rail transport technology into five product groups (mainline trains, regional trains, local trains, wayside systems and miscellaneous), each of which contained the relevant individual product markets of electrical and diesel locomotives, electrical and diesel multiple units, passenger coaches and freight wagons, trams and underground trains, components, spare parts and maintenance. Trams, including urban railways, are sometimes referred to Light Rail Vehicles ("LRV").
- (112) In subsequent decisions, the question of whether regional trains had to be subdivided into electrical motor-trains (EMUs) including diesel-electric motor-trains and diesel motor-trains (DMUs) was left open since such a subdivision was not relevant.⁶⁴
- (113) ETR manufactures only electrical traction systems and is a competitor with Siemens only in this area. ETR's product range includes electrical traction for trams, underground trains, regional trains and locomotives. The relevant product market can be left open for the locomotives sector as the competition assessment does not change even assuming a separate market for electrical locomotives. The same

⁶² <http://www.talgo.de/talgo22.htm>.

⁶³ See paragraph 9 of Commission Decision IV/M.580 ABB/Daimler Benz of 18 October 1995.

⁶⁴ See paragraph 10 of Decision COMP/M.2139 Bombardier/ADtranz; even in ABB/Daimler Benz, this question was left open; see paragraph 75 of Commission Decision IV/M.580 ABB/Daimler Benz of 18 October 1995.

applies to regional trains, where the competition assessment does not change, even assuming a separate market for EMUs, including diesel-electric regional trains. This view is also taken by Siemens. Accordingly, for the purposes of this Decision, the relevant product markets are trams, including urban railways, underground trains, regional trains and locomotives, with the distinction in the case of locomotives between electrical and diesel traction being left open.

2. Relevant geographic markets

(a) Electrical traction systems for rail vehicles

- (114) In its Decision in ABB/Daimler Benz the Commission assumed a national market for the electrical part at least in the case of Germany.⁶⁵ In the later decision in Alstom/Fiat Ferroviaria, however, an EEA-wide market for subsystems, in particular electrical traction, was assumed.⁶⁶ Siemens argues that a restriction to national markets is not appropriate. It argues that there are sufficient examples of the supplier of the electrical part not originating in the country of the customer purchasing the rail vehicle. A system integrator of electrical traction such as ETR delivered supplies to Spain, for example, without having production facilities there. The market investigation confirmed this definition of the EEA market in the present case. All manufacturers of rail vehicles in the EEA, independent suppliers of electrical traction and component manufacturers were surveyed as part of the investigation. Only two companies took the view that national markets were involved in some member countries, although they did not further substantiate this. The Commission therefore assumes an EEA-wide market for electrical traction for rail vehicles.

(b) Rail rolling stock

- (115) In its decision-making practice to date, the Commission has accepted national markets for rail vehicles at least in those Member States in which there was a national supplier or national production capacity which met the demands of customers there. Germany, Belgium, France, Italy, the Netherlands, Sweden, Spain and Austria in particular were identified as national markets.⁶⁷ Other Member States, including Ireland and Greece, which do not have their own industry and therefore buy internationally, were included in a “rest of the EEA” market. In the present case there are horizontal overlaps or vertical links in Belgium, Germany, Austria, Poland, Spain and the Czech Republic, which all have their own production capacity.
- (116) Siemens argued that in recent years there has been a trend towards a uniform European market on account of the European contract award directives. In spite of recognisable signs of continuing Europeanisation, however, the information available to the Commission does not allow the conclusion to be drawn that an

⁶⁵ See paragraph 26 of Commission Decision IV/M.580 ABB/Daimler-Benz of 18 October 1995.

⁶⁶ See paragraph 19 of Commission Decision COMP/M.2069 Alstom/Fiat Ferroviaria of 18 September 2000.

⁶⁷ See IV/M.580 ABB/Daimler Benz, Commission Decision of 18 October 1995; IV/M.1064 Bombardier/Deutsche Waggonbau, Commission Decision of 29 January 1998; COMP/M.2139 Bombardier/ADtranz, Commission Decision of 3 April 2001.

EEA-wide market is appropriate for the assessment of the proposed concentration.⁶⁸ Even in the years since 2001, the year of the last Commission decision, national buying predominates in those Member States which have their own strong industry. For the most part, foreign firms are taken into account only through subsidiaries established within the country. Thus, in Austria, for example, contracts have been won only by the two suppliers Siemens and Bombardier, both of which, following earlier takeovers, have production capacities in the country. The same applies to Germany, where only Alstom, Bombardier, Siemens and Stadler have won orders for trams, underground trains and regional trains, all of these companies having their own production facilities in Germany as a result of earlier takeovers.

- (117) The market investigation confirmed this assessment. Apart from Siemens, only one other competitor took the view that the relevant market for the rail vehicles in question was the EEA, although a local presence in this industry was an advantage. All the others believed that the markets were national or saw the market as being in transition to a European market, with a national presence through manufacturing facilities continuing to be important.
- (118) For the purposes of this Decision, national markets have therefore been assumed for trams, underground trains, (electrical) regional trains and (electrical) locomotives in the case of those Member States which have their own strong rail vehicle industry. In the present case, these are Belgium, Germany, Austria, Poland, Spain and the Czech Republic.

3. Competition assessment

- (119) In the EEA there are eight fairly large suppliers of electrical rail vehicles as well as local suppliers of trams such as the Czech company Inekon or, as a new supplier, Leoliner Fahrzeugbau in Leipzig, which produced a new tram in 2003. Five of these suppliers are so-called systems producers, which are able to supply a complete train including electrical traction. These are AnsaldoBreda, Alstom, Bombardier, Siemens and Skoda. Four suppliers manufacture only the mechanical part. These are the two Spanish suppliers CAF and Talgo, Inekon and Leoliner. These four non-integrated manufacturers are not active over the whole product range. CAF does not manufacture electrical locomotives and Talgo does not manufacture trams or underground trains, while Inekon and Leoliner each manufacture only one tram.
- (120) Stadler was until 2001 a purely engineering firm but has in recent years developed into a systems producer by developing the ability to design the electrical traction for its trams and EMUs itself and to incorporate it into the vehicle using purchased components. Stadler does not supply underground trains or electrical locomotives. The other four non-integrated firms (CAF, Talgo, Inekon and Leoliner) must, in order to be able to supply a rail vehicle with electrical traction, find a supplier or cooperation partner for the electrical part. In principle, both the systems producers and independent suppliers of electrical traction could be considered for this.
- (121) Of the five systems producers, AnsaldoBreda does not sell its electrical traction systems to third parties, while Skoda has not yet had any success selling electrical

⁶⁸ “Analysis of the Rail Transportation Markets”, Expert report of Bearing Point, 2004, p.15: “At this stage, all subsegments have to be considered as national markets to be assessed. However, there is a clear trend towards Europeanisation for the highest technological sub-segments.”

traction systems in the EEA apart from in the Czech Republic. In addition to the three systems producers which do supply electrical traction for practically all types of rail vehicles to third parties, there are two independent European suppliers of complete electrical traction systems for rail vehicles which do not cover the whole product range. Kiepe, which belongs to Vossloh, manufactures only electrical traction for trams. The VA Tech subsidiary Elin EBG Traction ("ETR") supplies electrical traction for trams, underground trains, regional trains and electric locomotives.

(a) Trams

- (122) Siemens stated that on the market for **electrical traction** for trams in the EEA it had a joint market share with ETR of [20-30]*% (Siemens [5-10]*%, ETR [15-20]*%) in the period under consideration (1999-2003). According to Siemens, there was no overlap on a national basis. [...]*
- (123) In **Spain**, Siemens has, according to its own data, a market share in value terms of [20-30]*% for complete trams. The market leader is Alstom with [70-80]*%, while CAF has around [5-10]*%. The market investigation substantially confirmed these market shares. If we include 2004, there were 7 tenders for trams in Spain in the period from 1999 to 2004. Siemens and Bombardier each won [...]*, CAF [...]* and Alstom [...]*.
- (124) CAF won the order for the trams in Seville, which was awarded in 2004. It is fitting the 17 trams with traction manufactured by ETR. [...]*
- (125) In the last two years [...]*, CAF has not bid with any integrated supplier in Spain, only with ETR. There were in Spain three other projects with ETR acting as the planned supplier of the electrical part. However, these tenders went to the systems producers Alstom and Bombardier.
- (126) Siemens stated that CAF does not have to depend on ETR but has two alternatives which are also independent. These are Kiepe and TEAM/Ingelectric. With TEAM, CAF won the tender in Bilbao in 1999 for a total of nine trams ("EuskoTran").⁶⁹ This order for the Spanish firm TEAM, a subsidiary of Ingelectric, six years ago has, however, so far been the only one for TEAM, which has no other references. In addition to this, factors other than purely economic ones could have been decisive as TEAM is a Basque company which was given the order for the tram in its own town.
- (127) Kiepe has not so far been successful on the Spanish market. However, it has attempted, in particular through approaches to CAF, to gain a foothold on the Spanish market. Furthermore, its parent company, Vossloh, has since 2005 had a production facility in Valencia which manufactures primarily diesel locomotives, but it also has a tram in its programme. Although this is being equipped, for the orders already obtained, with electrical traction provided by the previous owner of the factory, Alstom, it is certainly not improbable that Kiepe will supply the traction for future orders for this tram. Kiepe must therefore be regarded as a credible alternative to ETR.

⁶⁹ Table 2, Orders for electrical equipment, municipal transport 11-12/04, p. 18.

- (128) The proposed merger would therefore do nothing to alter the situation on the Spanish market, with at least four credible suppliers of trams continuing to be available.
- (129) In **Austria** ETR is, together with Siemens, a consortium partner for the ULF (Ultra Low Floor Tram) and supplies the electrical traction for this vehicle, which has a [60-70]*% share of the tram market. ETR is also a consortium partner with Bombardier for the Cityrunner of the Linz type, which during the same period had a market share of [15-20]*%. The remaining [10-15]*% market share is accounted for by a Cityrunner manufactured by Bombardier and ordered in 1999 by Graz with traction provided by Kiepe.
- (130) Bombardier has already developed a traction system of its own for the Linz Cityrunner, which is now known as the Flexity Outlook, and has used it in orders for the Cityrunner in France, Belgium and Spain. However, in line with the commitment given in the Bombardier/ADtranz case, Bombardier is tied to ETR until April 2006 for further orders of the Cityrunner in Linz. This applies in particular to Linz city transport authority's option on 18 more trams of this type. The aim of the commitment given by Bombardier in the Bombardier/ADtranz case was to maintain an independent supplier for electrical traction systems, including for trams. This commitment would be made obsolete by the takeover of ETR by Siemens and, provided that Siemens, as intended and as currently notified, acquires sole control of VA Tech, will be set aside by a separate Commission decision, conditional on Siemens acquiring, as intended and notified, sole control of VA Tech.⁷⁰ This and the fact that Bombardier is no longer dependent on ETR for this product suggest that there will be no substantial reduction in effective competition on the Austrian market for trams.
- (131) In **Poland** there were four tenders during the relevant period. Bombardier won [...] of the tenders and Alstom and Siemens [...]*. ETR supplied the traction for [...]*. Consequently, following the takeover of ETR, Siemens would be the supplier of [...] of the four successful trams. However, neither Alstom nor Bombardier is dependent on ETR as a supplier of electrical traction since both have their own capacity here. Nor is ETR indispensable as a means of gaining entry to this market. Alstom has taken over the Polish company Konstal and thus has a strong base in Poland since Konstal has manufactured most of the trams in use in Poland. Bombardier has won a further order in Poznan with Kiepe as supplier. In addition to these three established suppliers, Skoda has now in 2005 also won its first order for eight five-section low-floor trams for Wroclaw. It is therefore not to be expected that the takeover of ETR will result in a substantial reduction in effective competition in Poland.
- (132) In the **Czech Republic** ETR is the supplier for Skoda's 03T Astra tram and for Inekon's Trio. Inekon had initially developed the Astra with Skoda, which also built it. The Trio tram is a further development of the Astra and is built by Dopravní Podnik Ostrava (DPO). Siemens has not been able to win any tenders for complete trams. It has, however, taken part in tenders, [...]*. So far, Skoda and Inekon share the Czech market for trams, with Skoda being the clear market leader, while Inekon has so far won orders for only four trams. Skoda has its own traction systems for trams, as with the "Vectra" tram for Cagliari in Italy, and is not dependent on ETR.

⁷⁰ See Commission Decision in Case COMP/M.2139 Bombardier/ADtranz of [...] July 2005.

If, following the takeover of ETR, Siemens were to increase prices or refuse to supply its products, Skoda could switch over to own manufacture. Both Skoda and Inekon would also be able to order the electrical traction from Kiepe as an independent supplier. Alstom, Bombardier and Siemens are also available as potential suppliers of both traction and complete vehicles.

- (133) Accordingly, the takeover of ETR by Siemens does not result in any significant impediment to competition on the market for trams in Austria, Spain, Poland and the Czech Republic.

(b) Underground trains

- (134) The combined market share of Siemens and ETR in the case of **electrical traction** in the EEA was, according to data provided by Siemens, [15-20]*% in the period 1999-2003 (Siemens [15-20]*%, ETR [2-5]*%). The market leader is Bombardier with [40-50]*%, ahead of Alstom with [15-20]*%, Ansaldo with [15-20]*% and Skoda with under [5-10]*%. The market share attributed to Ansaldo relates to orders for which the traction of existing vehicles was replaced. The market investigation confirmed the market leadership of Bombardier and a combined market share for Siemens and ETR of this order of magnitude. ETR's small market share and the relatively small joint market share do not allow the conclusion to be drawn that the proposed takeover would result in a significant impediment to effective competition on the market for electrical traction for underground trains.
- (135) Tenders for underground trains are much less frequent than those for trams and regional trains. In the period under review (1999-2003), there were only 14 projects in the whole of the EEA, and ETR was able to win orders in Austria and Belgium. [...]*. Therefore, the takeover changes nothing in the existing competitive relationships in Austria.
- (136) In **Belgium** ETR supplies the electrical traction systems to CAF, which has won this tender. [...]* As the other two possible suppliers for this project, Bombardier and Alstom, had offered to supply their own train,⁷¹ the number of suppliers for the electrical traction systems in this project would have fallen from two to only one, the merged company Siemens/ETR.
- (137) Even after the planned takeover of ETR by Siemens, a further independent supplier of electrical traction would remain in the EEA. Since 2003 the Japanese company Mitsubishi Electric has been operating in the EEA. To date, it has been able to win two projects as a subcontractor in Europe, both underground train projects. It is the supplier of the metro in Athens, the mechanical part of which is built by the Korean firm Rotem, which also operates as a full-line manufacturer. The second project is the Barcelona metro, for which CAF is responsible. Since 1999 CAF has won contracts once with ETR (Brussels) and once with Mitsubishi (Barcelona) as suppliers and has bid and lost with both of them almost as frequently in other tenders in the EEA. This shows that Mitsubishi is a credible supplier of underground train traction systems.

⁷¹ Doc. 6501 of 6 April 2005, letter from Siemens, p. 3.

(138) Both in Belgium and in Austria there is only a single metro. Tenders are therefore correspondingly rare so that the winner has a monopoly until the next tender. Even after the planned takeover of ETR by Siemens, there would have been one more supplier for the electrical part of the tender for the Belgian metro. In addition, since 2003 there has been another independent supplier of electrical traction for underground trains active in the EEA in the form of Mitsubishi, which already supplies the traction for two projects. Furthermore, in the review period, CAF also won orders with systems producers, including the tenders for underground carriages in Madrid, Barcelona and Rome. For these reasons, the planned takeover of ETR by Siemens does not result in a significant impediment to effective competition in the Belgian market for underground trains.

(c) Regional trains

(139) For regional trains Siemens was not able to submit any separate market shares for the electrical part, on the grounds that the mechanics and the electrics are awarded separately on very rare occasions. ETR is the only credible independent supplier of electrical traction in the EEA which can also supply the electrical part for regional trains and has done so. Kiepe does not have traction for regional trains in its programme, and outside Japan Mitsubishi has no references for regional trains.

(140) ETR is at present an electrical system integrator for only on tried-and-tested and available regional trains. Together with Bombardier, it forms the consortium manufacturing Talent, a regional train, which is available with diesel traction, diesel-electrical traction or simply with electrical traction. It is responsible for the electrical traction system, which, in the case of the electrical ("EMU" and diesel-electrical ("DE-DMU") Talent, accounts for [...]%% and more of the value, and owns patent and protective rights for this traction system.

(141) ETR is also in a consortium with Talgo for the double-decker regional train Talgo 22, which is the first double-decker train to provide inter-car gangways on both levels. The concept of the vehicle is based on a combination of wheel set and articulated train technology from the Talgo XXI and the experiences of Talgo Oy (Finland) in building double-decker vehicles. The Talgo 22 is a new development which is not yet in use. It will become available in the course of 2005 both as an electrical multiple-unit train with traction by ETR and as a simple train set with or without multiple-unit control cars.

(142) According to ETR, EMU and DE-DMU Talents were sold during the relevant period only in Germany, Austria and Norway. In Norway, according to Siemens, there was no overlap as Siemens has sold neither electrical traction systems nor regional trains there. In 2000 Bombardier/ETR won an order for a very small number of electrically driven trains which do not lead to any significant market shares.

(143) In **Germany** Siemens has, according to its own data, a market share of [15-20]%% in the market for regional trains, behind the market leader Bombardier with [50-60]%% and Alstom with [20-30]%% and ahead of Stadler with [5-10]%%. In a separate market for electrical and diesel-electric regional motor-trains, it would, according to its own data, have a [10-15]%% market share and Bombardier a [60-70]%% market share, followed by Alstom with [20-30]%% and Stadler with [5-10]%%. According to Siemens, the Talent's share is [40-50]%%, with [...] trains sold. These figures were essentially confirmed by the market investigation. Since ETR supplies the electrical

traction for the Talent, there would be a vertical link between Siemens and Bombardier, which together supply [50-60]*% of the German market for electrical regional trains (EMUs and DE-EMUs). However, the demand side is equally strongly concentrated. The four hitherto successful suppliers in the German market, all of which have production facilities in the German market, are matched by Deutsche Bahn and a number of smaller regional railways. At least Deutsche Bahn, which accounted for the bulk of the orders during the relevant period, enjoys buyer power.

- (144) In **Austria** [...] Bombardier won orders from the ÖBB for EMUs, namely for its EMU Talent, in the relevant period. [...] By contrast, during the relevant period, Siemens won the [...] for regional diesel traction trains, which means that in the overall market for regional trains in Austria Siemens had a [15-20]*% share and Bombardier an [80-90]*% share. With its product Desiro, which like the Talent is available both as a DMU and with diesel electric or electric traction, Siemens is a close competitor of Bombardier on the Austrian market for electrically driven regional trains. Bombardier and Siemens are the only two suppliers to have their own production facilities in Austria. On the demand side, there was during the relevant period only one customer, the ÖBB, which enjoys market power as a monopsonist. On the other hand, in 2004 the Swiss company Stadler won an order for six of its electrical GTWs. Even though this involved the exercise of an option by the Linz local railway company, this order shows that Stadler too, with its GTW, which like the Desiro and the Talent exists as an EMU and as a DMU, must be seen as a credible supplier on the Austrian market for regional trains.
- (145) Siemens estimates that Bombardier requires approximately [...] to replace ETR as a supplier.⁷² This estimate was broadly confirmed by Bombardier. The latter has already developed its own electrical traction system. Since, however, ETR has industrial property rights to its own components, in particular the control and guidance system of its traction, it would be impossible for Bombardier to provide a number of important functions of ETR's traction, e.g. multiple traction with the Talent trains already delivered and fitted out by ETR. This would be a serious disadvantage for Bombardier when supplying customers who already have the Talent in their fleet. For these functions Bombardier would have to rely on ETR, which after the merger would belong to its direct competitor Siemens. In addition, Siemens would gain access to the technical knowledge of a direct competitor.
- (146) A link between Bombardier and Siemens would reduce competition between the two companies in tenders in Germany and Austria. Siemens would be in a position to dispense with price concessions in the discussions following the tenders and, instead of this, to earn profit as a supplier of the electrical traction, which constitutes up to [...] of the value of a regional train.
- (147) However, Siemens has concluded a contract with Bombardier that enables Bombardier to [...] and to supply the Talent as a wholly independent competitor. This means that the number of independent suppliers of EMU regional trains remains unchanged. Consequently, the planned takeover of ETR by Siemens would not result in a significant impediment to effective competition in the German and Austrian markets for regional trains or in the market for electrical regional trains.

⁷² [...]*.

(d) E-locomotives

- (148) ETR also supplies electrical traction for e-locomotives. Siemens is a manufacturer of electrical locomotives. The takeover of ETR would mean the removal of an independent manufacturer of electrical traction for locomotives from the market. However, ETR did not have any success in tenders in the last [...] years. Furthermore, there is still at least one other manufacturer of traction for electrical locomotives in the EEA. The Spanish supplier Team/Ingelectric is the supplier of the traction for the 44 variable-gauge electrical locomotives which have been ordered by Renfe from the manufacturer Talgo and the prototype of which was presented in December 2004. It is therefore not to be expected that the proposed takeover of ETR by Siemens would result in a significant impediment to effective competition.

(e) Changed market situation due to the removal of ETR

- (149) Siemens claims that there will be no decisive change in the structure of the market due to the takeover of ETR. Already [...] of ETR's order book was taken up with orders from Siemens. The [...] set of orders resulted from projects with Bombardier, which could also manufacture electrical traction systems itself. According to data from Siemens, on average in the four years from 2001 to 2004 [50-60]% of orders came from Siemens, [30-40]% from Bombardier and [5-10]% from CAF. This order of magnitude for the figures was confirmed by VA Tech. However, these figures refer to the past. The proportion of orders carried out with CAF grew significantly only as from 2004 and, according to targets, should rise further. Nor has the Talgo 22 project yet been taken into account in these figures, although preliminary work on it has been carried out and orders are expected as from 2006.
- (150) These figures show that ETR is an increasingly important partner for the two non-integrated manufacturers of rail vehicles, which have no competence in the electrical part. Furthermore, for certain markets and products ETR is also an important partner for systems producers, in particular for Bombardier and the Talent.
- (151) However, Siemens takes the view that the removal of ETR would not pose any competition problems since, on the one hand, there are sufficient alternatives to ETR for the supply of electrical traction and on the other, even if the worst came to the worst and the non-integrated suppliers of electrical rail vehicles were removed, there would still be sufficient competition.
- (152) Whereas trams and underground trains each still have an independent supplier of electrical traction with up-to-date references, it is questionable whether the same situation applies in the case of regional trains. Siemens argues here that there are still independent Japanese electrical manufacturers for regional trains and that there are two new market participants in the shape of ABB and Medcom. The market investigation has, however, shown that hitherto ABB has supplied only essential components, in particular the frequency converter, but not the entire package. Therefore, from the point of view of those customers who cannot undertake integration of the electrical components, ABB is not an alternative to ETR.
- (153) Siemens also refers to the company Medcom in Poland, which has won a first order supplying the electrical traction of a commuter train of the Polish company PESA. Commuter trains are the simplest trains in the regional train sector with a

configuration for speeds of normally not more than 80-120 km/h. This order is so far the only reference for Medcom. yet references are enormously important in this business.⁷³ It is therefore highly questionable whether in the next two to three years Medcom will become a credible supplier outside Poland.

- (154) In addition, Siemens argues, the Japanese suppliers Toshiba and Hitachi are active on the European market. So far Toshiba has only been able to obtain orders in Ireland in which it acted as a subcontractor to another Japanese company Tokyu Car. The last of these orders already dates back three years. The general assessment of the Asian suppliers, therefore, is that they are more likely to become serious competitors in the longer term.⁷⁴
- (155) To date, Hitachi has been able to win one tender. It was selected in October 2004 as the preferred supplier for 30 trains for the “Channel Tunnel Rail Link” project.⁷⁵ However, it is not an independent supplier of electrical traction systems, but an integrated supplier of rail vehicles.
- (156) The proposed takeover therefore reduces the number of independent suppliers for electrical traction on the European markets for regional trains from one to zero. There would then no longer be a credible alternative to the systems producers. Siemens is, however, of the opinion that the non-integrated suppliers are in no way reliant on independent suppliers of electrical traction. The integrated suppliers of rail vehicles often supplied the electrical part separately to non-integrated suppliers. Siemens refers here in particular to the cooperation with CAF in Spain on the regional train Civia, for which Siemens is supplying the electrical traction system.
- (157) This is therefore a rational decision if the customer as a non-integrated supplier of rail vehicles has the option of buying in the electrical traction system from an independent supplier and can therefore in any case make a bid. If, however, this option no longer existed as a result of the proposed takeover of ETR by Siemens, the incentive for the integrated suppliers to make a bid for a total package for the electrical part would change. Bombardier has already made it clear that it follows the strategy, in tenders, of first offering its own complete rail vehicle.⁷⁶
- (158) [...] Bombardier also said that it always offers its own complete product first, before offering the traction to a competitor. Hence, in the case of regional trains, the two independent manufacturers CAF and Talgo would be competing with the integrated systems producers in all those tenders in which they first want to supply their own product.
- (159) But even in cases in which an integrated supplier is prepared in a given tender, at the same time as making a bid for the complete train, to pass on the electrical part to a non-integrated supplier, the non-integrated supplier will be at a competitive disadvantage. In order to match the mechanical and electrical parts with each other, an exchange of technical information is necessary which will give the integrated supplier useful information about the strength of its competitor. Furthermore, the

⁷³ Bearing Point expert report, 44.

⁷⁴ Bearing Point expert report, 46.

⁷⁵ http://www.hitachi-rail.com/rail_now/hot_topics/hot_topics_2004/ctrl.html.

⁷⁶ Doc. 5157 of 15 March 2005, Bombardier, reply to question 3.

integrated supplier will also have control of a block of costs which, on delivery of the overall electrical part, can account for up to [...] % of the total train. This leads to a considerable lessening of competition. The integrated supplier is therefore able to make the non-integrated supplier's bid more expensive or make a less price-aggressive bid with his own product.

- (160) On the other hand, the systems producers do not participate in each and every tender. Almost all of them pursue what is known as a platform strategy, under which a platform such as [...] is adapted to suit the customer's special requirements. Particularly in the case of trams and underground trains, with their special bend curvatures, tunnel dimensions, slope gradients, etc., the car boxes and configurations of these standard products are often unsuitable. It is often not worthwhile adapting them to meet the requirements. [...] Consequently, although non-integrated manufacturers of rail vehicles cannot rely in each tender on receiving a competitive offer from a systems producer for the electrical part, systems producers are, in a not inconsiderable number of tenders, unable to supply a suitable product and then have a very strong incentive to participate at least in the supply of the electrical traction. For example, this is true for the Talgo 22, the only regional train so far with two stepless decks running through the entire train, a product which none of the integrated suppliers can offer.
- (161) On the other hand, the market investigation showed that it is possible to acquire the capacity to plan and integrate an electrical traction system within two or three years. The necessary know-how is relatively easy to acquire. The example of the Swiss company Stadler demonstrated that it was possible, in the three years since the complete takeover of all rights to the GTW regional train and to the Variotram following the Bombardier/ADtranz merger, to develop this integration skill and to assemble the electrical traction from electrical components from, among others, ABB. In view of the long lead times in the rail industry between the issuing of a tender, the picking of the winner and the delivery of the train, two to three years for acquiring the competence for electrical traction do not seem overly long a time.
- (162) Even if the non-integrated suppliers of rail vehicles, including the main non-integrated supplier CAF, were eliminated from the market for electrical rail vehicles, there would continue to be in the individual Member States a sufficiently large number of actual and potential competitors in the overall train market. It must also be borne in mind that, at least in the case of regional trains, the demand side enjoys market power.

(f) Conclusion

- (163) The planned takeover of ETR by Siemens reduces the number of credible independent suppliers on the two markets for tram and underground train traction and for electrical traction for locomotives from two to one and eliminates the last independent credible supplier for electrical traction for regional trains. However, for several reasons, this will not result in the existing effective competition for electrical traction for tram and underground train vehicles, regional trains and locomotives being significantly impeded.
- (164) First, a credible independent supplier will still remain in each of the two markets for tram and underground train traction and for electrical traction for locomotives. Second, the systems producers will also continue to be suppliers for all traction

systems. Third, there is the real possibility of acquiring within two to three years the ability to integrate the electrical part. Lastly, even in the hypothetical event of a successful strategy designed to squeeze non-integrated suppliers of electrical rail vehicles from the market, sufficient competition would remain in the relevant downstream market for rail vehicles.

C2. CONTACT LINE ENGINEERING

1. Relevant product markets

- (165) Railway contact lines are transmission systems for supplying trains with electric current via current collectors. In most cases the current is supplied by overhead lines suspended above the locomotives. In the case of underground railways and to some extent overhead railways as well, it is supplied by a live third rail.
- (166) Siemens considers that, as in the ABB/DaimlerBenz decision, there is a uniform market for contact lines, which cannot be subdivided by final consumer, e.g. suburban or long-distance railways, or by system (overhead contact line versus third rail). Some customers submitted, however, that it is correct to differentiate first between third rail and overhead contact lines and then to subdivide overhead lines between local/urban traffic and mainline traffic. This question can be left open in the present case, however, since even on a narrow definition – overhead contact lines for mainline traffic in this case - effective competition will not be significantly impeded.

2. Relevant geographic markets

- (167) The proposed takeover of VA Tech leads to overlaps in Germany only. In its ABB/DaimlerBenz Decision the Commission assumed that the markets for contact systems were national.⁷⁷ Siemens considers that they have since grown to become more like the EEA market. The market investigation revealed a very uneven picture, in particular among German urban transport companies, ranging from national to worldwide markets. Since dc networks and similar voltages in the 600-750 kV range are usually used for tramways and underground railways throughout the EEA, the market for contact lines in an urban context is more homogeneous than for contact lines in long-distance transport. It is therefore simpler, at least theoretically, to commission foreign suppliers. None of the urban transport companies surveyed, however, has commissioned a supplier of contact lines that does not have its own branch in Germany. In the case of current supply lines, VA Tech serviced the first projects on the German market from Austria, but very soon with its own branch set up a support centre in Germany. Given present demand behaviour in Germany, however, an EEA-wide definition does not seem appropriate. For the purposes of this Decision, therefore, national markets continue to be assumed.

3. Competition assessment

- (168) The proposed takeover of VA Tech leads to overlaps in Germany only, since Siemens has transferred its Austrian business to SPL under a management buy-out. According to Siemens, the parties' joint share of the German market for all contact

⁷⁷ See IV/M.580 ABB/Daimler Benz, Commission Decision of 18.10.1995; IV/M.1064, paragraphs 30 and 41.

line engineering in 1999-2003 is [40-50]*% (Siemens [30-40]*%, VA Tech [2-5]*%). The market survey confirmed that the joint market share is of this order of magnitude (Siemens [30-40]*%, VA Tech [0-5]*%). The competitor Balfour Beatty is roughly as strong, so that the two largest suppliers together have a share of [70-80]*%. The other suppliers such as Bahnbau, Elpro, Fahrleitungsbau (RWE), Spitzke and Amec Spie have a market share of in some cases significantly less than 10%.

- (169) At just under [2-5]*%, VA Tech's market share in Germany is relatively small. VA Tech is one of the altogether five smaller suppliers in the German market. The merger will not result therefore in a considerable change in market structure. Moreover, only in overhead contact lines for mainline transport are there any overlaps. Even if overhead contact lines for mainline transport were defined as a separate product market, competition would not be appreciably reduced. Siemens and VA Tech would then have a joint market share of under [30-40]*%: the market leader in this segment would be Balfour Beatty. Even if VA Tech is somewhat stronger in this market than in the overall market, it is nevertheless one of five smaller suppliers which each have a market share of clearly less than 10%. At the same time, Deutsche Bahn is the only customer in that market and has buyer power.
- (170) Deutsche Bahn has submitted that after a takeover of VA Tech by Siemens, in the market segment for large contact line projects in mainline transport with a volume of over EUR 10 million there would only be two suppliers left: Siemens/VA Tech and Balfour Beatty. In DB Bahnbau GmbH, however, Deutsche Bahn has its own subsidiary in the contact lines sector, which is managed like an independent firm.⁷⁸ In the period under consideration this had a [5-10%]* share of Deutsche Bahn's orders. In the past, Bahnbau has won individual projects with a volume of over EUR 5 million and framework agreements worth over EUR 10 million. It must therefore be assumed that it is able to submit a credible bid for individual contracts in excess of EUR 10 million.
- (171) Analysis of the tenders in the period 1999-2004 also supports the conclusion that the market structure has not been substantially changed. Siemens and VA Tech were both involved in only [...] of the total 5 749 Deutsche Bahn tenders, i.e. in a little more than [...] percent. In [...] cases the two firms were first or second and hence the closest competitors for the particular project. These [...] orders account for [2-5]*% of the total volume of orders in the period under consideration.
- (172) If one considers only tenders for projects in excess of EUR 10 million, the picture is as follows: of the [...] orders in question, [...] went to Siemens, [...] to Balfour Beatty and [...] to VA Tech, Spitzke and DB's own subsidiary Bahnbau. The latter, however, was a framework contract covering several smaller projects. [...]*, it cannot be inferred from this that competition in the German market for contact line engineering will be substantially reduced by the takeover.
- (173) Moreover, the breakdown of orders shows that Spitzke, as well as Siemens and Balfour Beatty, is able to handle large orders of this kind. Thus Deutsche Bahn has three suppliers in this market segment. Furthermore, during the period in question, Elpro was able to win an order in the EUR 5 million category. While this order was

⁷⁸ DB Netz AG, Annual Report 2003, p. 28.

six years ago, it shows that, potentially at least, Elpro is capable of submitting a credible bid for tenders worth over EUR 5 million, especially if prices should rise as a result of the merger. In addition, DB's own subsidiary Bahnbau can be used at any time as a corrective. As a further possibility, the smaller competitors could form a consortium for large orders in excess of EUR 10 million.

- (174) Nor does the takeover of VA Tech increase the risk of tacit coordination by a duopoly of Siemens and Balfour Beatty in the German market. In the market for the construction of contact lines for mainline transport, prices and margins have been falling for some years, as the only customer, Deutsche Bahn, is reducing investment, in particular because of the decline in Federal funds for railway infrastructure until 2008. For this reason, Siemens had intended to sell this sector to Leonhard Weiss.⁷⁹ Another supplier was also supposed to be sold. Tacit coordination in a market with shrinking volumes and margins is difficult, however, since every rational supplier has an incentive to circumvent that coordination and secure for itself today a larger share of the profit from the sector, which will already be smaller tomorrow. Nor, given the tender data, is the argument convincing that, as a relatively new supplier in the German market, VA Tech acts as a corrective or "maverick" which can successfully disrupt the tacit coordination between Siemens and Balfour Beatty.
- (175) In view of the above, the Commission finds that the proposed takeover will not lead to a significant impediment to effective competition either in the German overall market for contact lines or in a possibly narrower German market for overhead contact lines for mainline traffic.

C3. TRACTION POWER SUPPLY

1. Relevant product markets

- (176) The market for supplying power to electric railway vehicles can basically be divided into three segments: the generation of electricity in power stations and substations for frequency conversion, the traction current cables and the power supply points in the traction network.
- (177) These can be further subdivided according to the type of railway. While tramways, underground railways and most regional railways operate on direct current with a voltage of 600 V, 750 V or 3 kV, intercity railways use alternating current at a substantially higher voltage of 15 kV or over. The operators of traction current networks for long-distance traffic, such as Deutsche Bahn or ÖBB, often have their own power stations or at least their own generators in national grid power stations, while regional and urban railways generally draw their power supplies from the networks of the publicly-owned energy supply companies EVU.
- (178) Generation and transmission via overland cables to the traction current network are not usually specific to the railway field. This does not apply, however, to the five countries Germany, Switzerland, Austria, Norway and Sweden. These have their own traction current networks, which are operated with single-pole alternating current at a frequency of 16 2/3 Hz and 15 kV voltage. This traction current cannot be procured direct from the energy suppliers' distribution networks, but is generated

⁷⁹ Frankfurter Allgemeine Zeitung No 47, 25.2.2005, p. 20. The sale failed for collective bargaining reasons.

partly in the railways' own power stations and partly in ordinary power stations by generators and inverters specifically installed for the purpose and, in Germany's case, transmitted via 110 kV lines to the traction current network.

- (179) From the demand angle it is not possible to replace plant for generating 16 2/3 Hz/15 kV traction current with turbines on account of the special voltage and frequency. However, the producers of power stations and generators are also able, without exception, to make plant for the special requirements of railways that use 16 2/3 Hz/15 kV traction current. Given this flexibility on the part of suppliers, it is therefore not appropriate to assume an independent market for the generation of 16 2/3 Hz/15 kV traction current. Moreover, traction current can be generated not only with turbines but also with static inverters on the basis of semiconductor components. This technology will become increasingly important compared with conventional generation using turbines.⁸⁰
- (180) The situation is otherwise with regard to the servicing of such plants, which often run for decades. With repairs and maintenance, the firm which produced the plant is at an advantage here, since it has the working drawings and the appropriate experience.
- (181) As regards the installation of the overhead lines, which transmit the traction current from the power station to the power supply points, there is no overlapping in the present case, since Siemens has sold this business, which now operates as an independent company under the name FBG Freileitungsbau.
- (182) The supply of traction current proper, i.e. the supply of electricity to the traction current network, is ensured by power supply points, also known as substations, transformer stations or switchgear. By means of these substations the electricity from the energy suppliers' distribution networks is converted to the voltage required by the particular railway and fed into the traction current network. Substations consist basically of high and medium voltage switchgear, transformers, inverters and rectifiers, station control engineering and the necessary auxiliary equipment.
- (183) In accordance with the ABB/DaimlerBenz decision, Siemens considers that in the case of traction power supply, a sector where Siemens and VA Tech operate *inter alia* through their subsidiary SAT, the market is uniform and cannot be further subdivided. The market survey confirmed that all major suppliers of traction power supply equipment offer complete installations, even if they do not manufacture individual components themselves and hence buy them additionally or have them provided by the customer.
- (184) A fairly large number of customers and some competitors consider, however, that separate markets should be defined for these components, in particular for control engineering. Some customers also procure only individual components or do not award a substation to a general contractor, but hold a separate tender. One competitor submitted in this respect that a merged Siemens/VA Tech would have some key components that would in practice give it a monopoly for certain segments of traction power supply for mainline traffic. However, even if, as suggested by Deutsche Bahn, one were to make a further division between switchgear with

⁸⁰ Doc. 4750 Deutsche Bahn, 11.3.05, reply to question 8.

network control, remote control and safety engineering on the one hand and components for those systems on the other,⁸¹ the proposed merger would not lead to a significant impediment to effective competition.

- (185) To sum up, therefore, the following product markets are differentiated in the traction power supply sector: complete substations, railway specific components for substations and servicing turbines for generating traction current.

2. Relevant geographic markets

- (186) In its ABB/DaimlerBenz decision the Commission assumed that the markets for the supply of traction current proper were national. Siemens considers that they have since grown to become more like the EEA market. The market investigation revealed a very mixed picture. Although a majority regarded national markets as too narrow and sees the EEA as the relevant geographic market, not a few customers assume national markets. None of the urban transport companies surveyed, however, has commissioned a supplier of substations or components that does not have its own branch in Germany or Austria. In addition, all safety-relevant components of traction power supply must be accepted by a national authority. Given present demand behaviour in Germany and Austria, therefore, an EEA-wide definition does not seem appropriate. For the purposes of this Decision, therefore, national markets continue to be assumed. The same applies to the servicing of turbines for generating traction current.

3. Competition assessment

- (187) According to Siemens, Siemens and VA Tech achieved a joint market share of [30-40]*% (Siemens [15-20]*%, VA Tech [20-30]*%) in the Austrian market for complete substations. Other competitors are ABB with [10-15]*% and Areva (ex-Alstom) with [10-15]*%, plus a number of smaller suppliers.
- (188) The market investigation revealed that, averaged over the five years 1999-2003, the Austrian market was worth EUR 10 million. Siemens's market share was [10-15]*%, that of VA Tech [30-40]*%, and the joint market share [40-50]*%. Areva had 20-30%, ABB 10-20%, Balfour Beatty and SAG, a subsidiary of RWE, 5-10%. The remainder is shared among relatively small suppliers, such as Sprecher Automation.
- (189) Because there are few projects, the market shares fluctuate very considerably from year to year. Thus, in the period under review, Siemens' market share was between [2-5]*% and [30-40]*%. In 2004 ABB won a large order for renewal of the traction power supply (substations) for Wiener Linien's U1 and U2 lines, worth over EUR 10 million; this makes ABB the outright market leader for 2004. On the supplier side, as well as the three established internationally active competitors of Siemens and VA Tech - ABB, Areva and Balfour Beatty - there is also a relatively small supplier that can offer complete substations. In 2002 Sprecher Automation took over Alstom Austria's former control technology business and is thus able to position itself in the market as a complete supplier of substations.
- (190) On the demand side in Austria there are basically only two customers which have buyer power: Österreichische Bundesbahnen and Wiener Linien. Both these

⁸¹ Doc. 1047 Deutsche Bahn, 24.1.2005, reply to question B6.

customers put their orders out to tender. Since these are tender markets and only very few substations are put out to tender every year, effective competition prevails, as the range of the market shares shows.

- (191) In the case of components, by taking over VA Tech's subsidiary SAT, Siemens acquires one of the three station control technology systems approved by ÖBB. The two other approved systems are produced by ABB and Sprecher. Even if Siemens, after taking over VA Tech, no longer markets the SAT product to third parties, the sole customer for this system, ÖBB, would still have at least three suppliers of complete substations, which use their own station control system approved by ÖBB. Added to this, ÖBB is quite at liberty to approve further suppliers of such systems if necessary.
- (192) Siemens's and VA Tech's joint share of the German market for complete substations is [40-50]*% (Siemens [30-40]*%, VA Tech [5-10]*%). The most important competitors are Balfour Beatty with 20-30%, ABB with 10-20%, Elpro with 10-20% and Spitzke with 5-10%.
- (193) VA Tech, through its subsidiary SAT, is largely active in the mainline sector, i.e. supplying Deutsche Bahn with traction power (alternating current of the 16 2/3 Hz and 15 kV variety) and only to an insignificant extent in the mass transit segment, i.e. the direct current segment. In the mass transit segment, none of the market participants surveyed, in particular all the approximately 20 customers, saw the proposed merger as raising competition concerns.
- (194) In the mainline traction power segment, where Siemens and VA Tech have a joint market share of some [20-30]*%, one competitor and in particular the main customer, Deutsche Bahn, considered that SAT should not be taken over by Siemens, since otherwise in the case of some major components while there would be no horizontal overlapping there would be a problem of market foreclosure.⁸² SAT offers in particular station control technology, remote technology, network control systems (SCADA) and associated automation components.
- (195) Some traction power supply engineering components and remote technology and network control systems products, such as SCADA and Remote Terminal Units, are standard products from the T&D sector (see above, T&D paragraphs XY), which are adapted to the requirements of the railway networks. As well as the large manufacturers there are also smaller competitors, which have specialised in the rail segment with its 16 2/3 Hz/15 kV network, such as Kayser-Threde, a leading supplier of control technology for monitoring and regulating substations. Other products are so specific to the railways that they require a special licence from the German Federal Railways Office (EBA). In the case of three components for traction power supply proper, SAT is one of the few manufacturers, or even the only one, which has already received, or has good prospects of receiving, the necessary licence. SAT supplies a local control device (LCD), a product which is used in remote technology. As well as SAT, however, AEG ursatronics and ABB are also present in the market. Siemens has no LCD of its own which is licensed by the EBA.

⁸² Doc. 1047, 24.1.2005, Deutsche Bahn's reply to a request for information, questions 21 and 23.

- (196) Under the Federal Railways Office's directive on improving tunnel safety, tunnels in Germany must be provided *inter alia* with a contact line voltage tester (CLVT). SAT was hitherto the only CLVT supplier licensed by the EBA. Balfour Beatty too has recently brought out an EBA-approved system, which is based on the SAT system. [...]*
- (197) The third product concerns junction-related tests (JRTs). This product was developed for the protection design of Deutsche Bahn's contact line installations. It is not yet in use, but will soon be tested and then presented to the EBA for final approval. SAT would then be the sole supplier of such a novel testing system for Deutsche Bahn's contact lines. However, Deutsche Bahn already has an automated system for testing contact lines when switching on a route section (ASTCL). Compared with the ASTCL the JRT testing system is an innovation, since test resistance including the test cell disappear and the product is therefore lighter and smaller.
- (198) Siemens does not have any of these three products. Consequently, the number of suppliers present in the market is not altered by Siemens's takeover of SAT. Market foreclosure by Siemens is also improbable. Thus, as before, there are three LCD products, but only one customer. With CLVTs in the past Deutsche Bahn has either provided the general contractor with the product or prescribed it. It is not yet possible to tell whether JRT will supersede the ASTCL. Deutsche Bahn has admitted, however, that innovations in this area can possibly also be generated by other suppliers. It should not be expected, therefore, that the takeover of the VA Tech subsidiary SAT will appreciably restrict effective competition in components for traction power supply.
- (199) Both Siemens and VA Tech supply the service of maintaining turbines for generating 16 2/3 Hz traction current. Deutsche Bahn has suggested that, as a result of Siemens's takeover of VA Tech, competition in the market for the high-tech maintenance of such turbines in Germany would be lost on account in particular of the bundling of working drawings and available experience. VA Tech, however, has built only one plant for Deutsche Bahn. The plant, which was built in 1998, was the last of its type, since new plants are only being built on the basis of static inverters. Static inverters are supplied by Areva, ABB and Siemens, but not VA Tech.
- (200) Apart from by Siemens, such plants, of which there are about 20 in Germany, have been built by BBC in particular. This business was taken over by Alstom, which continues to supply in this market. There are also firms which, while they do not have the engineering plans, have many years' experience of maintaining and adapting such plants. These include in particular the RWE subsidiary SGB. It should not be expected therefore that the takeover of VA Tech, which has built only one plant, will lead to a significant reduction of effective competition in maintenance.

C4. LEVEL CROSSINGS

- (201) Both Siemens and VA Tech supply level crossings. VA Tech operates only in Austria. VA Tech does not have its own product but markets exclusively the BUES 2000 computer-controlled level crossing safety technology of the German manufacturer Scheidt & Bachmann. BUES 2000 is basically an electronic control system and is delivered by VA Tech to Zelisko, a subsidiary of Knorr Bremse, which incorporates it in its level crossings and also supplies it in Austria. VA Tech holds

the operating licences for BUES 2000, which are issued by the Austrian Ministry of Transport. Given these legal barriers to entry, national markets are probably appropriate. Siemens has no sales at all in Austria and is therefore only a potential competitor.

- (202) One market participant feared that, after the takeover of VA Tech, Siemens would only supply its own level crossings in Austria. The market surveys have shown, however, that there are no major legal obstacles to transferring the licence to Scheidt & Bachmann, which recently set up a subsidiary in Austria. Scheidt & Bachmann is quite able, therefore, to assume the further marketing of BUES 2000 in Austria.⁸³ The number of competitors in the Austrian market for level crossings would not therefore be altered by the takeover of VA Tech. Thus the merger would not significantly impede basic competition in the market for level crossings in Austria.

D. FREQUENCY INVERTERS

1. Relevant product markets

- (203) Frequency inverters are part of an electric drive. The drive consists of a motor and a switchgear. A frequency inverter is a switchgear which regulates the speed of the motor. To this end the usual ac network frequency of 50 hertz is converted into a higher or lower frequency.
- (204) Siemens proposes that the market be divided into simple inverters up to and including 100 kW and heavy-duty inverters of over 100 kW. Inverters up to and including 100 kW are a mass market, while inverters over 100 kW are usually high-tech products tailored to the customer's needs. Frequency inverters with an output of up to 100 000 kW are supplied. Such inverters are used in heavy machine construction and industrial plants, in particular in energy-intensive sectors, such as rolling-mill drives and ships' engines or in the oil and gas industry.
- (205) The market investigation revealed that there is a mass market, served by many firms, some of which operate at regional level only. On the other hand the number of firms which can supply frequency inverters with a high to very high output falls as the output required increases. The overwhelming assessment of the market participants surveyed, however, was that 100 kW was an acceptable ceiling for defining the mass market. For the purposes of this Decision, therefore, a limit is placed at 100 kW.
- (206) Some market participants thought that the market for frequency inverters over 100 kW should be subdivided further. Thus there is a market for water-cooled frequency inverters and for four-quadrant frequency inverters, which can feed current back again into the network. Water-cooled inverters are used in particular in mining and for tunnel-boring machines. In these applications air-cooled drives are not possible, since the heat and penetrating dust would very quickly put the inverter out of action. Four-quadrant inverters are used, for example, in engine test beds.
- (207) Whether a further breakdown by water-cooled inverters and four-quadrant inverters is appropriate can be disregarded for the purposes of this Decision, however, since

⁸³ Doc. 5571, 22.3.05, reply from Scheidt & Bachmann.

the competition assessment would not be any different even if separate markets were assumed.

2. Relevant geographic markets

- (208) Siemens considers that the relevant geographic market is the world, or at least the EEA. VA Tech, too, opts for a worldwide market. According to Siemens there are only two technical standards worldwide. The IEC standard of the International Electrotechnical Commission applies around the world; only in North America is there a variant standard (ANSI). The IEC applies in the EEA, where there are no variant standards. ABB considers that in the EEA there are definitely variant standards in individual countries. Thus, in the UK the *Harmonics Standard* applies, in Norway everything has to be aligned on 110 kV three-phase current, and in France the earthing has to be different.⁸⁴ However, since all major suppliers are in a position to meet these additional requirements, it does not seem appropriate to assume national markets on the basis of these technical provisions.
- (209) Siemens maintains that the prices for frequency inverters in the European Union are similar. This was basically confirmed by the market investigation. Since there are neither technical obstacles nor large price differences and the overwhelming majority of replies to the Commission's market survey assumes at least an EEA-wide market, an EEA-wide market is taken as the basis for this Decision.

3. Competition assessment

- (210) Suppliers in the market for frequency inverters can be divided into three large groups. In the first are the firms operating on a European or worldwide basis, such as ABB, Alstom, Danfoss, Schneider Toshiba and Siemens. In the second group belong firms such as Vacon and Lenze, which are represented in many countries of the EEA but are regional in emphasis. The last group is made up of small firms, which operate in the up-to-100 kW sector in particular and often actively supply in only one member country.
- (211) According to Siemens, the combined market share of the EEA market for frequency inverters ≤ 100 kW in 2003 was [15-20]*% (Siemens [15-20]*%, VA Tech [<2]*%). The market survey broadly confirmed this, as the following table shows:

Inverters ≤ 100 kW EEA		
Competitors	Turnover 2003, € m	Share
Siemens	[...]*	[15-20]*
VA Tech		[0-5]*
Schneider/Toshiba STI		10-15
Total		[30-40]*

⁸⁴ Doc. 4861, ABB, Second questionnaire on inverters, reply to question 13.

ABB		10-20
Alstom		0
Danfoss		10-20
Fuji Electric		0-5
Lenze		5-10
SEW Eurodrive		5-10
Vacon		5-10
Yaskawa/Omron		5-10
Others	0	0
Total	800-900	

(212) The most important competitors are ABB, Danfoss and Schneider with a market share of 10-20% and Lenze, SEW Eurodrive Vacon and Yaskawa/Omron with 5-10%. The market investigation showed, however, that since 2004 VA Tech has been associated with Schneider Electric and Toshiba (Schneider Toshiba Inverter VA Tech, STI VA Tech) in a joint venture, which is planning the joint development and production of inverters both below and above 100 kW. The total market share controlled by Siemens after the proposed merger would be [30-40]*%.

(213) It should be borne in mind, however, that these market share data show the highest possible values, since no value for Others was given in the table. Siemens gives its sales as EUR [...] million, which corresponds to a market share of [20-30]*%. The Commission could not verify this figure. It has established that, apart from a few medium-sized firms operating at local level such as Baumüller, among others US suppliers like Rockwell are selling in the EEA. In any event, therefore, the real market share of Siemens and VA Tech, including STI, is lower than [30-40]*%. Moreover, in this market there are several credible alternatives that operate Europe-wide, such as ABB, Danfoss, SEW and Vacon, which at any time could thwart the attempts of a merged Siemens/VA Tech to raise the prices of its inverters above the competitive price, and a number of smaller manufacturers, which have a strong position locally or nationally.

(214) According to its own figures, after the proposed takeover of VA Tech, Siemens would have [10-15]*% of the market for inverters >100 kW (Siemens [10-15]*%, VA Tech [<2]*%). While the figures for Siemens were confirmed by the market survey, VA Tech's market share is significantly higher, so that the joint market share would be [15-20]*% (Siemens [10-15]*%, VA Tech [5-10]*%). With STI, it would be [20-30]*%. The clear market leader is Alstom with a market share of [30-40]*%, followed by ABB with [20-30]*% and Vacon with [5-10]*%.

Inverters >100 kW EEA		
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Competitors	Turnover 2003, € m	Share
Siemens	[...]*	[10-15]*
VA Tech		[5-10]*
Schneider/Toshiba STI		0-5
Total		[20-30]*
ABB		20-30
Alstom		30-40
Danfoss		0-5
Loher ⁸⁵		0-5
Lenze		0-5
Vacon		5-10
Others		0
Total	400-500	

(215) Here too it should be borne in mind, however, that this [20-30]*% shows the highest possible value, since no value for Others was given in the table. Siemens gives its sales as EUR [...]* million, which corresponds to a market share of [40-50]*%. The Commission could not verify this figure. It has established that apart from firms such as Bombardier and SEW Eurodrive, which have a very small market share, a number of medium-sized European firms, such as Baumüller and Breuer, and US suppliers like Rockwell and Eaton are selling inverters of over 100 kW in the EEA. In any event, therefore, the real market share of Siemens and VA Tech, including STI, is lower than [20-30]*%.

(216) In the case of water-cooled frequency inverters of over 100 kW, which are used in tunnel-boring machines in particular, Siemens and VA Tech have a joint market share of [5-10]*%. The market leaders in this segment are Alstom with 60-70% and ABB with 20-30%. Other substantial suppliers are Vacon Baumüller and the US firm Eaton with its Cutler-Hammer brand. These figures and the existence of credible alternatives are enough to show that Siemens/VA Tech would not be in a position significantly to impede effective competition. Even in the tunnel-boring

⁸⁵ Loher is a subsidiary of Flender Holding GmbH. In its decision of 30 June 2005 in case COMP/M.3809 Siemens/Flender the Commission has cleared the takeover of Flender by Siemens. Even if Loher is included, the combined market share of Siemens and VA Tech remains 20-25%.

machines segment with its special requirements, the proposed merger does not raise any competition concerns. In this segment there are basically the two German firms, Herrenknecht and Wirth, and the US firm Robbins, which is also present in Europe; together they meet much of the worldwide demand. The market survey showed that these firms use water-cooled inverters from four different manufacturers, but none from Siemens. Thus the proposed merger does not result in any structural change in this market segment.

- (217) In the case of four-quadrant frequency inverters of over 100 kW, Siemens together with VA Tech and STI had a market share in the EEA of [15-20]*% in 2003. The market leader is ABB with 40-50%, followed by Alstom with 20-30%. As well as these large suppliers there are many smaller ones. One cannot conclude from this market share that there are competition concerns.
- (218) Four-quadrant frequency inverters are used *inter alia* for engine test beds. The customers are mainly the large motor vehicle groups but also include universities and research institutes. Siemens is active in this downstream market. According to its own data, the world market leader is the Austrian firm AVL List with, according to Siemens, some [40-50]*% of the EEA market, followed by Siemens with [20-30]*% and Schenck Pegasus with [10-15]*%. Of the two main competitors, only AVL List uses VA Tech inverters on a relatively large scale. However, AVL also has other current suppliers and, with ABB and Alstom, credible potential suppliers (whose products would have to be adapted for test bed purposes) which are not themselves active in the market for engine test beds. In addition, there are suppliers offering inverters specially developed for engine test beds, such as the US firm Unico, which has been present in Europe also for some time.
- (219) For these reasons the Commission considers that the proposed takeover of VA Tech by Siemens does not significantly impede competition in the market for frequency inverters below and above 100 kW.

E. METAL PLANT BUILDING AND OTHER INDUSTRIAL PLANT BUILDING

1. Relevant product markets

(a) Fundamental distinctions

Distinction according to sectors

- (220) In industrial plant building a distinction can be made firstly by sector (metal, chemicals, paper, cement, etc.). Although Siemens and VA Tech are active in several sectors as plant builders, it is particularly important for the purposes of this Decision to take a closer look at metal industrial plant building, since it is in this sector that most of VA Tech's plant building activities are concentrated. In metal plant building there are separate sectors for the manufacture and processing of ferrous and non-ferrous metals. The main non-ferrous metal is aluminium.

Distinction between mechanical plant building, electrical plant building and maintenance and service

- (221) A further fundamental distinction exists between mechanical industrial plant building electric industrial plant building and plant maintenance and servicing.

- (222) Mechanical industrial plant building plans the use of machines for the relevant industrial production process, obtains these machines and installs them in the production plant. Traditionally it includes the area of process technology, but does not include the civil engineering building of the plant (e.g. constructing the building). Through its subsidiary company VAI, VA Tech acts as a supplier of mechanical plant building. Siemens itself is not active in this area as a supplier, but in the metallurgical sector has an important [...] holding⁸⁶ in one of the two keenest competitors of VA Tech, SMS Demag. Through this stake Siemens gains an insight into key aspects of SMS Demag's competitive position. Furthermore, Siemens has its own know-how in metals processing technology.⁸⁷
- (223) Electrical industrial plant building includes firstly the general electrification of the plant ("electrics"), the configuration and assembly of drive solutions, consisting of motors and inverters ("drives") and, if necessary, the configuration and assembly of sensors ("sensors"), and secondly the area of actual automation, which basically consists of electric monitoring and control systems as well as of process automation. In addition there is a third area, which concerns IT solutions for plant logistics. Both Siemens and VA Tech act as suppliers in electrical industrial plant building. VA Tech is active in electrical industrial plant building through its subsidiary VAI (in the metallurgical sector) and Elin EBG (in various sectors).
- (224) Plant maintenance and plant servicing are not to be confused with plant modernisation, which is a part of both electrical and mechanical plant building. Ongoing maintenance work and service provision are part of plant maintenance and plant servicing, but there is no new designing of parts of the plant. Siemens and VA Tech are both active in the metallurgical area in plant maintenance and plant servicing.

Differentiation by process area and process stage

- (225) In the procedurally more complex process industries (such as metals, chemicals, oil and gas), plant building can also be broken down into individual process areas and process stages. In metal plant building, which includes the whole process flow of blast furnace engineering and rolling mill technology, metal production and processing in the iron and steel sector contains the following different stages.
- First of all, metal plant building is divided into process areas. The most important process areas are the blast-furnace area (liquid phase) and the two process areas for the production of flat-rolled products, namely the hot phase and the cold phase. A special area is the rolling of long products.⁸⁸
 - The individual process areas can be subdivided by process stage. The blast-furnace area (also known as the liquid phase process area) is made up of ironmaking and steelmaking process stages. The hot phase process area consists of the continuous casting and hot rolling process stages. The cold phase process area consists of the

⁸⁶ See reply to the request for information of 29 March 2005, Annex 1a, sheet 30.

⁸⁷ See paragraphs (253) and (316).

⁸⁸ Long-rolled products and flat rolled products have the process stages of pig iron making and steelmaking in common, after continuous casting, in which they still display many common features, they are separate. In the production steps after continuous casting, long-rolling (e.g. section rolling) is then clearly separate from the technique for rolling flat products (hot rolling, cold rolling, strip-processing).

cold rolling and strip treatment process stages. The most important process stages in the production of long rolled products are section rolling mills and pipe manufacturing plants. Pressing and forging can be taken as being a separate process stage.

– Fundamental process stages can be broken down further (e.g. into sub-process stages or by type of plant), but these are not relevant to this Decision.

– *(b)Mechanical metal plant building*

(226) Siemens assumes that use of the mechanical part of industrial plants is sector-specific and therefore assumes a separate product market for mechanical metal plant building. However, Siemens does not follow the further subdivision adopted by the Commission in its SMS/Mannesmann Demag decision⁸⁹ corresponding to the process stages⁹⁰, but assumes that these are only segments of a larger market for mechanical metal plant building. Siemens furthermore argues that there is sufficient supplyside substitutability as also smaller competitors could usually offer mechanical plant building services for various process steps.

(227) In the context of the Commission's market surveys, the majority of market participants were in favour of a further subdivision of the market into the respective process stages or groups of related process stages.⁹¹ In VA Tech's view, only a few suppliers, so-called "full-liners", can supply the mechanical plant for all process stages. According to VA Tech these include its own subsidiary VAI and SMS-Demag and Danieli, whereas smaller suppliers specialise in individual technologies and generally do not win any orders above a certain size. VA Tech also states that because of financing problems, such businesses also have no access to consortia of small suppliers. The Commission shares these views.

(228) It can first be stated that the process technologies of the individual production steps vary enormously and there are no substitution options on the demand side.

(229) Beyond that, the market investigation has shown that the supplier structure in the various process steps of mechanical plant building in the iron/steel sector is clearly different. There is a clearly separate supplier structure not only in special areas such as pipe production, moulding and forging, aluminium (rolling) plants⁹² and copper plants but also for the main process stages of producing flat steel products and long steel products a clear differentiation of the supplier structure can be seen. First, smaller suppliers do not offer in all process steps. E.g., some competitors such as Andritz and MINO essentially offer in the process steps of cold rolling and processing lines.⁹³ Other competitors such as Paul Wurth and Küttner only supply in

⁸⁹ IV/M.1450 - SMS/Mannesmann Demag.

⁹⁰ Pig iron making, steelmaking, continuous casting plants, hot rolling mills, cold rolling mills, section rolling mills, strip plants, pipe manufacturing plants, pressing and forging, aluminium rolling mills and copper mills.

⁹¹ Thus the market survey revealed that the large majority of the market participants surveyed regard the continuous casting process stage as a separate market and that aluminium rolling is to be differentiated from steel rolling for the purposes of the product market definition.

⁹² It must be noted that there is a clear specialisation of suppliers in the area of aluminium rolling (e.g. by Achenbach and Fata Hunter).

⁹³ This at the same time indicates that there is insufficient supplyside substitution between hot rolling and cold rolling.

iron- and steelmaking. Second, there is even among the „full-liners“ a clear internal specialisation of different subsidiaries and business units with regard to individual process steps. This is reflected in significant variations in the suppliers' self estimates concerning its ranking per process step.⁹⁴ Third, the market investigation has shown that not only suppliers but also customers differentiate their market view, as expressed in rankings of suppliers, clearly by process step. Not all full liners are seen as equally good alternatives for each process step. Smaller specialists have only been mentioned in specific process steps.⁹⁵ Therefore, there is insufficient supply side substitution between mechanical plant building for the process steps in iron and steel production and processing and in the processing of non-ferrous metals such as aluminium and copper.

- (230) For these reasons the breakdown applied in the SMS/Mannesmann Demag decision⁹⁶ corresponding to the production stages for mechanical industrial plant building can be retained for the purpose of this Decision. Accordingly, a distinction must be drawn between product markets for pig iron making, steelmaking, continuous casting plants, hot rolling mills, cold rolling mills, strip plants, section rolling mills, pipe manufacturing plants and hot pressing and forging. Likewise in accordance with the SMS/Mannesmann Demag decision, a distinction has to be drawn between metal plant building for iron and steel on the one hand and non-ferrous metals, in particular aluminium and copper, on the other.⁹⁷
- (231) Since, for the purposes of this Decision, a division into individual submarkets of mechanical metal plant building (i.e. into the markets for pig iron making, steel making, continuous casting plants, hot rolling mills, cold rolling mills, strip plants, section rolling mills, pipe manufacturing plants and hot pressing and forging, and aluminium rolling, copper and other non-ferrous metal plants) is not absolutely necessary, however, the question of the precise product market definition in mechanical metal plant building can therefore ultimately remain open.
- (232) It can also remain open whether a separate overall market for mechanical iron and steel plant building should be assumed or whether an overall market for mechanical metal plant building covers both ferrous and non-ferrous metals. In its notification of the merger project, Siemens assumes, as already mentioned, that there is a larger market for mechanical metal plant building, which comprises the following segments: pig iron making, steel making, continuous casting plants, hot rolling mills, cold rolling mills, section rolling plants, strip plants, pipe manufacturing plants, hot pressing and forging, aluminium rolling mills and copper and other non-ferrous

⁹⁴ With regard to the distinction between the process steps ironmaking and steelmaking it must also be pointed out that SMS, as is shown in SMS-internal papers is planning an exit from mechanical plant building for ironmaking (Cf Meeting of the Shareholders' Committee of SMS Demag of 21 March in Munich, presentation of the SMS Board)

⁹⁵ Market investigation, Phase II - replies to competitor and customer questionnaires. Smaller specialists are moreover usually ranked lower than full liners by competitors and customers in regard to their competitive strength. This also holds true for (isolated) mentionings of specialised non-European competitors. SMS-internal information (Cf Meeting of the Shareholders' Committee of SMS Demag of 21. March in Munich) and information supplied by market participants (Market investigation, Phase II - replies to competitor and customer questionnaires) shows that e.g. with regard to Chinese companies that these are considered capable of a market entry outside China predominantly in ironmaking (and to a much lesser extent in steelmaking and not at all in other process steps).

⁹⁶ IV/M.1450 - SMS/Mannesmann Demag.

⁹⁷ See also IV/M.1450 - SMS/Mannesmann Demag.

metal plants. All these sectors, with the exception of aluminium rolling mills and copper and other non-ferrous metal plants, concern process stages in iron and steel production and processing. According to Siemens,⁹⁸ [...] The Commission's market survey produced nothing to disprove this. The fact that non-ferrous metals are of secondary importance in mechanical plant building means that, for the purposes of this Decision, the assessment of a possible overall market in mechanical metal plant building does not depend on whether non-ferrous metals are included in such a market or not. Another reason why this is so is that the market strength of SMS and VA Tech in non-ferrous metals (especially in the only significant non-ferrous sector, aluminium rolling) is, according to the market survey, roughly the same as in the cold rolling of iron and steel.⁹⁹

(c) Electrical metal plant building

(1) Overview of the individual electrics and automation areas

- (233) Both Siemens and VA Tech are active in the area of electrical metal plant building.
- (234) Electrical metal plant building comprises firstly "level 0" automation, secondly actual automation (levels 1 and 2) and thirdly the more recent area of IT solutions for plant logistics/MES (level 3).
- (235) Level 0 automation means the electrics (general electrification of the plant), drives and sensors.
- (236) Actual automation consists of level 1 and level 2 automation.
- (237) The components of level 1 are the IT platform (automation system), the human-machine interface or HMI (the control unit), the basic automation and a series of technological control systems (such as thickness, width, surface evenness and temperature of the metal).¹⁰⁰ Frequently the drive control (as opposed to the drives themselves) is allocated to this area.
- (238) Process automation ("level 2") consists of complex mathematical process models for calculating the relevant correct adjustment and conversion of the plant (segment) and the quality of the products produced, taking the individual pre-calculated production parameters as a basis and processing a large number of individual production measurement data.
- (239) IT solutions for plant logistics, also known as manufacturing execution systems (MES) or level 3 automation, are a rapidly developing special area, which is no longer part of the automation itself, but also forms part of electrical metal plant building in the broad sense. These are essentially integrated solutions for controlling and monitoring the logistics of a production plant.

(2) No uniform market for electrical industrial plant building: at least a separate market for electrical metal plant building

⁹⁸ Notification of the merger project (Form CO).

⁹⁹ See below, paragraph (319).

¹⁰⁰ The concept of the technological control system (TCS), however, is also generally applied to level 1/level 2.

- *Siemens' standpoint*

(240) Siemens does not assume that electrical industrial plant building for the metallurgical sector is a separate market, but takes the view that electrical industrial plant building is as a whole independent of any sector. According to Siemens, tailoring the products and services to a specific use such as the metallurgical sector takes place through process technology. Consequently, applying this line of argument, the fact that among electrical plant builders a certain focusing on particular customer segments for strategic reasons is not unusual does not invalidate the general nature of electrical industrial plant building.

(241) Siemens emphasises in the statement on the decision under Article 6(1)(c) of the Merger Regulation and in the comments on the statement of objections [*There follow comments on the use of standardised products*]*

(242) Siemens also indicates that major electrical industrial plant builders are active in various sectors. Sector-related specialisation is the exception among the suppliers of electrical industrial plant.

(243) Finally, Siemens says [*There follow comments on the level of specialisation of the engineers used and on the importance of references* ¹⁰¹]*

- *Results of the market investigation*

(244) In the context of the market investigation carried out by the Commission, however, the majority of market participants felt that special know-how was necessary for constructing electrical plants in the metallurgical sector.

(245) Competitors particularly stressed the specialisation of their metal plant building engineers in their statements.

(246) Siemens' citing of the limited degree of specialisation of its metal plant building engineers is not conclusive on this point. [*There follow comments on the importance of the level of skills of the engineers employed and on the internal organisational structure of Siemens*]* ¹⁰² Also, from other statements made by Siemens, it is unlikely that there is a low degree of specialisation among staff.¹⁰³

(247) Furthermore, the frequently mentioned importance of reference lists in the replies to the market investigation suggests that the majority of customers demand relevant experience in the metallurgical sector from the respective suppliers. [...] ¹⁰⁴*

(248) In addition to this, the view of the market [...] ¹⁰⁵ [*There follow comments on the sector-specific or non-specific nature of electrical metal plant building*]*.¹⁰⁶ This fact alone indicates that a separate product market is assumed.

¹⁰¹ See, for example, presentation text "Discussion with DG Competition on 15.4.2005".

¹⁰² [...]*

¹⁰³ [...] (reply to the request for information of 29 March 2005, Annex 1.c, sheet 45).

¹⁰⁴ [...]*

¹⁰⁵ Reply to the request for information of 29 March 2005. [...]*

¹⁰⁶ See reply to the request for information of 29 March 2005. [...]*

- (249) Marketing in electrical metal plant building is sector-specific. [*There follow comments on marketing expenditure* .¹⁰⁷]*
- (250) [*There follow comments on Siemens' research and development activities...*¹⁰⁸]*
This [...] research activity is reflected in a significant number of patents.¹⁰⁹ VA Tech also has a considerable number of copyright-protected developments for electrical metal plant building. [*There follow comments on Siemens' research and development activities*]*¹¹⁰
- (251) The significant development costs and the long time it takes to develop products and services were also confirmed in the Commission's market investigation.¹¹¹
- (252) A further indication of an increasing sector-related specialisation is the advance of the earlier mechanical metal plant building specialists, Danieli, SMS Demag and VAI, into the area of electrical metal plant building. These companies are almost exclusively active in a sector-specific way in metal plant building. Market share gains by these companies confirm the trend toward sector specialisation in electrical metal plant building. Even medium-sized companies such as Küttner, MINO, Kleinknecht and Gefeba are focused very strongly or exclusively on metal plant building.
- (253) This trend towards specialisation in the metallurgical sector, in which, in both mechanical and electrical metal plant building, specialised process technology know-how is needed (and not only, as perhaps in the past, in mechanical industrial plant building) [*There follow comments on the availability of process-technology know-how at Siemens and on the internal assessment of mechanical metal plant building by Siemens*]*^{112 113}
- (254) Through this moving closer together or meshing of mechanical and electrical metal plant building, electrical metal plant building too is becoming increasingly sector-specific.
- (255) The Commission's market investigation also showed that in the area of electrical equipment, drives and partly also sensors (i.e. in the level 0 area), at product and component level there is only relatively little specialisation.¹¹⁴ Electrical and drive

¹⁰⁷ Siemens' reply to the Commission request for information of 2.3.2005, Annex 10.

¹⁰⁸ Siemens' reply to the Commission request for information of 2.3.2005, Annex 9.

¹⁰⁹ Siemens' reply to the Commission request for information of 2.3.2005, Annex 8.

¹¹⁰ [...]*

¹¹¹ One competitor stated that the costs of developing products and solutions for this industry are so high that only major global companies could think about going into this business (anonymised results of the market survey).

¹¹² See, for example, the sheet which was presented by Siemens at the discussion with the Commission on 23 March 2005 [...]*

¹¹³ [...]*

¹¹⁴ For example, one competitor referred to special requirements of engines used in the rolling mill sector which need to be particularly shock-resistant. Siemens replied that even engines which are used to drive winding gear in underground and opencast mining, paper machines or on ships must have comparable high shock tolerance. For the purposes of this investigation, however, it is not necessary to decide this question, since VAI does not make such engines. While the fellow subsidiary Elin EBG manufactures drives, the market survey shows that they are comparatively insignificant for metallurgical applications.

products and sensors of measuring instruments (components) used in metal plants can also be used in other industrial plants in a similar form.

(256) On the other hand, this does not apply to the products in the area of automation proper (levels 1 and 2), where increasing specialisation is being seen. Indeed, it is also true here that certain HMI products and IT platforms (automation systems) are exhibiting general characteristics.¹¹⁵ What is important, however, is that these systems require special sector solutions (software modules) in order to be usable.¹¹⁶ Siemens and its competitors develop sector solutions such as these in electrical industrial plant building in sector-specific product families, the core use of which is in the level 1 and level 2 areas of automation. For example, Siemens has two of these sector-specific product families (“Simelt” for the blast furnace area and “Siroll” for the rolling mill area), SMS Demag has one (“X-Pact“ for the whole metallurgical area),¹¹⁷ as has VAI (“Vaioneer”).

(257) In any case, from the buyer's point of view, the products and services of other electrical metal plant building, with the exception of non-specific individual components, are not exchangeable with the products and services of electrical industrial plant building. From the supplier's point of view as well, clear specialisation in electrical metal plant building is necessary which, as in the case of Siemens, does not conflict with the parallel development of a general electrification and automation basis.

- *Discussion of Siemens' opinion in the comments on the statement of objections*

(258) Siemens refers in its comments to what it sees as the high degree of supply substitutability, since solutions rely on standardised products, which only need a little sector- and customer-specific adaptation, suppliers require specialised engineers only to a slight extent and there are no particular obstacles to suppliers from (other) electrical industrial plant building starting to operate in the metallurgical sector.

(259) Siemens' argument is not valid. First, while metals-specific products and services (solutions) often rely on general products and services that can also be used in other industries, the sector-specific value added is so significant that it cannot be developed and supplied at all for a large number of the products and services required by customers without spending considerable extra time and money. This applies in particular to the in-line aspects of these products and services, and especially to the area of automation proper. To put it at its starkest, many firms may be able to supply the lighting installations or even the power supply for a metal plant without special metallurgical experience, but they cannot supply the appropriate

¹¹⁵ [...] * Even with Simatic TDC the Siemens product information stresses its use in the metallurgical sector: “The most complex control loops in the shortest scanning times are calculated with it, such as is needed in large plants in the blast furnace and rolling mill sector.”

(http://www2.automation.siemens.com/simatic/regelsysteme/html_00/produkte/rb-tdc.htm).

¹¹⁶ Anonymised results of the market survey: one competitor declared that of 4 specific products/solutions which he developed for electrical metal plants, only one of the products can be used to more than a small extent in other electrical industrial plants and two of these products cannot be used at all in those plants. [...] *.

¹¹⁷ “X-Pact [is] one of the most successful sector solutions in the world of blast furnace and rolling mill engineering.” (SMS homepage).

technological control and regulatory systems or the quality control and calculation models for the actual production process, where, according to market participants, there are considerable barriers to entry. When, as regularly happens, a contract is awarded for the all the electrical installations in a plant, including the metallurgy specific aspects (i.e. a total package including components purchasing, systems integration and equipment installation and putting into service), there is insufficient supply substitution among suppliers operating in other sectors. This accords with the view of a clear majority of customers that electrical plant building in the metallurgical sector should be regarded as sector-specific.¹¹⁸

- (260) Second, given the results of the market survey, it is not correct that suppliers require specialist engineers only to a slight extent. A majority of suppliers indicated even that electrotechnical plant building engineers operating in the metallurgical sector are often “highly” specialised in metallurgy.¹¹⁹
- (261) Third, for the reasons mentioned (need to build up specific metallurgical know-how, need for metallurgical references, costs incurred by and time required for this), there are particular obstacles to suppliers from electrical industrial plant building starting to operate in the metallurgical sector.¹²⁰
- (262) For the reasons given, therefore, for the purposes of the product market definition in this Decision, electrical plant building is assumed to be specific for at least the metallurgical sector.¹²¹ As emerges from the discussion below of IT solutions for plant logistics/MES/level 3¹²² and of aluminium hot and cold rolling,¹²³ such an overall market can be defined either as an overall market for electrical metal plant building including all possible submarkets discussed below or, more narrowly, as a possible overall market for electrical metal plant building at automation levels 0-2 in the iron and steel sector.¹²⁴

(3) Possible separate markets for individual process areas or steps

- (263) Market participants, moreover, assume that the market for electrical plant building is further subdivided by metal manufacture process stage.¹²⁵ Thus a clear majority of responding competitors stated that their electrotechnical engineers working in metal plant building have either a “certain/partial” or even a “strong” intra-metallurgical specialisation.¹²⁶

¹¹⁸ Results of the market survey, Customers, Phase I.

¹¹⁹ Results of the market survey, Competitors, Phase II. More than two thirds of the responding competitors assumed that their electrotechnical plant building engineers were either highly or partly specialised in metallurgy.

¹²⁰ The example of an “entry” cited by Siemens should be understood as such. At best, it is a partial entry, as is clear from the following statement of this market participant: “Our focus is only the steel market in Upper Austria. As we are doing business there for only 5 years, we are not able to answer this question properly.” [NB The question concerned the listing of competitors operating in a particular process stage.] In the reply to the statement of objections, Siemens does not go into these barriers to entry specifically.

¹²¹ Siemens itself notes in this respect, in its comments on the statement of objections, that such an approach “can still be justified possibly” (p. 9).

¹²² See paragraph (274).

¹²³ See paragraphs (271)-(273).

¹²⁴ See also paragraph (275).

¹²⁵ See explanation of process stages in paragraph (225).

¹²⁶ See replies to the competitors’ questionnaire Metallurgy, Phase II.

- (264) References to a more extensive subdivision of the relevant product markets can also be found in Siemens' internal papers.¹²⁷ Similarly, Siemens' product development takes account of the differences in process areas and process stages. Siemens clearly distinguishes the liquid phase process area terminologically and in marketing terms from the hot and cold phase process areas by using the product family name "Simelt" for the former and "Siroll" for the latter. *[There follow comments on the Simelt and Siroll product families and the relevant internal assessment of the competitive situation by Siemens. ...]*^{128 129}
- (265) The main technological requirements are also clearly different for each process area: while in the liquid phase the controlling of the smelting process and what happens during smelting is paramount, it is the rolling process which is the defining element for both the hot rolling and the cold rolling phase. In addition to this, in the hot phase the controlling of the cooling process is of central importance, while surface evenness monitoring and controlling are of decisive importance for the cold phase. There are even clear technological differences within the process areas for the individual process stages.¹³⁰
- (266) The Commission's market investigation showed that among [...] competitors there are comparable internal differentiations by process area and process stage, e.g. separate business units. Competitors also arrange their marketing very differently according to the individual process areas and process stages.¹³¹
- (267) Reference lists are drawn up per process stage and, as the Commission's market investigation has shown, orders are mainly awarded separately for one process stage. Suppliers must therefore try to be able to offer as complete an automation package as

¹²⁷ See the sheet in the Siemens presentation "Discussion with DG competition on 15.4.2005 and GSL Jour Fix, 29.1.2001, Annex 2. Reply to the request for information of 7.4.2005 (part 2). Reply to the request for information of 29 March 2005, Annex 1.b, sheets 6 and 7 and Annex 1.d, sheet 4. Reply to the request for information of 29 March 2005, Annex 1.n, sheet 85. [...] Reply to the request for information of 29 March 2005, Annex 1.a, sheet 37. [...] See reply to the request for information of 29 March 2005, Annex 1.n, sheet 33. See also Siemens' reply to the request for information of 7 April 2005, Annex 4 [...] Reply to the request for information of 29 March 2005, Annex 1.c, sheet 4. [...] See also "Innovation Roadmap IP 3 Hot" as well as "Innovation Roadmap IP 3 Cold". Reply to the request for information of 29 March 2005, Annex 1.b., sheets 34 and 35. [...] Reply to the request for information of 29 March 2005, Annex 1.a, sheet 18 [...].

¹²⁸ Reply to the request for information of 29 March 2005, Annex 1.n, sheet 33.

¹²⁹ [...] Reply to the request for information of 29 March 2005, Annex 1.c, sheet 6.). Sheets 8, 12 and 13 [...].

¹³⁰ Thus the Commission's market survey clearly revealed that the technological regulating systems and control models for level 1 and 2 automation show considerable technological differences between the continuous casting and hot rolling process stages. For instance, in continuous casting, the element of rolling controlling found in hot rolling is lacking. There are also clear differences between hot rolling and cold rolling. In strip processing lines, drive solutions are substantially simpler than in cold rolling plants etc.

¹³¹ See for example the tender lists submitted by competitors, including VA Tech's list. See on this also VA Tech's information brochure: "The World of VAI Automation" (www.vai.at), in which electrical metal plant building is broken down into the following individual areas: "Ironmaking", "Steelmaking", "Continuous Casting", and "Rolling/Processing". The "Rolling/Processing" area is subdivided further by VAI in this brochure as well as in other parts of the homepage into "Hot Rolling" (hot rolling of strip steel, so-called hot strips), "Plate Mill" (hot rolling of steel plates, so-called thick plate mills), "Cold Rolling", "Strip Processing" as well as "Long Product Rolling" and "Aluminium Rolling". The last area mentioned in this brochure, "Plant-wide Solutions" refers to Level 3/MES. See also SMS's website and its automation brochures.

possible for each process stage. Both the costs of entering the market for each process stage and the development time are considerable.¹³²

(268) In addition to the above division into process areas and process stages it should be noted, on the basis of the findings of the market survey, that there are clear signs that the rolling of long products forms a separate product market to the flat-product hot and cold rolling process stages, with different technological requirements, different customers and suppliers set up differently.¹³³

(269) For the purposes of this Decision, however, it can ultimately be left open whether separate electrical product markets exist for the three main process areas of electrical metal plant building (liquid phase, hot phase, cold phase) and the special area of long product rolling. Similarly, the question of a further subdivision by process stage can be left open for the purposes of this Decision.

(4) Separate sub-markets for level 1 and 2 automation

(270) As to whether for the purposes of defining the relevant product markets a distinction should be made according to the individual levels of automation, in particular levels 0, 1 and 2, the market survey showed that both demand and supply in the individual automation levels are different overall and as regards each process stage. For the purposes of this Decision it can remain open, however, whether separate product markets should be assumed, say, for levels 1 and 2 together, or subsets thereof, or for level 0.¹³⁴

(5) Separate markets for the iron and steel sector and the aluminium sector, in particular for aluminium hot and cold rolling

(271) The distinctiveness of the electrical iron/steel plant building markets in the process stages which come *before* hot and cold rolling in the manufacturing process is evident from the very fact that Siemens and VA Tech, like other major suppliers in the iron and steel sector, are hardly active, if at all, in the corresponding areas outside the iron and steel sector. There is therefore insufficient supply and demand substitution.

(272) In the context of the Commission's market survey, it was also said that aluminium hot and cold rolling too (including foil rolling), in which Siemens and VA Tech are active, form separate product markets. This was justified by the different process

¹³² See anonymised results of the market investigation: "One competitor explained that development work for various specific products/solutions for hot rolling steel mills took 3-10 years."

¹³³ Reply to the request for information of 29 March 2005 (Annex 1.a, slides 37 and 38). [...] * See also the clearly different assessment of customers (and competitors) concerning the list of suppliers in long product rolling and flat product rolling. In the case of long products, Danieli clearly heads this assessment, while in the rolling of flat products (both in the process stages and, aggregated, in the process areas) it clearly comes behind other market participants, such as Siemens, VAI and SMS. The replies of competitors to the question whether for long product rolling other software for technological control modules and models is necessary than for the hot rolling of flat products also suggest a separation into different product markets.

¹³⁴ In the context of this Decision, however, level 0 does not need to be discussed further in the metallurgy part, since the products in question, in so far as horizontally affected markets are present, are discussed in the sections on energy transmission and distribution (T&D) and drives. On the absence of vertical effects, see generally paragraphs (397) – (400). On the question of further delimitation regarding level 3 automation (IT solutions for plant logistics) see paragraph (274) below.

engineering requirements for steel and aluminium, in particular in the hot rolling process, especially as regards temperature behaviour, rolling speed and surface characteristics.

(273) For the purposes of this Decision, however, the question of product market conformity/separation as between the rolling markets in the iron/steel and aluminium sector can also remain open.

(6) Possible market for IT solutions for plant logistics/MES/Level 3

(274) The Commission's market investigation also revealed a number of indications of a separate, possibly emerging metals-specific product market for IT solutions for plant logistics/ MES/level 3.¹³⁵ However, the question of the latter's sector specificity and its inclusion in, or separation from, an electrical metal plant building market can ultimately be left open for the purposes of this Decision, since, although in this sector there is product overlapping between Siemens and VA Tech, no competition concern was established in the Commission's market investigation, however the product market was defined. From today's standpoint at any rate this area is not part of electrical metal plant building proper in the narrow sense (levels 0-2).¹³⁶ Moreover, the precise product market definition of the IT solutions area for plant logistics/MES/level 3 can remain open for the purposes of this Decision.

(7) Two possible overall markets for electrical metal plant building

(275) It should be repeated for the sake of clarification (see paragraph (262)) that, as a result, two possible "overall markets" for electrical metal plant building should be investigated: (i) an overall market for electrical metal plant building, including all the possible electrical metal plant building submarkets mentioned, and (ii) a possible (more narrowly understood) market for electrical metal plant building at automation levels 0-2 in the iron and steel area (i.e. excluding the possible markets for aluminium rolling and IT solutions for plant logistics/MES/level 3).

(d) Maintenance and servicing

(276) The activities of Siemens and VAI also overlap in the field of maintenance and servicing of industrial plant, in particular in electrical metal plant.

(277) Siemens assumes a separate service market for providing services to metal plants, which, in addition to carrying out maintenance work, also includes advisory and support services such as education and training events.

(278) [...] *¹³⁷

(279) The Commission's market investigation has shown that such services are indeed to a large extent separate from actual plant building and are sought from other suppliers.

¹³⁵ [...] *. Reply to the request for information of 29 March 2005, Annex 1.c, sheets 15-20). [...] * (See, for example, reply to the request for information of 29 March 2005, Annex 1.k, sheet 46 and all similar points. [...] *)

¹³⁶ [...] *

¹³⁷ See for example reply to the request for information of 29 March 2005, Annex 1.k, sheet 46 and all similar points. [...] *

Furthermore, a considerable proportion of these services is looked after by the buyer itself. Given the results of the market investigation¹³⁸ it can be concluded, however, that the area of maintenance and service provision is not part of the electrical metal plant building market. For the purposes of this Decision, however, a more comprehensive, precise market definition can be left open in this area.

(e) Electrical industrial plant building in non-metal sectors

- (280) As mentioned, Siemens assumes a common product market for all areas of electrical industrial plant building.
- (281) In non-metal electrical industrial plant building, VA Tech operates exclusively through its subsidiary Elin EBG, unlike in metal industrial plant building where it is (mainly) represented by its subsidiary VAI. Electrical installations are manufactured in particular for plants in the motor vehicles, oil and gas, pharmaceuticals, paper, cement and food, beverages and tobacco industries. Siemens operates in particular in the oil and gas, pharmaceuticals, paper, cement and food, beverages and tobacco industries.
- (282) For the purposes of this Decision, the question of the sector-specific market definition of non-metal electrical industrial plant building can be left open, since the proposed merger does not raise competition concerns under any possible market definition (i.e. either as a market covering several sectors or as a separate market per sector).

(f) Summary of the product market definition in metal plant building and in industrial plant building in other sectors

- (283) For the purposes of this Decision, therefore, in the area of mechanical metal plant building, the following product markets are assumed:
- an overall market for mechanical metal plant building (either restricted to ferrous metals or comprising both ferrous and non-ferrous metals);
 - the possible submarkets for mechanical metal plant building (see paragraph (231)).
- (284) For the purposes of this Decision, in the area of electrical metal plant building, the following product markets are assumed:
- the overall market for electrical metal plant building, including all possible consequent submarkets;
 - the possible (more narrowly understood) overall market for electrical metal plant building at automation levels 0-2 in the iron and steel sector;
 - the possible submarkets for electrical metal plant building of the liquid phase, hot phase, cold phase and rolling of long products (process area markets) in the iron and steel sector and the possible process stage markets (or further subdivisions e.g. by automation level), and possible level 1 and 2 submarkets;

¹³⁸ [...] * See reply to the request for information of 29 March 2005, Annex 1.i, sheet 14 [...] * Reply to the request for information of 29 March 2005, Annex 1.c, sheets 21-32). [...] *

- the possible markets for aluminium hot and cold rolling;
 - the possible market for IT solutions for plant logistics/MES/level 3.
- (285) For the purposes of this Decision, moreover, at least one separate product market should be assumed for metal plant maintenance and servicing.
- (286) The product market definition in electrical industrial plant building in other sectors can be left open for the purposes of this Decision.

2. Relevant geographic markets

(a) Mechanical metal plant building

- (287) Siemens assumes that the market for mechanical metal plant building is a world market. It asserts that, in the context of tendering procedures, there is a worldwide demand for the services in this area. The products and services are basically the same in all parts of the world and aimed at the – globally uniform - physical, chemical and mechanical characteristics and properties of metal processing. Quality differences between the plant builders operating worldwide play no part, only price determines which supplier is selected. However, prices do not vary greatly worldwide. Transport costs in particular are of no consequence in this area.
- (288) In its comments on the statement of objections, Siemens takes the view that the market is at least EEA-wide, with a strong tendency to become worldwide.
- (289) The Commission's investigations have revealed that demand in this area is EEA-wide and possibly even wider. While within the EEA there are definite remnants of national and language-area-related demand patterns,¹³⁹ the essential competition parameters are at least EEA-wide. However, so far in the EEA non-European suppliers have clearly been awarded orders only on a small scale. Even if, according to the market participants, transport costs scarcely play a role in this respect, the majority of customers perceive the quality of European products¹⁴⁰ to be more reliable. Historical closeness to the supplier clearly also plays a part, as do the costs of regional market entry (e.g. through the need to set up engineering branches without having already worked out their capacity utilisation). It should also be noted that regional price comparisons in this heterogeneous market/these very heterogeneous markets are very difficult. However, the Commission's market investigation showed that the general price level of metal plant building in China is lower.¹⁴¹ The remarks in paragraph (299) below, which apply in this respect to mechanical metal plant building too, should also be noted.
- (290) The European suppliers, at any rate the large ones, are organised globally, however, in the sense that they relate to several continents and make a large proportion of their turnover outside the EEA.

¹³⁹ The reasons given for this were partly different legal provisions as well as tenders written in the language of the country. Furthermore, the geographical proximity to the customer, in particular in connection with support in problems of a technical nature, seems to play some role.

¹⁴⁰ Where European firms also use non-European components, this also applies to the European quality control/guarantee of these non-European components.

¹⁴¹ [...]*

(291) For the purposes of this Decision it is not necessary, however, to decide the question of geographic market definition, since under each possible geographic market definition (EEA-wide or wider than the EEA), the concentration gives rise to competition concerns. The same applies for the same reasons to all possible submarkets in mechanical plant building.

(b) Electrical metal plant building

(292) In the area of electrical industrial plant building, too, Siemens assumes that there is a world market and asserts that particularly in large projects tenders and bids take place on a global level. Siemens also says that the end-customers are predominantly internationally active companies which operate plants in several countries.

(293) In this area too, the Commission's findings have revealed that demand from the majority of the customers in the EEA for electrical metal plant building is EEA-wide. Even if, in this area, transport costs play a rather subordinate role, the geographical or linguistic proximity to the respective suppliers still appears to customers to be important, in order to be able to make contact rapidly and without complications in the event of technical problems. Even within the EEA certain customer preferences¹⁴² for or against certain suppliers and certain regional strengths and weaknesses still result from this and from historical links, but from the point of view of most of the customers and suppliers these features do not invalidate the assumption of an, at least, EEA-wide geographic market.

(294) [...] ¹⁴³ [...] ¹⁴⁴ For the efficient handling of project orders it is also necessary to have strong regional branches, just as the involvement of local value added greatly increases the chances of a bid being accepted or is even a precondition for winning an order.

(295) Asian companies in particular have so far hardly received any orders in the EEA. Conversely, successful business activity appears to many European companies to be difficult, for example, in Japan because of the existing competition situation. In discussions about the market by European companies, it is typically assumed that there is a theoretical world market volume and a clearly smaller "accessible" world market volume. [...] ¹⁴⁵ Even if European customers require European suppliers to operate successfully worldwide (and therefore to be able to produce extra-European references as well), this does not allow the opposite conclusion that non-European suppliers without references in the EEA are seen by European customers as equivalent alternatives to European suppliers. The small number of EEA references for non-European suppliers is thus also an obstacle to extending the relevant geographic market.

(296) On the other hand it was clear from the Commission's market survey that a not inconsiderable number of customers considered that it was quite possible that in the next 2-3 years Japanese companies would enter the European market and therefore

¹⁴² Reply to the request for information of 29 March 2005 [...]*

¹⁴³ Reply to the request for information of 29 March 2005, Annex 1 b sheet 11 [...]*

¹⁴⁴ Reply to the request for information of 29 March 2005, Annexes. [...] * Reply to the request for information of 29 March 2005, Annex 1.c, sheet 6.).

¹⁴⁵ [...] * Reply to the request for information of 29 March 2005, Annex 1.1, sheet 5: [...]*

appeared not to have fundamental quality reservations about these companies.¹⁴⁶ It does not yet follow from this information, however, that there is sufficient effective, direct supply substitutability.¹⁴⁷

(297) It therefore seems appropriate for the purposes of this Decision to define the market as at least EEA-wide. Whether the market is EEA-wide or worldwide can, however, remain open for the purposes of this Decision.

(298) This applies for the same reasons to all the possible electrical metal plant building submarkets and markets, including the possible market for IT solutions for plant logistics/MES/level 3.

(299) In considering the competitive position of the individual competitors, the following is to be taken into account.

- Even if the analysis is confined to a market which is only EEA-wide, consideration of the worldwide market shares of the competitors which are strong in the EEA is relevant. European customers have predominantly said that it is absolutely necessary even for a European competitor to be a strong supplier worldwide. Therefore, for marketing reasons too, worldwide market successes are of great importance for European competitors. Worldwide market shares of European competitors also give information about the market strength of these competitors in large projects and help to prevent a distortion due to possibly too small (and therefore not sufficiently representative) order volumes in Europe. This is of course particularly true for smaller submarkets.
- Even if it is assumed that there is a world market in the sense of a geographic market which extends beyond Europe and encompasses several continents, market relations on such a worldwide market are by no means homogeneous. It is even possible that a considerable part of the hypothetical world market volume is not accessible due to regional peculiarities or follows different market rules. For instance, in the Peoples' Republic of China - one of the most important customers on such a world market for electrical metal plant building - the volume of plant building continues to be strongly controlled. [*There follow comments on Siemens' internal assesment of the demand situation in China and Japan*]*^{148 149}

(300) Siemens agrees with the Commission's geographic market definition in electrical metal plant building only in so far as the Commission considers the possibility of a market which extends beyond the EEA, but it rejects the view that certain Asian regions cannot be included in the relevant market. The corresponding submarkets are completely accessible even to foreign suppliers.

(301) The Commission maintains its view, however, that certain geographic world regions have clearly different competitive behaviours. As established, it can however remain open whether there is an EEA-wide or a worldwide market (the latter

¹⁴⁶ Account should be taken, however, of the constraint expressed in paragraph (324) regarding this expectation, which also applies mutatis mutandis to electrical metal plant building.

¹⁴⁷ Within the meaning of the Commission notice on the definition of the relevant market for the purposes of Community competition law (OJ C 372, 9.12.1997, p. 13, paragraph 20).

¹⁴⁸ [...]*

¹⁴⁹ See [...]* Reply to the request for information of 29 March 2005, Annex 1.1, sheet 20, [...]*.

including/excluding in particular Japanese demand and a possibly “inaccessible” part of the Chinese market).

(c) Maintenance and servicing

- (302) From Siemens' point of view, the market for servicing and maintenance work is to be defined as being EEA-wide, but is perceived by the majority of market participants as being narrower, since geographical proximity to the supplier and partly also sharing a common language are seen as being particularly relevant here. A number of customers would also not select a supplier from a different Member State than the location of their own production site, if the prices for services from their current suppliers were to rise by 5-10%. This applies to both the mechanical and the electrical sector.
- (303) For the purpose of this Decision, a precise market definition can ultimately be left open. The relevant geographic market, in any event, is not smaller than national and not bigger than EEA-wide.

(d) Electrical industrial plant building in other sectors

- (304) The corporate organisation of VA Tech, with the metal plant builder VAI as a company operating worldwide and Elin EBG which provides electrical plant building generally, is largely concentrated in Austria and is also increasingly active in industrial plant building in central Europe, suggests that the market/markets for other electrical industrial plant building should be defined more narrowly in geographical terms than those for specialised electrical metal plant building. This view was confirmed in the Commission's market investigation, where many of the responding industrial firms assumed, if anything, national markets or markets comprising several Member States in their replies. If necessary, a larger than transnational regional geographic market can be considered for some specialised process industries, such as paper and chemicals. But there were no indications in the Commission's market survey that the geographic market should be perceived as bigger than the territory of the EEA.
- (305) For the purpose of this Decision, a precise market definition can ultimately be left open. The market/markets concerned, in any event, are not smaller than national and not bigger than EEA-wide.

3. Competition assessment

(a) Mechanical metal plant building

- (306) The merger would lead, essentially as a result of Siemens' shareholding in SMS and the special rights arising from this shareholding, in the EEA-wide or worldwide market for mechanical metal plant building or its submarkets for mechanical plant building for steelmaking and for continuous casting to a substantial weakening of competition between Siemens/VA Tech and its main competitor SMS. This in turn would lead to a significant impediment to effective competition in the above-mentioned submarkets in particular as a result of the creation of a dominant position on the part of Siemens/VA Tech.

(1) *Market conditions*

- (307) Only VA Tech, and not Siemens, is active in this area. According to Siemens, in 2003 VA Tech's share of the world market came to less than [5-10]*% and of the EEA market to less than [10-15]*%. Looking at individual submarkets, Siemens assumes that VA Tech's shares in mechanical plant building in pig iron making and steelmaking and also in continuous casting at EEA level are about [5-10]*%. Regarding the other possible submarkets (hot rolling mills, cold rolling mills, section rolling mills, strip mills, pipe mills, pressing and forging, aluminium rolling mills and copper plants), Siemens estimates the EEA-wide share of VA Tech at about [10-15]*%.
- (308) By contrast, market participants assumed considerably higher market shares for VA Tech in individual possible product markets in mechanical plant building. Thus, the worldwide and EEA market shares of VA Tech in the mechanical metal plant building market were seen in some cases as being close to those of the previous sole market leader SMS-Demag (hereinafter: "SMS") (followed by the third and only other complete supplier active in the EEA, Danieli). In individual possible mechanical submarkets VA Tech is in any case seen as the clear market leader.¹⁵⁰ Statements by market participants also suggest that the market or markets for mechanical metal plant building are to be regarded as highly concentrated.
- (309) Siemens' internal documents and documents drawn up on its behalf do not confirm the above market view presented by Siemens within the framework of this proceeding.

*[There follow comments on Siemens' internal strategic and analytical investigations of the competitive environment]** ^{151 152 153 154 155}

- (310) SMS sees VAI as its main competitor in most of its business areas. SMS gives its own market shares and those of VAI in mechanical metal plant building overall as [20-30]*% and [20-30]*%. In individual process stage markets the combined market shares of the two leading firms are significantly higher, namely in steelmaking ([30-40]*%, [30-40]*%), continuous casting ([20-30]*%, [60-70]*%), hot rolling ([50-60]*%, [15-20]*%) and cold rolling ([40-50]*%, [10-15]*%).¹⁵⁶
- (311) At the shareholders' committee meeting of SMS GmbH/MDKM of 18 May 2004 a planning document for 2004/2005 was presented. This shows the market share in mechanical metal plant building of SMS and its competitors for the period 1999-2003. SMS is considered to have a share of [30-40]*%, VAI [15-20]*%, Danieli [10-15]*%, Japanese suppliers [5-10]*% and "others" [30-40]*%. In individual process stages SMS and VAI have a much larger market share (e.g. steelmaking/converters: SMS Demag: [40-50]*%, VAI [30-40]*%; continuous

¹⁵⁰ See paragraph (319) for details.

¹⁵¹ [...]*

¹⁵² [...]*

¹⁵³ [...]*

¹⁵⁴ [...]*

¹⁵⁵ [...]*

¹⁵⁶ SMS, Key Document.

casting/slab casting: SMS Demag: [20-30]*%, VAI [50-60]*%).¹⁵⁷ By and large, the latter figures are confirmed publicly by VAI.¹⁵⁸

(2) Overall market for mechanical metal plant building in the area of iron and steel or overall market for mechanical metal plant building including non-ferrous metals: significant impediment to effective competition

(312) [...]*,¹⁵⁹ on the basis of the facts it cannot be assumed that solely with the removal of this potential competition there would be a significant impediment to effective competition in the common market.

(313) The Commission's market investigation has shown, however, that the merger would lead to a substantial weakening of the current competition between VAI and SMS owing to Siemens' minority stake in SMS. Because of VAI's market strength in this highly concentrated market and the very close competition between VAI and SMS¹⁶⁰ and because other competitors alone would not be able to restrict Siemens/VAI's competitive room for manoeuvre sufficiently, the merger would in any event pose a significant impediment to effective competition through uncoordinated behaviour and possibly also by creating a dominant position for Siemens/VAI.

(a) VAI and SMS are the market leaders in a highly concentrated market

(314) VAI and SMS are the strongest competitors in the highly concentrated market for mechanical metal plant building, as can be seen from the remarks made at the beginning on market structure.

(315) [...]*

(316) [...]*¹⁶¹

(317) [...]*¹⁶²

(318) Thirdly, the importance of market shares in tender markets is relative and must be interpreted in the light of the specific impact of the merger proposal on bidding behaviour.

¹⁵⁷ [...]*

¹⁵⁸ "VAI has become the world market leader in slab casting technology. During the past five years, for example, our company has supplied 43% of all new slab casters and carried out 62% of all slabcaster upgrading projects." "VAI is one of the pioneers of slab casting technology. This is reflected by numerous trailblazing developments." "With a share of nearly 60% of all stainless-steel slab casters supplied during the past eight years, VAI is the world market leader in this field." (http://www.vai.at/view.php3?r_id=198&LNG=EN).

Further remarks in the same place referring to technological leadership are: Strip casting "is perhaps the most exciting leapfrog technology in the iron and steel industry today" "Eurostrip®: ThyssenKruppSteel, Usinor and VAI – more than 1000 patents in 100 patent families" – (two plants in Krefeld and Terni).

¹⁵⁹ See, for example, reply to the request for information of 29 March 2005, Annex 1.n, sheet 17, See reply to the request for information of 29 March 2005, Annex 1.l, sheet 17 [...]* and sheet 14 [...]* .

¹⁶⁰ See the results of the market survey, Phase II, in particular as regards the ranking of the market leader and closest competitor.

¹⁶¹ See also paragraph (312) on the potential competition from Siemens, whose elimination must be included in an overall view of the effects of the merger on mechanical metal plant building.

¹⁶² Reply to the Commission's request for information, submitted on 1 March 2005.

(b) VAI and SMS are particularly close competitors

(319) VAI and SMS are the closest competitors in the relevant market or markets. Because of this close competition between VAI and SMS, a customer who decides against VA Tech in a particular metallurgical project would very probably regard SMS as the next best alternative. This is shown, for example, by the ratings given by the competitors and customers questioned during the Commission's market investigation. VAI was regarded overwhelmingly as the leading and SMS as the second-strongest and next-ranking company in the following areas: pig iron making, steelmaking and continuous casting. SMS was regarded overwhelmingly as the strongest and VAI as the second-strongest and next-ranking company in the following areas: hot rolling, cold rolling, strip processing, pipemaking, aluminium cold rolling and aluminium hot rolling¹⁶³. In the case of copper and other metal plants, SMS was regarded as the market leader and VA Tech was considered one of the more important competitors. In only one area, the rolling of long products, was the third-largest supplier, Danieli, ranked first, while VAI and SMS followed in more or less equal second place).

(c) Insufficient competitive pressure is exerted by other competitors

(320) According to Siemens in its reply to the statement of objections, even if Siemens' minority holding in SMS were to result in a lessening of competition between SMS and VAI, there would continue to be intense competition in the relevant market. In Siemens' opinion, VA Tech and SMS would be faced with a number of other suppliers which from the customer's point of view constitute viable alternatives.

(321) The major suppliers mentioned in this connection by Siemens (MHI/Hitachi, JP Steel Plantech and Aker Kvaerner¹⁶⁴) are, however, rarely or never active in Europe and so do not represent a viable alternative for European customers. They are accordingly included by the customers and competitors surveyed only to a limited extent, and even then only in a few areas, among the five strongest suppliers in the mechanical metal plant building market as a whole or in one of the possible submarkets. As far as the smaller suppliers mentioned are concerned, contrary to the view taken by Siemens their capacity to bid successfully for major orders is called into question by many market participants (including by the smaller suppliers themselves). This also holds true for the possibility of forming consortia; according to market participants, these enable smaller suppliers to bid successfully only in a few cases, and then often only in conjunction with one of the larger suppliers.¹⁶⁵

(322) The Commission's market investigation showed, rather, that in the EEA the three full liners VAI, SMS and Danieli were almost exclusively mentioned as being the strongest competitors, accompanied, where appropriate, by smaller specialists such as Paul Wurth in iron and (partly) steelmaking and Andritz in cold rolling and strip processing. Worldwide, VAI, SMS, and Danieli were regarded in the context of the Commission's market investigation as by far the strongest competitors, accompanied by a few Japanese companies whose clear main focus is on orders in Japan and the

¹⁶³ In aluminium rolling VAI ranks more or less equally with Achenbach.

¹⁶⁴ "We are only active in the Americas market" (Aker Kvaerner, reply to the Commission's request for information on the metallurgy sector, Phase II)

¹⁶⁵ See answer to question 45 in the customer information request or question 19 in the competitor information request in Phase I.

Far East such as MHI¹⁶⁶, NSC, JP Steel Plantech and IHI and in the pig iron sector also by Chinese firms. [...] * Outside the three market leaders, then, competition is very fragmented and is not sufficiently capable of curbing the market power of the three leading suppliers.¹⁶⁷

(323) Danieli is usually regarded as the third strongest competitor, but on average well behind SMS and VAI. Danieli's strength lies primarily in flat rolling (section mills), where it is the market leader. Because of Danieli's market position and customer rating, it is unlikely to be able either to prevent competition from declining in the market for mechanical metal plant building as a whole or even to threaten the dominant position that VAI might gain as a result of Siemens/VAI's information advantage. This is also clear from the fact that, as is stressed by customers, the number of serious bids submitted to a customer is of decisive importance when it comes to the price the customer can achieve through negotiation. It was pointed out in the course of the Commission's market investigation that customers need at least three competitive bids in order to negotiate successfully in the field of metal plant building. This is also confirmed by what competitors have to say about the number of rival bidders in the final stages of contract award negotiations, which is often put at three.¹⁶⁸

(324) Siemens points out, lastly, that some customers and competitors expect within the next two to three years the market entry of viable suppliers from the Far East (Japan or China) in the EEA. This can be put into perspective by pointing out that many (if not most) market participants simply do not expect this to happen.¹⁶⁹ Moreover, the possibility of the market entry of such suppliers in the EEA is played down by the very market participants who in principle expect it to materialise. [*There follow comments on VA Tech's assessment of the market entry of Japanese and Chinese suppliers* ^{170 171}]* However, the market investigation did not turn up any further indications that this assumption can be made on the customers' side. Similar qualifications are also to be found in other statements by market participants.¹⁷² It should also be pointed out that, on a world measure, Far Eastern suppliers were ranked by customers far lower than the leading European suppliers. By and large,

¹⁶⁶ According to information supplied by VA Tech [reply to the request for information concerning metallurgy, Phase II (ranking of competitors)], which was confirmed in the course of the market investigation, MHI (the Japanese company mentioned most often by customers and competitors as being a relevant competitor) is active mainly in the possible submarkets of the mechanical building of hot and cold rolling plants and for belt installations and can therefore have no restricting effect on Siemens' market power in the entire possible market for mechanical plant building (and in particular in the submarkets for steelmaking plant and continuous casting plant).

¹⁶⁷ See also VAI's opinion, referred to in paragraph (227).

¹⁶⁸ To these must be added any further competitors who have already withdrawn. Particular mention should be made here of the multi-stage nature of the tender process, whereby there is some openness about the identity and the number of other tenderers.

¹⁶⁹ These include the [...] * competitor [...] * most often mentioned by customers and competitors.

¹⁷⁰ Reply to the Commission's request for information on the metallurgy sector, Phase II.

¹⁷¹ Reply to the Commission's request for information on the metallurgy sector, Phase II.

¹⁷² One Japanese supplier, for example, thus restricts the market entry possibilities of certain Japanese companies to specific process stage markets. The striking thing here is that the continuous casting market is not mentioned and the steelmaking market is mentioned only with reference to a single supplier. As regards Chinese suppliers, the market entry possibilities are restricted to non-ferrous metal plants. Another market participant understood the question in such a way that it also considered "VAI China", "Siemens China" and "ABB China" to be Asian suppliers.

therefore, these suppliers cannot be expected in the short term to be able effectively to curb the market power of the leading European suppliers, especially as far as customers in the EEA are concerned.

(d) Buyer power

- (325) Siemens took the view that, even on the assumption of competition restricted essentially to the three European full-liners and even in the event of a reduction in the number of equal-ranking suppliers competing head-on from three to two, there are no grounds for concern under merger control law, as in Europe the demand side is highly concentrated. Against this it can be objected that, as indicated in the statement of objections, although a concentration process is taking place in the metallurgical and rolling industries, the degree of concentration worldwide and also in Europe is still much lower than that, say, in the aluminium industry. The Commission's market investigation also showed that suppliers' customer structure is such that a large mechanical metal plant builder has a large number of customers accounting for the bulk of the firm's orders and is not therefore highly dependent on individual customers. Siemens' assertion that customers themselves create new suppliers or are able to turn individual smaller suppliers into general suppliers is unsubstantiated. Nor is such an assumption borne out by the findings of the market investigation.

(e) Substantial weakening of the competitive pressure exerted on Siemens/VAI by SMS

- (326) The merger would substantially weaken the competitive pressure currently exerted on VAI by SMS. It would give Siemens control of VA Tech in addition to its existing 28% holding in SMS. In view of the special circumstances of the case, it cannot be assumed with sufficient certainty that the 28% holding in SMS would, solely by reason of the financial participation in SMS's business success that this would normally entail, induce Siemens/VA Tech to compete less strongly with SMS (i). *[There follow comments on the corporate and organisational relationship between Siemens and SMS as regards the exchange of competitively sensitive information and its effect on bidding behaviour]**

(i) Insufficient certainty that the prospect of financial participation in SMS's business success would give Siemens less of an incentive to compete with SMS

- (327) The Siemens group's 28% holding in SMS might in principle from a financial point of view give Siemens/VA Tech less of an incentive to bid aggressively in those tender procedures in which SMS has a realistic prospect of winning the order. The (partial) internalising of competition between VA Tech and SMS would prompt Siemens/VA Tech (assuming maximisation of profits) to offer higher prices on average or grant lower discounts than are normal in the negotiating process, if SMS is a competitor with a good chance of success. For in the event of the contract being awarded to SMS Siemens would also participate financially through its 28% holding in this business success of SMS. [...] ¹⁷³*

- (328) In June 2004 Siemens, however, exercised with effect from 31 December 2004 a put option existing under the shareholder agreement to sell its 28% SMS holding to the

¹⁷³ [...]*

majority shareholder (SMS GmbH). The method of financial valuation of Siemens' 28% holding and hence the applicable purchase price is the subject of potentially lengthy litigation between Siemens and SMS GmbH.¹⁷⁴ Until the litigation has been settled and the sale is completed, Siemens retains ownership of the shares. The Commission's investigation showed that, according to concurring submissions by both parties in the action for determining the purchase price, the outcome will depend on the value of the share package as at 31 December 2004.¹⁷⁵ Siemens can therefore no longer proceed on the assumption that it will share in any future business success of SMS through a participation in the company's capital and possible future growth of its asset value. Although a financial participation through dividend payments does not appear to be ruled out, it is hard to predict especially in view of the pending litigation with the majority shareholder whether, and if so to what extent, such dividend payments will take place. Under the circumstances it cannot be assumed that Siemens would gear its competitive behaviour to any appreciable extent to a - for Siemens - uncertain participation in possible dividend payments. A competition-lessening effect from a financial point of view of Siemens' participation in SMS is therefore either non-existent or at most so slight that in itself it could not result in a significant impediment to effective competition.¹⁷⁶

(ii) Strengthening of the competitive position of Siemens/VA Tech through access to strategic knowledge about SMS's business policy

(329) *[There follow comments on the corporate and organisational relationship between Siemens and SMS as regards the exchange of competitively sensitive information]**

(330) *[There follow comments on the corporate and organisational relationship between Siemens and SMS as regards the exchange of competitively sensitive information]*¹⁷⁷*

(331) *[There follow comments on the composition, tasks and advisory role of SMS's corporate bodies]*^{178 179 180 181 182 183 184 185 186}*

¹⁷⁴ [...]*.

¹⁷⁵ See, for example, page 8 of the complaint presented by SMS GmbH on 22 December 2004 in the above-mentioned action: "According to the shareholder agreement, the valuation is to be carried out at year's end. As the year-end data were naturally not yet available in August and the investment banks did not consider the forecasts available at the time to be sufficiently reliable, the valuation was made on the basis of the interim statement of account of 30 June 2004. The parties are largely in agreement on this and on the individual figures." See also p. 34 of the complaint, where SMS GmbH states that the valuation of SMS Demag "will take place after 31.12.2004. [...]*.

¹⁷⁶ [...]*

¹⁷⁷ [...]*

¹⁷⁸ [...]*

¹⁷⁹ [...]*

¹⁸⁰ [...]*

¹⁸¹ [...]*

¹⁸² [...]*

¹⁸³ [...]*.

¹⁸⁴ [...]*

¹⁸⁵ [...]*

¹⁸⁶ [...]*

(332) The flow of competition-related information is not stifled by actionable duties of confidentiality under German law (Article 116 of the Companies Law). While there is such a duty on the part of supervisory board members, [*There follow comments on the duties of confidentiality of the members of SMS's corporate bodies*]*

(333) [*There follow comments on possible effects of the minority holding on bidding behaviour*]*¹⁸⁷ Given Siemens' indefinitely continuing 28% share in SMS, the merger would thus substantially weaken competition between Siemens/VAI and SMS.

(f) Conclusion on the possible overall market for mechanical metal plant building in the area of iron and steel and on the overall market for mechanical metal plant building including ferrous and non-ferrous metals

(334) It is clear that, even if an overall market for mechanical metal plant building (either only in the iron and steel sector or also including non-ferrous metals) is taken into account, VAI, like SMS, already has pre-merger considerable market strength and that the two market leaders VAI and SMS are particularly close competitors.

(335) Post-merger, the competitive pressure that SMS has so far exerted on VAI would be largely lost as Siemens' access to strategic knowledge about SMS would enable Siemens/VAI to anticipate SMS's competitive behaviour and react accordingly. As outlined, there is also insufficiently strong competitive pressure from other companies to effectively restrict Siemens/VAI's competitive room for manoeuvre. Whether the information advantage over its strongest competitor SMS and its lead over Danieli in terms of market power would give Siemens/VAI a dominant position may be left open. At all events the merger would have a serious harmful impact on competition as a result of uncoordinated behaviour by firms. For these reasons there would be a significant impediment to effective competition in the overall market for mechanical metal plant building.

(3) Submarkets of mechanical metal plant building: creation of a dominant position

(336) The conclusion set out in paragraph (335) holds true even more forcefully for the possible process stage submarkets in mechanical plant building for steelmaking and continuous casting, to which the above considerations concerning market conditions, buyer power and the impact of Siemens' holding and rights in SMS also apply.¹⁸⁸ In the other possible submarkets in mechanical metal plant building, however, it is impossible to state with sufficient certainty that the merger would constitute a significant impediment to effective competition.

(337) In the possible market for mechanical plant building for steelmaking VAI was the firm rated highest overall by competitors and customers in the Commission's market investigation. In second place, just behind, was SMS. The assessment of its own market leadership is shared by VAI in public pronouncements.¹⁸⁹ VAI and SMS

¹⁸⁷ [...]*

¹⁸⁸ See considerations in paragraphs (306)-(311), (325) and (326)-(333).

¹⁸⁹ See VAI's 2004 annual report in VA Tech 2004 Business Report (http://www.vatech.at/truman/up-media/2933_VAI_AR_2004_E.pdf). All statements refer to 2004: "[VAI] was able to further develop its world leadership position in the Steelmaking [...] technologies, especially in stainless steel technology"; "In electric steelmaking VAI Fuchs was able to attain worldwide

have high EEA and world market shares in a concentrated market. VAI and SMS each have estimated world market shares of between around 30–40%; their EEA market shares are very probably even higher. These high market shares suggest that the market is already highly concentrated, which makes a significant negative impact on customers more likely. This is especially true given the close competition between the two strongest players, which would diminish as a result of the merger in favour of the leading firm. VAI and SMS are the closest competitors. Danieli lies well behind in third place and is not in such close competition. The remaining competition is fragmented. Smaller suppliers cannot compete with the big players in major projects or else they rely on cooperation with the big suppliers or specialise in specific market niches.¹⁹⁰

(338) In the possible market for mechanical plant building for continuous casting VAI is clearly rated by customers and competitors alike as the market leader both in the EEA and worldwide. VAI very probably has market shares of over [40-50]*% in the EEA and worldwide.¹⁹¹ SMS ranks second and is VAI's closest competitor. Danieli is well behind in third place, its competitive strength lying elsewhere (the continuous casting of long products). In the areas of slab casting, thin slab casting and the new process of thin strip casting, VAI and SMS are particularly close competitors. Competition is fragmented and is not sufficiently capable of curbing VAI's market power.

(339) For these reasons Siemens would gain a dominant position in the possible markets for mechanical plant building for steel production and mechanical plant building for continuous casting, resulting in a significant impediment to effective competition. At all events the merger would have, in these possible markets also, a serious harmful impact on competition as a result of uncoordinated behaviour by firms.

(4) Examination of possible non-horizontal effects

(340) The notified merger would result in the integration of suppliers of, on the one hand, electrical (Siemens, VAI) and, on the other hand, mechanical (VAI) plant. It must therefore be examined whether this would have any anticompetitive effects for mechanical (or electrical¹⁹²) metal plant building.

(341) This question must be answered, at this point first of all with respect to mechanical metal plant building, in the negative. Even if VAI has until now had to buy in certain electrical metal plant building services (e.g. in the area of traction solutions or of level 0 electricity supply),¹⁹³ it cannot be concluded from this that the future probable intra-group supplying of VAI by Siemens would lead to an appreciable

market leadership". NB: here, electric steelmaking refers, not to electrical metal plant building, but to a subsector of mechanical metal plant building in the steelmaking process stage.

¹⁹⁰ See also paragraphs (320)-(324) above. It is also worth noting that in steelmaking Paul Wurth was ranked as one of the five strongest firms by far fewer market participants than in pig iron making.

¹⁹¹ See also paragraphs (320)-(324) above. On VAI's views regarding its market position in slab casting, see above, footnote 158. In VAI's 2004 annual report this is confirmed and even reinforced. "[F]urther extension of our market leadership for new slabcasters [and] caster modernisations" (See http://www.vatech.at/truman/up-media/2933_VAI_AR_2004_E.pdf)

¹⁹² See paragraphs (397)-(400) below.

¹⁹³ To some extent, however, supply possibilities already existed within the VA Tech group through Elin EBG.

strengthening of Siemens/VAI in the mechanical metal plant building sector. First, it is entirely possible that customers might consider being tied to Siemens for the supply of, say, drives to be a disadvantage and hence prefer suppliers (such as SMS or Danieli) who are independent in this respect.¹⁹⁴ Secondly, there would continue to be a large number of separate tender procedures (and contract awards) for electrical and mechanical plant building on which this possibly strengthened link between electrical and mechanical plant building would have no impact and in which a mechanical plant builder would be entirely competitive even without any link-up with an electrical plant builder. Thirdly, other, originally primary mechanical suppliers (such as, for example, Danieli, MHI, Achenbach and Andritz) would remain free to forge closer ties with traditionally electrical suppliers. This would be all the more easy as, when performing simultaneous contracts for the mechanical and the electrical parts of a plant (as is typically the case with new plants), the mechanical supplier has traditionally assumed a certain leadership or general contractor role in relation to the electrical metal plant supplier.

(5) *Summing-up on mechanical metal plant building*

(342) The notified merger would accordingly result in a significant impediment to effective competition due to anticompetitive effects stemming from uncoordinated behaviour by firms and possibly also from the establishment of a dominant position on the part of Siemens/VAI, both in the EEA and worldwide, in the market for mechanical metal plant building (whether limited to iron/steel or extended also to non-ferrous metals) and its possible submarkets for steelmaking plants and continuous casting plants.¹⁹⁵

(b) *Electrical metal plant building*

(1) *Market for electrical metal plant building (level 0-2, iron/steel), possible process area and process stage submarkets*

(i) *Market structure and market shares*

- *Market position of the parties and competitors*

(343) According to Siemens' view as expressed in the merger notification (Form CO), Siemens' main competitors in the market for *electrical metal plant building* are ABB, Alstom and TMEIC-GE. This view was confirmed by the Commission's market investigation, where those firms were mentioned as being important competitors, although TMEIC-GE is active mainly outside Europe. Other important competitors are the former mechanical plant building specialists VAI, SMS and Danieli. [...] ¹⁹⁶

(344) [...] ¹⁹⁷ [...] ¹⁹⁸ [...] ¹⁹⁹

¹⁹⁴ VAI's independence or openness vis-à-vis electrical subcontractors used to be regarded as one of its competitive strengths.

¹⁹⁵ On the commitments submitted by Siemens to remove these effects and their assessment by the Commission, see paragraphs (489) and (491) and paragraphs (493)-(496).

¹⁹⁶ Reply to the request for information of 29 March 2005, Annex 1.b, sheet 11.

¹⁹⁷ Siemens' reply to the request for information of 7 April 2005, Annex 4 [...] ^{*}.

¹⁹⁸ Reply to the request for information of 29 March 2005, Annex 1.a, sheet 37.

(345) [...] *²⁰⁰

(346) The Commission's market investigation has shown that Siemens is seen by many market participants (customers and competitors) as the most important and best-known supplier of electrical metal plant building in the iron/steel sector in the EEA and worldwide. This is true for the possible overall market and in most of the submarkets, except in the possible long-rolling submarket, where Danieli is seen as the leader. In all these areas VAI is regarded as a strong competitor, usually in second place in the market; and in the field of continuous casting it is even regarded as roughly on a par with Siemens.²⁰¹ It should be borne in mind, however, that the customers surveyed were predominantly (European) customers of VAI and Siemens who might tend to rate the importance of VAI and Siemens more highly.

(347) It is significant in this connection that, besides the parties, other competitors were mentioned by competitors and customers as being strong suppliers. In the liquid phase process area, these are above all ABB and Alstom; in the ironmaking process stage Corus and Posco as well,²⁰² and in the steelmaking process stage SMS and Danieli as well. In the hot phase process area, ABB, SMS, Alstom, Danieli, and in the hot rolling process stage Toshiba (or TMEIC-GE) (which, however, has so far won only a few orders in Europe) as well, were mentioned.²⁰³ These firms, together with Sundwig-Andritz, were also regarded as strong suppliers in the cold-rolling process area. A few other competitors also received a mention (e.g. Ingelectric and ASI Robicon).²⁰⁴

(348) In the light of these data from customers and competitors it must therefore be concluded that, in the electrical metal plant building market (iron/steel, level 0-2) and in its possible submarkets categorised by process area and process stage, the present merger is a merger between important, possibly even leading, suppliers, but that, both in the possible market for electrical metal plant building (level 0-2, iron/steel) and in all submarkets, a substantial number of at least four other credible suppliers, including SMS, are active.

- Market shares in the overall market and in process area or process stage submarkets

(349) Market shares are rather difficult to quantify objectively in this very varied and differentiated product or service area. The Commission has several estimates from Siemens, some produced for the purpose of the proceedings and others produced well before they started. The Commission also has estimates drawn up by VA Tech before the proceedings began as well as estimates drawn up during the proceedings at the Commission's request. Finally, estimates drawn up by SMS for the purposes of the proceedings were also submitted to the Commission. The estimates give quite a wide range of figures for market shares. Siemens' estimates (apart from a few process stage estimates in internal documents) generally assume combined market shares of less than [15-20]*%, whereas VAI's estimates are considerably higher, somewhere in the region of 40–50%. The highest figures, albeit not for the overall

¹⁹⁹ Reply to the request for information of 29 March 2005, Annex 1.b, sheet 13.

²⁰⁰ Reply to the request for information of 29 March 2005, Annex 1.c, sheet 10.

²⁰¹ Results of the market investigation, assessment of the questionnaires on phase II.

²⁰² Other competitors were mentioned, including Yokogawa, Honeywell and Metso Automation.

²⁰³ Other competitors were mentioned, including Reliance, Hitachi, Gefeba and ASI Robicon.

²⁰⁴ Results of the market investigation, assessment of the questionnaires on phase II.

market but only for 3 possible process stage markets (continuous casting, hot rolling and cold rolling), appear in SMS's (60 – approx. 70%).

(350) Although in the view of the Commission (and of some of the competitors mentioned)²⁰⁵ none of these estimates can be regarded as very reliable, they are examined briefly below. This is followed by a calculation of actual market shares produced by the Commission.

(ii) *Market share estimates from Siemens, VAI and SMS*

(351) In Siemens' view the parties' combined market share in the overall EEA market for *electrical metal plant building* in 2003 came to [5-10]*% (Siemens [2-5]*%, VA Tech [2-5]*%).²⁰⁶

(352) During the Commission's in-depth examination Siemens also estimated the combined market shares by process stage to be low. In the iron/steel sector VAI's worldwide market shares were put at [0-5]*% (2000-2004), while Siemens estimated its own market shares at predominantly less than [5-10]*%, with the exception, however, of hot rolling ([10-25]*%) and cold rolling ([5-15]*%). In this estimate, EEA market shares for VAI were the same or slightly higher and for Siemens even lower.²⁰⁷ With regard to the liquid phase, Siemens later submitted other estimates which gave Siemens' average market share for 2002-2004 in the EEA as [5-10]*% and VAI's as [10-15]*% or [10-15]*%.²⁰⁸ Siemens also submitted a market share calculation for the EEA carried out by an economic consulting firm, which reaches the conclusion in a scenario described as conservative that the parties' combined market share in an overall electrical market in the EEA comes to no more than [10-15]*%. The study suffers from certain shortcomings, however, and cannot therefore be regarded as providing a sufficiently reliable market share estimate.²⁰⁹

(353) [...] ²¹⁰ [...] ²¹¹

(354) In its business plan for 2002-04, VAI estimated its market position in electrical metal plant building overall at [10-15]*% and that of Siemens, which VAI considered to be the market leader, at [20-30]*%. In western Europe, Siemens' market share came according to these data to [30-40]*% and that of VAI to [15-20]*%. The relevant world market volume came in VAI's opinion to EUR [...] * million (i.e. much less than Siemens assumes).²¹² VAI saw itself in this estimate as more or less on a par with ABB. Other firms lagged well behind: Alstom: [10-15]*%, SMS Demag: [2-5]*%, Danieli: [2-5]*%.²¹³ A later market share estimate for the years 2001-03 submitted by VAI puts

²⁰⁵ See below VAI's qualification regarding the validity of its own market estimates.

²⁰⁶ GE and TMEIC have set up a joint venture in the electrical metal plant building sector and are therefore no longer to be regarded as independent competitors.

²⁰⁷ See Siemens' reply to the relevant Commission request for information of 2.3.2005, Annex 3.

²⁰⁸ [...] *.

²⁰⁹ [There follows a discussion of the aspects of the study which the Commission regards as "shortcomings" ...] *.

²¹⁰ Reply to the request for information of 29 March 2005, Annex 1.a, sheet 13.

²¹¹ Reply to the request for information of 29 March 2005, Annex 1.b (as at 12/2003), sheets 6 and 7. [...] * (reply to the request for information of 7 April 2005, Jour Fixe 29.1.2001, Annex)

²¹² [...] *.

²¹³ [...] *.

Siemens' worldwide market share at [20-30]*% and VAI's at [15-20]*%. The market shares of competitors (SMS Demag, Alstom, ABB, Danieli) ranged between [5-10]*% and [5-10]*%. The corresponding market shares for Europe in this estimate were: Siemens: [20-30]*%, VAI: [10-20]*%, Alstom, SMS, ABB: [5-10]*%.²¹⁴ A further market share estimate by VA Tech relating to iron- and steelmaking, including continuous casting, for the period 2001-03 for Europe gave VAI: [20-30]*%; Siemens: [20-30]*%; Alstom: [5-10]*%; SMS Demag: [10-15]*%; ABB: [5-10]*%.²¹⁵ VA Tech itself reduced the significance of its market share estimates, however, when it stressed that they represented only the subjective, limited view of a firm active mainly in the mechanical plant building sector whose market view did not encompass the whole market. The Commission shares this opinion.

(355) SMS provided the following estimate of EEA market shares for *electrical metal plant building as a whole*: Siemens: [30-40]*%, VAI: [10-15]*%, SMS: [5-10]*%.²¹⁶ SMS estimated the combined market shares of Siemens and VAI in the process stage submarkets studied somewhat higher still. When asked to substantiate these estimates, SMS submitted an assessment of the largest worldwide projects in the market during the last 4 years worth more than EUR 5 million on the assumption that market shares in the actual market behaved in the same way as in this, the largest project segment. This gave a combined Siemens/VA Tech market share of [60-70]*% for continuous casting ([5-10]*% + [50-70]*%), [70-80]*% ([60-70]*% + [5-10]*%) for hot rolling and [60-80]*% ([50-60]*% + [10-15]*%) for cold rolling.²¹⁷ For SMS itself, it resulted in market shares of [20-30]*% (continuous casting) and [5-10]*% each for hot rolling and cold rolling. For other process stages, SMS did not submit any substantiated estimate.²¹⁸ Siemens criticised SMS's estimates as being too high and argued that, even in SMS's view, the limitation to projects worth more than 5 million resulted in only 40-60% of the market being covered, which Siemens moreover doubted as the number of projects taken into account by SMS annually was far too small. This was due to the fact that, as a firm active mainly in the mechanical plant building sector, SMS necessarily had a limited view of the electrical metal plant building market. SMS had thus failed to include a substantial number of major projects in the basis for its assessment.²¹⁹ Siemens' criticism is justified above all with regard to the leaving out of account of projects in SMS's project lists. Inasmuch as SMS's market share in electrical metal plant building is far smaller than in mechanical metal plant building, this omission might, as Siemens maintains, quite rightly be put down to SMS's limited market view as a firm primarily active in the past in mechanical metal plant building. SMS's estimate is therefore to be regarded as no more than the subjective market view of an important market player.

(iii) *The Commission's market share calculation*

(356) In view of the above-mentioned weaknesses in all of the above market share estimates and calculations and in view of their considerable divergences, the Commission carried

²¹⁴ Reply to the request for information of 14.1.2005, question 18.

²¹⁵ Reply to the Commission's request for information of 18.1.2005, question 16.

²¹⁶ SMS, non-confidential version of 9.2.2005.

²¹⁷ SMS, reply to the request for information of 21.2.2005, made non-confidential on 21.4.2005.

²¹⁸ SMS's overall market estimate can therefore also be regarded as unsubstantiated.

²¹⁹ Siemens thus points out that the project list submitted by Siemens both for hot and for cold rolling contains more than 20 projects with an order value that is greater than the smallest project in the SMS list.

out an analysis of the strength of the major competitors in the main part of the markets referred to above, i.e. for orders worth more than EUR [0.5-3]* million, for the years 2002-2004. It asked competitors about all the orders they had won during the relevant period and aggregated the figures.²²⁰ The results of the inquiry therefore reflect only the relative size of the firms questioned, but, due regard being had to this fact, they constitute the best information available in the present case.

(357) At a late stage in the proceedings, in connection with the liquid phase Siemens provided information on other competitors which had won specific orders in the EEA during the period in question and which had not been included in the Commission's original calculation. The Commission checked the information and took it into account where it was confirmed by the customers and/or competitors concerned.

(358) In the Commission's view, this calculation represents a meaningful approximation of actual market shares. Admittedly, it ignores that area of the market which includes orders worth less than EUR 1 million. However, the importance of that area when it comes to establishing the actual market strength of firms in the overall market is reckoned to be relatively minor inasmuch as firms that are competitive only or chiefly in the area of small orders may be regarded by customers as being not fully competitive. A more important qualification is that account has to be taken of the possibility, not to say the probability, that suppliers not represented in the table may also have won orders in the area and period in question.²²¹ For this reason, the market shares indicated must be regarded as the upper limit and the actual market shares are very probably somewhat lower.²²²

Order value > 1 million '02-'04	<i>Total worldwide</i>	<i>Liquid phase worldwide</i>	<i>Liquid phase EEA</i>	<i>Hot phase worldwide</i>	<i>Cold phase worldwide</i>
Siemens	<25%	<20%	<15%	<25%	<30%
VAI	<20%	<30%	<30%	<20%	<15%
Parties	35-40%	40-45%	35-40%	35-40%	35-40%
SMS	<10%	<10%	<10%	<10%	<10%
Danieli	<15%	<20%	<5%	<15%	<10%
ABB	<20%	<10%	<5%	<20%	<20%
Alstom	<15%	<5%	<5%	<10%	<20%

²²⁰ In two cases, instead of the sum of the projects, annual turnover figures for projects worth more than EUR 1 million were used.

²²¹ Suppliers are involved who either were not mentioned in time to the Commission by Siemens as being competitors and so could not be contacted or who were unable to provide the required information in good time.

²²² It must also be taken into account here that in the case of one supplier, Danieli, it was not possible to clearly allocate certain order volumes to individual process stages or process areas, which in Danieli's case resulted in a certain amount of double counting and hence higher market shares. It is much more likely, however, that the volume increase due to the inclusion of disregarded competitors far exceeds any volume decrease due to a corresponding correction of Danieli's order volumes.

Ingelectric	<5%	<5%	<5%	<5%	<5%
TMEIC-GE	<15%	<5%	0%	<15%	<15%
Other EEA competitors for liquid phase ²²³	<5%	<20%	<50%	--	--

Order value > 1 million '02-'04, worldwide	Continuous casting	Hot rolling flat	Cold rolling flat	Strip plant
Siemens	<10%	<30%	<30%	<25%
VAI	<40%	<15%	<15%	<20%
Parties	40-45%	35-40%	35-40%	35-40%
SMS	<20%	<5%	<10%	<10%
Danieli	<35%	<10%	<10%	<15%
ABB	<5%	<25%	<20%	<15%
Alstom	<5%	<15%	<20%	<25%
Ingelectric	<5%	0%	0%	<10%
TMEIC-GE	<5%	<20%	<15%	<10%

(359) These tables show that, as a result of the merger, very probably (given the presumably larger market volume in real terms) no market shares will be more than [30-40]*%. This also applies to the possible worldwide market for the liquid phase, since it is unlikely that, worldwide, there would be higher market shares for Siemens and VAI than in the EEA and Siemens' view that also other competitors not shown in the tables are active worldwide is to this extent credible.²²⁴ In the possible worldwide market for continuous casting too, this should be assumed for the same reasons. In every process area and every process stage there will be at least four efficient suppliers left in the market, which may be expected to exert sufficiently strong competitive pressure on the merged undertaking. Basically, these competitors also include SMS. Not represented in the tables is the special area of long rolling, where, however, on account of Danieli's clear market leadership there are no concerns either.

²²³ These are those competitors with respect to whom Siemens on 29.5.2005 mentioned specific projects worth more than EUR 1 million in the liquid phase which the Commission was able to verify.

²²⁴ The somewhat higher market share in the possible worldwide market is explained by the fact that as regards other competitors for the liquid phase Siemens has concentrated on EEA projects because they are easier to check for the Commission and because of their greater relevance for competition purposes.

(360) It should be added that, with the exception of TMEIC-GE, the competitors represented in the table are European competitors, for which as suppliers of European customers there can be no special entry thresholds. In fact, the EEA market shares not shown in the tables also change in roughly the same order of magnitude as the world market shares shown.

(361) Even excluding the internal Japanese sales of TMEIC-GE, given the assumption of a world market without Japan,²²⁵ results in market shares that either do not increase the worldwide joint market share spreads of the parties contained in the above tables, which as mentioned should otherwise be interpreted as upper limits, or only exceed them very slightly by 1-2%. The conclusion that there would very probably be no market shares of more than [30-40]*% therefore applies as well to the assumption of a geographically reduced “accessible” world market. In each of the possible markets mentioned, TMEIC-GE, even on this premise, remains a substantial competitor, so that, from this standpoint too, there is no fundamental change in the competition analysis.

- Tendering analysis for the overall market (iron and steel, levels 0-2) and the process area and process stage submarkets

(362) The markets in question are of course tendering markets, where market shares only have an indicative function. The decisive factor is the strength of the competitive pressure which undertakings exert on each other as bidders, although long-term market shares act as an important indicator of that strength. As already emphasised in the analysis of mechanical metal plant building, after the bid submission and opening phases there is usually an intensive negotiating phase where it is possible for bidders to grant price discounts. It is also possible to adapt parts of the order qualitatively to customers’ wishes or, for customers, to change the scope of the order.

(363) The Commission has analysed the tendering data of some competitors in these markets. The analysis of Siemens’ tendering data revealed that, with regard to the overall market (iron and steel, levels 0-2) for electrical metal plant building, worldwide 3 other undertakings²²⁶ and EEA-wide 2 other suppliers in electrical metal plant building competed with Siemens more frequently than VAI. There was a similar result in terms of its trend with hot rolling, cold rolling and strip processing lines. Analysis of VAI’s tendering data confirmed, both for the overall market and for the process areas and stages mentioned, that Siemens is not VAI’s closest competitor in them.²²⁷

(364) In the case of continuous casting plants,²²⁸ VAI, according to the analysis of Siemens’ tendering data, was worldwide just behind another firm, and EEA-wide was in first place. However, analysis of VAI’s tendering data showed that Siemens’

²²⁵ The scenario which excludes an inaccessible part of the Chinese market has, however, no effect on the above calculation, since this part would be equally inaccessible for all the suppliers shown in the table.

²²⁶ This finding applies both to a world market which includes Japan and to one which excludes it. The inclusion/exclusion of a part of Chinese demand (which continues to be reserved for Chinese suppliers) has no effect on this finding.

²²⁷ This would probably be because the area of level 0 automation (electrics and drives) in the cold and hot rolling phase (and proportionately in the overall market as well) is the traditional domain of electrical engineering firms such as Siemens, ABB, and Alstom, while the “mechanical engineers” in this area have advanced only slowly, as they do not manufacture electrics and drives themselves.

²²⁸ The number of such bids was admittedly small.

significance as a competitor of VAI in continuous casting is relatively small, and that SMS and Danieli are the most important competitors for VAI in this process stage. Since it is clear from the analysis of market shares that VAI is the strongest competitor with the highest market share in continuous casting, greater importance should be attached to its tendering data. From this information it follows, therefore, that in the hot phase and cold phase process area markets too Siemens and VAI are not the closest competitors.

- (365) An exact analysis of the tendering data in the case of long-rolling plants is not necessary as Danieli is the leader in this submarket.
- (366) In the process area market for iron and steel plants (liquid phase), Siemens competed, according to its own tendering data, in the EEA and worldwide most frequently with VAI, and worldwide equally with ABB. An expert's report commissioned by Siemens shows that the difference between VAI and the second or equally placed firm, ABB, is not statistically significant and therefore both firms can rank as equally close competitors of Siemens. Analysis of VAI's tendering data showed however that, in the iron and steel production area, SMS was the clearest competitor of VAI, and Siemens only one of two other important competitors. Here too it should be noted that greater importance must be attached to the tendering data of VAI in view of that company's probably higher market share.
- (367) The tendering data show, therefore, that Siemens and VAI can at best be regarded as close competitors in individual possible submarkets (continuous casting, liquid phase). Even in these few submarkets, however, they are not each other's closest competitors.

- Effect of the Siemens shareholding on SMS

- (368) In the assessment of Siemens' competitive position in the market under consideration and its possible submarkets, it should also be borne in mind that, through its minority shareholding in SMS, Siemens has access to the strategic knowledge of this competitor. For the same reasons as discussed for the area of mechanical metal plant building (see paragraphs (326)-(333)), the competitive pressure on Siemens exerted by SMS could be weakened therefore.
- (369) Unlike in the field of mechanical metal plant building, however, such reduced competitive pressure in the relation between Siemens and SMS would not be created only by the merger but would affect competition even without the merger, because Siemens is already operating in the field of electrical metal plant building.²²⁹ Also, Siemens and VAI are not closest competitors in electrical metal plant building, unlike SMS and VAI in mechanical metal plant building.
- (370) In any event, the commitments concerning its shareholding and [...] shareholder's rights in SMS given by Siemens, which are necessary for removing the competition concerns in the field of mechanical metal plant building, provide the solution to Siemens/VA Tech's link to SMS from the competition angle for electrical metal plant building too. In electrical metal plant building too, therefore, it can be ruled out

²²⁹ Thus it is quite possible that the link hitherto to Siemens has delayed SMS's entry into electrical metal plant building. At any rate, according to the results of the market investigation, SMS is clearly behind VAI in electrical metal plant building and entered the sector significantly later.

that this shareholding and the [...] information rights associated with it will significantly impede competition as a result of the merger between Siemens and VA Tech. The de facto dissolution of the link between Siemens and SMS has the positive effect, moreover, of intensifying competition between Siemens and SMS.

- *Conclusions*

(371) An overall assessment of the information concerning the competitors, the structure of the market and, in particular, the bidding data, which also took account of Siemens' minority holding in the competitor SMS, reveals that the merger will not create a dominant position in the abovementioned market or markets of electrical metal plant building (level 0-2, iron/steel) or significantly impede effective competition in any other way.

(2) Possible markets for level-1 and level-2 automation

(372) The market investigation confirmed that competitors consider level-1 and level-2 software solutions relevant indicators of market strength.²³⁰

(373) [...] [VAI] [...] [sees] [...] [itself] in a technological leadership role in such possible automation markets.²³¹

(374) However, it is still true to say that enough viable competitors will remain even in these possible markets. SMS followed VAI in developing automation technology for metal plant building, somewhat late but with a clear strategy and rapid growth.²³² The third leading company in mechanical plant building is still Danieli, a company that has also greatly expanded its automation activities and is a major supplier of level-1 and level-2 automation technology. The Commission has information regarding the technological performance of and/or research being conducted by Alstom,²³³ ABB and TMEIC-GE.²³⁴ There are also a number of other suppliers also competing with the merger parties, particularly in level-1 markets, where the barriers to entry are lower than in level-2 markets, or which offer niche solutions.

(375) When conducting its market investigation the Commission asked the parties and competitors for their reference figures for various software modules of process models and technical control systems for three process stages (continuous casting, hot rolling and cold rolling). Nine firms replied, namely Toshiba-TMEIC-GE, Andritz, Danieli, SMS, Siemens, VAI, Ingelectric, ABB, and Mino. As solution bundles are used for each process stage and it is in part the customer who decides whether a particular individual solution is needed or not, figures regarding specific solutions are less relevant than those covering a solution bundle for a specific process stage. For this reason, the Commission aggregated the figures to 6-8 single

²³⁰ [...].*

²³¹ [...] VAI also sees itself as “the leading supplier of advanced automation solutions for the international iron and steel and aluminium industries” (VAI homepage, brochure) [...].*

²³² Turnover in electrics and automation (order entry planning) 2002:35 mn, 2003:60mn; 2004:74 mn; 2005: 93 mn; 2006:100mn. [...].*

²³³ [...] (Reply to request for information of 29 March 2005, Annex 1.1, sheet 12. [...].*

²³⁴ [...].*

modules for each process stage to produce an overall figure for the stage. As no figures were obtained from a number of relevant competitors, at least one of which is certainly a major supplier (Alstom), the percentages must be seen as *absolute upper limits*. *The actual market shares are sure to be lower.*

Level-1 and level-2 software modules; plant equipment, worldwide	Siemens	VAI	Siemens +VAI	Competitor 1	Competitor 2	Competitor 3
Continuous casting	5-10%	35-40%	45-50%	25-30%	15-20%	5-10%
Hot rolling	15-20%	25-30%	45-50%	25-30%	20-25%	5-10%
Cold rolling	30-35%	15-20%	45-50%	15-20%	15-20%	5-10%

(376) The figures in the table tally with the other findings of the market investigation, showing that while after the merger the parties would become the market leaders in the possible level-1 and level-2 automation markets for the process stages in question there would still be a sufficient number of technologically viable competitors in the market.

(377) This also applies to possible markets for automation solutions (levels 1 and 2) in the process stages not covered by the table, and therefore automatically in the overlying process areas, and finally in a possible total market for level-1 and level-2 automation solutions for the iron and steel industry. The market investigation findings show certain similarities between automation solutions for strip processing and cold rolling. This is also true of the competitive conditions, about which no specific concerns were expressed in the market investigation. With regard to automation solutions for iron and steel production, Siemens produced information pointing in the same direction and confirming the existence of a sufficient number of other competitors.²³⁵ The investigation suggested that automation solutions for the special field of long rolling were less useful. Moreover, Danieli is the market leader in this field, which is why there are generally no competition concerns in this specific area.

(378) Comments from customers to the effect that the merger would have the greatest impact on the automation field, and level 2 in particular, but that there would still be a sufficient number of competitors at the same technological level, confirm these findings. No key technologies could be identified that would enable the merger parties to prevent competitors from being successful in the market.

(379) As regards the impact of Siemens' holding in SMS, what was said in relation to electrical metal plant building (levels 0-2; iron/steel) applies (see paragraphs (368)-(370) above).

²³⁵ [...] * statements were corroborated by other market participants.

(380) For these reasons in none of the possible level-1 and level-2 automation markets in iron and steel plant building is a dominant market position created or effective competition restricted appreciably in any other way.

(3) *Electrical plant building for aluminium hot and cold rolling*

(381) Siemens does not believe that there is a relevant separate market for electrical plant building for aluminium hot and cold rolling, and the product market definition left this question open. The Commission's market investigation showed clearly that, in comparison to steel rolling, these possible markets would be very small (in all likelihood accounting for less than 10% of the turnover of electrical steel rolling mill building). This alone means that the existence of combined markets for rolled steel and aluminium could not significantly influence the completed analysis of rolled steel markets. As will be shown, this follows as there are no competition problems on possible aluminium markets. The same argument applies to any possible total market for electrical plant building that would include aluminium rolling mills.

(382) [*There follow comments on Siemens' internal assessment of the field of aluminium rolling*]*. However, the Commission's market investigation revealed that a number of competitors and customers viewed Siemens as the strongest supplier of electrical plant building for both aluminium hot rolling and aluminium cold rolling.²³⁶

(383) VAI says that ABB and TMEIC are significant suppliers of aluminium hot rolling plants.²³⁷ It adds that there are also other, smaller suppliers (Alstom, ASI Robicon, IAS).

(384) VAI is of the view that ABB and Alstom are significant suppliers of aluminium cold rolling plants. For new plant, the mechanical suppliers (Achenbach, Fata Hunter, SMS) apparently used their own automation systems. Although a smaller supplier, IAS is becoming more active in the market. In terms of technical control systems for aluminium foil rolling mills VAI sees itself as the market leader but considers that there a number of serious competitors, most notably ABB.

(385) According to VAI, the building of aluminium hot rolling mills is quite a small market.²³⁸ [...] ²³⁹ In its public statements VAI sees itself as the world leader in the modernisation and automation of aluminium rolling mills.²⁴⁰

(386) The majority of customers do not think that the merger will cause any problems in the area of electrical plant building of aluminium hot and cold rolling mills. While both parties are often named as leading suppliers, a number of other companies have won tenders.

²³⁶ Results of the market survey, assessment of the phase II questionnaires.

²³⁷ VAT Tech's reply to the Commission's request for information of 29 March 2005 (received on 6 April 2005).

²³⁸ Other statements regarding sales in this field confirmed that in comparison to the steel rolling mills markets electric aluminium rolling mills markets are relatively small.

²³⁹ VAI Tech's reply to the Commission's request for information of 29 March 2005 (received on 6 April 2005).

²⁴⁰ "VAI is the world leader in the Modernisation and *Automation* of Aluminium Rolling Mills", VAI refers to special control systems; 28 hot rolling plants; 58 cold rolling plants; 72 foil rolling plants in 10 years (homepage, brochures).

- (387) Even if there are barriers to entry in the area of aluminium, these are, however, considerably smaller for two groups of suppliers, namely, on the one hand, specialist or non-specialist suppliers of mechanical aluminium plants, such as Fata Hunter, Achenbach, Mino (as smaller suppliers, it could, however, be easier for these companies to tender for smaller plants) and SMS, which is also able to undertake larger projects; and, on the other hand, companies that are already supplying level-1 and level-2 automation to the steel industry (above all for hot and cold rolling).
- (388) There are no competition concerns with regard to aluminium cold rolling and foil rolling mills, as there are enough competitors in this market, and plants are often smaller.
- (389) In the case of aluminium hot rolling mills the thresholds to entry are higher and are mainly in the area of technological control systems and process models (i.e. possible level-1 and level-2 submarkets). Smaller suppliers seem to have problems overcoming these technological and size-related barriers, although they are named by some potential customs as possible alternatives. However, they can meet the requirements for supplies in the field of aluminium hot rolling with support from the highly concentrated demand side, which most definitely has some buyer power.
- (390) The main source of competition to the merger parties are the major electrical suppliers in the steel sector, such as TMEIC, ABB and Alstom. All these suppliers have experience in aluminium. As yet not all necessarily have sophisticated special level-2 process models. In the case of TMEIC it should also be borne in mind that the company has rarely tendered successfully in Europe. Moreover, however, there are a number of companies that have been named as possible market entrants and have been found to be plausible or appear to have already set about entering the market. The companies in question are SMS, Achenbach and IAS. As IAS and Achenbach are relatively small companies, of the three SMS seems to have the best chance. With active support from a major customer SMS is likely to be in a position to enter the market successfully within a relatively short time.
- (391) As regards the impact of Siemens' holding in SMS, what was said in relation to electrical metal plant building (levels 0-2; iron/steel) applies (see paragraphs (368)-(370) above).
- (392) For these reasons in neither of the aluminium plant building markets affected will the proposed merger create or strengthen a dominant market position or significantly impede effective competition in any other way.

(4) IT solutions for plant logistics/MES/Level 3

- (393) In this relatively young and highly dynamic sector the proposed merger does not give rise to any competition concerns. It should be remembered that the sector is relatively small, accounting for no more than [5-10]*% of the total market volume for electrical metal plant building,²⁴¹ and that therefore the inclusion or exclusion of this sector cannot make much difference to any assessment of the total market for electrical metal plant building. It follows, however, that there are no competition concerns in a total market for electrical metal plant building only in the light of the

²⁴¹ [...]*

fact that there are no competition concerns in the possible segment (or possible separate market) for IT solutions for plant logistics /MES/Level 3.

(394) While both Siemens and VA Tech offer solutions on this possible product market, they are at a relatively early phase of development. When surveyed by the Commission, market participants expressed no concerns whatsoever regarding such a market. There are currently few obstacles to entry into this market and, given the predicted growth of the market, there are clear incentives for competitors to invest. There are enough current and potential competitors, as the merger parties' competitors are also working on such solutions in other markets for electrical metal plant building and moreover the market is also accessible to companies offering general control technology and logistics solutions.

(395) For these reasons the proposed merger will not significantly impede effective competition in a possible market for IT solutions, in particular as a result of the creation or strengthening of a dominant position.

(5) Conclusion regarding a possible total market for electrical metal plant building including all the abovementioned sub-markets

(396) As no competition concerns could be detected in any of the possible sub-markets of an overall market for electrical metal plant building, the same necessarily holds true for a possible overall market, and in such a market the merger would neither create nor strengthen a dominant position or significantly impede effective competition in any other way.

(6) Additional assessment of possible non-horizontal effects

(397) The proposed merger will lead to the integration of supplies of electrical plant building (Siemens, VAI) and mechanical plant building (VAI). An assessment must therefore be made as to whether this will have the effect of restricting competition in the electrical metal plant building sector.

(398) The answer must be negative. Even if VAI has until now acted as a principal for other companies in the electrical metal plant building sector (e.g. in connection with drive solutions or level-0 electricity generation), it does not follow that VAI's subcontractors, as independent suppliers, will leave the market for electrical plant building because subcontracts are switched to Siemens. There will continue to be a large number of separate calls for and awards of tenders for electrical and mechanical plant building and orders concerning only the electrics of a plant. An electrical plant builder with no links with any mechanical plant builder is fully competitive in this field. Secondly, the loosening and certain ending of the ties between Siemens and SMS increase the likelihood that SMS will try to obtain supplies from electrical subcontractors other than Siemens. Thirdly, other primarily mechanical suppliers (such as Danieli, MHI, Achenbach and Andritz) will continue to be potential customers in the market. Fourthly, other competitors could attempt to become general contractors for both mechanical and electrical orders, as Siemens has done with initial success.

(399) The merger cannot create a market lock-in or any other foreclosure effects in electrical metal plant building or between electrical metal plant building and markets upstream or downstream. Firstly, it should be pointed out that a clear majority of

customers for electrical industrial plant building stressed that they do not automatically award modernisation or extension contracts to the original suppliers of the electrics. This shows that manufacturers cannot currently tie the sale of one product to the sale of another (extension or modernisation) product to any great extent. As the merger does not create a dominant position in a possible electrical metal plant building market or any upstream or downstream market, the merger cannot have these consequences. Should suppliers, such as the parties, actually pursue such a strategy and should the situation be to the disadvantage of customers, they could react by covering their requirements from another supplier.²⁴²

(400) For these reasons even hypothetical non-horizontal effects of the proposed merger will neither create nor strengthen a dominant market position in any market for electrical metal plant building, or significantly impede effective competition in any other way.

(c) Maintenance and service of metal plants

(401) In this market too Siemens' and VA Tech's activities overlap. The Commission's market investigation, however, found no evidence that there would be competition concerns in the market for the maintenance and service of metal plants. The barriers to entry in this market are significantly lower than in the electrical and mechanical plant building markets. There are enough local competitors for the maintenance and servicing of metal plants. In some cases, customers of the metal plant-building sector are also able to carry out this work themselves.

(402) For these reasons the proposed merger will neither create nor strengthen a dominant market position in this market, or significantly impede effective competition in any other way.

(d) Electrical industrial plant building in other sectors

(403) In other (non-metal) areas of electrical plant building VA Tech is not active (mainly) through its subsidiary VAI, as is the case with metal plant building, but solely through its subsidiary, Elin EBG. Electrical plants are produced above all for the vehicle industry, for oil/gas, chemicals, pharmaceuticals, paper, cement, quarrying and food, beverages and tobacco.

(404) Siemens operates mainly in the oil/gas, chemicals, pharmaceuticals, paper, cement, quarrying and food, beverages and tobacco sectors.

(405) There are no competition concerns regarding the planned merger in connection with any possible product market definition (i.e. in relation to a market covering several sectors or taking each sector as a separate market).

(406) According to Siemens, geographically speaking, the only significant overlaps with combined shares that could technically denote an affected market are in Austria, where Elin EBG focuses much of its activities.

(407) Customers in Austria consulted by the Commission raised no concerns regarding competition. The general view was that the disappearance of VA Tech as a supplier

²⁴² This would make the strategy economically questionable from the supplier's point of view.

would reduce the number of competitors but there would still be enough competitors in the market or industrial companies that were potential customers could enable other suppliers to enter the Austrian market.²⁴³

(408) If the geographical confines of the markets are extended beyond Austria (for specialist sectors, for example) the merger will have only a slight impact. No competition concerns were raised in this connection that are relevant to this assessment.

(409) For these reasons the merger will not significantly impede effective competition in any market for (other) industrial plant construction, in particular as a result of the creation or strengthening of a dominant position.

(e) Summary regarding the electrical metal plant building markets and the market(s) for electrical industrial plants in non-metal sectors

(410) For these reasons the proposed merger will neither create nor strengthen a dominant market position in any of the markets for electrical plant building or the market(s) for electrical industrial plants in non-metal sectors or significantly impede effective competition in any other way.

F. LOW-VOLTAGE SWITCHBOARDS

1. Relevant product markets

(411) Siemens and VA Tech both produce low-voltage (LV) switchboards. While Siemens manufactures the components for the switchboards itself, VA Tech purchases them from other companies, including Siemens, and incorporates them in its LV switchboards. LV switchboards are used to feed in and distribute energy to connected electricity users and to protect and support them. The main components of LV switchboards are circuit breakers and switch disconnectors, programmable logic controllers and contactors. In the Schneider/Legrand Decision the product market for circuit breakers and switch disconnectors was subdivided into the three categories of ACB, MCB and MCCB LV circuit breakers.

(412) Market participants held the view that there were three separate product markets for LV switchboards, depending on which of these circuit breakers and switch disconnectors were incorporated in the switchboard. This were held to the main LV switchboard, which contains an air circuit breaker (ACB), the intermediary distribution panel, which contains a moulded case circuit breaker (MCCB), and the final distribution panel, which contains a miniature circuit breaker (MCB). The question of whether these three LV switchboards constitute separate markets can however be left open, as the competition assessment is unaffected by any assumption of separate product markets.

²⁴³ Particular reference should be made to the discussion of the technical general contractor for building engineering (non-industrial plant engineering and construction) in this Decision. The competitive conditions in the industrial plant building sector in Austria are similar to those set out there, with the added factor that ABB is another competitor in the industrial plant building and engineering sector in Austria.

- (413) One competitor took the view that, in addition to the three submarkets based on the circuit breakers, there is also a separate market for busways. Like heavy-duty cables, busways transport and distribute electricity to the final consumer in buildings and factories from medium voltage switchgear via LV switchgear. In a decision in 2004 the Federal Cartel Office held that busways were part of the single market for busways and heavy-duty cabling (cables including cable tray systems).²⁴⁴ There is no need for any decision here as to whether this is the case here, as the competition assessment remains unchanged even if it is assumed that there is a separate market for busways.
- (414) Other components built into LV-switchboards are programmable controllers („PLC”) and load feeders.
- (i) PLC are used to control the other components of a switchboard. PLC are electronic control devices, where the control sequences are determined by a programming language. Siemens is of the opinion that PLC should not be subdivided according to end-use. The only sector for which the market investigation of the Commission has pointed towards a possible sector specific application is the use of PLC in automation solutions for metallurgical plants. However, for the purpose of this decision it is not necessary to decide whether these applications, also referred to as application platforms, constitute a separate product market.
 - (ii) load feeders are used to protect and switch electrical consumers (e.g. motors) and consist of protection components (protection switches for motors, overload relays) and a switching device. It is not necessary to further segment the market, since all suppliers normally offer the entire range and customers typically order a complete package from suppliers.

2. Geographic markets

- (415) According to Siemens the market for LV switchboards has traditionally been determined by national factors. Today, both for individual components and LV switchboards competition is EEA-wide. Siemens points out that at component level there are no technical or legal trade barriers, and that transport costs are low. In relation to components for electrical installation, however, Siemens notes that in its decision in Schneider/Legrand the Commission concluded that such components were traded at national level and the market(s) for them were to be defined in national terms.²⁴⁵
- (416) LV switchboards are often produced to customer specifications. For this reason many customers emphasised the importance of national competition factors, especially the importance of and need for proximity to the customer as a prerequisite for responding quickly to customers’ special requirements. Many of those consulted viewed strong, technically competent national branches as a minimum requirement for success in the market, frequently going as far as to argue that national production plants were necessary. As Siemens’ takeover of VA Tech is unlikely to create

²⁴⁴ Federal Cartel Office decision in Siemens/Moeller, Ref.: Z. B-7, 36-04, <http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion04/B7-36-04.pdf>, paragraph 11.

²⁴⁵ COMP/M.2283 - Schneider/Legrand.

significant impediments to effective competition even if the markets are defined nationally, the question of the relevant geographic market for components and ready-assembled switchboards can be left open.

3. Competition assessment

- (417) If the market is taken to be the EEA, there would be no affected market for LV switchboards according to Siemens, since Siemens and VA Tech together have a market share of only [2-5]*%. If the markets were to be defined nationally, Austria would be a horizontally affected market. According to Siemens' figures, their joint market share in 2003 was [20-30]*% (Siemens [5-10]*%, VA Tech [10-15]*%), where the market volume was €[50-60]* million.
- (418) The market investigation has however revealed that, given a similar total volume of €[50-60]* million, their market share is actually higher. It showed that Siemens and VA Tech together accounted for [...] (Siemens [2-5]*%, VA Tech [...]*). Their chief competitors are Mehler with [30-40]*% and Moeller with [20-30]*%. Schneider Electric and Sprecher Automation are also competitors.
- (419) If one assumes separate markets for LV switchboards, which operate as main distribution, sub-distribution and final distribution boards, there are overlaps only in the case of main distribution boards, not with sub-distribution or final distribution boards. In the case of main distribution switchboards (ACB) Siemens and VA Tech together would have a market share of [...] (Siemens [10-15]*%, VA Tech [...]*). Mehler would remain market leader with a share of [40-50]*%, ahead of Moeller, which has a share of [20-30]*%.
- (420) Siemens produces and supplies all major components needed for fitting and assembling LV switchboards. In addition to the ACB, MCCB and MCB circuit breakers, this includes busways. VA Tech buys all its components from a number of suppliers. As Siemens and VA Tech together have over 25% of the Austrian market for the downstream market in LV switchgear, the market is vertically affected. The market investigation revealed, however, that in 2003 Siemens did not have a market share of more than 15%-20% for any of the circuit breakers or disconnecter switches in the EEA or in Austria. In Austria the clear market leader for ACBs and MCCBs is Schneider Electric, while Moeller is the leader in the market for MCBs. There is therefore little danger of market foreclosure, especially as such a strategy could result in suppliers from neighbouring countries such as Germany or the Czech Republic expanding their presence in the region into Austria.
- (421) Siemens has been supplying busways on a large scale only since 2004, when the company took over the busways business from Moeller.²⁴⁶ On the overall market for busways and heavy-duty cable claimed by Siemens, the company would have a market share of less than [5-10]*% in Austria. According to the market investigation, on a separate market for busways Siemens had a market share of [20-30]*% in 2003, followed by Schneider Electric with 20-25% and smaller suppliers such as EAE Elektrik and Pogliano. In view of these market shares, the existence of credible competitors and the fact that suppliers from neighbouring countries could

²⁴⁶ Federal Cartel Office decision in Siemens/Moeller, Ref.: Z. B-7, 36-04, <http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion04/B7-36-04.pdf>.

enter the Austrian market if prices were to rise suggest that market foreclosure is again unlikely.

- (422) With regard to PLC in the automation of metallurgical plants (automation platforms) there is an overlap, since both Siemens and VA Tech are suppliers, although VAI does not produce the hardware itself and developed the software for the automation platforms in cooperation with third parties. It is, however, not necessary to decide, whether there could be a separate horizontally or vertically affected market, since there are in any event sufficient alternatives to the products of the two suppliers²⁴⁷. All major suppliers of automation solutions for metallurgical plants offer comparable products: SMS Demag (X-Pact), Alstom (Alspa, previously Logidyn), ABB (Industrial IT), TMEIC (Toshiba V- Series), Ingelectric (Sisteam OCS), Rockwell Automation (Automax), Danieli (HiPac).
- (423) In all other applications of PLC there are no horizontal overlaps. Concerning vertically affected areas such as LV-switchgear or control gear of energy generation, transmission and distribution, there will be no market foreclosure effects either, since competitors of the parties, which do not have their own PLC, have sufficient alternatives such as Schneider Electric, Rockwell, Omron, Mitsubishi, B&R, Beckhoff, Moeller or ABB.
- (424) For the same reasons, i.e. no horizontal overlap, sufficient number of credible competitors, this is also true for load feeders. Important competitors are Schneider Electric, Moeller, ABB, Rockwell, GE and Lovato.
- (425) To sum up, it is unlikely that after taking over VA Tech Siemens would be in a position to significantly impede effective competition in the Austrian market, or any other national or EEA-wide market, for LV switchboards and the requisite components.

G. BUILDING SERVICES ENGINEERING AND FACILITY MANAGEMENT

G1. BUILDING SERVICES ENGINEERING

1. Relevant product markets

- (426) Siemens and VA Tech are active in the field of building services engineering, which in Siemens's view must be segmented into three levels: the component level, the system level and the installation level. Siemens states that, although there are markets for facility management (see G.2), other services should be allocated to the respective primary market.²⁴⁸ The component and system levels should be divided according to area of application. At the component level, a distinction should be made above all between the areas of electrical installation technology, safety technology, control and instrumentation technology and HVAC (heating, ventilating and air-conditioning), and at the system level between safety technology and control and instrumentation technology. Lastly, at the installation level, a distinction must be drawn between electrical and mechanical contracting.

²⁴⁷ Siemens: Simatic S7 and Simatic TDC; VA Tech: Vantage. [...]*

²⁴⁸ The market survey found no evidence to the contrary.

(a) Component level

(427) At component level the activities of Siemens and VA Tech do not overlap, as VA Tech is not active in this segment.²⁴⁹ There are, however, component markets that may be vertically affected. At component level Siemens distinguishes between three affected segments: components for technical management, safety technology components and components for electrical installation technology.

(1) Building management technology

(428) Building management technology involves the measuring, controlling, regulating and using of heating, ventilating, air-conditioning and other technical equipment (but not the controlled heating, ventilating and air-conditioning systems themselves, which are part of the HVAC system, a field in which neither of the parties are active). Based on the findings of its market investigation, the Commission shares Siemens' view that there is at least a separate market for building management technology components. The question of a further subdivision of building management technology components can remain open for the purposes of this Decision.

(2) Safety technology

(429) With regard to the market for safety technology components proposed by Siemens, the Commission's market investigation suggests a distinction ought to be made at least between the areas of fire protection and access control/intruder detection. The question of a further subdivision can remain open for the purposes of this Decision.

(3) Electrical installation technology

(430) With regard to electrical installation components, Siemens distinguishes between low-voltage switchboards and all other low-voltage products, such as switches, outlets, bus systems and cables. With the exception of bus system components, which the Commission's market investigation suggested constituted a separate market, the question of the market definition of the other electrical low-voltage products can remain open for the purposes of this Decision.

(b) System level

(431) At system level, there are overlaps in the control and instrumentation and safety technology segments, and in the case of safety technology a distinction ought to be made at least between the areas of fire protection and access control/intruder detection.²⁵⁰ At system level, system integrators assemble electrical operating systems from the abovementioned components tailored to meet the needs of the specific user.

²⁴⁹ As regards components in the special field of low-voltage switchboards see section F above.

²⁵⁰ Even if there may be requests for both fire protection and access control/intruder detection, orders are usually placed separately. Moreover, the areas have different legal bases, with fire protection in particular being subject to special public regulations and standards. The vast majority of market participants therefore saw the two areas as separate product markets.

(432) Although there may be further subdivisions at system level, it is sufficient for the purposes of this Decision to distinguish between relevant product markets for fire protection systems, access control/intruder detection systems and control and instrumentation systems.

(c) Installation level

(433) In Siemens' view the installation level covers in particular universal electrical contracting by a contractor. The complete electrical installation covers the design and installation of the energy supply infrastructure. The maintenance of general electrical equipment is also covered.²⁵¹ As the individual systems for the building safety and control and instrumentation technology (also known as "works") are regularly put out to tender with the electrical installation as an overall package and awarded as such, suppliers of electrical installation technology usually build the entire electrical system. It is their job to integrate the individual systems in the overall system, connect them to the energy supply and take full responsibility for the electrical system. The individual systems are either produced by the builders themselves or purchased from subcontractors. The single products used in the electrical installation are also regularly bought in. In Siemens' view, it is often impossible to make a clear distinction between installation level and system level.

(434) Siemens views installation in the non-electric area of HVAC (the electrical control of which comes under the separate building management technology, as shown above) as a separate market in mechanical contracting. This market encompasses the complete value chain, consisting of design, engineering, assembly, installation, commissioning, project management and the maintenance of heating, ventilating and air-conditioning systems and sanitary installations.

(435) Both Siemens (through the joint venture Siemens-Bacon) and VA Tech are involved in electrical and mechanical plant building in Austria. VA Tech sees the focus of its operations in the area of building services engineering as being an EPC contractor (EPC = engineering, procurement and contracting), responsible for integrating the various systems (the works). VA Tech includes HVAC in this field of operations. The market investigation showed that there may be a separate, overlapping market for the construction of electrical and mechanical building installations by a technical general contractor (TGC) bearing overall responsibility.²⁵² TGCs offer comprehensive technical installation of buildings from one source. While TGCs are responsible for all planning, coordination and installation of building services engineering, they often do not carry out parts of the installation themselves, using subcontractors instead. Tenders for TGCs are issued in particular in connection with major projects.

(436) For the purposes of this Decision it can be left open whether there are separate markets for electrical and mechanical installation in the buildings segment, as Siemens claims, or whether there is a separate market for TGC services that covers both electrical and mechanical installation.

²⁵¹ Where they cannot be allocated to facility management, which Siemens views as a separate product market; for further details, see G.2.

²⁵² The parties' activities in this area relate as a rule to non-industrial building installations (residential and office buildings and such structures as concert halls, museums, hospitals and tunnels).

(437) In any case, it should be noted that neither Siemens nor VA Tech take the view that the market(s) include the civil-engineering planning and execution of buildings, an area in which the parties are not active. This was confirmed by the Commission's market investigation.

2. Relevant geographic markets

(438) In Siemens' view, all the markets referred to above in part G1 (with the exception of the market for installation technology components) are at least EEA-wide.

(439) At component level, Siemens points out that in general there are no technical or legal trade barriers and only occasional variations on European standards particularly the standards and norms prepared by the European Committee for Electrotechnical Standardization (CENELEC). With regard to electrical installation technology components Siemens points out, however, that in its Schneider/Legrand decision the Commission concluded that the components were traded on national markets and the market(s) for such components was (were) to be defined in national terms.²⁵³

(440) At system level, Siemens argues that standardisation at product level makes it easier to offer systems throughout the EEA. In many areas no national permits were needed, and where they were needed differing requirements were only minor obstacles. Customers bought EEA-wide and suppliers were active at European level at least. Custom-built systems could be used anywhere in the world and there were no regulatory trade barriers.

(441) At installation level Siemens assumes that the market is at least EEA-wide, as there is a bidding market with the major suppliers of electrical installation operating EEA-wide and tenders are also regularly issued at European level. Transport costs are low on the market for electrical contracting. In the case of mechanical contracting the only differences are climate-related, with emphasis either on heating or air conditioning. In Siemens' view this does not justify making regional distinctions.

(442) In the Commission's view, it cannot be excluded that there are national markets at all three levels. Contrary to the view adopted by Siemens, they are in fact likely to exist.

(443) At component level there are significant national differences with regard to market shares and it must be borne in mind that the process of regulating and standardising at European level is by no means complete. This can also be seen from an announcement by Siemens that notes, when writing about [...]*'s work, that the work on harmonisation in preparation for the Construction Products Directive is being "continued and stepped up with the [...]* working groups." There still seem to be clear national differences with regard to consumption patterns. Similarly, products seem to be distributed at national level. This is the case notwithstanding the fact that many components are manufactured at supranational level.

(444) At system level, the Commission's market investigation produced the following results. On the one hand the market participants questioned (competitors and customers) said that in many cases systems manufacturers and suppliers operated

²⁵³ COMP/M.2283 – Schneider/Legrand.

transnationally, EEA-wide or even further afield. However, they also pointed out that the systems were often actually assembled at national level and were subject to national regulations, particularly in the case of fire protection. In addition to the international operators, there are also smaller national suppliers who have a major influence on competition at system level. Demand from consumers was also primarily at national level, with customers attaching great importance to the proximity of the service providers. A large number of the customers and competitors asked considered supply and demand to be nationally structured in the (at least) two product markets for safety technology systems and the product market for building management technology systems.

- (445) Lastly, at installation level, it is true that the cost of transporting the equipment is relatively low. However, this certainly does not apply to the labour force, a particularly important factor with regard to installation, and mobility across large areas would increase costs considerably. Siemens' and VA Tech's conduct on the market itself indicates that the markets are national at installation level. [...]*
- (446) However, the market investigation also produced evidence that bidders from other EU Member States were increasing tendering for major building projects in Austria, particularly for TGC contracts, and a number of such contracts had already be performed. The question of whether the market definition for TGCs can be broader than a national market can remain open for the purposes of this Decision, as, even if the market were defined as national, the merger does not significantly impede competition in the EEA or in a substantial part of it.

3. Competition assessment

- (447) At the component level, it is only in a vertical respect that there can be any relevant markets inasmuch as VA Tech is not itself active in these markets and buys products in. Siemens states that it has a market share of over 25% only for building management technology components, in Belgium, Finland, Luxemburg, the Czech Republic, Sweden and Slovakia. However, in these national markets there are no horizontally affected system or installation markets. Siemens estimates its market share in Austria at [20-30]*%, but a number of market participants questioned by the Commission in the course of its market investigation thought it could be larger.
- (448) In Siemens' view there are no vertically affected markets for components for building safety technology (fire protection or access control/intruder detection), where it has a total market share of [5-10]*% in Austria and no more than [5-10]*% in any other Member State.
- (449) Siemens also maintains there are no affected markets for installation technology components. On an overall market for installation technology components,²⁵⁵ which – as stated above – the Commission does not accept, only in Latvia would Siemens have a market share of just over [15-20]*%. In Austria the market share would be only [5-10]*%.

²⁵⁴ In Austria Siemens operates in the installation area primarily through a joint venture (with Ortner AG) under the name of Siemens Bacon.

²⁵⁵ For components in the special area of low-voltage switchboards see section F above.

- (450) During the Commission's market investigation, however, one competitor raised concerns primarily regarding Siemens' strengthened position in various markets for components for installation and building management technology in Austria. This competitor feared that VA Tech's demand that was not linked to any manufacturer would be switched to Siemens, which would enable Siemens to achieve or bolster a dominant position on components markets. In particular, fears were expressed regarding Siemens' large market shares in component markets for a number of disconnectors and in the market for busbar systems. It should also be noted that Siemens states it has a relatively large market share of a possible Austrian market for contactors (2003: [30-40]*%) and a possible market for programmable logic controllers (2003: [30-40]*%), which Siemens also sees as vertically affected markets.
- (451) The market investigation provided insufficient evidence that the merger would put Siemens in a position to foreclose the said component markets in Austria to its competitors. As shown below, there is sufficient competition in the markets for downstream systems and installations. At the immediate downstream systems level, the addition of market shares due to the merger would, moreover, be very small. In the said component markets themselves, Siemens faces competition from large, internationally established companies (in the case of installation technology components, among others ABB and Möller, and in the case of building management technology components, Honeywell, Johnson Controls and Sauter).
- (452) According to Siemens, at system level the fire protection systems market would be horizontally affected in Austria, where it has a market share of [30-40]*%, and this might also be the case in some other Member States (however, only on the hypothetical basis of the highest assumption of VA Tech's sales). According to Siemens' figures, at national level the market for intruder detection and other security systems (above all access control) would be horizontally affected only in Austria ([15-25]*%; Siemens: [15-20]*%, VA Tech: [2-5]*%).
- (453) In the case of management systems/building management works Siemens believes the market in Austria is horizontally affected, as the combined market share in 2003 was [20-30]*% (Siemens: [20-30]*%, VA Tech: [2-5]*%), and some markets could be affected in other Member States.
- (454) According to the company itself, VA Tech is not at all active at the systems level. VA Tech attributes all of its turnover in this area to contracting. VA Tech's figures and Siemens' market assessment also show that the horizontal impact of the merger in the area of individual works outside Austria are marginal, and within Austria there are no relevant markets with a market share addition of more than [5-10]*%.
- (455) The Commission's market investigation revealed only occasional and minor concerns regarding the possible impact of the merger at system integration level in the area of individual works in Austria. This is particularly true in the case of fire protection and other security systems (intruder detection, access control). The market participants stressed that there were a sufficient number of alternative systems providers and integrators. Mention was made of companies including Tyco, Schrack-Seconet, Fiegl und Spielberger, Minimax and Labor Strauss (fire protection systems), PKE, ARS, Group 4 Securicor, EVVA, Tyco, Bosch or Securitas/Schrack (intruder detection and other security systems), as well as Johnson, Honeywell and Sauter whom Siemens estimated to each have market shares of [15-20]*% in 2003

(building management systems). There are also value added partners (VAPs), which according to Siemens are medium-size systems producers and electrical contractors with engineering and IT expertise that offer systems-level integration using bought-in components and are increasingly offering ancillary services.

(456) The merger will not create any significant vertical impediment to competition, as there is genuine competition upstream at component level and downstream at installation level (as is shown below) and Siemens is unlikely to be able to foreclose the market to competitors.

(457) At installation level, there are significant overlaps between VA Tech and Siemens only in Austria.²⁵⁶ Siemens puts its share of the market for electrical building installation in Austria at [2-5]*% and VA Tech's at [5-10]*%, while their combined share of the market for mechanical building installation is put at [2-5]*%. Therefore, according to Siemens' figures, neither of the markets for electrical and mechanical contracting is affected. The market investigation confirmed this claim in the case of mechanical contracting. There are, however, doubts as to whether, contrary to Siemens' estimation, Siemens und VA Tech together may not have over 15% of the market for electrical contracting. Most pronounced is the direct competitive position and the respective market strengths of Siemens and VA Tech in the possible submarket for technical general contractors, where there are fewer medium-sized and small companies active than in the area of general electrical and mechanical contracting. A number of market participants in Austria believe that the combined market share is well over 15%, although in some cases estimates vary considerably and do not produce a clear picture. There is general agreement that Siemens und VA Tech would have the strongest market position regarding TGC contracts in Austria. These contracts are often awarded by tendering procedures. Some of the customers consulted pointed out that the merger would reduce the number of suppliers in Austria. However, only a few said that where they awarded TGC contracts to VA Tech or Siemens the respective other company was otherwise the most promising competitor.

(458) VA Tech's and Siemens' key competitors for TGC contracts in Austria are the international operators RWE Solutions and MCE. In recent years MCE has taken over activities such as non-industrial building services engineering from ABB Österreich. Other major international suppliers of TGC services, such as the Dutch Imtech group (through its German subsidiary) and M+W Zander (Germany) perform TGC contracts in Austria. The market investigation also showed that medium-sized electrical contractors such as, for example, Klenk & Meder, Landsteiner and Bostelmann operate in the market through consortia with HVAC companies. Through the acquisition of suppliers of mechanical contracting, both Klenk & Meder and Bostelmann have recently acquired their own internal HVAC capacity, which puts them in the position to take on TGC contracts alone. There are also some smaller Austrian companies operating as technical general contractors (e.g. Elmont).

²⁵⁶ This is based on the assumption that Siemens is not active in the controlling function in the Czech Republic. This means that the company Eltodo, in which, according to market participants, Siemens has a 49% holding and which appears to be active in the area of electrical contracting, is not controlled by Siemens.

- (459) The mere presence of several major international operators shows that even in the case of major building projects that would make particular demands on the financial resources of TGCs, it cannot be assumed that after the merger Siemens' and VA Tech's operational scope would extend beyond the control of competition. The market investigation also revealed that if there were not enough bidders for TGC contracts, particularly for major projects, customers would simply issue individual tenders for several systems/works instead of a global TGC contract and take over planning and integration themselves or engage the services of engineering consultants. This is already happening today. In particular large customers such as the major construction companies Porr and Strabag have in recent years developed their own building services capacities to perform TGC tasks themselves.
- (460) For these reasons, it is therefore unlikely that the merger will significantly impede competition by creating or strengthening a dominant market position in TGC services in Austria. This is also the case with electrical contracting, where, in addition to the above-mentioned companies, there are also a wide variety of medium-sized and small suppliers.

G2. FACILITY MANAGEMENT

1. Relevant markets

- (461) Both Siemens and VA Tech offer facility management services. Facility management includes technical facility management (including energy management, inspection, and the maintenance and repair of building services equipment), commercial facility management (especially accountancy) and general facility management (including security services, cleaning and caretaker services). According to Siemens, these three forms of facility management (technical, commercial and general) constitute a single product market. The market investigation, however, found that they are separate markets, since while the three forms of facility management are sometimes requested together, demand is mostly for individual forms and a number of competitors do not offer the full range of services. However, the market investigation substantiated Siemens' view that any further distinction based on types of building (such as residential and office buildings, shopping centres or industrial plant) or size of buildings was unnecessary. As the merger does not give rise to any competition concerns whatever the market definition, i.e. whether there are separate markets or a single market, the question of the precise product market definition can be left open.

2. Relevant geographic markets

- (462) Siemens takes the view that the market for facility management is EEA-wide. However, most of the market participants consulted as part of the market investigation felt that the markets for the three different forms of facility management were national.²⁵⁷ The question of the precise geographical market definition can, however, be left open for the purposes of this Decision as effective competition is not significantly impeded in any of the alternative geographical markets examined.

²⁵⁷ Cf. COMP/M.3172 – Ferrovial/Amey (ultimately left open).

3. Competition assessment

- (463) According to Siemens, irrespective of whether the markets are defined as national or larger, neither the facility management market as a whole, nor the technical facility management, commercial facility management and general facility management markets would be affected. In the cases of commercial and general facility management, the Commission's market investigation discovered no evidence that the planned merger would have any impact on competition. The market investigation also reveals that even in the case of technical facility management in Austria, where the direct competitive position and the respective market strengths of Siemens and VA Tech are most pronounced, competition is unlikely to be impeded significantly and Siemens/VA Tech are unlikely to achieve a dominant position.
- (464) Siemens' figures for its share of the technical facility management market in Austria and those of VA Tech and its most important competitors are as follows: Siemens [5-10]*%, VA Tech [5-10]*%, Energiecomfort [10-15]*%, Honeywell [5-10]*%, Axima [5-10]*%, MCE [5-10]*%, M+W Zander [5-10]*% and Vamed [2-5]*%. The other market participants, however, believe Siemens and VA Tech to be in a stronger position on the Austrian market. Competitors' estimates are basically as follows: Siemens 15-25%, VA Tech 10-22%, Axima 12-20%, VAMED 20%, M&W Zander 10%, Energiecomfort 9%, Teletech 8%, MCE 8%. Customer estimates reflect this discrepancy, although customers tend to lower estimates of the market shares of Siemens (6-20%, in one instance 30%) and VA Tech (6-20%) and estimate that MCE's and Teletech's shares are somewhat larger (both 5-15%).
- (465) Most of Siemens's and VA Tech's customers indicated in the market survey that the respective other party was not the most promising competitor in the context of the tendering or negotiated procedure. Many replies pointed out that in Austria there are a number of other suppliers whose services in the area of technical facility management are from a customer standpoint basically equivalent to those of VA Tech and Siemens. Even smaller companies would, especially at regional level, exert competitive pressure on the above-mentioned larger competitors. Customers also consider foreign suppliers of technical facility management services, who are not yet operating in Austria or operating only on a small scale, to be serious potential competitors (e.g. WISAG, Dussmann, HOCHTIEF and DIW, all of which come from Germany). Hochtief and DIW are already working on projects in Austria. Finally, the market investigation also revealed that in view of the various financially strong actual and potential competitors there are no grounds to fear that competition will be impeded significantly even in the case of major contracts.

H. INFRASTRUCTURE INSTALLATIONS AND ELECTRICAL EQUIPMENT FOR ROPEWAYS

HI. TRAFFIC INFRASTRUCTURE INSTALLATIONS

1. Relevant markets

- (466) With respect to traffic infrastructure installations, there is a small amount of overlap between Siemens and VA Tech in Austria only.

(a) Street lighting, traffic signalling equipment and parking-lot management systems

(467) Siemens and - to a lesser extent - VA Tech are both active in street lighting, traffic signalling equipment and parking-lot management systems. The merger raises no competition concerns under any of the possible market definitions, i.e. taking the above infrastructure installations as separate markets or an overall market. The exact definition of markets can therefore be left open for the purposes of this Decision. The same applies to the question of whether, as Siemens believes, there is an EEA-wide market or markets, or whether national markets should be assumed.

(b) Traffic control systems

(468) There is also an overlap between the activities of Siemens and VA Tech in traffic control, although VA Tech's activities have hitherto been confined solely to Austria – and even there they are of minor significance. In the traffic control sector a distinction can be drawn between national/regional traffic management systems for the trunk road network (motorways and expressways) and municipal traffic computer centres for controlling traffic on major urban roads.

(1) National/regional traffic management systems

(469) National/regional traffic management systems for the trunk road network consist mainly of a central traffic control centre (which gathers, processes and disseminates traffic-related data) and various outlying installations (route stations with traffic data logging equipment and traffic control equipment). The market investigation showed that – in Austria at least – traffic control centres (including subcentres) were commissioned separately from the various outlying installations. The fact that different companies tender for outlying installations and for control centre technology also suggests that the product markets are distinct. From a geographical point of view, it is worth noting that the technical standards laid down for the Austrian traffic management system are the same as those applied in Germany for example and that, as a result, German companies have already taken part in calls for tenders in Austria. In the end the product and geographic market definition can remain open for the purposes of this Decision, as the merger raises no competition concerns under any of the possible market definitions.

(2) Municipal traffic computer centres

(470) Municipal traffic computer centres control traffic detection and flow management in urban areas. They consist essentially of a traffic computer (or interconnected computers under an overarching traffic management system), control devices for light signalling equipment and detection equipment. According to customers and competitors surveyed by the Commission, the standards and technical requirements for municipal traffic computer centres differ widely from those applied to national traffic management systems. In the case of municipal systems, the control centre technology and individual control installations are usually commissioned as a package, which is not the case with national systems. Here too there is no need for an exact product and geographic market definition for the purposes of this Decision, as the merger would not significantly impede effective competition in the EEA or in a substantial part thereof, no matter which of the possible definitions were applied.

2. Competition assessment

(a) Street lighting, traffic signalling equipment and parking-lot management systems

(471) The merger has only a marginal effect on municipal infrastructure - even if the markets in question are defined as national ones - as the only horizontal market affected is that for *light signalling equipment* in Austria, but even there Siemens states that the added market share is less than 1%, barely strengthening Siemens' current position of [30-40]*%. Moreover, public tendering is mandatory in this field, so that market entry appears to be possible in Austria (the market investigation even produced some evidence of an emerging European market) and there are sufficient alternatives to Siemens, namely Swarco, Signalbau Huber (M-Tech), Gesig, Dambach, Kapsch and Peek Traffic.

b) Traffic control systems

(1) National/regional traffic management systems

(472) In the field of national/regional traffic management systems for motorways and expressways, VA Tech has hitherto been active solely in Austria and has only set up two small route stations for traffic flow management. [...] on the one occasion when there was a call for tenders for control centre technology and IT for the Austrian traffic management system, but the contract was awarded to a joint venture between Siemens and Heusch/Boesefeldt. The market investigation confirmed Siemens' statement that, for the foreseeable future, there is no demand in Austria for further control centre technology and IT at the core of the national traffic management system. Furthermore, the same technical standards apply in Austria as in Germany, so that suppliers operating in Germany could easily take part in calls for tenders in Austria (should demand resurface). The only potential buyer (Asfinag, the state-owned enterprise responsible for Austria's entire motorway and expressway network) raised no objections to the merger. Moreover, taking into account Asfinag's power as a buyer, it cannot be stated that the merger would significantly impede effective competition.

(473) The same applies to the setting-up of outlying installations of the Austrian traffic management system for motorways and expressways, which are the subject of separate calls for tenders. Asfinag estimates that in the next ten years the total value of orders for outlying installations to be put out to tender will be EUR 350 million. Of the contracts awarded to date, most have been won by Siemens or by consortia involving Siemens. VA Tech has taken part in award procedures alongside a number of other tenderers (in particular construction firms with their own electrical departments, such as Strabag and Alpine Energie). To date VA Tech has only set up two route stations for traffic flow management. The sole customer in Austria, Asfinag, claims that, after the merger, there will be a range of firms able to fill VA Tech's role in the market and compete with Siemens for contracts for outlying installations: Alpine Energie, Strabag ATG, Grimm DÜRR and RWE. Asfinag has therefore raised no objections to the merger. The market investigation also revealed that, given the identical technical standards in Germany, firms operating there (such as Weiss Electronic, Dambach, QSG and ave) are also in a position to set up outlying installations for the Austrian traffic management system.

(474) Irrespective of whether the relevant product market is considered as a whole or divided into control centre technology and outlying installations, the merger does not lead to any significant impediment to competition in the EEA or in a part thereof and in particular does not lead to the creation or strengthening of a dominant position.

This also applies even if the relevant geographic market is still considered to be Austria, as VA Tech's activities are essentially confined to Austria.

(2) *Municipal traffic computer centres*

- (475) VA Tech is less active in municipal traffic computer centres than in national/regional traffic management systems. According to its own statements, VA Tech has obtained [...] in the last five years - to expand an urban traffic computer centre in Austria. Its main competitors in this field are Siemens, Signalbau Huber and Gesig. The market investigation also found that Zetsch, Pichler and Alpine Energie are significant competitors, to which must be added the actual or potential competitors from Germany - Dambach, Stoye and Weiss Electronic. Dambach for one states that it has already taken part in calls for tenders in Austria. The customers surveyed by the Commission (local authorities in major Austrian towns and cities) raised no objections to the merger on competition grounds. Given VA Tech's hitherto weak market position and the presence of a range of serious current and potential competitors, the merger does not lead to any significant impediment to competition in the EEA or in a substantial part thereof and in particular does not create or strengthen a dominant position. This applies whether the relevant geographic market is defined as national or as extending beyond Austria's borders (as VA Tech only operates in Austria).
- (476) Since the merger does not lead to any significant impediment to competition in either national/regional traffic management systems or municipal traffic computer centres, no competition concerns would be raised either if these two sectors were deemed to overlap to form a single market.

H2. WATER TREATMENT INSTALLATIONS

1. Relevant markets

- (477) The question of the relevant market can also remain open in the water treatment field, as the proposed merger raises no competition concerns. Siemens assumes that the market is at least EEA-wide. In an earlier Commission decision the scope of the geographic market was left open, although the Commission's investigations also pointed to an EEA-wide market.²⁵⁸ In the end the exact geographic market definition can remain open in the present case, as effective competition would not be significantly impeded in any of the alternative geographical markets in the EEA - or in a substantial part thereof - that have been investigated.

2. Competition assessment

- (478) In the water treatment field the only slight overlap is in electrotechnical components for water treatment installations, where in any case the market shares do not exceed [2-5]*% even if the market is defined as national and subdivided further (e.g. biofiltration, dosing systems). The merger does not therefore lead to a significant impediment to effective competition.

H3. ELECTRICAL EQUIPMENT FOR ROPEWAYS

²⁵⁸ Case IV/M.1514 Vivendi/US Filters, paragraphs 14 *et seq.*

1. Relevant markets

(479) In other non-industrial plant building, the planned merger leads to overlaps as regards electrical equipment for ropeways. Both Siemens and VA Tech supply ropeway manufacturers with electrical components and ropeway operators with all the electrical equipment they need as a package.

(a) Supply of electrical components to ropeway manufacturers

(480) There are now essentially two large manufacturers of ropeway installations worldwide - Doppelmayr/Garaventa and Leitner/Pomagalski. Both firms supply their customers mainly with turnkey systems, encompassing both mechanical and electrical installations. The two manufacturers used to buy in a large proportion of their electrical equipment, but they have since considerably expanded their own electrical capabilities and now obtain only a very small fraction of the electrical components they need from third parties (e.g. Siemens, Pilz and ABB). Siemens states that the specifications for electrical ropeway building are not fundamentally different from those for other electrical industrial plant building. In particular, the components used are said to be similar and there are now no longer any separate developments for ropeway technology as regards power and automation. The Commission's market investigation also found some evidence to support this view. An exact definition of the relevant market can therefore be left open, as the merger would not seriously impede effective competition in the EEA or in a substantial part thereof, even assuming a narrow definition of the product market (specific electric components for ropeways). The same applies to the geographic market definition, although the market investigation points to an EEA-wide market.

(b) Supply of electrical equipment to ropeway operators

(481) While the great majority of ropeway operators buy turnkey systems, others purchase individual components of ropeway installations (mechanical parts, cables, electrical and automation technology, etc.) separately from different suppliers and either assemble them themselves to produce a complete ropeway or commission engineering firms to do this for them. Such customers report that they do not normally buy components as separate individual parts (e.g. engine, power converter, control system, display system, instrumentation and control technology, etc.) but obtain all electrical equipment for ropeways from suppliers as a unit. The question of whether packages of electrical equipment for ropeways could constitute a separate product market can however remain open, as the merger would not significantly impede effective competition in the EEA or a substantial part thereof, even assuming such a product market definition.

(482) From a geographical point of view, Siemens claims that the market is EEA-wide. By contrast, most of the customers surveyed by the Commission argue that the market is a national one. The market investigation also showed that previously existing barriers to market entry (legal standards for ropeway electrics) were removed by Austria's implementation in 2004 of Directive 2000/9/EC of the European Parliament and of the Council of 20 March 2000 relating to cableway installations designed to carry persons²⁵⁹ and that, since the uniform standards came into effect,

²⁵⁹ OJ L 106, 3.5.2000, p. 21.

bidders from other Community Member States have increased their presence in Austria. However, the question can remain open, as the merger would not significantly impede competition in any of the alternative geographic markets that have been investigated.

2. Competition assessment

(a) Supply of electrical components to ropeway manufacturers

(483) In response to the market investigation, it was stated that Siemens/VA Tech would acquire a monopoly in the supply of electrical components to ropeway manufacturers. However this is incorrect. Both of the large global players in ropeway manufacturing - Doppelmayr/Garaventa (Austria/Switzerland) and Leitner/Pomagalski (Italy/France) - produce much of the electrical equipment for their ropeways themselves. Only to a very small extent do they buy in electrical components for their ropeways. [...] However, the manufacturers also purchase electrical components from a whole series of other suppliers. VA Tech provides only a very minor part of these supplies. Consequently, Doppelmayr/Garaventa and Leitner/Pomagalski stated in the market survey that the merger would have no implications for competition in electrical components for ropeways. It can therefore be assumed that the planned concentration would not lead to a dominant position for Siemens and VA Tech, even on a narrow definition of the relevant product market (electrical components for ropeways) and geographic market (Austria), or to any other significant impediment to competition.

(b) Supply of electrical equipment to ropeway operators

(484) There is also an overlap between Siemens and VA Tech in the supply of separate electrical equipment to ropeway operators who do not buy turnkey installations or who renew part of their installations. At present Siemens and VA Tech are the biggest suppliers of electrical equipment to ropeway operators in Austria. Siemens argues that, even after a merger between VA Tech and Siemens, there would still be no shortage of independent suppliers. This view was also largely confirmed by the market investigation. Up to now Doppelmayr/Garaventa and Leitner/Pomagalski have generally supplied complete ropeway installations, but, given their growing in-house expertise in the electrical field, they are also exerting competitive pressure on firms that supply only electrical equipment for ropeways. According to customers, both Doppelmayr/Garaventa and Leitner/Pomagalski are also able and willing to supply electronic equipment for ropeways separately.

(485) Furthermore, the market investigation found that smaller firms are gaining ground. In Austria this applies in particular to the firm Berchthold, which customers readily expect to take over the market role currently played by VA Tech. Foreign suppliers of electrical equipment for ropeways are also playing a bigger part, for example Frey (Switzerland),²⁶⁰ SISAG (Switzerland), BEW (Italy) and Seirel (France). The two Swiss firms in particular can already cite projects in Austria as a reference. Access was made much easier for foreign suppliers when Austrian technical standards for

²⁶⁰ The firm was previously active in Austria only through its subsidiary STG, which filed for insolvency in 2004. However, Austria has been and still is among Frey's areas of activity, as evidenced by its participation at the Austrian trade fair "INTERALPIN" (see the list of exhibitors at <http://www.congress-innsbruck.at/events/interalpin/deutsch/Ausstellerliste2005.pdf>).

ropeways (including electrical equipment) were brought into line with the requirements of Directive 2000/9/EC²⁶¹ in 2004.

- (486) In view of these facts, it cannot be assumed that the concentration would impede effective competition in the common market or in a substantial part thereof, particularly not as a result of the creation or strengthening of a dominant market position.

I. OTHER IT SERVICES

1. Relevant market

- (487) In addition to their activities in the various markets described above, Siemens and VA Tech also operate in other areas of information technology. There is no overlap between their respective commercial activities as regards hardware and software, the only area in which there is such an overlap being IT services. Siemens assumes a uniform product market for IT services. However, the exact definition of the market can remain open, as the merger has no relevant implications for competition from either a sector-specific angle or applying a distinction based on the size of buyers. The same applies to the question of whether the market is EEA-wide, as Siemens argues, or whether it should be considered as narrower, i.e. corresponding to national level or to a certain language area (the fact that VA Tech operates only in Austria and Germany points to such a conclusion).

2. Competition assessment

- (488) No market is affected in the field of IT services. The Commission's market investigation unearthed no evidence that the concentration would have any relevant implications for competition. It cannot therefore be assumed that there will be any significant impediment to effective competition in the field of other IT services.

VI. COMMITMENTS

- (489) By letter dated 25 May 2005, Siemens submitted commitments under Article 8(2) of the Merger Regulation in order to address the Commission's competition concerns. These commitments were slightly amended by letter dated 13 June 2005. The full text of the commitments is set out in Annexes I and II to this Decision and forms an integral part of the Decision.
- (490) The gist of the commitments relating to equipment and services for hydroelectric power stations is as follows: Siemens undertakes to sell VA Tech Hydro GmbH & Co. ("VA Tech Hydro"), a power-generation company forming part of VA Tech, to a suitable buyer that is independent of the parties and subject to the Commission's approval. VA Tech Hydro will be sold as a going concern, i.e. including all tangible and intangible assets existing at the time the commitment was given, and its entire workforce. Siemens promises to keep intact the viability and competitiveness of the business to be divested. It also undertakes to manage the business separately up to the time of the sale.

²⁶¹ OJ L 106, 3.5.2000, p. 21.

(491) To dispel the Commission's competition concerns in the field of metal plant building, Siemens makes the following commitments:

- (1) Siemens will exercise its right to be represented on the shareholders' committee of SMS, as enshrined in the SMS shareholders' agreement, by appointing as its representative an independent trustee, with the Commission's approval; in the period up to the appointment of the trustee, Siemens will not take part in meetings of the shareholders' committee.
- (2) Siemens will do its utmost to ensure that the seats it holds on SMS' supervisory board pursuant to the shareholders' agreement and the concomitant legal status are assumed by two independent trustees appointed by Siemens, with the Commission's approval. The trustees will also exert all other information rights, consultation rights and administrative rights, including voting rights, instead of Siemens. [...]*
- (3) Siemens will ensure that only the aforementioned trustees and not Siemens will receive information from SMS that is not publicly available. The only exceptions to this obligation are as follows:
 - information required by Siemens to meet its legal obligations regarding financial reporting and drawing up the group's financial statement [...]*
 - information on the valuation of Siemens' holding in SMS at 31 December 2004 and relating solely to the period up to that date [...]*
- (4) Siemens will not contest, cancel or revoke the exercise of the put-option at 31 December 2004;²⁶² for a specified period it will not acquire any shares in SMS, unless the Commission has found that the market structure has changed in such a way that this undertaking is no longer necessary.

VII. COMPETITION ASSESSMENT OF THE PROPOSED CONCENTRATION IN THE LIGHT OF THESE COMMITMENTS

A. EQUIPMENT FOR HYDROELECTRIC POWER STATIONS

(492) The sale of VA Tech Hydro removes entirely the overlap for competition purposes between Siemens and VA Tech in the market for equipment for hydroelectric power stations. The commitments were presented to customers and competitors as part of a market test. They considered that Siemens' divestment of VA Tech Hydro was an entirely effective measure to remove the competition concerns raised by the proposed merger as originally notified. A number of respondents to the market test pointed out that VA Tech Hydro's activities in fossil-fuel power generation (i.e. a field in which there are no competition concerns) would have to remain with the business being divested in order to guarantee its market viability. It was also pointed out that the business divested would have to have access to products relating to network control technology for hydroelectric power stations. Such access is ensured

²⁶² [...]*

at present by the 50% share in VA Tech SAT GmbH & Co. ("SAT"). The remaining shares in SAT are held by VA Tech. The wording of the commitment meets both of these concerns.

B. METAL PLANT BUILDING

- (493) In the light of the Commission's investigations, the commitments concerning SMS as described at paragraph (491) are sufficient to reasonably dispel the competition concerns regarding the markets for metal plant building. The commitments ensure that Siemens cannot use its position as minority shareholder [...] to obtain any strategic knowledge about SMS' business policy. In addition, Siemens' voting rights will be transferred to the trustee or trustees to be appointed. Furthermore, the commitments ensure that Siemens will permanently and irrevocably sell its holding in SMS by exercising the put-option or by other means. There is therefore no reason for any weakening of competition between Siemens/VAI and SMS in the markets affected, something which would be expected in the absence of such commitments.
- (494) Siemens' undertaking to transfer the exercise of its aforementioned rights to an independent trustee appointed with the Commission's approval takes due account of the fact that, with effect from 31 December 2004, Siemens exercised the put-option for the purposes of transferring its holding to SMS, and that the sale of this holding to an independent buyer, which would have been required otherwise, has already been initiated. Siemens' commitment not to obtain information on SMS that is not publicly available allows exceptions that are necessary to enable Siemens to meet its legal obligations regarding financial reporting and drawing up the group's financial statements and to allow Siemens to defend its legal position in the ongoing legal dispute. In each case they are confined to what is strictly necessary for the purpose in hand. In particular, the exception for information that is relevant to the legal dispute is confined to information relating to the past, thereby excluding from the outset any information that might be significant for SMS' future competitive strategy. The transfer of the voting rights to the trustees ensures that Siemens cannot, even as a minority shareholder, influence any strategic decisions of SMS.
- (495) The commitments were presented to customers and competitors as part of a market test. The overwhelming majority of those canvassed believe that the commitments are suitable to prevent the transmission to Siemens of strategic knowledge about SMS and hence to meet competition concerns. Any criticism of the commitments was directed mainly at the general choice of a trusteeship solution rather than the immediate sale of Siemens' holding in SMS. It was suggested by some that the trusteeship solution could in itself dampen competition if it were to be maintained over a long period - depending on the duration of the legal dispute on the valuation of Siemens' holding in SMS. However, such criticism is irrelevant to the competition concerns raised by the Commission in this Decision relating to the markets for metal plant building. As has been explained, the Commission's concerns are based on the expectation of a weakening of competition between Siemens/VAI and SMS because Siemens might have access to strategic knowledge by dint of its rights as minority shareholder. This access to strategic knowledge is no longer possible as a result of the commitments. Also, it can be assumed that the capacity of SMS' corporate bodies to act is guaranteed on the basis of the legal provisions, in particular as the business management of the company is determined by the majority

shareholder. There is therefore no indication that the trustee solution as such will lead to an impediment to competition.

- (496) Finally, it was argued that Siemens would not be able to fulfil these commitments as they would encroach on the legal position of the majority shareholders of SMS under the shareholders' agreement. However, this is not the case. [...] The appointment of trustees to represent Siemens on the shareholders' committee and the supervisory board changes neither Siemens' position as shareholder nor the legal status of the shareholders' agreement. In particular the trustees do not acquire the legal status of SMS shareholders in Siemens' place. Under these circumstances it is not clear why Siemens should be unable to fulfil the commitments or why this would constitute encroachment on the rights of third parties.

VIII. CONDITIONS AND OBLIGATIONS

- (497) In accordance with the first sentence of the second paragraph of Article 8(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.

- (498) Measures that give rise to a structural change to the market must be made subject to conditions, while the implementing steps necessary to achieve this result constitute obligations on the parties. Where a condition is not fulfilled, the Commission decision declaring the merger to be compatible with the common market is null and void. Where the parties commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(6)(b) of the Merger Regulation; fines and penalty payments may also be imposed on the parties under Article 14(2)(d) and Article 15(1)(c) of the Merger Regulation.

- (499) In accordance with the fundamental distinction described above, the Commission makes its decision subject to the condition of full compliance with the commitment to sell VA Tech Hydro as a going concern, including all of its activities in the field of equipment and services for hydroelectric power stations, by the end of the extended deadline for sale to a purchaser approved by the Commission.

- (500) All remaining parts of the commitments set out in Annex I, in particular the obligation to maintain temporarily and manage separately the business to be divested and the details concerning the trustee to be appointed by the parties, must be made the subject of obligations, since they are meant to only implement the aforementioned conditions.

- (501) In view of the undertakings in Annex II, the Commission makes this decision conditional on full compliance with the commitment that Siemens will not contest, cancel or revoke its exercise of the put-option as of 31 December 2004 and will not, for a specified period, acquire any shares in SMS, unless the Commission finds that the market structure has changed in such a way that this undertaking is no longer necessary. The remaining commitments set out in Annex II regarding the rights enjoyed by Siemens as a shareholder of SMS under the shareholders' agreement must also be the subject of obligations.

IX. CONCLUSION

(502) Provided that the commitments entered into by Siemens are complied with in full, it can be accepted that the planned concentration does not lead to a significant impediment to effective competition in the common market or in a substantial part thereof and in particular that it does not create or strengthen a dominant position. Subject to full compliance with the commitments set out in the Annex, the concentration can therefore be declared compatible with the common market in accordance with Articles 2(2) and 8(2) of the Merger Regulation and compatible with the functioning of the EEA Agreement in accordance with Article 57 of that Agreement,

HAS ADOPTED THIS DECISION:

Article 1

The notified concentration by which Siemens acquires control over VA Tech within the meaning of Article 3(1)(b) of the Merger Regulation is hereby declared compatible with the common market and with the functioning of the EEA Agreement.

Article 2

Article 1 shall apply on condition that the commitments entered into by Siemens and set out at points B.1 to 3 of Annex I to this Decision and in the first and third sentences of point B.IV of Annex II to this Decision are complied with in full.

Article 3

This Decision is issued subject to the obligation that the other commitments entered into by Siemens and set out in Annexes I and II are complied with in full.

Article 4

This Decision is addressed to:
Siemens Aktiengesellschaft
Wittelsbacherplatz 2
Germany - 80333 Munich

For the Commission
Neelie KROES
Member of the Commission

EN

ANNEX 1

The full original text of the conditions and obligations referred to in Articles 2nd and 3rd may be consulted on the following Commission website:
http://ec.europa.eu/comm/competition/index_en.html



EUROPEAN COMMISSION

The Hearing Officer

FINAL REPORT OF THE HEARING OFFICER
IN CASE COMP/ M.3653 - SIEMENS / VA TECH

**(pursuant to Articles 15 and 16 of Commission Decision (2001/462/EC, ECSC)
of 23 May 2001 on the terms of reference of Hearing Officers
in certain competition proceedings – OJ L162, 19.06.2001, p.21)**

The notified concentration

On 10 January 2005, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004 of 20 January 2004 (“the Merger Regulation”) whereby Siemens AG of Germany (“Siemens”) acquires within the meaning of Article 3(1)(b) of the Merger Regulation control of the whole of the Austrian company VA Tech AG (“VA Tech”) by way of public bid announced on 10 December 2004.

The proposed transaction would lead to numerous horizontal and vertical overlaps in the fields of power generation, power transmission and distribution, automation & drives, rail transport equipment, metallurgy and electrical plant engineering, building technology and communal infrastructure.

The initiation of proceedings and the issue of access to key documents

At the end of the first phase of the investigation, the Commission concluded that the concentration raised serious doubts as to its compatibility with the common market and with the EEA Agreement. On 14 February 2005, the Commission therefore initiated proceedings in accordance with Article 6(1)(c) of the Merger Regulation.

On 2 March 2005 Siemens was provided with access to the “key documents” in the Commission file in accordance with chapter 7.2. of the “Best Practices on the conduct of EC merger control proceedings” (“Best Practices”), as determined by the Directorate General for Competition. By letter of 16 March 2005 Siemens requested access to further documents. In particular, they considered that documents transmitted by VA Tech ought to be of particular interest for the case and should therefore qualify as key documents. In their reply of 6 April 2005, the Directorate General for Competition confirmed their view that the documents in question did not constitute key documents. It was considered that irrespective of their source, the documents requested did not constitute substantiated submissions of third parties running counter to the notifying parties’ views as set out as definition of key documents in the Best Practices. Siemens did not officially request me to intervene in this respect.

The issuance of the statement of objections and the procedural issue created by Voith Siemens with their request for an oral hearing: The notion of other involved parties

A statement of objections was sent to Siemens on 22 April 2005. In the following days, access to the Commission's file was granted. Siemens was asked to reply by 6 May 2005. This deadline was complied with.

Neither Siemens, nor VA Tech requested to develop their arguments in a formal oral hearing.

However, with a letter dated 6 May 2005 and registered 10 May 2005, the joint venture Siemens Voith Hydropower Generation GmbH & Co. KG ("Voith Siemens"), between J.M. Voith AG and Siemens AG, requested in writing a formal oral hearing pursuant to Article 14(2) of Commission Regulation (EC) 802/2004 of 7 April 2004 ("the Implementing Regulation"). They considered that, given that they might be directly affected by a remedy that Siemens might propose to the Commission, they should be considered as "other involved party" in the sense of Article 11 (b) of the Implementing Regulation.

In my written response of 13 May 2005, I took the view that Voith Siemens did not qualify as an "other involved party" and was therefore not entitled to request a formal oral hearing, in the presence of the Member States and of the associated services of the Commission, although they could of course request to be heard by the people in charge in writing or orally at any point in time. Thereinafter, the seller and the target of a concentration, companies which are indicated as examples for "parties to the proposed concentration" in Article 11 (b) of the Implementing Regulation constitute "other involved parties", because they are directly and inevitably concerned by the implementation of the proposed concentration. This determines the fact that they are "Parties to the proposed concentration" as expressed in the Regulation.

By contrast, it is uncertain and can only be determined at the end of a merger proceeding whether companies will be directly affected by commitments which need to be proposed by the notifying parties and have to be accepted by the Commission.

Therefore, the mere fact that the remedies agreed on in the context of a merger proceeding might have an impact on a company cannot justify that the latter qualifies as an "other involved party", since they do not fall under the denomination of "Parties to the proposed concentration"

The market test

On 25 May 2005, Siemens offered commitments which were slightly amended on 7 June 2005. The market test of the proposed undertakings has been generally positive.

I have not been asked to verify the objectivity of the enquiry.

The further requests for access to documents also in relation to the notion of other involved parties.

By letter to the relevant Commission service dated 9 June 2005 and by letter to me dated 22 June 2005, SMS Demag AG, and its parent company SMS GmbH ("SMS") requested access to the case file. This request was rejected by the Directorate General for Competition on 22 June 2005 on the ground that SMS was recognized as an interested third party and not as an "other involved party" in the sense of Article 11 (b) of the Implementing Regulation

and was therefore not entitled to have access to the file under the Implementing Regulation. By decision of 6 July 2005 pursuant to Article 8 of the Hearing Officer's Mandate, I confirmed the point of view taken by the Directorate General for Competition on the grounds that the mere fact that the remedies envisaged in the context of a merger proceeding might have an impact on a third company could by no means justify that the latter qualifies as an "other involved party" in the sense of Article 11 (b) of the Implementing Regulation.

This is confirmed by whereas 11 of Regulation 802/2004 according to which, upon request, other involved parties must be granted the opportunity before notification to discuss the intended concentration informally with the Commission. This shows that the legislator acted on the assumption that the identity of an "other involved party" results from the intended concentration itself, this being determined before potential remedies are proposed. Accordingly, the qualification of a company as an "involved party" cannot depend on the manner in which the remedies eventually proposed affect certain companies.

Notwithstanding the above, SMS was provided with a non-confidential version of the Statement of Objections and was given the opportunity to comment thereon. Furthermore, SMS received non-confidential versions of the commitments in the context of the market test, insofar as they related to the metallurgical markets in which SMS have an interest. Therefore, I take the view that SMS had ample opportunity to state its views during the proceeding.

On 24 June 2005 Siemens requested access to the file for non-confidential documents received by the Commission since the statement of objections. The company was provided with the opportunity of obtaining access to these documents on 1 July 2005.

In the light of the above, I consider that the rights to be heard of all participants to the present proceeding have been respected.

Brussels, 6 July 2005

(signed)

Serge DURANDE



EUROPEAN COMMISSION

Competition DG

Policy and Strategic Support

OPINION

of the ADVISORY COMMITTEE on CONCENTRATIONS

given at its 133rd meeting on 29 June 2005

concerning a draft decision relating to

Case COMP/M.3653 – SIEMENS/VA Tech

1. The Advisory Committee agrees with the Commission that the notified operation constitutes a concentration within the meaning of Article 3(1)(b) of Regulation 139/2004 and that it has a Community dimension.
2. The Advisory Committee agrees with the Commission that for the purposes of assessing the present operation, the relevant product markets are:

In power generation:

- a) the equipment for hydro power plants;
- b) the provision of turnkey combined cycle gas-fired power plants;
- c) the supply of gas turbines, the exact delineation of this(these) market(s) can be left open;
- d) the supply of generators, the exact delineation of this(these) market(s) can be left open;

In transmission and distribution:

- e) High voltage products (>52kV);
- f) Transformers;
- g) Energy automation and – information;
- h) Turnkey projects;
- i) T&D services;

with a possible further delineation according to individual components; the exact scope of the relevant market being left open;

In rail:

- j) Electrical traction for trams, metros, regional trains and locomotives;
- k) Trams, metros, electrical and diesel powered regional trains and locomotives;
- l) Catenary wire, the exact delineation of this(these) market(s) can be left open;
- m) Rail power supply: substations, components for substations and servicing of rail power generation plants;
- n) Level crossings;

Frequency inverters:

- o) the exact delineation of this (these) market(s) can be left open;

In metallurgy:

- p) Mechanical metallurgical plant building (limited to iron/steel or including non-ferrous metals) or mechanical metallurgical plant building per process step and metal, whereby the exact delineation of this(these) market(s) can be left open;
- q) Electrical metallurgical plant building (as a whole) or electrical metallurgical plant building per process area, process step and metal, or Level 1 and 2 automation of metallurgical plants (as a whole or parts thereof, for entire metallurgy or per process step and metal), or Level 3 automation, whereby the exact delineation of this(these) market(s) can be left open;
- r) Maintenance services for metallurgical plants;
- s) Electrical plant building for non-metallurgical industrial plants, whereby the exact delineation of this(these) market(s) can be left open;

In LV-switchgear:

- t) Fully fitted LV-switchboards, or, in the alternative, separate for the three components ACD, MCB and MCCB;
- u) Components: busways, the exact delineation of this(these) market(s) can be left open;
- v) Components: PLC [the exact delineation of this(these) market(s) can be left open] and load feeders;

In building technology and facility management:

- w) Components for building control technology, safety technology separate for fire alarm and access/intruder control and electrical installation technology;
- x) Systems: entire security systems and control systems;
- y) Electrical and mechanical contracting, possibly also a market for general technical contractors;
- z) Facility management, the exact delineation of this(these) market(s) can be left open;

In infrastructure and ropeways

- aa) Traffic infrastructure: Street lighting, traffic lights, parking space control, the exact delineation of these markets can be left open;
 - bb) Traffic control, the exact delineation of this(these) market(s) can be left open;
 - cc) Water purification plants;
 - dd) Electrical equipment for ropeways, the exact delineation of these markets can be left open.
3. The Advisory Committee agrees with the Commission that for the purposes of assessing the present operation, the relevant geographic markets are as follows :
- a) the markets for power generation are EEA-wide in scope;
 - b) the markets for T&D is EEA-wide in scope;
 - c) the markets for electrical traction are EEA-wide in scope;
 - d) the markets for trams, metros, electrical and diesel powered regional trains and locomotives are national where there is a strong national industry (here: Austria, Belgium, Germany, Poland, Czech Republic, Spain), and the EEA for the rest;
 - e) the market for catenary wire is national in scope;
 - f) the markets for rail power supply are assessed on a national basis but it can be left open whether they are national or EEA-wide;
 - g) the market for level crossings is assessed on a national basis;
 - h) the market for frequency inverters is EEA-wide in scope;
 - i) the markets for electrical and mechanical metallurgical plant building are at least EEA-wide in scope, the market(s) for maintenance services is/are EEA-wide in scope, and the market(s) for non-metallurgical plant building is/are national or EEA-wide in scope;
 - j) the markets for LV-switchgear and components are assessed on a national basis but it can be left open whether they are national or EEA-wide;
 - k) the markets for building technology and facility management are assessed on a national basis but it can be left open whether they are national or EEA-wide;
 - l) the markets for infrastructure and ropeways are assessed on a national basis but it can be left open whether they are national or EEA-wide.
4. The Advisory Committee agrees with the Commission that the notified concentration will significantly impede effective competition in a substantial part of the common market within the meaning of Article 2(3) of the Merger Regulation:
- a) In the market for hydro power generation;
 - b) In the market for mechanical metallurgical plant building or in the markets for mechanical plant building for steelmaking and for continuous casting.

5. The Advisory Committee agrees with the Commission that the commitments submitted by the parties are sufficient to remove :
- the competitive concern in the market for hydro power generation resulting from the horizontal overlap of the concentration;
 - the competitive concerns in the market(s) for metallurgical plant building resulting from horizontal effect of the concentration, in particular the privileged access of Siemens to strategic information of SMS Demag; and that, as a result, the concentration should be declared compatible with the Common Market.
6. The Advisory Committee asks the Commission to take into account all the other points raised during the discussion.

<u>BELGIË/BELGIOUE</u>	<u>ČESKÁ REPUBLIKA</u>	<u>DANMARK</u>	<u>DEUTSCHLAND</u>	<u>EESTI</u>
J. MUTAMBA	---	---	M. WEIDENFELLER	M. PADDO
<u>ELLADA</u>	<u>ESPAÑA</u>	<u>FRANCE</u>	<u>IRELAND</u>	<u>ITALIA</u>
---	L. CUEVAS RIAÑO	B. ALOMAR	---	L. ARNAUDO
<u>KYPROS/KIBRIS</u>	<u>LATVIJA</u>	<u>LIETUVA</u>	<u>LUXEMBOURG</u>	<u>MAGYARORSZÁG</u>
---	---	---	G. BLESER	O. FÜREDI
<u>MALTA</u>	<u>NEDERLAND</u>	<u>ÖSTERREICH</u>	<u>POLSKA</u>	<u>PORTUGAL</u>
---	---	T. HÖLZL	---	---
<u>SLOVENIJA</u>	<u>SLOVENSKO</u>	<u>SUOMI-FINLAND</u>	<u>SVERIGE</u>	<u>UNITED KINGDOM</u>
---	---	M. OKSANEN	P. HANSSON	P. FRASER

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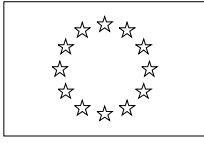
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Case No COMP/M.3696 E.ON/MOL

Only the English text is authentic.

**REGULATION (EC) No 139/2004
MERCER PROCEDURE**

Article 8 (2)
Date: 21/12/2005



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 21/XII/2005

C(2005)5593 final

PUBLIC VERSION

COMMISSION DECISION

of 21/XII/2005

**declaring a concentration to be compatible with the common market
and the EEA Agreement**

(Case No COMP/M.3696 – E.ON/MOL)

**Commission Decision
of 21/XII/2005**

**declaring a concentration to be compatible with the common market
and the EEA Agreement**

(Case No COMP/M.3696 – E.ON/MOL)

(Only the English text is authentic)

(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings¹, and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 7 July 2005 to initiate proceedings in this case,

Having given the undertakings concerned the opportunity to make known their views on the objections raised by the Commission,

After consulting the Advisory Committee on Concentrations²,

Having regard to the final report of the Hearing Officer in this case³,

WHEREAS:

¹ OJ L 24, 29.1.2004, p. 1

² OJ C ...,...200. , p....

³ OJ C ...,...200. , p....

- (1) On 2 June 2005, the Commission received a notification pursuant to Article 4 of Regulation (EC) No 139/2004 (“the Merger Regulation”) of a proposed concentration by which the undertaking E.ON Ruhrgas International AG (“ERI”) acquires, within the meaning of Article 3(1)(b) of the Merger Regulation, control of the whole of the undertakings MOL Földgázellátó Rt. (“MOL WMT”, Hungary) and MOL Földgáztároló Rt. (“MOL Storage”, Hungary), currently solely controlled by MOL Hungarian Oil and Gas Rt. (“MOL”, Hungary), by way of purchase of shares. ERI will also acquire MOL’s shareholdings in Panrusgáz Magyar-Orosz Gázipari Rt. (“Panrusgáz”, Hungary), a joint venture company between OAO Gazprom (“Gazprom”, Russia) and MOL.
- (2) After examination of the notification, the Commission has concluded that the notified operation falls within the scope of the Merger Regulation and raises concerns as to its compatibility with the common market.

I. THE PARTIES

A. E.ON

- (3) ERI is a solely-controlled subsidiary of E.ON Ruhrgas AG, which is in turn an indirect subsidiary of E.ON AG (Germany). The three companies are members of the E.ON group of companies which is a privately owned energy company with a focus on the supply of electricity and gas. The acquiring party will be henceforth referred to as “E.ON”.

B. MOL

- (4) MOL is an integrated oil and gas group which is primarily active in Hungary on the markets for natural gas, oils, fuels and chemicals. It is a public company listed on the Budapest stock exchange. The Hungarian state still owns 12% of share capital, plus a golden share.

II. THE OPERATION AND THE CONCENTRATION

A. Operation

- (5) The companies which are being acquired are the following solely-controlled subsidiaries of MOL:
 - MOL WMT (an acronym for Wholesale, Marketing and Trading) is a public utility wholesaler and gas trader which supplies natural gas to regional gas distributors, industrial customers and large power plants in Hungary;
 - MOL Storage operates five natural gas storage facilities located in Hungary and is only active in providing storage services.

- (6) E.ON will acquire an interest of 75 % minus 1 share in both MOL WMT and MOL Storage. The agreements provide for a 5-year put option under which MOL can sell its remaining 25 % plus 1 share interests in MOL WMT and MOL Storage to E.ON.
- (7) E.ON is also acquiring MOL's 50% shareholding in Panrusgáz. Panrusgáz is a joint venture between OOO Gazexport ("Gazexport"), a subsidiary of Gazprom and MOL. 50 % of the shares in Panrusgáz are currently held by MOL, whereas 40 % of the shares are held by Gazexport and 10 % by Interprocom (a company having close ties with Gazprom).
- (8) MOL Földgázz szállító Rt. ("MOL Transmission"), another solely-controlled subsidiary of MOL, is not acquired by E.ON through the present transaction. MOL is instead granted a put option under which MOL can require E.ON to purchase a 25 % plus 1 share or a 75 % minus 1 share interest in MOL Transmission during the next two years.
- (9) Finally, MOL retains control over its gas exploration and production business (the MOL upstream gas Exploration and Production division ("MOL E&P")). However, as part of the transaction, MOL and MOL WMT have entered into a new long-term gas supply agreement for the gas produced by MOL E&P (the "Supply Agreement").

B. Acquisition of MOL's shareholding in Panrusgáz

- (10) The parties claim that the only business of Panrusgáz is to purchase gas from Gazexport for onward sale to MOL WMT. Therefore, Panrusgáz is only active for its shareholders and has no business relationships with third parties. It is thus submitted that Panrusgáz is technically not a party to the concentration because it does not constitute a full-function joint venture. Based on the information available, the Commission is inclined to regard Panrusgáz as a non full-function joint venture and its acquisition is therefore not part of the concentration assessed in the present case.
- (11) In any event, the acquisition of MOL's stake in Panrusgáz will have to be taken into account in the competitive assessment of the transaction in view of the crucial importance of access to gas resources from abroad and in particular from Russia.

C. Put option relating to MOL Transmission

- (12) The proposed transaction does not result in a change of control of MOL Transmission and this company is therefore not part of the concentration assessed in this case.
- (13) In any event, the put option foreseen by the agreements will be considered in the competitive assessment of the transaction in view of the crucial importance of access to the gas transmission network.
- (14) Finally, the Commission notes that the change in control that may result from the exercise of the put option would at any rate constitute a concentration for merger

control purposes and would thus be closely scrutinised by the competent competition authorities (either the Commission or national competition authorities).

D. Concentration

- (15) In view of the structure of the transaction, the acquisition of sole control over MOL WMT and MOL Storage by E.ON constitutes the concentration assessed in this case.

III. COMMUNITY DIMENSION

- (16) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million⁴. Each of the undertakings concerned has an aggregate Community-wide turnover in excess of EUR 250 million, but they do not achieve more than two-thirds of their aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension.

IV. PROCEDURE

- (17) On 7 July 2005, the Commission initiated proceedings in accordance with Article 6(1)(c) of the Merger Regulation.
- (18) On 2 August 2005, the procedure was suspended for eight days pursuant to Article 10(4) of the Merger Regulation owing to the fact that E.ON did not respond in a comprehensive and timely manner to a decision requiring information pursuant to 11(3) of the Merger Regulation.
- (19) A Statement of Objections (“SO”) was sent to E.ON on 19 September 2005. As agreed between E.ON and MOL, a version of the SO without E.ON's business secrets was transmitted to MOL by E.ON's legal representatives. In the following days, access to the Commission's file was granted. E.ON and MOL were given the opportunity to comment on the Commission's preliminary findings as set out in the SO by 3 October 2005. This deadline was subsequently extended to 6 October 2005 at E.ON's request. E.ON's reply was received on 5 October 2005. MOL's comments were received on 6 October 2005.
- (20) The parties did not request to develop their arguments in a formal oral hearing.
- (21) On 21 October 2005, the request of Energie Baden-Württemberg AG to be admitted as an interested third party was granted by the Hearing Officer. The same day, the Commission sent them a non-confidential summary of the SO.

⁴ Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Notice on the calculation of turnover (OJ C66, 2.3.1998, p25).

- (22) On 20 October 2005, E.ON offered commitments which were amended on 11 November, 15 November and 8 December 2005 respectively. Further to the market testing of the proposed undertakings, E.ON substantially improved its draft commitments, in particular as regards the duration of the gas release program and the price mechanism of the gas release auctions.
- (23) In agreement with and following an express request by E.ON, to which MOL agreed, the Commission issued a decision on 10 November 2005 pursuant to Article 10(3) second paragraph of the Merger Regulation in order to extend the procedure by 11 working days.
- (24) The Advisory Committee on Concentrations discussed the draft decision on 6 December 2005.

V. RELEVANT MARKETS

- (25) The transaction affects the gas and electricity sectors. Natural gas and electricity activities can be delineated in several distinct product markets. The following analysis will deal first with the definition of the relevant natural gas markets and secondly with the definition of the relevant electricity markets.
- (26) According to previous Commission decisions, the definition of the relevant product market(s) must take into account the existing and foreseen degree of opening thereof⁵. Accordingly, each chapter will contain a description of the regulatory framework including the state of the opening of the gas and electricity markets in Hungary and their expected evolution.
- (27) It should be noted at the outset that, in their reply to the SO, the parties did not contest any of the relevant product market definitions.

A. *Relevant gas markets*

(i) *The natural gas sector in Hungary*

a. **Gas demand**

- (28) Natural gas is the largest source of energy in Hungary. Gas currently satisfies 48% of Hungary's primary energy consumption, which is the highest share in the Community⁶. Approximately 80% of the population consumes natural gas, and natural gas accounts for 25% of the electricity produced in Hungary. In 2004, the total Hungarian gas market represented 14.0 billion cubic meter ("bcm"), including 5.6 bcm for industrial and commercial customers, 3.2 bcm for power plants and 5.2 bcm for residential customers. Gas demand is expected to grow from 14 bcm in

⁵ See, inter alia, Commission decision of 9 December 2004 in Case COMP/M.3440 – EDP/ENI/GDP.

⁶ By comparison, natural gas accounts for 40% of the Netherlands' primary energy consumption and 39% of the UK's primary energy consumption. Contrary to Hungary, the Netherlands – as well as the UK until last year – is a net exporter of gas.

2004 to [15-20]* bcm in 2020 (about [0-2 %]* compounded annual growth rate), due to the increase in Hungarian gross domestic product and the increase in gas-fired electricity generation.

*Projections for Hungarian gas demand:*⁷

In bcm	Residential	Industrial	Power plants	TOTAL
2005	[5-7]*	[6-8]*	[3-5]*	[14-20]*
2010	[5-7]*	[6-8]*	[3-5]*	[14-20]*
2015	[5-7]*	[6-8]*	[3-5]*	[14-20]*
2020	[5-7]*	[6-8]*	[3-5]*	[14-20]*

[...]*

b. Gas sources

- (29) Natural gas is either imported from foreign sources or bought from Hungarian gas producers for it to be delivered to customers on the Hungarian market.

Domestic production

- (30) Hungarian gas production is not negligible and amounted to approximately 3 bcm in 2004, accounting for about 20% of national gas consumption. The entire national production is handled by the MOL E&P. It should be added that besides MOL E&P there is another small independent gas producer in Hungary, El Paso, who also sells its entire production to MOL WMT (around 0.2% of Hungarian national gas consumption)⁸.
- (31) There are different qualities of gas in Hungary. Most of the gas produced by MOL E&P is high-calorific gas⁹ ([2-4]* bcm in 2004). MOL E&P produces small quantities of low-calorific gas¹⁰ ([0-1]* bcm in 2004), and a gas of a lesser quality

* Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

⁷ Parties' submission dated 29 August 2005.

⁸ The US company POGO is also active in gas exploration in Hungary but does not yet produce natural gas. POGO's Hungarian subsidiary POGO Hungary Kft. was acquired in June 2005 by the US company Toredor Resources Co. and will change its name to Toredor.

⁹ High-calorific gas is gas with higher combustion properties according to the Hungarian Standard 1648 MSZ 2/H.

¹⁰ Low-calorific gas is gas with lower combustion properties according to the Hungarian Standard 1648 MSZ 2/S. This gas has different parameters from the low-calorific gas in other countries (CO₂ rather than nitrogen prevails as a non-combustible component due to special geological reasons).

called “inert gas”¹¹ ([0-1]* bcm in 2004). The Hungarian gas production (for both high-calorific and low-calorific gas¹²) is declining.

Imports

- (32) Although there is a domestic natural gas production in Hungary, imports are key to satisfy the domestic natural gas demand, and Hungary is a net gas importer. In 2004, approximately 80% of natural gas consumed in Hungary was imported. The share of imports is expected to increase as Hungary’s natural gas production decreases.
- (33) Hungarian gas imports are traditionally and predominantly Russian gas. There are only two cross-border pipelines (“entry points”) through which gas is imported into Hungary: the Hungarian/Ukrainian entry point Beregovo (Brotherhood pipeline, capacity of 15.01 bcm/year or 43.1 million m³/day) and the Hungarian/Austrian entry point (Hungary-Austria Gasleitung (“HAG pipeline”) at Baumgarten, capacity of 4.5 bcm/year or 12.3 million m³/day). In addition, there is an exit point at the Hungarian/Serbian border through which Serbia and Bosnia-Herzegovina import Russian gas that transits through Hungary.
- (34) Capacities available at these entry points are essentially booked and used by MOL WMT to import gas under its long-term supply contracts. Capacities booked by MOL WMT for the gas year 2004/2005 were [10-12]* bcm/year and [25-35]* million m³/day (out of 15.01 bcm/year and 41.3 million m³/ day) at Beregovo and [1-4]* bcm/year and [6-10]* million m³/day (out of 4.5 bcm/year and 12.3 million m³/day) at the HAG entry point¹³. In addition, a transit capacity of [3-5]* bcm/year and [10-13]* million m³/day are booked at the Beregovo entry point by the Serbian company Nis and the Bosnian Herzegovinan company BHGas for transit. As a result, free capacity on the Hungarian entry point is very limited for other market players¹⁴.
- (35) Two additional gas pipelines are envisaged to link Hungary with Romania [...]*. The pipeline between Romania and Hungary has been contemplated for several years by MOL and Transgaz (Romania). Transgaz has already completed the Romanian section of the pipeline but the construction of the Hungarian section [...]*. The pipeline would link Algyő and Csanádpalota (100 km transmission line, 45 km of which in Hungary) and would have an initial capacity of [1-3]* million

¹¹ Inert gas is gas whose combustion properties are lower than for the MSZ 1648 2/S standard. Inert gas contains more carbon-dioxide and more nitrogen.

¹² Low-calorific gas fields will be empty within [...]*.

¹³ MOL WMT has booked [2-4]* bcm on the HAG pipeline with OMV, the Austrian gas incumbent, on a ship-or-pay basis until [...]*.

¹⁴ Although actual imports amounted to approximately [10-13]* bcm in 2004 (excluding transit), total annual booked capacities reached approximately [15-20]* bcm in 2004. This suggests that there is contractual congestion at the entry points (capacity booked but not fully used).

m³/day (approximately [0-2]* bcm/year). MOL's internal documents¹⁵ indicate [...]*.

- (36) In addition, Nabucco is a project for a new pipeline going from Turkey to Austria, crossing Bulgaria, Romania, and Hungary to bring Caspian and Middle East gas (from Azerbaijan, Iran, Syria, Egypt and Iraq, and even Kazakhstan and Turkmenistan) to European markets. The feasibility studies have already been performed and the project is currently at its planning stage. The operation phase is expected to start in 2011 and its yearly capacity will be either 25 bcm (base case scenario) or 31 bcm (high case scenario). According to parties involved in the project, it is expected that around [10-20]* bcm will be available at the Baumgarten hub for further transmission and distribution in Europe.
- (37) Prior to the market opening, the MOL group had a monopsonistic position on all gas procurement activities, with exclusive rights to purchase Hungarian gas and to import gas into Hungary. In order to secure its gas supply, MOL WMT has entered into long-term supply agreements (up to [...]* years) with [...]* to import gas through the Hungarian Western and Eastern entry points.
- (38) The long-term gas supply agreements of MOL include Take or Pay ("TOP") obligations. TOP obligations in gas supply contracts require the purchaser of the gas to pay in any event for a certain percentage (generally [70-90%]*) of the contracted quantities of gas, even if it does not take the whole contracted quantities. It means that the purchaser is obliged to pay the full price even if it has no opportunity to use or resell the gas. TOP losses typically occur if – due to market liberalization – certain customers switch, the consumption of which has been calculated by the given gas supplier when sourcing its gas to be resold. In such a case, the supplier does not need the whole amount of contracted gas, but it is obliged under the TOP obligation of its agreement to pay the TOP level. In the Hungarian gas system, TOP losses can be suffered by the Regional Distribution Companies ("RDCs") and by MOL WMT if eligible customers currently supplied by them switch to an alternative supplier. [...]*
- (39) As far as MOL WMT's Russian gas imports are concerned, Gazexport, the sole exporter of Russian gas, sells the relevant gas quantities to Panrusgáz, which in turn sells the same quantities onwards to MOL WMT. Imported natural gas flows thus directly through Panrusgáz to MOL WMT, on the basis of two "mirror contracts" concluded between Gazexport/Panrusgáz and Panrusgáz/MOL WMT. According to the agreements, natural gas is supplied to MOL WMT through the Brotherhood pipeline at Beregovo on the Ukrainian border and, to a lesser extent, through the HAG pipeline at Baumgarten on the Austrian border.
- (40) MOL WMT also buys gas from other sources, notably [...]* through the HAG entry point. Under pressure from the Hungarian government with the aim to improve the country's security of supply, MOL diversified its gas purchase portfolio ten years ago. It signed in 1995 and 1997 additional gas supply contracts (two contracts with duration of [10-20]* years with [...]* and one [...]* contract with [...]*) and established a new route connecting the country to the West European transmission

¹⁵ Proposal to MOL Executive Board Meeting [...]*, 9/12/2002, [...]*.

system¹⁶. The gas volumes supplied by [...] to MOL WMT are sourced from [...] overall gas purchase portfolio. This means that the gas sold by those companies to MOL WMT comes from all of [...] gas suppliers¹⁷ and cannot be linked to a specific supply contract of those companies.

- (41) Finally, MOL WMT had concluded gas supply contracts in 1998 with O&G Minerals Ltd. and Eurobridge which are suppliers of non-Russian gas. These contracts have now been terminated, and replaced by a 2004 contract (for an annual quantity of [0-2]* bcm) with Bothli-Trade, a Swiss company, affiliated with Eural Trans Gas. Eural Trans Gas was a Hungarian-registered company which was the sole distributor of Turkmen gas “with Gazprom and NAK Ukraine support”¹⁸.

c. Gas infrastructure

Transmission and distribution of gas

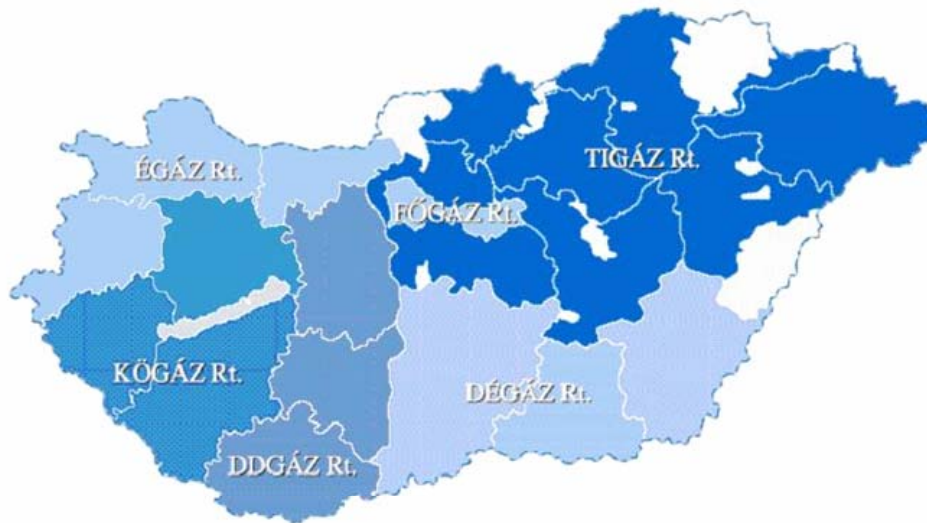
- (42) The Hungarian high-pressure natural gas transmission pipeline network is owned by MOL Transmission, which transports both domestic and imported natural gas to the RDCs, natural gas-fired power stations and certain other large industrial users that are directly connected to the transmission network.
- (43) The low- and medium-pressure distribution pipeline networks are extensive in Hungary, where 91% of the settlements are already connected to a natural gas network. The distribution networks are owned by the RDCs. There are six main RDCs in Hungary, each covering a different region of the country, and seven smaller ones¹⁹. The six main RDCs are TIGÁZ Rt. (“TIGÁZ”), FÓGÁZ Rt. (“FÓGÁZ”), DÉGÁZ Rt. (“DÉGÁZ”), ÉGÁZ Rt. (“ÉGÁZ”), KÖGÁZ Rt. (“KÖGÁZ”) and DDGÁZ Rt. (“DDGÁZ”). In 2004, approximately 76% of the total natural gas sales volumes of MOL WMT were accounted for by sales to the RDCs.

¹⁶ See minutes of the meeting with HEO on 26 July 2005.

¹⁷ See response of E.ON of 10 May 2005 to Question 39 on the draft Form CO: “E.ON Ruhrgas, parent of ERI, has a gas supply portfolio including different sources. E.ON Ruhrgas sells gas to its customers based on this diversified portfolio. It is not possible to break down the origin of the gas for the sales per country as E.ON Ruhrgas serves each customer out of the whole diversified portfolio.”; response of GDF to question 33 of the request for information of 19 July 2005.

¹⁸ Minutes of the Executive Board of MOL of 6 April 2004.

¹⁹ DBGÁZ Kft., TIGÁZ 2 Kft., OERG Kft., DUNAFERR ESZ. Kft. 1, DUNAFERR ESZ. Kft. 2, Csepel ESZ Kft., and Magyar Gázzolgáltató Kft. These RDCs are not further dealt with in the competitive assessment section of this decision, as they have marginal sales.



- (44) It should be noted that there are separate transport and distribution networks (owned by MOL Transmission and the RDCs respectively) for the 2/H and 2/S gas, as these different qualities of gas cannot be mixed. The low-calorific gas is distributed via separate regional systems coming from the gas fields of MOL E&P to mostly domestic customers. The low-calorific gas only represents 5% of total Hungarian gas production, or 1% of total Hungarian gas consumption. The regions currently supplied with 2/S gas [...]*
- (45) The inert gas produced by MOL E&P is transported via a direct pipeline and sold to [...]*. Inert gas represents [0-10%]* of total Hungarian gas production, or [0-5%]* of total Hungarian gas consumption.
- (46) Historically, the RDCs were also owned by MOL but were sold to private investors in a large privatisation process in 1995. E.ON has sole control of two RDCs (KÖGÁZ and DDGÁZ) and a participation in a third one (FŐGÁZ), which is controlled by the municipality of Budapest. Three large international energy groups own majority or minority stakes in the other RDCs: GDF (sole control of DÉGÁZ and ÉGÁZ), RWE (minority stakes in TIGÁZ, FŐGÁZ and DDGÁZ) and ENI/Italgas (sole control of TIGÁZ).

Ownership of the gas RDCs:

KÖGÁZ	71.2% E.ON 13.3% Julius Bar Holding AG 11.6% Swisspartners AG 3.9% Others
DDGÁZ	50.01% E.ON 49.9% RWE 0.1% Others
FÖGÁZ	50% +2 Municipality 32.7% RWE 16.4% E.ON 0.9% Others
DÉGÁZ	99.8% GDF 0.2% Others
ÉGÁZ	99.4% GDF 0.6% Others
TIGÁZ	50% +1 ENI-Italgas 44.2% RWE 7.9% Others

Storage of gas

- (47) MOL Storage owns and operates the five existing underground gas storage facilities in Hungary. All the underground storage facilities in Hungary are depleted gas fields. Storage allows in particular covering the variation between gas procurement, which is relatively constant throughout the year, and gas needs which vary greatly according to seasons. For technical geological reasons, the storage facilities in Hungary can only be used to cover seasonal variations of demand, but not for peak shaving²⁰. There is also a contract with the gas transmission system operator (“TSO”) to use the storage for system balancing purposes. The flexibility of the storage sites is not high, but it is sufficient to handle the balancing demand in Hungary along with line pack.
- (48) The five storage facilities have a total storage capacity of 3.38 bcm (with a withdrawal capacity of 44.5 million m³/day). There are two large storage sites (Hajdúszoboszló in the east with [1-2]* bcm, and Zsana in the south with [1-2]* bcm, undergoing capacity extension). The three other storage sites are much smaller ([250-400]* million, [150-250]* million and [100-200]* million m³). In addition, MOL E&P has more than 50 depleted gas fields. Almost every depleted gas field is convertible into an underground gas storage facility and the convertibility has been concretely examined for [...]*.

²⁰ It is not possible to use storage sites in Hungary for peak shaving for geological reasons, as these are sandstone depleted gas fields. Sandstone is too fragile and technically not suitable for rapid injection and withdrawal of gas into and from the storage facilities.

(ii) *Regulatory framework*

a. Current regulatory framework

- (49) The Hungarian natural gas sector is at the initial stage of the liberalisation process. The first European directive liberalizing the gas market was implemented in Hungary, with the entry into force on 1 January 2004 of the Hungarian Gas Act (Act 42 of 2003 – “HGA”)²¹. This law was further implemented by Government Decree No. 111/2003 on the execution of certain provisions of the HGA (“Executive Decree”) and Government Decree No. 112/2003 (as amended by Government Decree No. 219/2003) (“Eligibility Decree”). A law amending the HGA (Act 63) was adopted on 28 June 2005 to implement Directive 2003/55/EC of the European Parliament and the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC²² in Hungary, and it entered into force on 1 August 2005. Further implementing decrees are being adopted.

Regulatory bodies

- (50) The Hungarian Energy Office (“HEO”) is the energy regulator in Hungary. The HEO is the general supervisory body for the gas market. It issues the various licences for gas and electricity activities, supervises the operation of the market players, approves their terms of business, examines customer complaints, undertakes price reviews and sanctions non-compliance.
- (51) The Hungarian Mining Office (“HMO”) is the special supervisory body dealing with the construction and operation of transportation pipelines and underground storage facilities. Licensing concerning the construction of these facilities also falls within the powers of the HMO.
- (52) The Ministry of Economy and Transport (“MET”) issues decrees on the more technical and specific fields (such as operational safety, general technical conditions etc.) and also sets official prices (tariffs) on the basis of a proposal by the HEO.
- (53) The Network Code (or Grid and Commercial Code) contains the detailed technical rules concerning the operation of the gas system, such as the definition and allocation of free capacities, the rules of nomination, the minimum content of trade, metering and accountancy agreements. The Network Code is prepared by a Network Code Committee and approved by the HEO. The Network Code Committee comprises representatives of the licensees (system operator, public utility

²¹ In addition to the Hungarian laws and decrees implementing the Gas Directives, other relevant legislation in the gas sector includes the Community Regulation on the conditions for access to the gas transmission networks (OJ L 289, 3.11.2005, p. 1), which will enter into force on 1 July 2006. This regulation ensures that the voluntary Guidelines for Good TPA Practice for Transmission System Operators adopted at the Madrid Forum will be implemented in all the Member States. Last, Guidelines for Good TPA Practice for Storage System Operators (“GGPSSO”) were adopted by the European Regulators Group for Electricity and Gas (“ERGEG”) on 23 March 2005, but compliance with these guidelines is voluntary and not mandatory at this stage (http://europa.eu.int/comm/energy/gas/madrid/jwg/ggpsso_23.3.2005.pdf).

²² OJ L 176, 15.7.2003, p. 57.

wholesaler, storage system operator, distribution system operators, public utility suppliers, gas traders, cross-border traders) and of the registered eligible customers²³.

Eligibility

- (54) Since 1 July 2004, all non-residential customers have become eligible customers free to choose their supplier under Hungarian law²⁴. Residential customers will become eligible on 1 July 2007.

Coexistence of regulated and liberalized segments

- (55) The Hungarian gas sector is characterized by a hybrid model, with the coexistence of a regulated segment of the market (or “public utility market”), resulting from the old gas regime in Hungary, and a liberalized segment of the market (or “open segment of the market”). Eligible customers have the right but not the obligation to exercise their eligibility and switch suppliers to enter the open segment of the market. They have the choice between remaining supplied within a public utility contract by their historic gas supplier (their RDC or the public utility wholesaler, MOL WMT if the customer was supplied directly by MOL WMT) or terminating their public utility contract and purchasing their gas requirements from a trader or a producer or importing natural gas themselves²⁵.
- (56) The procedure of switching is described under the Eligibility Decree (Articles 3-7/B) and has been somewhat changed by the recent amendment to the HGA. An eligible customer can terminate its public utility contract at any time by a written notice addressed to its previous public utility supplier. The notice terminates the public utility contract with effect on the first day of the fourth month following the notice of termination (the parties may agree on a different date). According to the parties, switching does not entail any significant costs or time investment on the part of the eligible customer. Customers that have switched to the open segment of the market are allowed to switch back to the regulated segment.
- (57) Customers that have actually switched supplier accounted for 5-6% of the total Hungarian gas consumption at the end of 2004 ([5-15%]* of the gas consumption of eligible customers)²⁶. According to MOL, this share will increase to [5-15%]* in October 2005 ([5-15%]* of the eligible customer market) as more eligible customers have terminated their public utility contract with effect from October 2005.
- (58) The old gas regime (under the old Hungarian gas act), now the regulated regime, consists of a vertical chain of exclusive supply/purchase relationships. The public utility wholesaler, MOL WMT, sells natural gas to the RDCs. The public utility

²³ See slide 41 of the Presentation “Natural Gas Market II” of the HEO, 26 July 2005.

²⁴ Article 36 of the HGA and Article 1(1) of the Eligibility Decree.

²⁵ Article 36(2) of the HGA.

²⁶ MOL presentation of 27 July 2005.

wholesaler is under an obligation, by law, to cover the full natural gas demand for public utility purposes of the RDCs, whereas the RDCs are under an obligation to source their natural gas needs for their public utility customers exclusively from the public utility wholesaler. To fulfil this obligation, the RDCs and MOL WMT have entered into long-term framework supply contracts, with duration from [...] years.²⁷ Detailed supply conditions and quantities are set in yearly contracts. The RDCs, the public utility suppliers, have in turn the exclusive right and obligation to supply the customers situated in their territory. MOL WMT also supplies directly certain large customers connected to the transmission network²⁸. The prices for the supply of natural gas and other services at the different levels of the vertical gas supply chain²⁹ are also heavily regulated³⁰.

- (59) In contrast with the public utility contracts, the relationship between the eligible customers that switched suppliers and their various possible commercial partners (traders, importers, etc.) is largely subject to the principle of contractual freedom.

Legal unbundling of the transmission network and storage facilities

- (60) Until end 2003, MOL owned and operated the entire high-pressure transmission network and all the underground storage facilities in Hungary. Since January 2004, the transportation network and the storage facilities have been legally unbundled from MOL WMT in two separate wholly-owned subsidiaries of MOL, MOL Storage and MOL Transmission respectively.

Distribution networks

- (61) The local medium and low-pressure distribution networks through which natural gas is distributed to the final customers (except those that are directly connected to the transmission network) are owned and operated by the RDCs. However, RDCs are not confined to mere distribution, since they also sell gas to eligible and non-eligible customers, as public utility suppliers and, in theory, as traders in the case of eligible customers having switched suppliers. Under the HGA, an RDC is entitled to have three licenses: distribution, public supply, and trading (on the open segment of the market). At this stage, there is thus no unbundling other than accounting unbundling between the different activities of the RDCs (distribution, supply as public utility supplier and supply as trader). In practice, however, most RDCs have set up a

²⁷ The contracts with [...] and [...] expire at [2005-2020]

²⁸ The public utility wholesaler is only entitled to supply for public utility purposes natural gas to a restricted number of customers which are listed in the licence of the public utility wholesaler.

²⁹ These services are the following: transmission, distribution, public utility storage, gas supply between the public utility wholesaler and the public utility suppliers (i.e., sales by MOL WMT to the RDCs), gas supply between the public utility suppliers, or in some cases the public utility wholesaler, and the public utility customers (i.e., sales by the RDCs or in some cases MOL WMT to residential customers and to non-residential eligible customers which have not switched suppliers).

³⁰ Pursuant to Article 48(2) HGA, the official price shall provide coverage for the costs of the assets that were part of a justified investment and the costs of efficient operation, and also the profit necessary for permanent operation. This is the so-called cost-plus principle.

separate company to be active as trader on the open segment of the market³¹, and none of the RDCs or their trading subsidiaries has any customers on the open segment of the market at this stage.

- (62) Under Directive 2003/55/EC, by July 2007 at the latest, the RDCs will have to split their activities into separate legal entities, one in charge of operation of the distribution network and the other one in charge of supply to end customers.

Licenses

- (63) It is one of the fundamental principles of the HGA that, for reasons of public interest, the performance of the gas related activities is subject to the *ex-ante* control of the HEO. The *ex-ante* control is performed by way of licensing. Under Articles 7 and 9 of the HGA, the following activities are subject to licensing: transmission (operation of the high-pressure transmission network), storage (operation of the five storage facilities located in Hungary), distribution (operation of the local distribution pipelines), trade, public utility wholesale, public utility supply (RDCs), establishment and operation of the organised gas market (gas exchange), system operation, and access to cross-border natural gas pipelines.
- (64) MOL Transmission is the transmission licensee and the system operation licensee, and MOL Storage is the storage licensee. MOL WMT holds a public utility wholesale license (for its supply of gas in the regulated segment of the market), a trading license (for its supply of gas in the open segment of the market), and two cross-border licenses (one as a gas trader, and one as a public utility supplier). The RDCs hold distribution licenses and public utility supply licenses (for their supply in the regulated segment of the market). The RDCs (or in some cases a separate subsidiary of the RDC) also hold trading licenses (for their supplies in the open segment of the market).
- (65) Thirteen entities currently have a natural gas trading licence in Hungary³². Seventeen entities currently hold a cross-border license (which is necessary to transmit natural gas through the cross-border transmission pipelines) in Hungary. These are the same entities as those holding a trading license, plus El Paso Kft., MOL Transmission, NITROGÉN MŰVEK Rt. (a customer of gas), and POGO Kft.

³¹ Édenenergia Kereskedelmi Kft., the separate joint trading subsidiary of the two RDCs of Gaz de France, ÉGÁZ and DÉGÁZ; Fővárosi Gázkereskedelmi Kft., the separate trading subsidiary of FŐGÁZ Rt. (RWE, E.ON and the Municipality of Budapest); and E.ON EK, the trading subsidiary of the E.ON group in Hungary (separate from E.ON's two gas RDCs, DDGÁZ and KÖGÁZ). TIGÁZ (Italgaz/ENI and RWE), however, holds a gas trading license itself.

³² MOL WMT, PANRUSGÁZ Magyar Orosz Gázipari Rt., Első Magyar Földgáz- és Energiakereskedő és Szolgáltató Kft. ("EMFESZ"), E.ON Energiakereskedő Kft. ("E.ON EK"), BC Energiakereskedő Kft., CENTREX Rt., DBGÁZ Kft., DUNAFERR Központi Beszerzési Kft., EURO-BRIDGE Kereskedelmi és Szolgáltató Kft., Édenenergia Kereskedelmi Kft. (a subsidiary of Gaz de France's two RDCs, ÉGÁZ and DÉGÁZ), ENERGY CAPITAL Energiakereskedő Kft., Fővárosi Gázkereskedelmi Kft. (a subsidiary of FŐGÁZ Rt.), and TIGÁZ Rt. (a subsidiary of Italgaz/ENI).

Access to the gas networks and to storage

- (66) Under the HGA, the system operator (to the extent it is necessary to ensure the stability of the system), the public utility wholesaler, the public utility suppliers, the traders, the gas producers (to the extent of their production) and the eligible customers (to the extent of their own consumption) have a right of Third Party Access (“TPA”) to the free capacities in the transmission³³, distribution³⁴ and storage³⁵ systems. Access must be granted on a non-discriminatory basis to all operators³⁶.
- (67) It is a fundamental principle pursuant to Article 30(6) of the HGA that free capacity may only be booked on the basis of a confirmed customer demand. The HGA thus expressly envisages a system whereby capacity reservation is directly linked to actual gas demand. As a consequence, capacity without underlying customer demand cannot be subject of trade on its own right. This, for the time being, excludes any secondary trading of capacity rights.
- (68) The HGA provides for a priority order in the allocation of capacities for transmission, distribution and storage of gas. Pursuant to the HGA, first the system operator for the balancing of the network, then the suppliers of residential customers and so-called “communal customers” specified in separate regulations (e.g., customers which are active in the public field of military, healthcare, education) enjoy priority over all the other infrastructure users. The exact rules regarding the customers enjoying priority are set out in the Executive Decree and Decree No. 81/2003 of the MET.
- (69) As regards the allocation of cross-border, transmission, distribution and storage capacities, the Hungarian gas regulation differentiates between (i) already allocated capacity, and (ii) free capacity, for which a new capacity booking may be requested.

³³ Article 30(1) HGA specifically obliges the transmission licensee to provide access to the free capacity of the system in its usage in return for a fee to (i) the public utility wholesaler, (ii) the traders, (iii) the eligible customers to the extent of their own usage, (iv) the natural gas producers to the extent of their gas production, and (v) the system operator to the extent that is necessary to ensure the stability of the system.

³⁴ Pursuant to Article 30(4), the distributor licensee shall provide access to the network in its usage in return for consideration to the (i) RDCs, (ii) the traders, (iii) the eligible customer to the extent of its own usage, and (iv) the natural gas producer to the extent of the gas produced by itself.

³⁵ Under Article 30(2) and (3) the storage licensee is obliged to provide access to the free capacity of the system in its usage in return for consideration to the system operator to the extent that is necessary to ensure the stability of the system. If, having fulfilled the needs of the system operator, the storage licensee still has free capacity, it is obliged to provide access on open, transparent and non-discriminatory commercial conditions in return for consideration to (i) the public utility wholesaler, (ii) the eligible customers to the extent of their own usage; and (iii) traders.

³⁶ Article 30(5) of the HGA stipulates that the conditions for access may not include any unjustified discrimination, may not give ground for any abuse, may not include any unjustified restriction and may not endanger the safety and quality of supplies. According to Article 31 of the HGA, access to transmission and distribution networks or to storage may be refused if (i) the free capacity for the satisfaction of demand is missing, (ii) the access would impede the supply of gas to priority customers, (iii) there is a serious malfunction or crisis in the co-operative gas system or (iv) the quality of the gas to be put into the system does not comply with the minimum qualitative requirements set out in the Network Code.

In accordance with Article 1(30) of the Executive Decree, the capacity which is covered by an agreement for the supply of gas (contracted or allocated capacity) is already allocated capacity, the rest is free capacity. Existing capacity demands (already allocated capacity) have priority over new demands. If the demand for free capacities exceeds the amount of free capacities actually available, the free capacities are allocated through an auction³⁷. There are special and detailed capacity booking rules for eligible customers exiting the public utility market (see below in recitals 73 to 79).

- (70) The amount of free capacities is defined on a monthly basis. MOL Transmission, the transmission licensee, is required to publish on its website the available capacities for each entry and exit point of the transmission system³⁸.
- (71) Competitors of MOL WMT and the RDCs (on the open segment of the market) have a right of TPA to the transmission and distribution networks, which are natural monopolies, at regulated tariffs³⁹. The access to storage capacities is only regulated in respect of MOL WMT as a public utility wholesaler⁴⁰ (*i.e.*, as regards the supply of households and eligible customers which have not switched to the open segment of the market). The fees for access to storage in the open segment of the market are negotiated, *i.e.* set by individual agreement between the user of the storage (including MOL WMT as a trader) and the storage licensee.
- (72) Capacities at the two cross-border entry points (Beregovo at the Ukrainian/Hungarian border and Baumgarten at the Austrian/Hungarian border) and for storage are booked (contracted) for a gas year⁴¹. Since the beginning of 2005, the amended grid code allows capacity reservation agreements for a longer duration. According to the parties, there are currently [...]*. It is also possible to book capacity for shorter (monthly) periods but the fees in this case are much higher.

³⁷ Point 5.1.3.1 (g) of the Network Code.

³⁸ Article 5.1.3.2 (a) of the Network Code. The capacities to be published are the maximum daily (in m³/day) and hourly (in m³/hour) technical capacities; the hourly and daily capacities already booked by system users; and the available capacities. They must be published 12 months in advance, in monthly breakdowns, and updated every month. The method used by the transmission licensee to determine free capacities must be approved by the HEO and is also published on the website. *See* slides 37 and 38 of the presentation of HEO “Hungarian Gas Market II”, 26 July 2005; response of E.ON to Question 4 of the request for information of 29 June 2005.

³⁹ On the open segment of the market, the system operation fee, the transmission fee and the distribution fee are normally paid by the gas trader to the system operation, transmission, and distribution licensees, and then passed on to the eligible customer by the trader.

⁴⁰ It should be noted that RDCs are not entitled to book for and obtain free capacities in the Hungarian storage system for their public utility supply (but they can book storage capacities to supply customers on the open segment of the market).

⁴¹ The gas year runs from 1 July to 30 June for transport; and from 1 April to 31 March for storage.

Customer-driven capacities along the gas supply chain

- (73) As indicated, there are special and detailed rules for capacity booking for eligible customers exiting the public utility market. The capacities used by these eligible customers in the public utility market are considered to be already allocated capacities, to which the customers remain entitled even after switching to the open segment of the market. Pursuant to Article 36(7) of the HGA and Article 3(4) of the Eligibility Decree⁴², when an eligible customer leaves the public utility sector, it is entitled to “take along” all the cross-border, transmission, distribution and storage capacities that it was using as a public utility customer⁴³. In other words, the capacities follow the customer, as long as the underlying demand of the customer subsists.
- (74) The purpose of this provision is to ensure that eligible customers are entitled to adequate background capacities from the system even after switching. The “already allocated capacities” only serve as a base demand for the capacities for eligible customers. They can vary in accordance with the actual demand of a customer (for example a customer may not want to have storage capacities, but rather to book more import capacities, or the customer’s gas consumption may increase at a later stage). These variations are treated as a demand for new capacities.
- (75) Essentially this system, the parties argue, can be described as a “customer-driven system”, that is to say that capacities (at all levels of the supply chain) automatically follow the customers switching supplier. This principle is also encapsulated, according to the parties, under Article 30(6) of the HGA and Article 32(11)-(12) of the Executive Decree which prescribes that cross-border, transmission, distribution and storage capacities may be booked, and later on held, by any licensee (or eligible customer) only on the basis of “confirmed customer demand” (or to the extent of its own demand). Article 32 (13) of the Executive Decree defines the term “confirmed customer demand” as the demand already covered by an agreement or a pre-contract (in the case of an eligible customer, it is defined on the basis of the business plan of the given customer).
- (76) The very detailed technical and administrative rules of the “customer-driven system” are contained in the Network Code (Chapter 5.1. of the Network Code). Of special relevance is the methodology for calculating for a given customer the already allocated capacity at the entry points of the transmission system (namely the storage

42 Article 3 (4) of Eligibility Decree provides as follows: “The registered eligible customer is entitled to the transmission, storage, distribution and cross-border capacity to the extent that is reserved in the public utility contract even after the termination of the public utility contract. The rules for the determination of this capacity are contained in the Network Code. This capacity is not deemed to be a demand for a new capacity reservation.” See also point 5.1.2 of the Network Code.

43 The public utility wholesale licensee (MOL WMT public utility arm) and the public utility supply licensees (the RDCs) are under an obligation under Article 32 of the Executive Decree to reduce the level of booked transmission, distribution and storage capacities with the decrease of demand as a result of eligible customers switching to gas trader licensees. This is furthermore mirrored in Article 3(5) of the Eligibility Decree which provides that the public utility wholesale licensee and the public utility supply licensees are entitled to amend, without any negative consequences, such as contractual penalties, their capacity reservation agreements with the transmission, storage and distribution licensees, if and provided that the reason for such amendment is the switching of supplier by eligible customers and thus certain capacities becoming free.

and cross-border capacities)⁴⁴. It is important to note that the basis for this calculation is the off-take (exit) capacity booked for the customer in the previous gas year, which is higher than the entry capacity booked by the public utility wholesaler for the customer as the public utility wholesaler could benefit from synchronicity, but an individual customer cannot⁴⁵. This means that the eligible customer switching to the open segment of the market is allocated import capacity equal to its off-take capacity at the exit point.

- (77) As regards cross-border capacity more specifically, Point 5.1.2 c) ii of the Network Code provides that this capacity shall be allocated as a maximum of 80% on the Beregovo entry point (East) and a minimum of 20% on the Baumgarten entry point (West). According to the parties, this 80-20 rule is designed to divide import capacities among the entry points reasonably, but respondents in the market investigation have stressed that this rule is difficult to satisfy for new entrants and constitutes a barrier to entry.
- (78) The already allocated capacity is capacity to which the customer is entitled, and which can serve as a base demand. This does not mean that the new supplier has the obligation to use the capacity to which it is entitled and which is calculated in accordance with the above-described formula. However, any other capacity request is treated as a demand for new capacity. Thus, if the cross-border capacity according to the allocation 80% Beregovo and 20% HAG does not correspond to the capacity needed where the new supplier has access to gas, the new supplier will have to request additional cross-border capacity. This request will be treated as a demand for new capacity, which has a lower priority level. This may not be so much a problem at the HAG entry point where there is some free capacity, but it is a problem at Beregovo where there is congestion.
- (79) The “capacity follows the customer” principle only applies to the allocation of the capacities used by existing customers switching to the open segment of the market, but not to the allocation of free capacities to new customers (for example, a new industrial plant consuming natural gas). As pointed out by the HEO, this is a problem for new customers without previous gas consumption⁴⁶.

⁴⁴ Point 5.1.2 of the Network Code.

⁴⁵ The synchronicity factor results from the fact that peak capacity demands at the exit points arise at different times for different customers. This means that the peak capacity at the entry point that a supplier with a large portfolio of customers must book (aggregated peak capacity of all the customers) is less than the sum of the peak capacities at booked at the exit points. For example, a synchronicity factor of 0.97 could be calculated for the 2005-2006 gas year. See slides 22-32 of the presentation of the HEO “Hungarian Natural Gas Market II” on 26 July 2005.

⁴⁶ See slide 32 of presentation “Hungarian Natural Gas Market II” of the HEO on 26 July 2005.

b. Evolution of the regulatory framework

- (80) It is not clear at this stage how the Hungarian hybrid model will evolve in the future. The HEO is expected to publish a proposal for a new model for the gas market in the fall of 2005. A new model for the electricity market was recently published for public consultation on the website of the HEO (See Electricity section below in recitals 181 to 207).
- (81) All Hungarian market players generally expect that in July 2007, when all residential customers become eligible, the current system of public utility supply (and thus the hybrid model) will disappear and be replaced with a Universal Service Provider (“USP”) concept for residential customers and some small non-residential customers which have not concluded a supply contract with a specific supplier. Such USPs would be appointed through an open competitive tender by the HEO and would have the competence to supply the relevant customers throughout Hungary at a regulated price. All other customers would be forced to enter the open segment of the market. This market model would be very similar to the HEO’s recommendation for the new electricity market model.
- (82) As a result, the public utility wholesaler function of MOL WMT and the public utility supply function of the RDCs would disappear. MOL WMT and the RDCs would operate purely as holders of trading licenses on the open segment of the market. The RDCs may also operate as USPs (if issued a USP operational license as a result of a successful tender). The obligation of RDCs to purchase gas exclusively from MOL WMT would also end.
- (83) The Commission notes that, in their reply to the SO, the parties did not challenge the description made in the SO of the future evolution of the regulatory framework for the Hungarian gas sector and its timetable. The expert report submitted by the parties notably confirms that *“The Hungarian government has disclosed its intention to remove the price cap in the natural gas sector”*.

c. The resolution of the HEO

- (84) Under Article 52 of the HGA, the HEO must approve the acquisition of a controlling shareholding in any licensed undertaking and the exercise of the associated rights. The HEO may refuse the approval or may impose conditions if the transaction would endanger the security of the natural gas supply, the performance of the licensed activities as well as the regulations applicable to the prices and quality of service in transmission, storage, distribution, system operation or public utility supply activities. The HEO may also refuse to approve the transaction if, as a result of the transaction, the licensee is not able to satisfy the requirements for licensing set out in the HGA.
- (85) On 27 June 2005, the HEO adopted a resolution approving the acquisition of certain gas businesses of MOL by E.ON, subject to eight conditions. It is only once E.ON has fulfilled these conditions (or submitted an irrevocable guarantee in respect of their fulfilment) and the HEO has adopted a second resolution approving such completion, that ERI will be allowed to exercise its shareholder’s rights.

(86) These conditions can be substantively summarized as follows:

- Condition 1: The HEO required the legal and organizational unbundling of the public utility wholesale and the natural gas trade activities of MOL WMT by 31 May 2006;
- Condition 2: E.ON is required to submit an implementation plan to the HEO regarding certain organizational changes to be undertaken at MOL WMT and MOL Storage. The HEO in particular emphasized the independence of the management of the respective companies and of certain joint services to the companies (data processing, controlling, etc.);
- Condition 3: E.ON is required to make the public utility wholesaler submit for approval and execute a programme to ensure the securing of natural gas resources and on the safety of supply in Hungary for a mid-term period. The HEO also outlined the main elements of such a programme (sufficient amounts, rules for auction, etc.);
- Condition 4: E.ON is required to ensure that the public utility wholesaler does not expand the scope of its customers directly supplied via the transmission network (excluding communal customers);
- Condition 5: E.ON and MOL Storage are required to implement a gas storage development scheme for 2005-2009, to be approved by the HEO. The HEO also required E.ON to declare by 31 May 2006 whether it undertakes the development obligations to be set out in the forthcoming development directive issued by the HEO. In case E.ON undertakes these development obligations, it will have to ensure that MOL Storage amends and submits the development plan accordingly;
- Condition 6: E.ON is required to ensure that MOL Storage will apply regulated access for all system users, i.e. also in the open segment of the market, until real competitive market situation between natural gas storages takes place, and to comply with the GGPSSO. E.ON is required further to ensure that MOL Storage amends and submits its general business terms accordingly by 31 May 2006;
- Condition 7: E.ON is required to ensure that MOL Storage revises and confirms its qualification granted by the Hungarian Mining Office, unless E.ON can ensure that the acquisition does not affect such qualifications (whereby a declaration has to be made in this regard);
- Condition 8: E.ON is required to initiate the amendment of the HEO's decision in case the decision to be issued by the Commission regarding E.ON's notification of the planned acquisition would affect the HEO's decision within 30 days after the receipt of the Commission's decision. In case the Commission's procedure is not closed by 31 March 2006 with a final and binding decision, or if the prolongation of the competition procedure significantly hinders or makes impossible the fulfilment of the obligation by E.ON, the latter may request the HEO to amend the 31 May 2006 deadline set for the fulfilment of the conditions contained in the decision.

(iii) *Relevant product markets*

- (87) In the Form CO, the parties have taken the view that the following activities are relevant to the proposed concentration, and constitute distinct product markets:
- Procurement (import and domestic production) of natural gas for onward wholesale and sale into the Hungarian market;
 - Wholesale of natural gas to the RDCs on the regulated segment of the market;
 - Sale of natural gas to eligible customers, distinguishing between (i) large power plants over 50 MW and (ii) industrial/commercial customers including smaller power plants;
 - Sale of natural gas to residential (non-eligible) customers;
 - Storage of natural gas; and
 - Transmission of natural gas.
- (88) The Commission has in the past identified the following activities as distinct product markets in the natural gas sector:
- Exploration and production;
 - Transmission (via the high-pressure pipeline grid);
 - Distribution (via low-pressure pipeline grids);
 - Storage; and
 - Trading and supply.
- (89) As regards gas supply activities, following the opening of competition of the European gas markets, the Commission has also drawn distinctions between eligible and non-eligible customers, and between customers according to their annual gas consumption and their type of activity (*e.g.*, power plants).
- (90) On the basis of the past practice and the investigation in this case, the Commission considers that the following product markets are relevant for the assessment of the present transaction:
- Gas infrastructure operations⁴⁷, including the transmission of gas, the distribution of gas and the storage of gas;
 - Supply of gas, including (i) the supply of gas to traders; (ii) the supply of gas to the RDCs; (iii) the supply of gas to large power plants; (iv) the supply of gas to large industrial customers; (v) the supply of gas to small industrial and commercial customers; and (vi) the supply of gas to residential customers⁴⁸.
- (91) This delineation of the relevant product markets in the gas sector only differs from the market delineation proposed by the parties as regard the combination of gas

⁴⁷ There are distinct infrastructures for the supply of the low-calorific gas (2/H gas) and inert gas, produced solely in Hungary, which may lead to the definition of separate product markets. However, these two qualities of gas only represent [0-5%]* and [0-5%]* of total Hungarian consumption, respectively. The Commission has therefore not further developed its analysis in this respect.

⁴⁸ The supply of gas to traders, RDCs and large customers is often referred to as “wholesale” supply, while the supply of gas to small customers is referred to as “retail” supply.

procurement and wholesale and the distinction between the market for gas supply to small industrial and commercial customers and the market for gas supply to large industrial customers. The parties did not contest the definition of the relevant product markets in the gas sector in their reply to the SO.

- (92) The market investigation has confirmed that the supply of gas to eligible customers should be further segmented in various product markets according to categories of customers due to distinct consumption profiles and supply conditions. The market investigation has shown that different categories of customers have different consumption patterns (quantities and consumption profile) and different flexibility needs. They are also characterized by different marketing approach from gas suppliers. MOL WMT itself distinguishes in its commercial and marketing organisation the following categories of customers: (i) RDCs; (ii) industrial customers; and (iii) power plants.
- (93) By contrast, the Commission investigation has indicated that the following three criteria are not relevant for market definition in this case:
- (94) First, the market investigation has confirmed the parties' view that, despite the current hybrid model, there should be no distinction between the regulated and open segments of the market. Eligible customers can easily switch back and forth between the free and the regulated segments of the market. Switching does not entail any significant costs or time for eligible customers and the recent amendments to the HGA have even made switching easier⁴⁹. Hence, the distinction between gas customers that have switched to another gas supplier and customers that remain in the public utility segment is not relevant for the definition of the relevant product markets.
- (95) Secondly, it does not appear relevant to distinguish customers depending on whether they are connected to the transmission network or to a distribution network. This makes a difference on the regulated segment of the market, as customers connected to the transmission network are directly supplied by MOL WMT, while those connected to the distribution networks can only be supplied by their local RDC. However, on the open segment of the market, traders (including MOL WMT as trader) compete to gain customers connected both to the transmission and distribution networks (and the transport and distribution fees are anyway pass-through fees for a gas supplier). While customers connected to the transmission network tend to be large or very large customers, there are also large customers connected to the distribution networks⁵⁰.
- (96) Thirdly, the market investigation has shown that prices may not be an appropriate factor to identify the distinct categories of customers, as only few customers have switched to a supplier on the open segment of the market in Hungary up to now.

⁴⁹ Pursuant to the amended Article 36 of the HGA, eligible customers can now terminate their public utility contract at any time with effect on the first day of the fourth month following, and can request their RDC or the Public Utility Wholesaler to switch back to the regulated market at any time with effect on 1 July of the following year. The parties may agree on different dates.

⁵⁰ Minutes of the meeting of 26 July 2005 with the HEO: "*Customers connected to the transmission are not that different from those connected to the distribution networks. This is more a question of location than size and industry. Some of the companies were built historically close to the transmission network.*"

Gas prices paid by different categories of eligible customers are thus still set in accordance with the categories set out in the price decrees, namely: (i) residential customers; (ii) customers with a consumption below 20 m³/hour; (iii) customers with a consumption of 20-100 m³/hour; (iv) customers with a consumption of 100-500 m³/hour; and (v) customers with a consumption exceeding 500 m³/hour.

a. Infrastructure

Transmission of gas

- (97) Consistently with previous Commission's decisions⁵¹, the parties have identified the transport of natural gas through high-pressure network of natural gas as a relevant product market. This approach has not been contested by the market investigation. Therefore, the Commission concludes that gas transmission constitutes a relevant product market for the purpose of this case. The transmission of gas constitutes a natural monopoly.

Distribution of gas

- (98) In previous decisions, the Commission has identified the distribution of natural gas through low- and medium-pressure networks as a relevant product market. The parties have not identified gas distribution as a relevant product market in their submission. However, the Commission takes the view that gas distribution constitutes a relevant product market for the purpose of this case⁵². The distribution of gas constitutes a natural monopoly.

Storage of gas

- (99) In previous decisions, the storage of natural gas has been consistently defined by the Commission as a distinct product market⁵³. The parties have also identified this activity as a relevant product market. This approach has not been contested by the market investigation. Therefore, the Commission concludes that gas storage constitutes a relevant product market for the purpose of this case.

b. Supply of gas

- (100) The procurement of natural gas for wholesale and sale into the Hungarian market which the parties have defined as a separate market is in reality the upstream activity of a gas wholesaler/importer which purchases gas from domestic or foreign producers or traders for onward sale to end users or traders⁵⁴. Procurement is therefore a pre-requisite to be active on the wholesale/retail supply of gas. This has been confirmed by the views of market players. The parties did not contest this approach in their reply to the SO.

⁵¹ See, inter alia, Commission decision of 8 October 2004 in Case COMP/M.3410 – Total/Gaz de France.

⁵² In Hungary, gas distribution networks are owned and operated by the RDCs.

⁵³ See, inter alia, Commission decision of 8 October 2004 in Case COMP/M.3410 – Total/Gaz de France.

⁵⁴ See, notably, the response of MVM to question 8 of the request for information of 3 June 2005.

Supply of gas to traders

- (101) In previous cases, the Commission has identified the supply of gas to traders as a separate product market. The market investigation has confirmed that there exists a separate product market for the supply of gas in Hungary, on which importers/producers sell gas to traders, and traders sell each other gas, for onwards supply on the open segment of the market. However, the market investigation has also indicated that, under the current regulatory framework, this market only exists marginally in Hungary, in light of the fact that (i) the open segment of the market has not developed much yet and there is little liquidity on the open segment of the market; and (ii) gas RDCs still have an obligation to purchase their gas requirements for public utility purposes exclusively from MOL WMT.
- (102) The Commission concludes that the supply of gas to traders constitutes a relevant product market for the purpose of this case.

Supply of gas to RDCs

- (103) Under the current regulatory framework, the public utility wholesaler (MOL WMT) has the exclusive right and also the obligation to supply the RDCs for their natural gas needs for public utility purposes (i.e., sales to non-eligible residential customers and eligible customers that have not switched to alternative suppliers) according to their demand. The RDCs have, in turn, an exclusive purchase obligation vis-à-vis the public utility wholesaler in respect of their natural gas demand for public utility purposes (no such exclusive purchase obligation exists in respect of the RDCs for their gas demand for the supply by them of eligible customers). Prices of the public utility wholesaler's to RDCs are regulated.
- (104) Thus, the supply of gas to RDCs constitutes a relevant product market for the purpose of this case. This market is not open to competition.
- (105) However, the gas regulatory framework is expected to change at the latest in July 2007. RDCs will be required to legally separate their supply activities and their distribution activities by July 2007 pursuant to Directive 2003/55/EC. RDCs will remain active in the supply of gas to end users as gas traders, through their trading subsidiaries already established as separate legal entities. RDCs could also be appointed as Universal Service Providers (for the supply of residential and some other small customers at regulated prices). It is expected that USPs will be free to choose their gas supplier.
- (106) Thus, under these assumptions, the market for the supply of gas to RDCs would cease to exist as a separate market from the market for the supply of gas to traders at the latest in July 2007.

Supply of gas to large power plants

- (107) The market investigation has shown that large power plants constitute a specific category of gas customers, and that the supply of gas to large power plants is a distinct product market.
- (108) Two types of gas-fired power plants may be distinguished. Conventional gas-fired power plants only produce electricity, and emit the heat created as a by-product of

electricity generation into the environment through cooling towers, as flue gas, or by other means. Cogeneration plants (or “combined heat and power” (CHP) plants) simultaneously produce electricity and heat. Cogeneration plants capture the excess heat for domestic or industrial heating purposes, either very close to the plant, or distributed through steam pipes to heat local housing (“district heating”). A cogeneration plant cannot produce heat without electricity and vice versa.

- (109) “Combined cycle gas turbine” (“CCGT”) plants can function as a conventional power plant (in which case the heat is only re-used to improve the efficiency of the power generation process) or as a cogeneration plant (in which case, the heat is used partly to improve efficiency of the power generation process and partly for domestic and industrial heating purposes as a cogeneration plant).
- (110) The consumption size and consumption profile of conventional and cogeneration power plants are similar. The main difference is that it is the demand for heat that is driving the generation of electricity in cogeneration plants, i.e. cogeneration plants are driven by the consumption of heat by the network, while electricity demand determines the operation of conventional power plants.
- (111) The market investigation has clearly indicated that large power generators constitute a customer category with unique demand requirements in terms of gas quantities and consumption patterns. In particular, according to Magyar Villamos Művek Rt. (“MVM”), the electricity public utility wholesaler in Hungary:

*MVM: “The gas consumption of power plants is much more significant than the consumption of any other eligible customer. They have a different consumption profile too. Cogeneration plants (heat/electricity production) have important peaks in winter and low consumption in the summer. The conventional power plants involved in the system balancing have also various consumption features within the same day.”*⁵⁵

- (112) Large power plants are the largest consumers of natural gas in terms of quantities. For example, the Dunamenti plant of Electrabel consumes [1-1.5] bcm of gas annually, which alone represents [10-15%] of the total Hungarian gas market. In addition, fluctuations of their demand are very high and reflect the variations in the power plants’ level of activity.
- (113) The market investigation has shown that since the opening of the Hungarian gas market to competition none of the large power plants has been able to find alternative suppliers to MOL WMT or their local RDC on the open segment of the market. This is due to the fact that their gas consumption is so large that it is not possible at this stage to purchase such large quantities of gas on the Hungarian free gas market (under the current regulatory framework, it is also not possible for large power plants to switch to the open segment of the market for only part of their needs). This is even more so for the power plants which provide balancing energy (the Electrabel Dunamenti, ATEL and AES power plants) and for cogeneration plants whose consumption is even more variable and cannot be predicted.

⁵⁵ Response of MVM to Question 11 of the request for information of 3 June 2005 (free translation).

- (114) Suppliers of large power plants must be in a position to ensure the security of supply for a long term (power plants' gas supply contracts are [...]*) and they need a critical size to be able to bear the huge variations in consumption of these power plants. EMFESZ notes that it is very difficult to supply power plants as they are regulated by the Hungarian electricity dispatcher. Their gas consumption is very variable: it may go from 100,000 m³ one hour to 20,000 m³ the next hour, and then 50,000 m³⁵⁶.
- (115) The parties have proposed to distinguish between large and small power plants on the basis of a 50 MW threshold for installed electricity production capacity. While the market investigation has suggested that this criterion (which is based on the different licensing requirements for large and small power plants⁵⁷) may be artificial, it has not provided indications that alternative criteria (such as the actual gas consumption of the power plants) may be more appropriate to distinguish large and small power plants. Therefore, the Commission takes the view that the supply of gas to large power plants with an installed electricity production capacity above 50 MW is a relevant product market for the purpose of this case.

Supply of gas to large industrial customers

- (116) The market investigation has revealed that it is relevant to distinguish between small and large industrial customers, due to distinct consumption profiles and commercial relationships. In particular, the category of large customers is specifically targeted by new entrants⁵⁸. In view of the current stage of development of the Hungarian gas market (with very few customers that have actually switched suppliers), the most appropriate consumption threshold to delineate large and small industrial customer is not clear-cut. However, market players have suggested that large customers are those with an hourly consumption exceeding 500 m³/hour (which corresponds to an annual consumption of close to 2 million m³). According to these respondents, customer with hourly consumption above 500 m³/hour have a more "sophisticated" relationship with their gas supplier, which implies for instance a different daily nominations regime and different flexibility clauses. Such large customers are usually attended by key account managers.
- (117) In any case, small power plants (conventional plants and cogeneration plants) as well as other heat producers (using gas-fired boilers) should belong to the category of large industrial customers. Most industrial customers using gas in their industrial process are also considered as large customers in view of the importance of their gas purchases.

⁵⁶ Minutes of the meeting with EMFESZ of 28 July 2005.

⁵⁷ Article 51 of the Hungarian Electricity Act required a license to establish and operate power plants with a capacity exceeding 50 MW, although but this difference will partially disappear following the recent amendments of the HEA which will also apply a similar licensing requirement to plants over 0.5 MW.

⁵⁸ [...]*; a third party active in gas has also indicated that "*We are targeting mainly large industrials and power plants because they are the most prepared clients for the free gas market (capability of nomination, daily consumption management, etc.) and they are the most demanding customers who request from their GDC free market offers as well. Large clients are specific customers with specific interests and demand; it is not possible to standardize their offers.*"

- (118) The Commission concludes that the supply of industrial gas customers with an hourly consumption over 500 m³/hour constitutes a separate relevant product market for the purpose of this case. While the consumption threshold of 500 m³/hour is most appropriate on the basis of the information available to the Commission, it may be subject to changes with the further opening of the gas supply markets.
- (119) In their reply to the SO, the parties did not contest the existence of a specific relevant product market for the supply of gas to large industrial customers.

Supply of gas to small industrial and commercial customers

- (120) In view of the above market definition for large industrial customers, the supply of gas to industrial and commercial customers with an hourly consumption below 500 m³/hour constitutes a separate relevant product markets for the purpose of this case.
- (121) From a supplier's perspective, there are a number of specificities in supplying these customers. The large number of locations and customers requires customer portfolio management tools. Suppliers develop standardized general offers for these customers as well as special offers such as dual offers for electricity and gas. Brand image plays a more important role for small industrial and commercial customers and they are generally less inclined to switch suppliers⁵⁹.

Supply of gas to residential customers

- (122) In previous decisions, the Commission has defined a separate product market for the supply of gas to residential customers. Under the current regulatory framework in Hungary, residential customers are not yet eligible and can only purchase gas from their local RDCs at regulated prices. Therefore, the supply of gas to residential customers constitutes a relevant product market for the purpose of this case. This market is not yet open to competition.
- (123) When residential customers become eligible, in July 2007, it is unclear at this stage whether they will be part of the same product market as small industrial and commercial customers or whether they will be part of a distinct relevant product market.
- (124) In any case, for the purpose of this case, the question of whether gas supply to residential customers will constitute a distinct product market in 2007 or whether residential customers will belong to the same product market as other small industrial and commercial customers can be left open.

(iv) Relevant geographic markets

- (125) The parties submit that all affected markets are national in scope, with the exception of the market for the supply of gas to residential customers which is sub-national (i.e., a specific region in Hungary) in scope. The market investigation carried out by the Commission has broadly confirmed this approach. The market investigation has

⁵⁹ See notably EDF response to questions of the Commission of 11 August 2005.

nevertheless shown that the market for the supply of gas to residential customers will also be national when residential customers become eligible in July 2007.

a. Gas infrastructure

Transmission of gas

- (126) The Hungarian gas transmission network is owned and operated by MOL Transmission at the national level. Therefore, the market for gas transmission is national in scope.

Distribution of gas

- (127) The Hungarian gas distribution networks are owned and operated by the RDCs. Therefore, the gas distribution market is sub-national in scope and each of the distribution grid regions constitutes a relevant geographic market.

Storage of gas

- (128) The parties submit that the market for gas storage is national in scope due to the existing regulatory framework and the organisation of the storage facilities at the national level. Although some respondents to the market investigation have highlighted that storage services for gas wholesale or retail activities in Hungary could technically be provided by storage operators located in neighbouring countries, the market investigation has also shown that the limited availability of cross-border pipelines⁶⁰ anyway makes the use of foreign gas storage facilities difficult for Hungarian operators under current market conditions⁶¹.
- (129) This is confirmed by the fact that market players currently active in gas supply only use exceptionally gas storage facilities in foreign countries. In 2003, MOL WMT used only [450-700]* million m³ of gas storage in Ukraine (Bogorodscany), compared to [2-5]* bcm in Hungary. EMFESZ does not use gas storage facilities outside of Hungary.
- (130) The Commission therefore concludes that the geographic scope of the gas storage market is indeed national in scope. The Commission notes that the geographic scope of the gas storage market may become broader than national with the further liberalisation of the European gas markets.

⁶⁰ As already indicated, capacities booked by MOL WMT for the gas year 2004/2005 were [10-12]* bcm/year and [25-35]* million m³/day (out of 15.01 bcm/year and 41.3 million m³/day) at Beregovo and [1-4]* bcm/year and [6-10]*million m³/day out of 4.5 bcm/year and 12.3 million m³/day at the HAG entry point. In addition, a transit capacity of [3-6]* bcm/y and [10-13]* million m³/day are booked at the Beregovo entry point by the Serbian company Nis and the Bosnian Herzogovinan company BHGas for transit.

⁶¹ Market players using gas storage in foreign countries would have to import more gas in peak period, which might prove difficult in view of the limited available capacity at entry points in Hungary.

b. Supply of gas

Supply of gas to traders

- (131) The parties submit that this market is national in scope. According to the parties, companies active on the market for the supply of gas purchase gas from foreign or domestic gas producers (or their intermediaries) for onward sale in Hungary. Thus, the relevant geographic market is defined by the destination of the product, which is the Hungarian gas markets⁶².
- (132) During the market investigation, some respondents have stressed that gas is procured by MOL WMT and EMFESZ from international companies (such as Gazprom, E.ON, GDF, etc.) and is commonly traded at the European level, including Russia. Therefore, the supply side (procurement) of the wholesale supply of gas is clearly international in scope. This activity is however carried out for Hungarian market players which source gas for onward sale in Hungary and pursuant to the regulatory framework set in the HGA. Competition is therefore taking place at the Hungarian level, as gas imported into Hungary is not re-exported⁶³ and is solely intended to meet Hungarian demand.

E.ON⁶⁴: “It is important to note that there are no exports from Hungary to third countries (...). The natural gas that enters Hungary serves import purposes.”

- (133) The market investigation has clearly confirmed the parties’ views. Accordingly, the Commission agrees with the parties that the geographic scope of the market of gas supply to traders is national.

Supply of gas to RDCs

- (134) Under Hungarian law, RDCs have to procure gas for public utility purposes from the public utility wholesaler, MOL WMT. The market for gas supply to the RDCs for public utility purposes is therefore national in scope.

Supply of gas to large power plants/large industrial customers/small industrial and commercial customers

- (135) The parties’ view is that the market for the supply of natural gas to eligible customers is national because (i) there are no restrictions as to the territories where an eligible customer may purchase its gas needs from when switching from its RDC, and for customers remaining with their respective RDCs, conditions of competition are regulated and similar across Hungary; (ii) there is a regulated access to the entire network in Hungary, which customers and traders may access from any exit point all around Hungary; and (iii) traders are in fact active in approaching customers located all around Hungary, regardless of the location of the customers and gas transport in Hungary is governed by a “stamp tariff system” (i.e., the cost of transport is always

⁶² Form CO, p. 110

⁶³ Except gas transit.

⁶⁴ Form CO, p. 96.

the same independently of the distance of the transport and the location of the customer).

- (136) This approach is consistent with the Commission's previous decisions⁶⁵, which generally considered the various markets for the supply of gas as national in scope. The market investigation has also confirmed that under the current regulatory framework competition takes place at a national level for eligible customers. The regulation is national, in particular as regards TPA to the transmission and distribution networks and to storage facilities. Traders do not privilege any specific geographic area within Hungary. As regards access to the transmission network in particular, Hungary constitutes a single balancing zone and under the new entry/exit fee system (introduced in July 2005 to replace the stamp tariff system), the tariff is the same for all points in Hungary. A third party active in the gas sector has stated:

“The applicable regulation allows eligible customers that have decided to exit the regulated market to choose their supplier, and the latter can conduct its business in the whole country. Moreover, conditions of access to the transmission network are the same all over the country and prices are established at the national level. The supply of gas to eligible customers is therefore a nationwide business.”

“Due to the different transformation levels of the liberalisation directives into national laws different national regulatory frameworks do exist. These different regulatory frameworks have an impact on access to transport/distribution networks, to storage facilities and of course lead to different price levels in different European States.”

- (137) After 2007, neither the parties nor the market investigation have provided any indication that the markets for supply of gas to eligible customers would become broader.
- (138) In conclusion, the different markets for the supply of gas to the three categories of eligible customers mentioned above (large power plants; large industrial customers; and small industrial and commercial customers) are national in scope.

Supply of gas to residential customers

- (139) Under Hungarian law, residential customers are obliged to procure gas from their local RDC and are not entitled to switch to traders on the open segment of the market. Therefore, the geographic scope of the market for the supply of gas to residential customers is sub-national in scope and each of the distribution grid regions constitutes a relevant geographic market.
- (140) After 2007, residential customers will be able to switch suppliers. The market for the supply of gas to residential customers will therefore acquire a national dimension for the same reasons as the other markets for the supply of gas to end users. The market investigation has largely confirmed this⁶⁶.

⁶⁵ Case COMP/M.3440 ENI/EDP/GDP.

⁶⁶ “As soon as residential customers will become eligible, this regional approach will end, as the customer will be able to decide which supplier / trader he/she should sign up”, Pannonpower's reply to the Commission's first phase questionnaire.

Conclusion on relevant markets in the gas sector:

- (141) The Commission has assessed the impact of the proposed transaction on the following gas markets:
- Gas infrastructure operations:
 - (i) Transmission of gas in Hungary,
 - (ii) Distribution of gas in the Hungarian RDCs' areas,
 - (iii) Storage of gas in Hungary,
 - Supply of gas:
 - (i) Supply of gas to RDCs in Hungary,
 - (ii) Supply of gas to traders in Hungary,
 - (iii) Supply of gas to large power plants in Hungary,
 - (iv) Supply of gas to large industrial customers in Hungary,
 - (v) Supply of gas to small industrial and commercial customers in Hungary,
 - (vi) Supply of gas to residential customers in the Hungarian RDCs' areas.

B. Relevant electricity markets

(i) The electricity sector in Hungary

a. Electricity demand

- (142) Hungarian electricity consumption increased from 38.6 TWh in 2000 to 41.2 TWh in 2004, a 1.6% compounded annual growth rate. In 2004, the largest end users sectors were manufacturing (30%), residential (27%) and transports (5%). According to the parties⁶⁷, electricity consumption in Hungary is expected to increase by [0-5%]* annually in the coming years. Electricity sold in Hungary is either produced by domestic power generators or procured from imports.

b. Electricity transmission and distribution

- (143) MVM owns and operates the Hungarian high-voltage electricity grid. The low-voltage grids are owned and operated by the RDCs. There are six electricity RDCs in Hungary (TITÁSZ, ÉDÁSZ, DÉDÁSZ, ÉMÁSZ, ELMŰ, DÉMÁSZ). E.ON has sole control of three of these six RDCs: TITÁSZ, ÉDÁSZ and DÉDÁSZ. Out of the three remaining RDCs, ÉMÁSZ and ELMŰ are controlled by RWE and DÉMÁSZ by Electricité de France (“EDF”). ELMŰ is the largest electricity RDC in Hungary as it covers the Budapest area.

Ownership of the electricity RDCs:

ÉDÁSZ	100% E.ON
DÉDÁSZ	100% E.ON
TITÁSZ	100% E.ON
DÉMÁSZ	61% EDF 20.6% Institutional investors 18.4% Others
ÉMÁSZ	54.3% RWE 26.8% EnBW 18.9% Others
ELMŰ	55.3% RWE 27.3% EnBW 10.5% Municipality 6.9% Others

- (144) The graph below shows the electricity RDCs’ respective territories and sales in 2002:

⁶⁷ Form CO, Page 192



c. Electricity generation

Current electricity generation capacities in Hungary

- (145) Total generation capacity in Hungary was approximately 8,000 MW in 2004, to be compared with the country's peak load of 6,350 MW. The Hungarian electricity generation is split between nuclear energy (1,800 MW installed capacity) and lignite, gas and coal power plants (5,700 MW installed capacity)⁶⁸. Renewable energies and hydro power are negligible. This generation mix differs slightly from neighbouring countries, where nuclear energy (Slovakia) or hydro power (Austria, Serbia, Romania) play a more significant role.
- (146) In 2003, 18 power plants had a generation capacity exceeding 50 MW, compared to 13 in 1997, while there are around 150 smaller power plants, compared to 50 in 1997. Almost 40% of electricity consumed in Hungary is generated by the Paks nuclear power plant, the remaining 60% is mainly generated by power plants burning coal and hydrocarbons and by imports.
- (147) The Hungarian power plants may be ranked according to their variable costs ("merit order curve"). The first power plant is the nuclear plant (with variable costs below [0-10]* EUR / MWh), followed by the lignite power plant (around [15-30]* EUR / MWh). The most expensive power plants are the gas-fired power plants⁶⁹ (from [15-40]* EUR / MWh to [15-40]* EUR / MWh) and the coal power plants (above [...] EUR / MWh). The following chart, drawn from the Form CO, shows the merit order curve of Hungarian power plants in 2003:

⁶⁸ Further details on the structure of electricity generation in Hungary are provided in Section V.(ii).a.

⁶⁹ It should be noted in the chart above that gas/oil power plants are using gas as primary fuel.

[...]*

- (148) Electricity generation capacities available for the open segment of the market are much lower than total installed capacities due to the existence of long-term Power Purchase Agreements (“PPAs”). According to the HEO, the capacity available for the open segment amounted to around [3,000-4,000] MW in 2005.
- (149) Capacities contracted by MVM under the long-term PPAs in excess of its needs as public utility wholesaler and auctioned by MVM may be added to this figure. At the last auction for the period between 1 July 2005 and 31 December 2005, MVM sold 85 MW of base load capacity, 190 MW of off-peak capacity and 54 MW of peak capacity to electricity traders.

Need for additional generation capacity

- (150) The Commission’s market investigation has revealed that the Hungarian generation capacity will need to be renewed and expanded to a large extent in the next few years. Starting in 2007, the peak load will no longer be covered by installed capacity and imports, showing the need for investment in electricity generation as of 2007. According to MAVIR Rt. (“MAVIR”), the electricity system operator, the electricity market could even experience a deficit of production capacity around 2010 due to the lack of sufficient new generation capacity planned and the long time needed for new power plant projects.
- (151) The HEO and MAVIR estimate that new generation capacity of approximately 5,000 MW has to be built until 2020 in Hungary to replace old power plants⁷⁰ (3,500 MW) and to satisfy the increase in demand. This figure accounts for roughly 60% of the total production capacity currently installed in Hungary. Accordingly the Hungarian electricity generation capacity should increase from 8,000 MW to approximately 10,500 MW. This estimate is also consistent with expectations from large market players which have estimated that half of the generation capacity in Hungary (approximately 4,000 MW) will need to be replaced in the next 5 to 7 years.

d. Electricity exports/imports in Hungary

- (152) In view of the limited domestic generation capacities available for the open segment of the market, imports have developed rapidly to supply the open segment. MAVIR is responsible for granting non-discriminatory access to cross-border capacities.
- (153) Hungary has a relatively high interconnection capacity with neighbouring countries, with 6 interconnectors. Import capacity amounts to approximately 3,000 MW, representing 38% of installed generation capacity in Hungary (by way of comparison with the most integrated regional electricity market in Europe, Nordpool, these figures are 18% for Norway, 29% for Sweden, 50% for Denmark, and 14% for

⁷⁰ A number of old coal-fired power plants have already been decommissioned in Hungary and most of the remaining ones are expected to close down for environmental reasons.

Finland)⁷¹. The cross-border power lines enable transmissions from and to Ukraine, Slovakia, Austria, Croatia, Serbia and Romania.

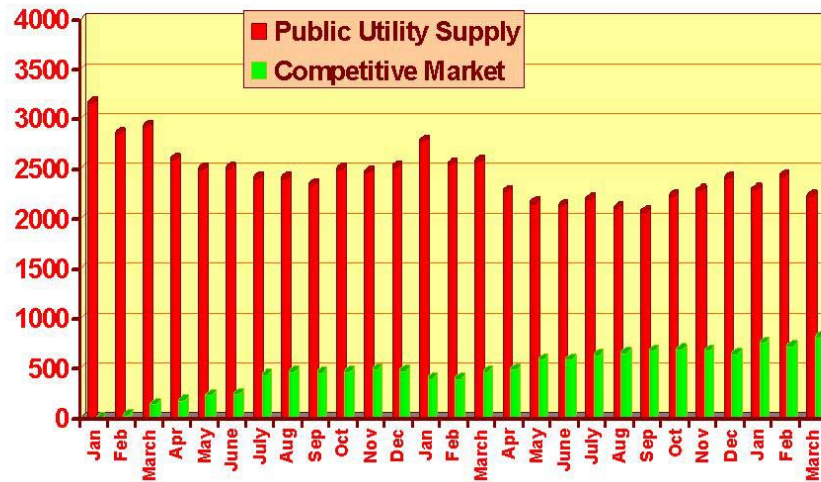
- (154) Some of these interconnections are not actually used for imports as there are either no or no cheaper electricity sources from some of Hungary's neighbouring countries. For example Serbia is a net importer following the destruction of the country's infrastructures in the war, and only one power plant in Ukraine is allowed to export electricity for technical reasons related to the stability of the Ukrainian electricity system. By contrast, all the import capacity for cheaper electricity (namely the Slovak interconnector) is fully used and congested.
- (155) New interconnection lines with Croatia, Slovakia and Romania are planned by MVM in 2007. However, they are not expected to lead to a significant increase in electricity imports into Hungary due to the reduction of Hungary's electricity generation capacity surpluses.

e. Development of the liberalised electricity markets in Hungary

- (156) The proportion of customers (in volume) purchasing electricity on the open segment of the market increased steadily from 2003 to 2005: approximately 3% on February 2003, 7% on February 2004 and 27% on February 2005. In June 2005, 1,129 eligible customers (1,530 consumption sites) had switched to the open segment, accounting for 10.5 TWh of annual consumption. Accordingly, the open segment represented 31.8% of the total electricity market.
- (157) According to statistics from the HEO, electricity end users on the open segment are mainly base load or "profile customers", for which the electricity consumption schedule is easily determined based on past statistics. These customers are active in various industry sectors (energy, chemicals, steel, food industry, retail, etc.). The market investigation has shown that most electricity market players consider the open segment of the electricity market in Hungary as competitive, while replies from electricity customers are mixed.

⁷¹ European Commission: "Annual Report on the Implementation of the Gas and Electricity Internal Market", 5 January 2005.

Development of the electricity free market from 2003 to March 2005:



Source: MAVIR Presentation, May 2005

(ii) *Regulatory framework*

a. Current regulatory framework

(158) The liberalisation process started earlier in the electricity sector than in the gas sector, with the old electricity act in 1994 (Act 48 of 1994), the privatisation of the regional distributions companies (“RDCs”) in 1995, and the entry into force on 1 January 2003 of the Hungarian Electricity Act (Act 110 of 2001 – “HEA”) adopted to implement Directive 92/96/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity⁷². Further measures were adopted to implement Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC⁷³ into Hungarian law. A law amending the HEA (Act 79 of 2005) was adopted on 6 July 2005 and entered into force on 1 September 2005, and a proposal for a new organization of the Hungarian electricity market was published by the HEO on June 2005 (“New Electricity Model”)⁷⁴.

⁷² , OJ L 27, 30.1.1997, p. 20.

⁷³ , OJ L 176, 15.7.2003, p. 37.

⁷⁴ Proposal for the Modification of the System of Market Relations of the Hungarian Electricity Market in order to Enhance the Efficiency of the Competition to Attract Consumers and to Achieve the Required Full Compliance with Relevant Community Directives, June 2005, http://www.eh.gov.hu/gcpdocs/200506/honlaprateljes2005jnius27_angol.pdf.

Coexistence of regulated and open segments

- (159) As the gas market, the Hungarian electricity market is also characterized by a hybrid model, including a regulated segment and an open segment of the market. Before the liberalisation of the electricity market in Hungary, cross-border electricity trading and transmission fell by law within the exclusive monopoly of MVM, a wholly-owned state company. Six regional suppliers had a monopoly to provide electricity services to customers in their respective regions.
- (160) On 1 July 2004, all non-residential customers became eligible customers⁷⁵. Residential customers will become eligible on 1 July 2007. As in the gas sector, eligible customers have the right, but not the obligation to switch suppliers, and may thus stay with their respective regional supplier in the context of a public utility contract. There are however more customers that have switched to the open segment of the market in the electricity sector than in the gas sector.
- (161) Recent amendments of the HEA have made switching between public utility supply and open segment easier. For example, electricity customers can switch in 30 days if the contract does not specify it differently and can switch back to public utility supply in 60 days.
- (162) The same chain of supply/purchase obligations exist in the public utility electricity sector as in the gas sector. Similarly, the relationships within the framework of public utility contracts remain, for reasons of public interest, heavily regulated both in terms of the applicable prices as well as other conditions of the contracts that are to be concluded among the various market players. By contrast, contractual freedom principally prevails in respect of the commercial relationship of eligible customers, having switched their supplier, and their commercial partners (traders, importers etc.).

Tariffs

- (163) Electricity prices applicable in the public utility segment are regulated. Under Article 95 HEA, the prices of the following electricity products/services are regulated: (i) the transmission and distribution of electricity, (ii) the grid control by the system operator, (iii) the electricity sold by the public utility wholesaler to the public utility suppliers (the RDCs); and (iv) the electricity sold to public utility customers.
- (164) Article 96 HEA states that the detailed rules pertaining to the tariff regime shall be drawn up by the HEO based on the least cost principle. The framework of the price regulations and the prices shall be determined by the MET. The HEO also has the

⁷⁵ Article 3 of Government Decree No. 181/2002 on the eligibility of electricity customers.

obligation to review the price levels and the prices at the request of any interested party and shall make public the results of such review.

Market operators

(165) As in the gas sector, all electricity-related activities are subject to the *ex-ante* control of the HEO, through licensing, namely: (i) construction and operation of power plant with an output over 0.5 MW; (ii) transmission; (iii) distribution; (iv) grid operation (or system operation); (v) trading; (vi) public utility wholesale; (vii) public utility supply; (viii) operation of a power exchange; and (ix) cross-border transmission of electricity.

- Generators

(166) There are currently 19 licensed electricity generators in Hungary. According to the recent amendments of the HEA, power generators having a capacity between 0.5 MW and 50 MW are now also required to obtain a license, which can be requested under a simplified procedure.

(167) The generators are obliged by law to offer their production capacity contracted for public utility purposes to the public utility wholesaler (MVM)⁷⁶. As result, the licensed generators and MVM have entered into PPAs, under which mutual selling and purchasing obligations were established on a long-term basis. The PPAs specify, inter alia, the annual capacity payment for generation capacity booked by MVM, the energy payments and the penalties for non-availability. PPAs are typically concluded for a period of twenty years.

(168) Under a PPA, the share of the generator concerned in MVM's total demand for the public utility segment is estimated and fixed in advance for the duration of the contract. The generator is obliged to reserve that production capacity and to supply the corresponding amount of electricity when requested. MVM, in turn, is obliged to remunerate the entire booked capacity, even if it is not used. MVM has therefore an economic interest to use all the capacities booked. The purchase prices for electricity are pre-fixed in the PPAs and are based on each generator's cost structure (fixed and marginal costs). The PPAs are scheduled to terminate between 2010 and 2015.

(169) As a result, the large majority of Hungarian power plants have long term PPAs with MVM, which cover a substantial part of Hungarian electricity needs. In 2003, capacities covered by the PPAs amounted to 4,800 MW out of 8,000 MW of installed capacity in Hungary, in comparison with a peak load of 6,300 MW and a base load of 3,500 MW.

- The public utility wholesaler

(170) The single-buyer public utility wholesaler MVM is obliged to supply electricity to the public utility suppliers (the RDCs) for public utility purposes (i.e. the electricity they need to supply their respective public utility customers). Article 65 HEA grants MVM an exclusive right to receive the "contracted electricity" of power plants under

⁷⁶ Article 17 of the HEA.

the long-term PPAs⁷⁷ concluded with the licensed power generators. PPAs may also be concluded between MVM and licensed importers⁷⁸.

- (171) The price of electricity sold by power generators was an official maximum price set by the MET until 1 January 2004 but is now freely negotiated between market players. The long-term PPAs contain complex price formulas for the calculation of prices. By contrast, the maximum price of the electricity sold by MVM to the RDCs continues to be regulated by the MET upon a proposal of the HEO.
- (172) Where the generation of electricity is requested but is subsequently not used by MVM in due time, the generator is allowed to sell that electricity freely or to assign it to MAVIR, the system operator⁷⁹. In practice, however, MVM has an economic interest in exploiting and reselling (domestically or by export) all booked capacities.
- (173) Small power plants without a long-term PPA with MVM, as well as other power plants with a long-term PPA with MVM beyond the quantities contracted under those, are free to sell their electricity output to any party, such as a trader or directly to eligible customers. There are, however, only limited capacities, beyond those booked under long-term PPAs, for such free sales.

- Public utility suppliers (RDCs)

- (174) The RDCs are, within the geographic territory specified in their licence, exclusively entitled and obliged to sell electricity to the public utility customers at a price determined by law. As in the case of gas RDCs, the electricity RDCs are the distribution grid licensees, but their activity is not confined to the mere distribution of electricity as they also sell electricity to eligible and non-eligible customers as public utility suppliers and in some cases as traders (in the case of eligible customers having switched to the open segment of the market).

- The system operator

- (175) The system operator, MAVIR, is responsible for the management and operational safety of the Hungarian power grid, as well as the functioning of the electricity market.

- The transmission and distribution network operators

- (176) The transmission network is owned and operated by MVM, and the distribution grids are owned and operated by the RDCs. These market players are obliged to provide Third Party Access (“TPA”) to the networks without discrimination, at regulated tariffs.

⁷⁷ The PPAs are typically concluded for a period of 20 years, although shorter durations for certain plants are possible.

⁷⁸ Article 3 (23) of the HEA.

⁷⁹ Article 18 of the HEA and Government decision No 1070/2005 of 8 July 2005.

- *Traders*

- (177) The licensed electricity traders are entitled to purchase electricity from the generators, other traders, the public utility wholesaler (if the latter has surplus electricity) and from abroad, and they are entitled to sell electricity to eligible customers, other traders and the public utility wholesaler. There are currently 23 licensed electricity traders in Hungary⁸⁰.

Imports of electricity

- (178) There are no legal restrictions on the volumes that electricity traders may import⁸¹. The other licensees are limited as to the volumes of cross-border transmissions permitted (e.g. an eligible customer may only import electricity to the extent of its own consumption pursuant to Article 46(3) HEA⁸²).
- (179) The allocation of cross-border capacities is performed and administered by the grid operator, MAVIR. Existing capacity demands (already allocated capacity) have priority over new demands. The amount of free capacity is defined on a regular basis for each cross-border power line. If the demand for free capacities exceeds the amount of available free capacity, the free capacities are allocated through an auction. Auctions are held on a yearly and monthly basis. Currently, cross-border capacity auctions are essentially used to allocate capacities at the Slovak interconnector, where demand is the most important due to lower electricity prices.

Co-generation power plants

- (180) Article 3 (19) HEA defines “co-generated electricity” as electricity produced with heat in the same generating installation⁸³. The operation of co-generation power plants is regulated by the HEA and its Executive Decree. According to the newly enacted Article 19 HEA, the use of renewable sources and waste power generation, as well as the use of co-generated electricity shall be endorsed by the state. The MET Decree 56/2002 of the Regulation on Taking-Over and Definition of Prices for Electric Energy Coming under the Feed-in Obligation provides detailed rules on the

⁸⁰ AES Borsodi Energetikai Kft., APT Hungária Kft., Árpád Energia Kft., Atel Energia Tanácsadó Kft., D-Energia Kereskedelmi Kft., DUNAFERR Központi Beszerző Kft., EFT Budapest Rt., Electrabel Magyarország Kft., Elektra Energia Kft., ENERGY CAPITAL Kft., ENKER-TEAM Kft., Entrade Hungary Kft., E.ON Energiakereskedő Kft., Észak-Budai Energiakereskedő Kft., ETC Hungary Kft., JAS Budapest Kereskedelmi és Szolgáltató Rt., Magyar Áramszolgáltató Kft., Mátrai Erőmű Rt., MVM Partner Rt., PANNONTRADING Kft., PCC Energie Kft., Sempra Energy Europe Kft. and System Consulting Rt.

⁸¹ Article 42(1) of HEA.

⁸² Article 44(1) as regards the public utility wholesaler.

⁸³ The additional conditions providing that co-generated electricity shall be produced with heat using identical fuels and by an energy conversion process with an efficiency of no less than 65% have been deleted by the latest amendment of the HEA.

mandatory take-over of electricity produced through co-generation as well as the definition of take-over prices. Subject to certain conditions, the public utility wholesaler is obliged to take over the co-generated electricity from power plants connected to the grid and receive subsidies from the system operator for these purchases.

b. Evolution of the regulatory framework

The New Electricity Model

- (181) The market investigation has focused on the evolution of the Hungarian electricity sector regulatory framework. The most relevant document in this matter is the New Electricity Model prepared by the HEO at the request of the MET. The proposal recently released by the HEO presents the objectives set by the MET and describes a recommended new market model. The Commission has discussed the content of this proposal and the likelihood of the adoption of its main elements with the HEO and the MET.
- (182) The objective of the Hungarian government is to bring the New Electricity Model into force at the complete liberalization of the Hungarian electricity markets.
- (183) In the absence of additional information about the future electricity model in Hungary, the Commission takes the view that it can base its forward looking competitive assessment of the proposed transaction on the current regulatory framework until July 2007 and on the recommended new market model as described in the New Electricity Model thereafter⁸⁴.
- (184) The objectives of the New Electricity Model, as set by the Hungarian government, are threefold. The first objective is to bring the Hungarian legal provisions into full compliance with Directive 2003/54/EC. The second aim is to increase competition on the electricity market to the benefit of end user customers, while preserving regulated prices for household customers. Finally, the third objective is to ensure high security of supply and to promote energy saving and environmental protection. Contrary to the current hybrid model, the New Electricity Model is a free market model with retail supply at a regulated price in a limited scope specified by law.

- Significant Market Power trader and Universal Service Provider

- (185) Under the recommended new model, the current system of public utility should be terminated and the public utility wholesale and the public utility service providers' functions should cease to exist. MVM and the RDCs would be able to continue their activities on the open segment of the markets respectively as a Significant Market Power Trader (SMP trader) and as Universal Service Providers (USP). As most significant change concerning the relation between market players, the obligation of RDCs to purchase electricity from MVM would disappear. USP should be allowed to procure electricity from any market player, at a competitive price.

⁸⁴ The recommended new market model as described in the New Electricity Model will most likely be implemented in July 2007.

(186) In order to correct the structural disparities and to support the emergence of competition, the HEO plans to introduce a special regulatory regime applicable to dominant market players. Under this regime, the HEO would have the power to impose additional obligations (e.g. mandatory capacity auctions, price control, supply obligations) in order to prevent abuse of dominant position from any SMP trader at the wholesale or the retail level.

- End users

(187) Under the New Electricity Model, regulated prices for industrial and commercial customers would terminate.

(188) Household customers would be granted the possibility to purchase electricity on the free market after 1 July 2007 but regulated prices should be maintained for those customers as a public utility service. Household customers would not be able to switch back to the regulated price service once they have switched to the open segment of the market.

- Power generators and electricity markets

(189) The obligatory capacity purchase currently present in the HEA should cease to exist and large power generators would not be obliged to reserve the most significant part of their capacity and electricity production to MVM anymore, unless they are required to do so under an existing long-term PPA with MVM.

(190) MVM would be entitled to sell on the open segment of the market the capacity and electricity purchased on the open segment of the market or through the long-term PPAs. Power generators would be entitled to sell on the open segment of the market capacity and electricity in excess of the quantities contracted in the long term PPAs and the capacity and electricity contracted in the long-term PPAs but not taken over by MVM.

(191) The recommended model foresees the establishment of two markets for the sale of electricity and capacity. An organized market should be established by a state owned Market Operator (a subsidiary of MAVIR) for hourly day-ahead trading. A “market” for bilateral transaction should also be available and will consist in (i) a set of Over The Counter transactions (“OTC market”) between power generators (to the extent of their free capacity) and traders and (ii) the sale of generation capacity released on mandatory auctions by MVM.

The evolution of the PPAs and of the electricity markets

(192) The functioning of the recommended new model will depend on the outcome of the long-term PPA renegotiations.

- The renegotiations of the PPAs

(193) In 2002, in the context of Hungary’s entry in the European Union, the Hungarian government issued a decree⁸⁵ on the determination and management of stranded

⁸⁵ Government Decree 183/2002.

costs, which entitled MVM to recover stranded costs and introduced at the same time imposed an obligation for MVM to renegotiate the PPAs before 31 January 2003. In accordance with those provisions, a round of renegotiations of the PPAs between MVM and the 10 power generators concerned took place in February 2004. This round of renegotiations failed as none of the parties involved appeared to have any interest in changing the existing PPAs. It is not likely that the government will impose a new round of renegotiations in the short term.

- (194) However, in parallel to the elaboration of the new electricity model, the HEO and the MET⁸⁶ are discussing with the Commission the validity of the system of long term PPAs and the possible volume of stranded costs (threshold price-mechanism). The aim is to ensure that the new regulatory framework is compatible with European competition law. Under the New Electricity Model, the government also intends to create the appropriate incentives for MVM and power generators to renegotiate the PPAs.
- (195) It should be noted that the Commission has opened in November 2004 a State Aid investigation on long-term PPA in Hungary⁸⁷. The opening of this procedure is likely to give all interested players an additional interest in a successful renegotiation of the PPAs.
- (196) If the PPAs are substantially modified before entry into force of the New Electricity Model in 2007 and if the process results in the release of important generation capacities and electricity quantities⁸⁸, power generators will be able to supply traders (open segment of the market and USP) and eligible customers either directly through bilateral contracts (OTC market) or indirectly through the newly created organized market (power exchange).

- Supply of electricity to end users

- (197) In terms of access to and supply of electricity to end users in Hungary and depending on the outcome of the long-term PPAs renegotiations, the New Electricity Model may bring the following changes.
- (198) First, approximately one third of the total demand originates from residential customers in Hungary. Although the electricity market will be fully opened in 2007, it is expected that most household customers will continue purchasing from the USPs.
- (199) Secondly, commercial and industrial users, which account for two thirds of total Hungarian demand, will potentially be supplied through four distinct supply channels: (i) OTC market, (ii) Organized market, (iii) Imports and (iv) MVM

⁸⁶ Minutes of call with Mr. Hatvani, Deputy Secretary of State, MET, on 23 August 2005.

⁸⁷ See Commission press release IP/05/1407 of 10 November 2005.

⁸⁸ The renegotiation of the PPA could result in the transformation of the current physical capacity and energy delivery agreements into financial payments obligations, whereby MVM will only act as a clearing house.

auctions. Large electricity end users may be supplied directly through those ways while small and medium electricity end users will be supplied indirectly through traders.

- (200) Large industrial users and traders may purchase through bilateral contracts, on the OTC market, from (i) current large power generators (provided the long term PPAs have been renegotiated or only for the quantities in excess of the long term PPAs), (ii) from smaller power generators (not subject to long term PPAs), (iii) from newly built power plants (not subject to long term PPAs) and (iv) from traders.
- (201) Certain quantities of electricity will be traded through the Organized Market (traders and large industrial customers). Based on the discussions with the HEO, in the long term, this proportion can be roughly estimated to one third of the electricity finally sold to commercial and industrial users.
- (202) Large industrial users and traders will continue importing electricity. Cross-border capacities will remain allocated among bidders through auctions. They will also be able to purchase power capacity through auctions imposed on MVM. The extent of these mandatory auctions is still unclear.
- (203) If the PPAs are not substantially modified before 2007 and the introduction of the new model, power generators will continue reserving the majority of their capacities and delivering the majority of their electricity production to MVM, which will then in turn most likely sell the majority of these quantities to the USP⁸⁹ or through mandatory auctions (monthly and / or yearly). In this case, even under the new electricity model, current power generators will not be able to contract directly with traders or end users and this will impede the emergence of a competitive and efficient OTC market. Large power generators will remain bound to MVM and traders will have to rely on imports or electricity not sold through PPAs, as in the current situation.
- (204) The negative impact of the PPAs on competition could be partially compensated by mandatory capacity auctions imposed on MVM either on the organized market or on the OTC market, which could be part of the additional obligations imposable on SMP traders on the wholesale market.
- (205) In order to base its competitive assessment on the most reasonable assumptions as regards the future electricity markets developments in Hungary, the Commission also consulted the most important market players on their expectations about the evolution of the electricity regulatory framework in July 2007. Although most of those players referred to a certain degree of uncertainty, they generally confirmed that the essential elements of the HEO recommended market model would most likely be adopted.
- (206) The market investigation has also pointed to a degree of uncertainty as regards the renegotiation of the long term PPAs. Although the PPAs are being scrutinised by the Commission under State aid rules to ensure they do not create any distortion of competition in the electricity sector, both MVM and power generators do not have

⁸⁹ In case of insufficient liquidity on the market, the SMP traders may be required by the HEO to supply the USPs so that they are able to perform their functions.

an interest in renegotiating the PPAs. The PPAs grant power generators relatively high electricity purchase prices and stable and reasonable profitability. Their termination would imply more competition between power plants and greater uncertainty with respect to electricity sales prices. It would decrease the size and the role of the public utility segment and would put an end to MVM's strong position as public utility wholesaler.

(207) The Commission notes that the evolution of the electricity regulatory framework and its timing have not been contested by the parties in their Reply to the SO.

(iii) Relevant product markets

(208) In view of the current regulatory framework in market conditions in Hungary, the parties distinguish the following relevant product markets for the supply of electricity to (i) residential or household customers, (ii) small industrial and commercial customers and (iii) medium and large industrial and commercial customers. The parties also identify the generation of electricity as a relevant product market in itself, separate from the market for electricity wholesale. The parties further submit that only the generation of electricity is an affected market for the assessment of the proposed operation⁹⁰.

(209) The Commission has in the past⁹¹ distinguished separate product markets for the generation and wholesale supply of electricity (i.e., production of electricity in power plants and physical import of electricity through inter-connectors and its sale on the wholesale market to traders, distribution companies or large industrial end-users), transmission of electricity (via high-voltage grid); distribution of electricity (via low-voltage grids), retail supply of electricity (to small commercial and industrial users and residential customers) and balancing services.

(210) On the basis of the past practice and the investigation in this case, the Commission considers that the following product markets are relevant for the assessment of the present transaction:

- Electricity infrastructure operations, including the transmission of electricity, the distribution of electricity
- Provision of balancing power;
- Generation and wholesale supply of electricity to traders, to MVM and to the RDCs;
- Retail supply of electricity to medium and large commercial and industrial customers, small and medium commercial and industrial customers and to residential customers.

⁹⁰ Form CO, Page 113.

⁹¹ Case COMP/M. 2947 Verbund/Energie Allianz, COMP/M. 3268 Sydkraft/Gräninge, COMP/M.3440 ENI / EDP / GDP.

- (211) This delineation of the relevant product markets in the electricity sector only differs from the market delineation proposed by the parties as regards the combination of electricity generation and wholesale activities in one single relevant product market. However, this difference (and the precise delineation) has no impact on the outcome of the assessment of this case. It should be noted that the parties did not contest the definition of the relevant product markets in the electricity sector in their Reply to the SO.

a. Infrastructure

Transmission of electricity

- (212) The operation and management of the high voltage grid (“Transmission of electricity”), has been consistently identified by the Commission as a relevant product market and as a natural monopoly.
- (213) In Hungary, the transmission grid is owned and operated by MAVIR, the transmission grid operator, which is a subsidiary of MVM. Access to the transmission grid is granted to third parties at a regulated tariff. Transmission lines may have a 750 kV, 400 kV or 220 kV voltage.
- (214) Although this product market is not an affected product market under the meaning of the Merger Regulation, the analysis of the access to available capacity on this grid and to cross-border inter-connectors is relevant for the assessment of the proposed transaction.

Distribution of electricity

- (215) The operation and management of the lower voltage grid(s) (“Distribution of electricity”) has also been identified by the Commission as a relevant product market and as a natural monopoly.
- (216) In Hungary, the distribution grids are owned and managed by the RDCs, which are the distribution grid operators. Access to the distribution grid is granted to third parties at regulated tariffs. Main distribution lines have a 120 kV voltage and secondary distribution lines have a voltage ranging from 35 kV to 220 V.
- (217) Although there are six regional distribution grids in Hungary, these grids cover different parts of the country and do not overlap. Each of these grids therefore constitutes a separate product market as, for any given customer, distribution through one distribution grid is not substitutable with distribution through another grid.
- (218) Although these product markets are not affected product markets under the meaning of the Merger Regulation, the analysis of the access to available capacity on these grids is relevant for the assessment of the proposed transaction.

b. Balancing power

- (219) In previous decisions, the Commission has distinguished a market for balancing power, in view of the lack of substitutability with other electricity supply at the wholesale level⁹².
- (220) In most electricity markets, the system operator is responsible for maintaining the tension in the grid within a very narrow bandwidth. If there is over-consumption, the tension in the grid would drop and this could cause at some point network stability problems. A problem also arises if there is under-consumption as then the tension in the grid rises above an acceptable tolerance level and the system operator must make sure that either some generation capacity is switched off or that some consumption is added. In Hungary, the system operator (MAVIR) operates the balance energy system and purchases energy in order to supply balance energy for the balance units. The system operator also purchases electricity in order to adjust the losses of the transmission grid as well as to provide network-related services.
- (221) The electricity used for system balancing is only produced by gas power plants as nuclear and lignite power plants do not offer the appropriate technical requirements (load charging, speed) and is purchased by the system operator at the national level. In addition, a large part of the electricity is purchased from MVM due to the existence of long term PPAs.
- (222) The Commission's investigation confirmed that the provision of balancing power constitutes a relevant product market for the purposes of this decision.

c. Generation/Wholesale supply of electricity

- (223) The Commission has in previous decisions considered the generation and wholesale supply of electricity as a separate product market⁹³. This encompasses the production of electricity at power stations as well as electricity physically imported through inter-connectors by traders⁹⁴. The parties distinguish the markets for the generation of electricity and the market for the wholesale of electricity⁹⁵. However, they do not provide any reasons why the two product markets should be separate.
- (224) The Commission's market investigation confirmed that the generation of electricity and wholesale of electricity in Hungary belong to the same relevant product market. The supply side of this product market is constituted by power generators, wholesale traders and electricity imports and the demand side is constituted by the various

⁹² The wholesale services that come closer to balancing power services are so called "intra-day" trading opportunities at which the companies in actual under- or over-supply can trade their surpluses or purchase their extra needs. However, if there is no continuous intra-day trading, with immediate delivery, this trading system is in itself insufficient to match supply and demand at any time.

⁹³ See Case COMP / M.3268-Sykraft/Granninge.

⁹⁴ Electricity may also be imported by large industrial customers directly. The activity of large industrial customers on the Hungarian market is however currently very limited.

⁹⁵ Form CO Page 113 and 114.

categories of electricity resellers, MVM, the RDCs and electricity traders. The market investigation has also indicated that these various categories of customers belong to distinct relevant product market due to the distinct regulatory framework.

- (225) The relevant product markets have to be seen against the background of the evolution of electricity regulatory framework in Hungary. For this purpose, a distinction has to be drawn between the current electricity sector structure and the structure that should soon be in place after the implementation of the New Electricity Model and the amendment of the long-term PPAs.
- (226) In their reply to the SO, the parties did not contest the Commission's conclusion that electricity generation and wholesale belong to the same relevant product markets.

Wholesale supply of electricity to traders

- (227) Under the current regulatory framework, traders that are present on the liberalised segment of the electricity wholesale market are entitled to purchase electricity from the power generators, from other traders, from the public utility wholesaler and from abroad, and they are entitled to sell electricity to the eligible customers, to other traders and to the public utility wholesaler. Electricity traders currently active in Hungary are generally subsidiaries set up by the RDCs to be present on the open segment of the market (referred to as "trading subsidiaries of the RDCs") or subsidiaries of recently established European trading groups⁹⁶. At the moment, the majority of electricity traders only supply electricity to other traders or to large industrial customers.
- (228) In view of the regulatory framework applicable to electricity traders, the wholesale supply of electricity to traders constitutes a relevant product market open to competition.
- (229) Under the new regulatory framework, the scope of the open segment of the electricity wholesale market will expand significantly as RDCs will also act essentially as traders. Depending on the reduction of the scope of the long term PPAs and on mandatory auctions imposed on MVM, additional generation capacity will also be released to be traded on the open segment of the wholesale market.

Wholesale supply of electricity to MVM

- (230) The current regulatory framework is based on a hybrid system (regulated and open segments of the market). On the one hand, a large part of the Hungarian wholesale market is organised according to a "single-buyer" scheme. In this regulated segment of the market, power generators offer the amount of electricity generated which has been contracted for public utility purposes to the public utility wholesaler, MVM. On the other hand, the open segment of the wholesale market is based on a competitive market. The volumes produced by power plants, not covered by a public utility contract, the electricity contracted by MVM for public utility purposes and imports are purchased by traders on the open segment of the wholesale market.

⁹⁶ MVM also owns the MVM Partner electricity trader.

- (231) In view of the existence of a public utility market segment and of the long term PPAs, the wholesale of electricity to MVM by large Hungarian power generators constitute a relevant product market not open to competition.
- (232) Under the new regulatory framework, the public utility wholesale segment will most certainly cease to exist in the regulatory framework. The Commission therefore considers that the wholesale supply of electricity to MVM will therefore progressively become part of the same product market as the wholesale supply of electricity to other traders, depending on the reduction in the scope of the long-term PPAs.

Wholesale supply of electricity to RDCs

- (233) Under the current regulatory framework⁹⁷, the public utility wholesaler has an obligation to supply the RDCs at an official price to the extent of the performance of the public utility contracts concluded between the RDCs and the public utility wholesaler. MVM and the RDCs are under an obligation to conclude an agreement for the allocation and receipt of the electricity required for the supply of public utility customers. These long-term PPAs between MVM and the RDCs provide that no discrimination shall be made by MVM among the RDCs. The RDCs are not allowed to purchase electricity for public utility purposes from other sources.
- (234) In view of this regulatory framework currently applicable to RDCs, the wholesale supply of electricity to RDCs constitutes a relevant product market not open to competition.
- (235) Under the new regulatory framework, the RDCs will not longer act as public utility suppliers but as Universal Service Providers (USP) and will be able to procure electricity from any electricity wholesaler. They will however obtain additional rights (privileged access to electricity sold by MVM) and obligations (public service of household customers). The Commission therefore considers that, after the introduction of the new regulatory framework, the wholesale supply of electricity to RDCs will most likely become part of the same product market as the wholesale supply of electricity to other traders.

d. Retail supply of electricity to end users

- (236) In its past decisions, the Commission defined the relevant product markets for the retail supply of electricity to end users based on categories of customers. The Commission has identified these customers groups on the basis of the relevant regulatory framework applicable to them and their consumption profile.
- (237) The parties submit that, for the purpose of the assessment of the present operation, the retail supply of electricity should be considered as a market distinct from the market for the wholesale supply of electricity. In accordance with the Commission past practice, the parties further distinguish three categories of end users (medium and large industrial and commercial customers (MLCs), small industrial and

⁹⁷ Article 43 of the HEA

commercial customers (SCs) and residential customers). In addition, the parties take the view that all eligible customers - not only those who have actually switched to the open segment of the market - belong to those group of end users.

- (238) Although a number of market respondents to the market investigation stated that end users in the regulated system and the non-regulated system should be distinguished as they have distinct supply conditions, the Commission supports the view of the parties that those end users belong to the same relevant product market. All eligible customers choose freely to be in the regulated or in the open segment of the market according to the price and conditions in each segment. Switching does not entail high costs for the customers. Hence, it has been confirmed that, not only customers switched to the open segment of the market, but also that customers switched back to the regulated segment of the market. Therefore, the Commission takes the view that the distinction between eligible customers that have switched to the open segment of the market and those that have stayed in the regulated segment of the market is not relevant for the purposes of the definition of the relevant product markets.
- (239) The market investigation has confirmed that the three groups of end users identified by the parties are the most relevant for the definition of product markets due to their consumption profile and the applicable regulatory framework. MLCs and SCs have distinct consumption profiles and residential customers constitute a separate relevant product market as they are currently not eligible.

Retail supply of electricity to large commercial and industrial customers and retail supply of electricity to small commercial and industrial customers

- (240) All non-residential customers (commercial and industrial customers) are entitled to switch supplier and purchase their electricity needs either on the regulated segment of the market from their local RDC or from an electricity trader on the open segment of the market. These end users are also entitled to change traders and to switch back to the regulated segment of the market. According to the parties, although the legal status of MLCs and SCs is similar, those two end user categories differ by their consumption profiles and the commercial relationship with their electricity suppliers.
- (241) The parties define MLCs as end users having an average annual electricity consumption of more than 0.5 GWh whereas SCs are defined as non residential customers having an average annual consumption of less than 0.5 GWh. The parties submit that the group of customers described as MLCs includes all customers that receive electricity at high and medium voltage⁹⁸ and chain customers whereas the SCs purchase lesser amounts of electricity and are supplied at low voltage (0.4 kV).
- (242) With respect to consumption profiles, the parties submit that MLCs' consumption profile is in general more stable than SCs consumption profile over the year and over the day. SCs have in general a fluctuating demand within the day, with a lower consumption in the evening and the night.

⁹⁸ 10-120 kV for TITÁSZ customers for instance – Source: Parties replies to the Request for Information dated 18/07/05 (Question 15). The parties underline that large industrial companies are often supplied on middle voltage (10-20-35 kW), such as [...]*

- (243) MLCs and SCs also differ in their approach of electricity procurement. MLCs usually have professional staff and resources available to effectively negotiate and compare the various offers presented by the traders/RDCs. They usually open tenders for electricity procurement and seek offers from various market players. As a consequence, they usually receive individual offers tailored to their needs from their electricity suppliers. They are usually dealt with by so-called key-account managers by their commercial partners. On the contrary, SCs have limited resources to compare terms and conditions and are characterised by a mass marketing approach from electricity suppliers. As a result of these distinct procurement patterns, as of August 2005, more MLCs have switched supplier (on the open segment of the market) than SCs.
- (244) E.ON's internal presentations⁹⁹ [...]*. According to those documents, [...]*.
- (245) Hence, the market investigation has confirmed the market definition proposed by the parties and, under the current regulatory framework, the retail supply of electricity to MLCs and SCs constitute two distinct relevant product markets for the purposes of the present decision. Although these product markets do not constitute an affected product market under the meaning of the Merger Regulation, the analysis of their competitive dynamics and of the evolution of E.ON's market position are relevant for the assessment of the impact of the proposed operation.
- (246) Under the new regulatory framework, the public utility segment is expected to be terminated for MLCs and SCs, which will have an impact on the competitive conditions on the retail supply of electricity to MLCs and SCs. As residential customers will become eligible, they may also become part of the SCs market (see below).

Retail supply of electricity to residential customers

- (247) In the current regulatory framework, residential customers are currently not eligible to switch supplier and purchase their electricity needs from their local RDC in a regulated environment.
- (248) In view of this regulatory framework currently applicable to residential customers, the retail supply of electricity to residential customers constitutes a relevant product market not open to competition.
- (249) As regards the regulatory framework after the market opening, the market investigation has not provided clear-cut indications on whether residential customers and SCs will belong to the same relevant product market.
- (250) However, the question of whether residential customers and SCs will belong to the same relevant product market after the opening of the residential customers market segment can be left open for the purposes of this case as the competitive assessment is the same under each alternative.

⁹⁹ E.ON's reply to the Commission's request for information of July 18, 2005. Binder Supplement I, Reply to Question 122. « E.ON Energie, Capital Market Day », Munich, September 6, 2004.

(iv) *Relevant geographic markets*

- (251) The parties submit that the relevant product markets in the electricity sector are national or sub-national¹⁰⁰ in scope, essentially due to the regulatory framework in Hungary. This approach was confirmed by the market investigation.
- (252) Although some respondents to the market investigation argue that the electricity wholesale market could have a broader geographic dimension, the majority of market players highlighted the specificities of the Hungarian market and supported the views of the parties. In view of those comments and of the significant imports to Hungary, the Commission carefully assessed the relevance of a geographic market wider than Hungary for electricity wholesale but came finally to the conclusion that, under the current regulatory framework, the most appropriate geographic scope of this relevant product market was national.

a. Infrastructure

Transmission of electricity

- (253) The Hungarian electricity transmission grid is owned and operated by MAVIR at the national level. Therefore, the electricity transmission market is national in scope.

Distribution of electricity

- (254) The six Hungarian electricity distribution grids are owned and operated by the six RDCs. Therefore, the electricity distribution market is sub-national in scope and each of the distribution grid regions constitutes a distinct relevant geographic market.

b. Balancing power

- (255) Electricity used for system balancing cannot be imported as it needs to be produced in the country and controlled by the national Hungarian TSO in accordance with the UCTE regulation. In addition, import nominations/schedules are done for the next day and it is not possible to re-nominate them during the day. Therefore, the geographic scope of the market for balancing power is national.

c. Generation / Wholesale supply of electricity

Wholesale supply of electricity to traders

- (256) The parties submit that the relevant product market is national in scope due to the Hungarian regulatory framework. They claim that, according to the relevant provisions of the HEA, in order to obtain a Hungarian license for electricity trading

¹⁰⁰ The Parties take the view that the market for the supply of electricity to residential customers has a sub-national scope; all other markets have a national scope.

it is necessary that a company is established in Hungary. It is therefore not legally possible for an electricity trader based outside of Hungary to sell electricity in Hungary without establishing a subsidiary in Hungary beforehand. The parties also underline that it cannot be excluded that with the ongoing liberalisation electricity wholesale markets will in the future be wider than national markets.

- (257) In the market investigation, a few market respondents claimed that the geographic dimension of electricity wholesale market in the current regulatory framework was broader than national due to the significant role played by imports.
- (258) Due to its central position in Eastern Europe, Hungary is highly interconnected with its neighbouring countries, notably Austria, Slovakia, Ukraine, Romania, Serbia and Croatia. In 2003, Hungary imported 11.4 TWh and exported 4.5 TWh, resulting in 6.9 TWh of net imports. According to MVM, the potential technical import capacity is even larger as connectors with Southern countries are not used for imports (Serbia, Romania). As a result, 18.1%¹⁰¹ of the electricity used in Hungary in 2003 was imported. This share of import is relatively high in comparison to other European countries: Italy (15.9%), Austria (11%), Belgium (7.3%) and Portugal (6.5%). In 2005, the net import balance is expected to reach 8 TWh based on MAVIR estimates¹⁰².
- (259) Although electricity imports appear to represent a significant share of the national consumption (and have a predominant role in the open segment of the market), the competitive conditions for the wholesale supply of electricity differ significantly in Hungary and its neighbouring countries.
- (260) First, Hungary has a significant role as a transit country and exported quantities amounted to around 40% of imported quantities in 2003. Electricity is essentially imported from the North (Slovakia and Ukraine) and exported to the South (Croatia and Serbia). The only country with which electricity flows take place in both directions is Austria. The real size of electricity transit through Hungary is difficult to estimate since there is no differentiation between export and import and transit under the CBT regime and cross-border capacities are attributed irrespectively of the ultimate use.
- (261) This means that gross import figures and the interconnection capacities are not entirely relevant for the assessment of the geographic scope of the market. Net Import figures reflect more the competitive constraints exerted by imports and imports capacity with Southern countries should not be taken into account. Similarly, the fact that the vast majority of electricity sold on the Hungarian open segment of the wholesale market comes from import is essentially related to the very low domestic production capacity available on the open segment of the market due to the existence of the long-term PPAs.
- (262) Secondly, the electricity interconnectors with Austria and Slovakia are almost all the time congested according to the HEO, so that no additional imports are currently

¹⁰¹ UCTE Statistical Yearbook, 2003.

¹⁰² MAVIR's presentation: « Information on the Hungarian Power System and on the Hungarian Power System Operator Company », May 2005.

possible without any additional interconnection capacity. The HEO further underlines that domestic congestion and the cross-border allocation methodology limit the import capacities.

- (263) As a result, the influence of imports on the electricity wholesale prices in Hungary is limited, as reflected in the differing price levels between Hungary and its neighbouring countries. Although electricity wholesale prices levels are difficult to estimate as most electricity wholesale markets in Hungary's neighbouring countries (except Austria) are not yet liquid and transparent, the market investigation showed that Hungarian electricity wholesale prices are lower than prices in Austria, Germany and Croatia but higher than in Slovakia, Romanian, Ukraine and Serbia. As an example, according to the parties¹⁰³, electricity wholesale prices in Romania, Slovakia and Serbia are currently respectively [0-5]* EUR/ MWh, [0-5]* EUR/MWh and [0-5]* EUR/MWh lower than in Hungary.
- (264) The market investigation has also indicated¹⁰⁴ that limited interconnection capacity with countries in the North of Hungary – where electricity production costs are lower – entails that interconnection capacity allocated through auctions is expensive. As a result, electricity prices between Hungary and its Northern neighbouring countries do not converge as auction prices offset the electricity prices differences.
- (265) Thirdly, as presented by the parties, the Hungarian regulatory framework explicitly specify that electricity traders should set up a Hungarian trading company and obtain a Hungarian trading license to be active on the Hungarian market¹⁰⁵. A cross-border trading license is required to import electricity. These requirements clearly restrict the possibilities for any foreign company to pursue electricity trading and wholesale activities on the Hungarian market.
- (266) Fourthly, the Hungarian regulatory framework and market opening rules still remain substantially different from those of neighbouring countries. A market operator has underlined that the legal framework concerning power plants primary fuel (state aid for local coal and nuclear) differ between countries as well as environmental and other regulations affecting power generation. As a result the power generation mix of Hungary and its neighbouring country differ much, which has an impact on the electricity wholesale market homogeneity.
- (267) It cannot be excluded that, in the future, depending on future developments such as changes in the regulatory framework, additional interconnection capacity and potential price convergence, the market for the wholesale supply of electricity to traders in Hungary will acquire a broader geographic dimension.

¹⁰³ E.ON's submission dated 2 September 2005.

¹⁰⁴ *"The congestion is due to the higher demand than supply. The TSOs are holding auctions for the cross-border transit capacity on each congested border connection. The result of these auctions is to be paid to the TSOs and practically the TSOs are gaining the price differences between the markets."*

¹⁰⁵ Article 34 of the Executive Decree to the HEA.

Wholesale supply of electricity to MVM

- (268) Under the current Hungarian law, MVM has to procure electricity for public utility purposes in the framework of long term PPAs with the largest Hungarian power plants. The geographic scope of the market for wholesale supply of electricity to MVM for public utility purposes is therefore national in scope.
- (269) Under the new regulatory framework, MVM will have the ability to source electricity on the open segment of the market for the wholesale market depending on the reduction in the scope of the long-term PPAs. The market for wholesale supply of electricity to MVM will therefore remain national for the same reasons as the market for wholesale supply of electricity to traders.

Wholesale supply of electricity to RDCs

- (270) Under the current Hungarian law, the RDCs have to procure electricity for public utility purposes in the framework of supply agreements with MVM. The geographic scope of the market for wholesale supply of electricity to the RDCs for public utility purposes is therefore national in scope.
- (271) Under the new regulatory framework, the USPs will have the ability to source electricity on the open segment of the wholesale market. The market for wholesale supply of electricity to RDCs will therefore become part of the market for the wholesale supply of electricity to traders.

d. Retail supply of electricity to end users

Retail supply of electricity to MLCs and SCs

- (272) In previous decisions¹⁰⁶, the Commission highlighted that a local presence is required for all electricity retail activities, whether to small or large customers, as brand recognition, marketing, customer service, metering and billing were essential.
- (273) In their submission, the parties consider the supply of electricity to all eligible Hungarian customers as national in scope due to the homogeneous competitive conditions throughout the country. Eligible customers may procure electricity from their RDCs, active at a sub-national level, or from electricity traders which are active nationwide.
- (274) The market investigation has confirmed that under the current regulatory framework competition takes place at a national level for eligible customers. First, electricity traders may target specific customers (essentially large industrial users or other traders) but do not privilege any specific geographic area within Hungary. Secondly, electricity import and export figures clearly indicate that very few eligible customers import electricity directly, although they are entitled to do so. According to the

¹⁰⁶ Case COMP/M.3440 ENI / EDP / GDP.

HEO¹⁰⁷, Hungarian eligible customers imported [500-1,000] GWh of electricity in 2003 and [0-500] GWh in 2004, which account respectively for [0-5%] and [0-5%] of the net Hungarian imports in those years.

- (275) The geographic scope of the market for retail supply of electricity to MLCs and SCs is therefore national in scope.
- (276) As regards the new regulatory framework, neither the parties nor the market investigation did provide any indication that this geographic dimension of retail supply of electricity would become broader.

Retail supply of electricity to residential customers

- (277) Under Hungarian law, residential customers are obliged to procure electricity from their local RDCs and are not entitled to switch traders on the open segment of the market. Therefore, the geographic scope of the market for retail supply of electricity to residential customers is sub-national in scope and each of the distribution grid regions constitutes a distinct relevant geographic market.
- (278) Under the new regulatory framework, residential customers will be able to switch suppliers. The market for retail supply of electricity to residential customers will therefore acquire a national dimension for the same reasons as the other electricity retail markets.
- (279) To conclude, the Commission has assessed the impact of proposed transaction in the electricity sector based on the following market definitions:
- Electricity infrastructure operations:
 - (i) Transmission of electricity in Hungary,
 - (ii) Distribution of electricity in the Hungarian RDCs' areas,
 - (iii) Provision of balancing power in Hungary,
 - Generation/Wholesale supply of electricity:
 - (i) Wholesale supply of electricity to traders in Hungary,
 - (ii) Wholesale supply of electricity to MVM in Hungary,
 - (iii) Wholesale supply of electricity to RDCs in Hungary,
 - Retail supply of electricity to end users:
 - (i) Retail supply of electricity to medium and large commercial and industrial customers in Hungary,

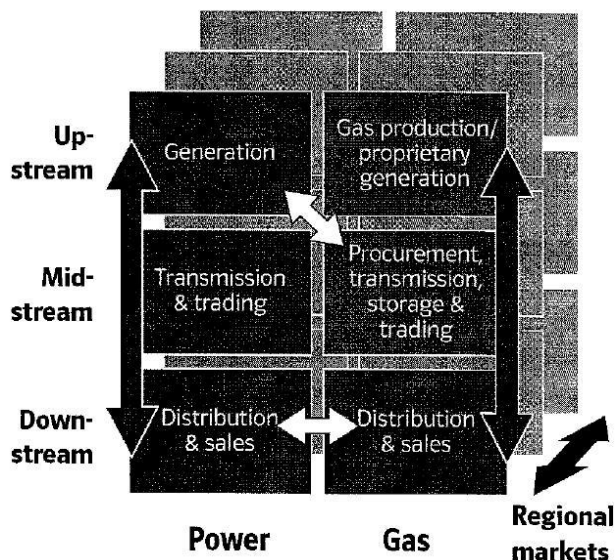
¹⁰⁷ HEO's presentation: "Hungarian Electricity Market", 26 July 2005.

- (ii) Retail supply of electricity to small commercial and industrial customers in Hungary,
- (iii) Retail supply of electricity to residential customers in the Hungarian RDCs' areas.

VI. COMPETITIVE ASSESSMENT

(280) Respondents to the Commission's market investigation have expressed concerns at all levels of the gas and electricity supply chains, from the upstream level of gas procurement to the downstream level of electricity production and supply. They underline that direct access to gas is essential for gas and electricity retail activities as well as for the production of electricity in Hungary. In view of these concerns, the Commission has carried out a detailed assessment of the impact of the proposed transaction on the gas and electricity markets defined in recitals 141 and 279, with the exception of five markets which are not affected by this transaction (the market for the distribution of gas in the Hungarian RDCs' areas, the market for the transmission of electricity in Hungary, the market for the distribution of electricity in the Hungarian RDCs' areas, the market for the provision of balancing power in Hungary, and the market for the wholesale supply of electricity to MVM in Hungary).

Gas and electricity supply chain (simplified flow chart):



Source: E.ON's reply to the Commission request for information dated 18 July 2005 – Binder Supplement I

(281) Prior to the transaction, MOL already has an almost exclusive control over the Hungarian gas infrastructures and supply contracts. The group also owns all the Hungarian gas storage facilities and has a quasi-monopoly on the gas wholesale markets. The essential change brought by the proposed transaction is that E.ON, unlike MOL, has strong market positions in the retail supply of gas through its majority and minority ownership in three gas RDCs, in the generation of electricity, and in the retail supply of electricity through its majority ownership in three electricity RDCs and its trading subsidiary E.ON EK.

(282) Therefore, the proposed merger will create a fully vertically integrated entity along the gas and electricity supply chains. The Commission has established on the basis

of its investigation and its economic assessment that such integration will directly result in the new entity having the ability and the incentive to significantly impede competition on the downstream gas and electricity markets by raising rivals' costs or by foreclosing their access to gas resources.

- (283) The Commission's competitive assessment of the transaction has been achieved both under the current regulatory framework and under the future regulatory framework. For the reasons developed below, competition concerns will arise in the gas and electricity sectors immediately after the transaction, already under the current regulatory framework. The concerns will be even greater when the regulatory framework will be modified, as expected by all market operators, in order to complete the liberalisation of the Hungarian gas and electricity sectors.

A. MOL WMT holds a dominant position in the wholesale supply of gas in Hungary

- (284) Prior to the liberalization of the Hungarian gas sector, MOL was the legal monopolist for the wholesale supply of gas in Hungary. On the regulated segment of the market which still coexists with the liberalized market in the Hungarian hybrid model, MOL WMT retains its former monopoly rights. On the open segment of the gas markets, MOL WMT is currently dominant on all the markets for the wholesale supply of gas in Hungary (gas traders and large power plants) and its dominant position is not likely to be threatened in the short to medium term by new entry for the following reasons.
- (285) In order to compete on the gas wholesale markets in Hungary, it is necessary to have: (i) access to a competitive source of gas in sufficient quantities¹⁰⁸; (ii) non-discriminatory access to the transmission network, in particular cross-border entry points (and to the distribution network, for customers connected to a distribution network); and (iii) access to storage (to respond mainly to seasonal variations in the gas consumption of customers). It is also necessary to obtain the relevant licenses from the HEO, although the investigation has not revealed any particular difficulties in this respect.
- (286) The market investigation has revealed the existence of significant barriers to entry on the Hungarian gas market. The main problem faced by new entrants in Hungary, including international energy operators, is the difficulty to access to competitive sources of gas, and the lack of liquidity¹⁰⁹ on the Hungarian gas wholesale markets. In addition, MOL WMT derives significant advantages from its incumbency position, notably in terms of balancing on the transmission network and storage costs (synchronicity).
- (287) There are basically two main possibilities to obtain natural gas for Hungary: domestic production and imports of gas. In 2004, gas imports accounted for around 80% of Hungary's total gas consumption and this share is expected to increase as

¹⁰⁸ See notably the response of EMFESZ to Questions to Question 23 d) and 25 d) of the request for information of 19 July 2005.

¹⁰⁹ Lack of market players and offers on the gas "secondary market" (sale of gas between gas traders).

domestic gas production gradually declines and gas consumption increases. Prior to the transaction, MOL WMT already controls almost all gas sources available for Hungary. Following the transaction, the new entity will continue to have an almost exclusive control over all competitive gas sources for the Hungarian gas market.

(i) *MOL WMT controls domestic gas resources*

(288) Access to Hungarian domestic gas production is relevant for the assessment of the transaction as it constitutes one of the potential gas sources for new entrants and as it is currently a competitive gas source. The following section will demonstrate that the new entity will have control over these gas resources for at least three years and that the quantities of gas available for third parties in the subsequent years will in all cases be limited.

(289) Hungarian gas is competitive compared to imported gas¹¹⁰:

	2004	
MOL	Gas total production cost	[25-35]* HUF/m ³ ¹¹¹
E&P	MOL WMT average purchase price	[25-35]* HUF/m ³ ¹¹²
Imports	MOL WMT average purchase price through the Beregovo pipeline	[25-35]* HUF/m ³
	MOL WMT average purchase price through the Baumgarten pipeline	[25-35]* HUF/m ³
	MOL WMT average purchase price	[25-35]* HUF/m ³

Hungarian domestic gas production

(290) The Hungarian domestic gas production is not negligible and amounted to approximately 3 bcm in 2004, accounting for about 20% of the total national gas consumption. This domestic production is however declining and is expected to decrease from around [1-4]* bcm in 2005 to [1-4]* in 2015. MOL E&P accounts for the vast majority of the Hungarian domestic production. Two US companies, El Paso and POGO (now Toreador), have acquired exploration blocks to carry out gas exploration activities. At the moment, however, only El Paso produces marginal quantities of gas (35 million m³ in 2004) sold to MOL.

The Supply Agreement

(291) As already indicated, MOL E&P is not being acquired by E.ON under the proposed transaction. Therefore the domestic gas resources belonging to MOL E&P will not be controlled by E.ON. However, MOL WMT and MOL E&P have signed, as part of the transaction, a long term supply agreement ([...]*) that entered into force on 1

¹¹⁰ See the Parties' submission dated 5 July 2005.

¹¹¹ MOL submission dated 8 September.

¹¹² In their reply to the SO, the parties claim that the lower average price of domestic gas is due to its lower calorific value. According to the parties, domestic gas and imported gas have the same price if calorific values are taken into account.

July 2005 (the “Supply Agreement”). The subject matter of the Supply Agreement is the delivery of domestic natural gas volumes produced by MOL E&P to MOL WMT.

- (292) The volumes of gas to be delivered by MOL E&P to MOL WMT under the Supply Agreement (Contracted Volumes) are set by reference to MOL E&P’s gas production forecasts. MOL’s current gas production forecasts are set out in Annex 7 of the Supply Agreement. MOL E&P has the obligation before 10 March every year to update its production forecasts for the remaining duration of the Supply Agreement.
- (293) The Supply Agreement foresees [...] to be contractually delivered for the [...] which correspond to MOL E&P gas production forecasts and are binding for those three years.
- (294) For the subsequent gas years, the Supply Agreement requires MOL E&P to provide by the 31st March preceding (e.g., by 31 March [...]) the contracted volumes which MOL E&P has the obligation to supply and MOL WMT the obligation to purchase. The Supply Agreement contains minimum delivery quantities of [0.5-2] bcm for the gas year [...] and [0.5-2] bcm for the gas year [...] and maximum quantities of [1-3] bcm from the gas year [...] to [...]. The Supply Agreement foresees a flexible system on the basis of which the actual yearly contracted volumes to be set by MOL E&P may deviate from its revised gas production forecasts, but by no more than 30%. In addition, the Supply Agreement states that MOL E&P has the obligation to make “reasonable efforts” in order to be able to set the gas production forecasts and the gas contracted quantities “as close to each other as possible”.
- (295) The Supply Agreement provides for a price formula, which takes into account a number of factors and is essentially linked to the [...] of natural gas in Hungary.

Availability of domestic gas for third parties

- (296) On the basis of the terms and conditions set by the Supply Agreement and of the Commission’s interpretation of the provisions relating to “Contracted Volume” in the Supply Agreement (including the [...] envisaged therein)¹¹³, the Commission has calculated the amounts that are likely to be delivered to MOL WMT in the gas years covered by the Supply Agreement. The results of these calculations are illustrated in the table below:

¹¹³ Response of E.ON of 6 July 2005 to Questions 5 and 6 of the Commission’s request for information of 29 June 2005.

Quantities in million m ³	MOL E&P Production Forecast		MOL WMT Contracted quantities	
	Total (1)	From existing fields (2)	Normal (3)	Min (4)
2005/2006	[1500-3000]*	[1000-2500]*	[1500-3000]*	[1000-2500]*
2006/2007	[1500-3000]*	[1000-2500]*	[1500-3000]*	[1000-2500]*
2007/2008	[1500-3000]*	[1000-2500]*	[1500-3000]*	[1000-2500]*
2008/2009	[1500-3000]*	[1000-2500]*		[1000-2500]*
2009/2010	[1500-3000]*	[1000-2500]*		[1000-2500]*
2010/2011	[1500-3000]*			[1000-2500]*
2011/2012	[1500-3000]*			[1000-2500]*
2012/2013	[1500-3000]*			[500-1500]*
2013/2014	[500-1000]*			[500-1500]*
2014/2015	[500-1000]*			[500-1500]*

- (297) Figures in column 1 reflect MOL E&P total production forecasts as indicated in Annex 7 of the Supply Agreement, including both expected production from existing fields and expected production from new fields, not yet exploited by MOL E&P.
- (298) Figures in column 2 reflect MOL E&P expected production of existing fields, already currently exploited. The Commission considers that these figures could represent a worst case scenario in case of difficult or unsuccessful exploitation of MOL E&P new gas fields.
- (299) Figures in columns 3 and 4 indicate the volumes of gas to be delivered by MOL E&P to MOL WMT under the Supply Agreement and on the basis of three scenarios (Normal and Min) taking into account the [...] foreseen by the Supply Agreement¹¹⁴.
- (300) Based on MOL's current production forecasts, the Commission has estimated the resulting gas volumes which may be available on the market for third parties in the three different scenarios:

¹¹⁴ The Agreement contains [...] for duration of the contract. Delivered quantities should also remain in a range of [...] around MOL E&P production forecast after the gas year [...].

Gas year	Quantities of MOL E&P production available for third parties (in million m ³)		
	Normal (1)-(3)	Worst case	Best case (1)-(4)
2005/2006	[0-500]*	[0-500]*	[0-500]*
2006/2007	[0-500]*	[0-500]*	[0-500]*
2007/2008	[0-500]*	[0-500]*	[0-500]*
2008/2009		[0-500]*	[500-1000]*
2009/2010		[0-500]*	[500-1000]*
2010/2011		[0-500]*	[500-1000]*
2011/2012		[0-500]*	[500-1000]*
2012/2013		[0-500]*	[500-1000]*
2013/2014		[0-500]*	[500-1000]*
2014/2015		[0-500]*	[0-500]*

- (301) The chart below (established by the Commission on the basis the Supply Agreement) gives a visual illustration of the very limited availability (if any) of domestic gas to third parties, even in the best case scenario:

Mol E&P's production available to third parties
(in million m³)

[...]*

Source: E.ON's reply to the Commission's request for information of 18 July 2005, Annex 21

Gas years [...]* to [...]*

- (302) The Commission has focused its assessment on the impact of the Supply Agreement on the [...]*, with the goal of assessing whether domestic gas produced by MOL E&P will be available on the market for third parties or not. As regards the subsequent years, the parties themselves acknowledge that [...]* it is difficult to predict which quantities of gas will actually be produced by MOL E&P, as it depends on its exploration activities, and which quantities will actually be delivered to MOL WMT on the basis of the Supply Agreement.
- (303) As shown clearly by the figures and the chart above, only marginal volumes of gas will be available on the market for [...]* and only in the best case scenario. These gas quantities, ranging between [200-600]* million m³, only represent [0-5%]* of the total expected Hungarian consumption needs.
- (304) The parties claim (also in their reply to the SO) that MOL WMT has no “*exclusivity rights*” over MOL E&P gas production, as no outright exclusivity clause is foreseen in the Supply Agreement. MOL E&P could theoretically sell gas produced from new fields and in excess of its production forecasts to third parties.

- (305) The Commission acknowledges that the Supply Agreement does not expressly provide MOL WMT with exclusivity purchasing rights over all of MOL E&P's domestic gas production. The Commission however considers that the most relevant figures to assess MOL E&P gas production quantities are MOL E&P's own current production forecasts. It should be pointed out that these figures already include expected production from new gas fields.
- (306) As the Supply Agreement explicitly indicates that the contracted gas quantities are MOL E&P's production forecasts [...]*, the Commission concludes that no domestic gas (at most minimal quantities due to [...]*) will be available for third parties during this period.
- (307) At any rate, most crucially, in their reply to the SO, the parties do not contest the Commission's finding that as a result of the Supply Agreement practically no quantities of domestic gas would be available for third parties on the market during the first three years. The parties state that "*already [...]* the agreement in fact allows MOL E&P significant discretion in deciding the amount of gas to be supplied to ERI/WMT*" while acknowledging that "*the forecast for [...]*) is binding*". Implicitly, they do not contest the Commission's finding that, as a result of the Supply Agreement, access to domestic gas will in practice be foreclosed to the new entity's gas and electricity competitors for at least [...]*.

Gas years [...] to [...]**

- (308) As regards the subsequent gas years, gas quantities potentially available to third parties increase to a maximum of [500-1300]* million m³ in [...]* in the best case, due to more flexible contracted volumes in the Supply Agreement. Although the Commission agrees with the parties that the quantities of domestic gas available to third parties after the [...]* period cannot be precisely evaluated, it should be noted that the Supply Agreement will in any case not allow third parties to have access to more than [25-35%]* of MOL E&P's gas production until 2014/2015 (slightly higher share taking into account the [...]*)).
- (309) The parties state, in their reply to the SO, that the figures elaborated by the Commission constitute a "*misrepresentation of the underlying agreement*" and that the Commission has made a "*significant factual error of assessment in its reading of the long-term supply agreement between MOL E&P and MOL MWT*"¹¹⁵. The parties however do not contest explicitly any of the figures presented in the tables in recitals 296 and 300. The Commission also underlines that this presentation is not only not misleading but even favourable to the parties as it only shows the figures for the "best case" scenario.
- (310) In their reply to the SO, the parties state that "*after the gas years [...]* and certainly after [...]*, a very significant if not all of the domestic production of MOL E&P will be available to be sold to third parties*" and that these quantities "*will continue to represent almost [15-25%]* of Hungarian gas consumption from 2008 to 2010*"¹¹⁶.

¹¹⁵ Parties' reply to the SO, II.4, page 17.

¹¹⁶ Parties' reply to the SO, II.4, page 17.

- (311) The Commission underlines that the [15-25%]* figure mentioned by the parties assumes that the entire domestic production would be available to be sold to third parties after the first three years of the contract, which seems at odds with the conclusion of a ten-year supply agreement between MOL E&P and MOL WMT. The Commission recognizes that MOL E&P's production forecasts beyond the gas years [...] is not binding. This gives MOL E&P some flexibility in its gas production activities, but not as regards the quantities that it is obliged to supply MOL WMT under the Supply Agreement which are based on MOL's production forecasts. The Commission notes that MOL E&P may not deviate by more than [...] from the production forecasts in setting the contracted quantities, and even has an obligation to make *reasonable efforts* to set the contracted quantities as close as possible to the gas production forecasts. In view of the figures presented above in recitals 296 and 300 (based on MOL E&P's current production forecasts and not contested by the parties), the Commission therefore estimates that the quantities will represent at most [5-15%]* of total expected Hungarian consumption needs. The quantities are in any case largely hypothetical and decline with the national gas production.
- (312) The parties also argue that "*the proposed transaction can only improve the potential for access to domestic gas production... [as it] creates the possibility of access by others, since the contracts with MOL exploration and production business falls short of either full ownership or exclusivity*"¹¹⁷.
- (313) The Commission acknowledges that the transaction, by which E.ON acquires MOL's gas wholesaling, marketing and trading business (MOL WMT) while MOL retains its gas production business (MOL E&P division), leads to an "ownership unbundling" of domestic gas resources by separating the supply and production activities of MOL. While prior to the transaction, MOL had no incentive to sell gas to any other third party that would have competed with its affiliate MOL WMT, MOL may as a result of the transaction have an incentive to also sell gas to unaffiliated parties.
- (314) However, in the Commission's view, this positive unbundling is strongly mitigated and offset by the ten-year supply agreement for domestic gas concluded, as part of the transaction, between MOL E&P and MOL WMT. To the extent of the volumes and duration of the Supply Agreement, MOL has already tied its "new freedom" to sell its domestic gas to whomever it pleases after the transaction. As demonstrated above, this agreement reserves most of MOL's future gas production for MOL WMT.
- (315) In addition, as MOL retains a 25%+1 shareholding in MOL WMT, the transaction does not remove all structural links between MOL E&P's domestic gas production and MOL WMT, contrary to what the parties claim. As a result of this structural link, MOL would still have the incentive to favour MOL WMT over third party traders in the sale of its domestic gas production¹¹⁸. MOL would naturally favour a

¹¹⁷ Parties' reply to the SO, Annex I, p. 11.

¹¹⁸ To avoid any potential confusion, the Commission does not state that MOL E&P's incentive to favour MOL WMT results from the proposed transaction. The Commission simply takes the view that the 25% minority shareholding that MOL will retain in MOL WMT will maintain MOL E&P's incentive to favour MOL WMT post transaction.

company in which it holds shares over any other company in view of its financial interest arising from the possibility to receive dividends and to obtain capital gains on the increase in value of its shareholding resulting from MOL WMT's greater profitability (even if no dividends were distributed). The [...] foreseen in the Supply Agreement may therefore lend themselves to being interpreted and resorted to so as to reduce the availability of gas to third parties.

- (316) The parties' argument that the Supply Agreement is necessary for MOL WMT to achieve [...], notably for its [...], does not appear convincing.
- (317) As a matter of fact, if gas suppliers other than MOL WMT were ever to purchase gas from MOL E&P, it would be by definition to serve customers in the liberalised sector. In view of the current "infancy" state of the liberalised sector in Hungary, these customers will have, in all likelihood, just exited the regulated segment of the market and signed a supply agreement with a gas trader. The amounts of gas previously needed by MOL WMT (or by any of the RDCs, which are, for the regulated segment of the market, exclusively supplied by WMT) to supply these customers will no longer be needed. Hence, MOL WMT will not need to retain gas resources to serve customers which are no longer in its portfolio.

Conclusion on access to domestic gas resources

- (318) The Commission believes that, even in the absence of a formal contractual exclusivity clause in the Supply Agreement (agreement between MOL and MOL WMT regarding MOL E&P domestic production), most (if not all) gas produced in Hungary by MOL E&P will be "captive" of MOL WMT, at the very least for the [...] of validity of the Supply Agreement and most likely also for the remainder of the contract¹¹⁹.
- (319) The Commission's market investigation has confirmed that the Supply Agreement will de facto provide the new entity with an exclusive control over the access to Hungarian domestic gas production and will prevent access to this resource by third parties during at least three years.
- (ii) *MOL WMT controls competitive import sources*
- (320) As indicated, there are only two entry points through which gas is imported into Hungary: Beregovo at the Ukrainian border and the HAG at the Austrian border.

¹¹⁹ To avoid any potential confusion, the Commission does not state that third parties' access to domestic production will be reduced as a result of the proposed transaction. The Commission however concludes from the new Supply Agreement concluded between MOL E&P and MOL WMT (as part of the transaction) that the new entity will have an almost exclusive access to domestic gas production during [...] (as MOL WMT before the transaction). This strongly offsets any pro-competitive effect that the (partial) unbundling realised by the proposed transaction between MOL E&P and MOL WMT may have had.

a. Competitive gas import sources in Hungary

- (321) With the exception of marginal quantities of Turkmen gas, all gas imported into Hungary is of Russian origin (i.e. Gazprom)¹²⁰. The market investigation has established that the only competitive source of gas in Hungary is coming from Russia, either Russian gas sourced from Gazprom or gas sourced from another country in the Commonwealth of Independent States (“CIS”)¹²¹, but which needs to be transported through Russia and Ukraine (via transit pipelines under the control of Gazprom).
- (322) Hungary is not geographically close to and/or connected through existing pipelines to other sources of gas in Europe, such as Norwegian gas, Dutch gas, Algerian gas or Middle East and Caspian gas. There is also no LNG (Liquefied Natural Gas) terminal close to Hungary. The HEO estimates that, due to the distance between Hungary and the gas sources and based on the current conditions of supply, the access to competitive alternative sources of gas is limited for Hungary. Due to the direction of gas flows and transportation costs, North African gas by pipeline or delivered as LNG to a North Adriatic port (e.g. Omisalj) is in any case more expensive than Russian gas. Due to North Sea gas flows directions, the only possible solution to source gas from this region is swapping, but the resulting gas price only matches the Russian import price in the best case scenario.
- (323) Alternative gas sources are not expected to be available in Hungary before 2011 with the completion of the Nabucco pipeline, through which gas from the Middle East (Egypt, Iraq, Iran) and the Caspian area could be imported. The other envisaged pipeline projects between Hungary and Slovakia and between Hungary and Romania, if ever constructed, would not bring additional sources of gas into Hungary as Slovakia is also supplied by Russian gas and as Romania initially only intends to import gas from Hungary due the decrease in its national production.
- (324) In their reply to the SO, the parties do not dispute that the only competitive sources of gas in Hungary are currently Russian and/or CIS gas.

b. MOL WMT’s gas sourcing portfolio

- (325) As indicated, prior to the market opening, MOL had a monopsonistic position on all gas procurement activities, with exclusive rights to purchase Hungarian gas and to import gas into Hungary. In order to secure its gas supply, MOL WMT has entered into long-term supply agreements with [...] to import gas through the Hungarian Western and Eastern entry points.

Overview of MOL WMT’s existing long-term gas import contracts

¹²⁰ Gazprom ultimately controls, directly or indirectly, also the access to Turkmen gas, as indicated by both EMFESZ and Centrex, the two trading companies importing (or planning to import) Turkmen gas into Hungary.

¹²¹ In particular gas from Turkmenistan.

- (326) As can be seen from the above table, MOL WMT has [...]* import contracts with [...]*, which account for the vast majority of its gas imports. MOL WMT purchases approximately [5-20]* bcm from Gazprom/Gazexport through Panrusgáz, its joint venture with Gazprom/Gazexport, which is delivered at the Beregovo (81.4%) and HAG (18.6%) entry points.
- (327) MOL WMT also purchase [0-2]* bcm of gas annually from EMFESZ, a Hungarian company affiliated with Eural Trans Gas. MOL initially concluded the contract with Bohlti Trade, a Swiss Company also affiliated to Eural Trans Gas to ensure Hungary's winter gas supply, at a price that is “*lower than the main market (dominant) PRG [Panrusgáz] price*”¹²³. Eural Trans Gas is a Hungarian-registered company which is the sole distributor of Turkmen gas “*with Gazprom and NAK Ukraine support*”¹²⁴. Bothli-Trade subsequently assigned its two gas supply contracts with MOL WMT to EMFESZ Kft.¹²⁵.
- (328) Finally, MOL WMT purchases [0-2]* bcm/year from E.ON and [0-2]* bcm/year from [...]* at the HAG entry point. This gas is approximately [...]* more expensive than the gas purchased from Gazprom/Gazexport via Panrusgáz or from EMFESZ. It is supplied from [...]* on the basis of their overall gas purchase portfolio, although physically it is Russian gas. This gas is clearly not competitive with the direct Russian gas supply from Gazprom/Gazexport.
- (329) In particular, gas imported through the Western entry point is less competitive due to the cost of transit through Slovakia and Austria, which is estimated at 4.0 HUF/m³ (or approximately [10-20%]* of MOL WMT's average gas purchasing price¹²⁶). A third party active in gas has stated that “*In theory, the minimum price difference for gas between Beregovo and Mosonmagyaróvár corresponds to the transport costs through Slovakia to Baumgarten, plus the transport costs through the HAG system, it can be estimated at around 1,3 - 1,6 €/MWh according to the conditions of delivery. In reality, this difference can be much higher as the prices at Baumgarten and at Beregovo are not linked. Indeed, the specialized press mentioned prices above 21 €/MWh at Baumgarten during the last Econgass' auctions, and prices below 15 €/MWh at the Ukrainian border.*”

¹²² The contract started [...]*; the normal annual quantity is [0-3]** bcm.

¹²³ [...]* ; and minutes of the meeting with EMFESZ on 28 July 2005, p. 2: “*Since 1 January 2005, EMFESZ is selling 1.2 bcm to MOL WMT. EMFESZ believes that it is selling to MOL WMT for its gas needs as a trader licensee (and not as a public utility wholesaler licensee). MOL WMT buys from EMFESZ the additional quantities it needs in winter, and buys a stable quantity throughout the year under its contract with Gazprom.*”

¹²⁴ [...]*.

¹²⁵ [...]*.

¹²⁶ Assuming a wholesale gas price of [25-35]* HUF / m³.

- (330) The parties indicated that the cost of transit of gas through the SPP network in Slovakia amounted to [0-2]* EUR/MWh under the presumption of 10 million m³/day, in addition to which customers have to contribute fuel gas in kind amounting to [0-5%]* of transported volumes¹²⁷. Assuming a cost of gas of approximately [28-32]* HUF/m³, the total cost of transportation through the SPP network is [2-4]* HUF/m³. Tariffs on the HAG pipeline were provided by OMV, owner of the pipeline, and amount to approximately [0-1]* HUF/m³ under the assumption of a 3 year capacity booking for 1 bcm/year.
- (331) As mentioned above in recital 40, the gas supply contracts with E.ON and GDF were entered into by MOL in order to diversify its gas sourcing portfolio, thereby increasing the country's security of supply, under the pressure of the Hungarian government.
- (332) It follows that anyone wishing to compete with MOL WMT on the market for the wholesale supply of gas in Hungary must have access to Russian gas (or gas from CIS countries transiting through Russia); and must preferably source a significant part of its gas portfolio through the Eastern entry point (the more competitive entry point)¹²⁸. The market investigation has clearly indicated that, until there are no alternative independent sources of gas (such as the Nabucco pipeline in 2011-2012¹²⁹), all gas sources will be controlled by Gazprom and no competition will be able to develop on the Hungarian wholesale gas markets.

c. Difficult access to Russian gas

- (333) The market investigation has shown that it is currently difficult for new entrants to get access to Russian gas in parallel to MOL WMT's existing contracts. It appears that there would be no incentive on the part of Gazprom to sell "more" gas for exports to Hungary, other than the gas necessary to meet the 2% yearly demand increase, to cover the "supply gap" between the future increase in the Hungarian demand and the demand already covered by the existing long-term import contracts of MOL WMT.

¹²⁷ Submission of the parties dated 14 October 2005.

¹²⁸ Response of Euro-Bridge to the request for information of 3 June 2005 (*"According to our experience, seeing the situation in the Hungarian gas industry and in particular with regard to E.ON's planned steps, we have doubts if there will ever be a real competitive market and competitive conditions in Hungary, as:*

- *The gas supply is practically dependent upon one gas source (the Russian Gazprom) coming through the Eastern cross-border pipelines. The Western pipeline has small capacity and only has a strategic role in case there is turmoil in the Eastern side. The gas coming from West (Russian as well) has a significantly higher price level, the Hungarian consumers could not afford purchasing exclusively this gas;*
- *The country's gas supply is practically in MOL's hands, the gas distribution companies buy gas from MOL, as there is no other more economic way. It is very obvious, that new market player cannot enter the market without the approval (interests) of MOL and Gazprom (an example of this is RoszUkrEnergo or EMFESZ)".*

¹²⁹ Although according to the HEO, due to the 3,000 kilometres pipeline planned, gas from the Middle East is not likely to be cheaper than the Russian gas.

- (334) Gazprom already supplies through Panrusgáz, its joint venture with MOL, gas quantities covering most of the needs of Hungary. The Commission believes that it is not possible to purchase gas from Gazprom to compete with MOL WMT: first, Gazprom has no incentive to sell gas to another gas trader at a cheaper price that would compete with the quantities it sells to MOL WMT through Panrusgáz and the quantities sold would simply displace the quantities it already sells for the Hungarian market¹³⁰; secondly, the only incentive would be if Gazprom could sell gas at a higher price. However, the gas Gazprom would sell at a more expensive price would not be competitive in Hungary unless the entrant was able to operate at a lower cost than MOL WMT, in spite of the latter's incumbency advantages, or if the price was not substantially higher.
- (335) In other words, it appears that Gazprom has no incentive to supply additional competitive gas to E.ON or any other operator(s) to the extent that it only risks displacing/out-pricing its current sales.
- (336) If anything, MOL WMT's privileged access to Russian gas (due to Gazprom's current lack of incentives to support independent entry of competitors of MOL WMT) will be strengthened due to the privileged relationship and strategic partnership between Gazprom and E.ON. In view of the fact that access to competitive gas (namely Russian gas or CIS gas transiting through Russia) is the main barrier faced by new entrants, the Commission believes that the new entity will be no less, or even more, dominant after the transaction, compared to MOL WMT prior to the transaction.
- (337) It is indeed even less likely that Gazprom would support the massive entry of a competitor of MOL WMT after the transaction in light of the close links and strategic partnership of Gazprom and E.ON. In particular, E.ON has a 6.5% ownership in Gazprom¹³¹ and has a representative at Gazprom's Board of Directors. The two groups have entered into various large scale and long-term supply agreements and intend to further expand their cooperation in various areas, as stated in [...]*. There also appears to be an agreement signed between Gazprom and E.ON to coordinate moves related to privatization of gas industry facilities, transit gas pipelines in Slovakia, Czech Republic and Hungary¹³².
- (338) In addition, the Hungarian press recently referred to plans of Gazprom to become a shareholder in MOL WMT or in other E.ON downstream subsidiaries¹³³. This is [...]*¹³⁴. E.ON has [...]*¹³⁵.

¹³⁰ A third party active in gas has stated that “*Supply in Hungary is dominated by Panrusgáz which buys from Gazprom. We do not think that a merger would change the situation as on the one hand long term supply contracts exist and on the other hand Gazexport has a stake in Panrusgáz. We do not think that Gazexport will create its own competition by supplying gas to new companies at lower prices.*”

¹³¹ E.ON has a 3.5% direct shareholding in Gazprom and a 3 % indirect shareholding through the Gerosgaz JV, an OOO Gazexport and Ruhrgas AG JV, created in 1999.

¹³² See Gazprom's website <http://www.gazprom.ru/eng/articles/article8925.shtml>, as of July 6, 2005.

¹³³ See, e.g. Agence France Presse of 1 April 2005 *Gazprom intéressé par 11,8% de MOL*.

(339) It is fair to say that E.ON (which will take over MOL WMT's position as Gazprom's partner in Hungary after the implementation of the transaction) is a more significant and valuable partner of Gazprom than MOL was prior to the transaction for several reasons. E.ON purchases greater volumes of gas from Gazprom in Europe and, given its extensive presence in European markets, is a more privileged partner than MOL to help Gazprom achieving its strategy to enter downstream European gas markets. Furthermore, as regards gas transportation, Germany, due its central position in Europe, is an essential transit country to reach significant gas markets, in particular France and the UK¹³⁶. Finally, E.ON (along with Wingas) will be a partner of Gazprom for the construction of major new pipeline between Russia and Western European markets (Baltic pipeline).

(340) In conclusion, no competitor of MOL WMT can enter the Hungarian gas market without the approval and support of Gazprom and E.ON/MOL and at most only for limited quantities corresponding to the future "supply gap" in Hungary. The table and charts below illustrate this "supply gap" and evidence the limited possibility for additional gas imports into Hungary:

<i>Data in million m³</i>	Total Hungarian gas demand	Hungarian domestic production	Total import quantities forecasted by E.ON/MOL under long-term contracts	"Supply gap"
2005	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2006	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2007	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2008	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2009	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2010	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2011	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2012	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2013	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2014	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*
2015	[13000-20000]*	[1000-3000]*	[11000-13000]*	[0-4000]*

Source: E.ON's reply to the Commission's request for information of 18 July 2005, Annex 21

¹³⁴ Niederschrift über die Sitzung des Vorstands der E.ON Ruhrgas International AG am 9. August 2004, per Telefonkonferenz, Vorlage für den Vorstand, p. 7, Annex 8 of Form CO.

¹³⁵ Response of E.ON of 10 May 2005 to question 19 on draft Form CO.

¹³⁶ See, e.g., article "Russian' energetic enigma" in The Economist of 6 October 2005: "Last month, Mr Putin and Gerhard Schröder, Germany's chancellor, presided over the launch of Gazprom's latest mega-project: a €4 billion (\$5 billion) pipeline that will run under the Baltic Sea to Germany, Gazprom's biggest foreign customer, and thence, eventually, to Britain. Mr Putin again extolled the scheme's importance at the EU-Russia summit this week. Almost half of the European Union's gas imports come from Russia. European demand is expected to double between 2000 and 2030. Gazprom and the Russian government say that the Baltic pipeline is a useful way to diversify supply routes to a growing market."

Hungarian gas supply

[...]*

Source: E.ON's reply to the Commission's request for information of 18 July 2005, Annex 21

(341) The difficulty/marginality of “independent” entry is evidenced by the entry of EMFESZ, the only entrant so far, and the planned entry of CENTREX, while other more established Western European market players also outlined the difficulty to enter the Hungarian gas market.

EMFESZ

(342) EMFESZ is the only new entrant on the Hungarian gas markets as of July 2005. The company purchases gas from Turkmenistan and has gained half of the customers that have switched to the open segment of the market. The gas supplier of EMFESZ is RosUkrEnergó (also referred to as RosUkrGazprom¹³⁷), a Swiss-registered company owned 50% by Gazprombank and 50% by Raiffeissen Investment AG, an Austrian investment company¹³⁸.

(343) The market investigation has suggested that EMFESZ' entry has been facilitated by Gazprom and MOL WMT. It depends on MOL for its access to customers and infrastructures (in particular it depends on a gas swap with MOL WMT to meet the 80/20 rule)¹³⁹. The main customers of EMFESZ are MOL WMT ([0-2]* bcm/year, see Bothli-Trade contracts in the table in recital 325) and Nitrogenmúvek, an industrial customer that is allegedly managed by former MOL executives ([0-2]* bcm/year)¹⁴⁰. According to some market respondents, the other customers targeted and quantities supplied by EMFESZ are not so significant¹⁴¹. EMFESZ itself planned to supply 0.3 bcm of gas in Hungary in the first year of its entry and up to 1 bcm in the long term¹⁴². The company currently supplies approximately 0.5 bcm to

¹³⁷ See the article in the issue of 23 August 2005 of *European Gas Markets* (published by Heren Energy) “RosUkrEnergó's activities scrutinised”.

¹³⁸ It is however unclear whether EMFESZ can become a long-term player on the Hungarian gas market as its supplier RosUkrEnergó is being investigated in the Ukraine. See, e.g., front page article in the *Financial Times* of 27 July 2005 “Probe into criminal link to Gazprom company”; article in the *European Gas Markets* (published by Heren Energy) of 23 August 2005 “RosUkrEnergó's activities scrutinised”. As a result, some multinational customers indicated that they would not purchase gas from EMFESZ due to concerns as to its reliability and bad reputation

¹³⁹ Response of EMFESZ to Question 42 of the request for information of 3 June 2005; minutes of meeting with EMFESZ on 28 July 2005.

¹⁴⁰ To avoid any potential confusion, the Commission does not state that MOL has an ownership interest or voting rights in EMFESZ or in Nitrogenmúvek.

¹⁴¹ Response of Euro-Bridge to the request for information of 3 June 2005; minutes of the teleconference with Centrex on 9 August 2005.

¹⁴² Response of EMFESZ to Question 13 k) of the Commission's request for information of 19 July 2005.

other customers. EMFESZ's dependency upon/cooperation with MOL is confirmed by [...]*

CENTREX

- (344) Centrex Hungary is a start up company, wholly-owned by Centrex Europe Energy and Gas AG, an Austrian group founded in April 2004. The Hungarian subsidiary was created in September 2004 to start activities on the Hungarian energy markets. CENTREX does not yet have any trading activities or customers but has already planned its entry on the Hungarian gas markets and to reach sales of approximately 0.5 bcm the first year of its entry and 2 bcm in the long-term¹⁴⁴.
- (345) CENTREX has privileged access to competitive gas sources through its cooperation with Gazprom. In particular, CENTREX executives claim to have close personal relationships with Gazprom executives¹⁴⁵. In Hungary, the company intends to import gas produced by the Centrex group through gas consortiums with Gazprom (in that case it depends on Gazprom to transport its gas to the European markets of Centrex) and gas procured from Gazprom. The company is currently negotiating its gas supply agreements with Gazprom.

Western European market players

- (346) The other European importers/wholesalers which already purchase gas from Gazprom at delivery points close to Hungary (such as GDF, OMV and ENI/Italgas in Baumgarten) do not appear to be potential competitors of MOL WMT¹⁴⁶. The main reason is that gas available at Baumgarten is not competitive in Hungary. To compete with MOL WMT, these operators would need a more competitive portfolio of gas, with a significant proportion sourced at the Eastern entry point, but Gazprom would most likely not allow these companies to enter the Hungarian gas market (with additional gas sourced at the Eastern border) at the detriment of Panrusgáz and MOL WMT, as explained above in recitals 333 to 340.
- (347) This is confirmed by MOL WMT's internal documents that [...] the risk of new entries in Hungary and [...] E.ON/MOL WMT essentially focuses on the access to gas of the new entrants on the Hungarian gas market when assessing their respective position and strengths, as evidenced by the table below¹⁴⁸:

¹⁴³ Minutes of the Executive Board of MOL of 6 April 2004.

¹⁴⁴ Minutes of the conference call with CENTREX of 9 August 2005 and response of CENTREX to Question 13 k) of the Commission's request for information of 19 July 2005.

¹⁴⁵ Minutes of the conference call with CENTREX of 9 August 2005.

¹⁴⁶ See, e.g., the response of FŐGÁZ to question 30 d) of the request for information of 19 July 2005 as regards E.ON's position as potential competitor of MOL WMT: *“Die EMFESZ Kft., CENTREX Rt. und eventuell andere Marktteilnehmer mit günstigen östlichen Bezugsquellen hätten bessere Chancen als die E.ON in einer Grosshändlerrolle gehabt.”*

¹⁴⁷ Report to the Supervisory Board of MOL of 2 June 2003, Budapest, “Gas Business Situation”, slide 6.

¹⁴⁸ Response of E.ON to Question 87 of the request for information of 18 July 2005 and Annex 87.

[...]*

- (348) Finally, even assuming that other operators could have access to sufficient quantities of gas at the Eastern entry point, the market investigation has clearly shown that MOL WMT controls and saturates the Eastern entry point¹⁴⁹. There are currently no available free capacities at the Beregovo entry point¹⁵⁰. As shown above in recital 34, almost all capacities are booked by MOL WMT, as well as by the Serbian company Nis and the Bosnian Herzegovinan company BHGas for transit.
- (349) Accordingly, the Commission believes that access to gas from Russia/CIS countries at Hungary's Eastern entry point is essential to compete on the Hungarian gas markets. These gas sources and/or their transport to Hungary is controlled by Gazprom, which supplies gas to MOL WMT, its partner in the country. As evidenced by the parties' internal document, access to competitive gas from Russia / CIS countries therefore constitutes a strong barrier to entry on the Hungarian gas markets.

d. The parties' reply to the SO as regards access to competitive gas imports

Gazprom incentives

- (350) In their reply to the SO¹⁵¹, the parties go a long way to try to “*demystify*” the “*special relationship*” between E.ON and Gazprom, as described by the Commission. The parties' argument is two-fold.
- (351) Firstly, it is argued that the Commission is mistaken in considering that the 6,4% shareholding and E.ON's having one representative in Gazprom's supervisory board do imply that the relationship between the two companies is “special”. To do so, the parties describe other allegedly “special” relationships that Gazprom would have with other Western companies.
- (352) However, what clearly emerges from the parties' line of argument is that none of the other Western companies has a shareholding in Gazprom and/or one representative

¹⁴⁹ See, e.g., the response of GDF to Question 29 g) of the request for information of 19 July 2005.

¹⁵⁰ Minutes of the meeting of 26 July 2005 with the HEO. According to the HEO, the Beregovo entry point is contractually congested (and physically congested in winter), as capacity is booked but not fully used. This contractual congestion is caused by transit. Transit flows to Serbia have seasonal variations because there is no storage capacity in Serbia, so that the transit capacity booked is not fully used during summer. The HEO wanted to force MOL Transmission to use the capacities booked for transit but not used for transit during the summer on the basis of use-it-or-lose-it principle but MOL Transmission brought the demonstration that under their long-term transit contract with the Serbian operator (the capacity is booked on a ship or pay firm basis and the Serbian operator paid for the cost of network development), MOL Transmission cannot use unused capacity for Hungarian transport needs.

¹⁵¹ Parties' reply to the SO, II.3.1, pages 11-13 and annex 1, pages 12-13.

in its supervisory board. These two elements, by themselves, suffice to qualify the E.ON/Gazprom relationship as “privileged” as compared to other allegedly “special” relationships.

- (353) Moreover, the parties have not even attempted to dismiss (and not even commented upon) the information contained in paragraph 341 of the SO as regards the possibility that E.ON and Gazprom may agree on Gazprom’s acquiring a [...]*.
- (354) To the Commission’s understanding, all this provides sufficient ground for considering the E.ON/Gazprom relationship as “privileged”, in spite of the parties’ arguments and attempts to dismiss such claims.
- (355) Secondly, and most importantly, still with the objective to “*demystify*” the E.ON/Gazprom relationship, the parties argue at length that, regardless of the nature of the relationship between the two companies and also in the absence of the transaction, Gazprom would have no financial incentives to “*undermine the price in existing contracts*”. The parties even quote, as confirmation of their analysis, the Commission’s statement that “*it is not possible to purchase gas from Gazprom to compete with MOL WMT: first, Gazprom has no incentive to sell gas to another gas trader at a cheaper price that would compete with the quantities it sells to MOL WMT through Panrusgáz and the quantities sold would simply displace the quantities it already sells for the Hungarian market*”¹⁵².
- (356) The parties’ argument is simple: “*if matters are so bleak, they cannot get any worse*”. Hence, it is argued that at any rate the “*special relationship cannot make matters worse*”.
- (357) The Commission believes that by developing this line of argument the parties have in fact blatantly supported the Commission’s assessment of MOL and E.ON relationship with Gazprom and the strategy and incentives of Gazprom for the supply of gas to Hungary.
- (358) As a matter of fact, even assuming (for the sake of the argument) that the E.ON/Gazprom relationship is not “privileged”, what really matters here is that the essential change brought by the proposed transaction is the creation of a fully vertically integrated entity along the gas and electricity supply chains.
- (359) While MOL WMT, even prior to the transaction, had the ability to exploit its dominant position in gas, it lacked any incentives to do so. In the pre-transaction scenario, Gazprom’s “financial incentives” not to sell gas to competitors of MOL WMT at lower prices than in existing contracts (as described by both the Commission and the parties) would not give rise to the risk of foreclosure. In the post-transaction scenario, the combination of Gazprom’s “financial incentives”, which would remain unchanged, and E.ON’s incentives, which would change, as compared to MOL’s, would directly result in the new entity having the ability and the incentive to significantly impede competition by foreclosing access to gas resources.

¹⁵² SO paragraph 338.

- (360) In conclusion, the Commission first notes that the parties' reply to the SO confirms the assessment in the SO on access to competitive gas for import into Hungary and Gazprom's lack of incentives in supplying gas to other companies in competition with the new entity. Secondly, the Commission does not state that E.ON's privileged relationship with Gazprom will dramatically change the possibilities to import competitive gas in Hungary but simply that it will further limit Gazprom's – already low – readiness to supply others competitors.

Availability of competitive gas in Baumgarten for import into Hungary

- (361) In their reply to the SO, the parties dispute the SO's conclusion that competitors of MOL WMT cannot enter the Hungarian wholesale gas market from Baumgarten. According to the parties, several large players in the European gas industry import gas via Baumgarten and could easily divert their imports to the Hungarian gas market. According to the parties, this will be made possible by the upcoming significant gas surpluses which these players will face and the upcoming removal of price regulation in the market to eligible customers in Hungary¹⁵³. According to the parties, Baumgarten (as the marginal entry point) will attract additional imports if Hungarian demand cannot be satisfied through imports made at the Eastern border.
- (362) The Commission first notes that the parties do not dispute that currently MOL WMT is more competitive due to its portfolio of existing long-term gas supply contracts¹⁵⁴, and arguably, that the new entity would immediately after the transaction have the ability to discriminate its downstream competitors. In addition, the parties do not dispute that the price of gas available in Baumgarten is higher than MOL WMT's gas prices under its portfolio of existing supply agreements.
- (363) The parties however take the view that, at a later stage, imports made through Baumgarten will become competitive. There appear to be three pre-requisites for the competitive scenario presented by the parties in their reply to the SO to unfold: (i) there must be significant gas surpluses that could be diverted to Baumgarten; (ii) there must be significant entry capacity available at Baumgarten; and (iii) there must be price and regulatory changes in Hungary.
- (364) The competitive scenario presented by the parties appears speculative and indirect at best and does not address convincingly any of three pre-requisites mentioned above in recital 363.

i) Gas surpluses that could be diverted to Baumgarten

- (365) The Commission has not found any compelling evidence as regards the existence or the development of significant gas surpluses that would corroborate the scenario presented by the parties' expert.

¹⁵³ Reply to the SO, II.1.1, page 6.

¹⁵⁴ MOL WMT's current gas sourcing portfolio is comprised at 90% of Russian and Turkmen gas at advantageous prices, which is for 81.4% imported through the Eastern entry point.

- (366) First, it is worth recalling that this scenario is in contradiction with MOL WMT's own internal documents quoted at paragraph 349 of the SO, that [...] ¹⁵⁵. The parties do not even try to explain this contradiction.
- (367) Secondly, as mentioned above in recitals 355 and 357, the parties do not dispute the argument developed in the SO that Gazprom has no financial incentives to supply at Baumgarten additional volumes of gas for the Hungarian market. This is because by doing so Gazprom would be undermining Baumgarten prices under existing contracts and supporting independent entries in competition with Panrusgáz/MOL WMT. The expert report provided by the parties even develops further the reasons why Gazprom has no financial incentives to sell gas to competitors at lower prices than in existing contracts and undermine Baumgarten prices:

“Assume that Gazprom signs a contract with MOL WMT at a high price, and then starts selling gas to a second importer at a low price because the relationship with MOL was not sufficiently special. The new importer could profitably reduce the gas price in Hungary. However, Gazprom would suffer as a result, as its low-priced sales to the second importer would displace the volumes that Gazprom previously sold to MOL. Gazprom would also risk facing demands by MOL to renegotiate the price. The standard European gas contract contains “price re-opener” provisions that protect buyers. The reduced price to the second importer would permit it to sell gas at a discount in Hungary. The discounts would prompt MOL WMT to complain that the market price in Hungary was falling, that the decrease lay beyond MOL's control, and that the gas price charged by Gazprom should fall to the level necessary to restore MOL's profitability. If Gazprom disagreed, MOL could have a neutral arbitrator evaluate the claim. (...)

[T]he discussion above suffices to establish Gazprom's incentives. If Gazprom starts selling gas at €1/MWh less than the price under existing contracts, then Gazprom will face two consequences. First, Gazprom will lose €1/MWh on every sale by the new importer who displaces the sale of high-priced gas by existing importers. Second, Gazprom will face the prospect of claims by the existing importers, to reduce the Baumgarten price by €1/MWh. Gazprom therefore opens up the prospect of selling gas to everyone in the market at €1/MWh less than previously. Gazprom's incentives are simple: sell as much gas as possible without undermining the price in existing contracts.”

- (368) As Gazprom is not willing to supply additional gas in competition for the volumes of gas it already supplies via Panrusgáz for the Hungarian market, only operators which *already* have access to competitive (Russian) gas at or near Baumgarten could be in a position to divert this gas to Baumgarten for supply in Hungary. Indeed, other operators with gas delivered far from Baumgarten would incur significant costs of transport to Hungary, which would make such imports non-competitive (assuming that the necessary transit capacity would be available and not fully booked under long-term capacity reservation agreements).
- (369) However, it appears that none of the operators having gas in Baumgarten has significant volumes of gas which it could divert to supply the Hungarian gas markets. In particular, earlier expectations of a gas bubble in Italy, on which the

¹⁵⁵ Report to the Supervisory Board of MOL of 2 June 2003, Budapest, “Gas Business Situation”, slide 6.

parties rely to a great extent in their reply to the SO, no longer appear likely, on the basis of the latest information from the Italian energy regulator¹⁵⁶. ENI has been able to renegotiate its gas supply agreement with Gazprom and to reduce the level of its take-or-pay obligations¹⁵⁷. It appears that gas volumes available to other gas market players in Baumgarten are fully committed under existing long-term supply agreements with other traders/customers, so that these operators would need to source additional volumes from Gazprom to be able to enter the Hungarian gas market¹⁵⁸.

- (370) Thirdly, the parties' arguments about surpluses of gas in Western Europe and their export to Hungary do not appear to rely on any solid evidence. The only figures provided to show the existence of gas surpluses are in another study¹⁵⁹ which the expert report refers to. The figures provided by the expert are either misinterpreted or irrelevant for the present case. For example, the report provides data on the capacities of LNG terminals in the South of France and discusses capacities of LNG terminals on the US Gulf Coast, which appear to the Commission of little relevance for the supply of gas in Hungary. In the same way, the graph presenting the balance between supply and demand in Italy (Figure 1, Page 8) clearly shows that TOP supplies are in line with the countries' projected demand, although the report uses it to show the (allegedly) excess of contracted gas over projected demand in Italy.
- (371) The expert report provided by the parties states (without any concrete evidence) that there are (will be) gas surpluses in various Western European countries, in particular Spain, Italy and the UK. This would result in gas companies diverting these surpluses to other European countries, in particular France, and would in turn create gas surpluses in France. ENI/Italgas and GDF would then use these surpluses for export into Hungary (Pages 1 to 9 of the Expert Report). As mentioned, this competitive scenario appears at best indirect, and presupposes that all the circumstances on these other European markets be met. The Commission notes that none of these circumstances or their causal relationship is demonstrated by the parties. All the relevant factors that would have to be assessed to support the parties' far-reaching conclusions are not mentioned (let alone analysed) in the report: evolution of gas demand in several European countries and their determining factors, evolution of the competitive environment of the gas sector in several European countries, development of new gas transport infrastructures, etc.
- (372) In addition, it appears speculative to assume that any excess volumes (assuming there will be gas surpluses) would be diverted specifically to Hungary and not to

¹⁵⁶ See e-mail of 24 October 2005 from the Italian regulator, Autorità Energia.

¹⁵⁷ See, inter alia, Financial Times article of 21 October 2005 "*Gazprom and Eni axe 'outdated' gas deal after contract dispute*": "*Eni will be anxious in any new agreement to preserve significant financial concessions that it won from Gazprom concerning the remainder of the gas that it purchases. Gazprom offered to extend the contract on the gas by 10 years to 2027 with its existing price-setting mechanisms and change a crucial "take-or-pay" clause that could save Eni millions of euros if the gas price fluctuates.*"

¹⁵⁸ [Confidential: Statements on gas quantities available in Baumgarten for a certain gas operator]

¹⁵⁹ Frisch, Carpenter and Lapuerta: "The Advent of US Gas Demand Destruction and its Likely Consequences for the pricing of Future European Gas Supplies", March 2005

other gas markets with a higher price level. For example, according to E-Control, the Austrian Energy Regulator, the largest part of the gas quantities sold in Econgass' auctions in 2005 was exported to Italy. The Commission therefore concludes that it is currently economically more interesting to export gas available in Austria to Italy than to Hungary. Finally, although it discusses the current and future developments of European gas markets, the other study to which the expert report refers does not even mention the possibility that these surpluses could be exported to Hungary¹⁶⁰.

- (373) In view of the above, it appears that the parties' allegations on potential gas surpluses that would be diverted to Hungary through Baumgarten are largely speculative. They are neither supported by any evidence brought forward by the parties nor by the information gathered by the Commission in the course of its extensive market investigation.

ii) Availability of entry capacity into Hungary

- (374) In Hungary, the Western entry point has only a 4.5 bcm/year import capacity while the Eastern entry point has approximately an 11 bcm annual capacity for imports into Hungary (4 bcm are reserved for transit). Therefore, in any event, the bulk of the gas used in Hungary will still be imported by MOL WMT (and other new entrants to the extent of Gazprom's support) through the Eastern entry point in the medium term.

- (375) In order to import gas from Baumgarten, potential new entrant would have, in addition to sourcing gas, (i) to book transport capacity on the HAG pipeline between Baumgarten and Hungary and (ii) to book cross-border transmission capacity at the Hungarian Western entry point. The market investigation showed that both of these capacities would be difficult to obtain due to the significant share of capacities already booked by MOL.

- (376) With respect to the HAG pipeline, the Commission believes that new entrants may face difficulties in obtaining access to transport capacity. As an example, E-Control, the Austrian regulator reported to the Commission:

“At present system access is on the basis of negotiated contracts, and is not regulated. Because of this no information is available as to how long-term transport rights on the transit pipeline are assigned, i.e. who has access to which second-level

¹⁶⁰ The above-mentioned study of Frisch, Carpenter and Lapuerta takes the view that the construction of planned LNG terminals will nevertheless proceed in the UK, and that, as surplus emerges, UK developers will try to re-export to continental markets through the Bacton-Zeebrugge Interconnector and the Bacton-Balgzand pipeline being constructed. The study also foresees the emergence of surplus in Italy, which Italy will try to avoid by reducing its imports and selling the excess gas via backhaul to countries located to its north and west, through which transit pipes serving Italy pass, namely Austria, Germany, France and Switzerland. The Spanish gas surplus could only be dealt with through onward sale of LNG cargoes (as Spain has limited pipeline capacity with France and therefore fewer opportunities to serve Northern European markets through the backhaul of pipeline gas). The Spanish oversupply (in the form of surplus LNG cargoes) could influence gas markets in North West Europe as well as Italy.

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wholesale markets (Germany, Italy, etc.). It is difficult for new entrants to obtain access to transit pipelines. No capacity is currently reserved for new customers on any of the cross-border pipelines."¹⁶¹

- (377) The Commission has analysed existing capacity bookings on the HAG provided by the OMV, the operator of the pipeline. [Confidential: Data on capacity bookings on the HAG pipeline].
- (378) The situation is similar for the cross-border capacity at Hungary's Western entry point. In this regard, the expert report fails to recognize that potential new entrants through the Western entry point would also face severe capacity constraints. The report indicates that "[u]nder the capacity allocation rule, the full 4.5 bcm could become available to competitors". This statement is misleading as MOL WMT has already booked a significant part of the cross-border capacities ([2-5]* bcm out of 4.5 bcm/year, or [5-15]* million m³/day out of 12.3 million m³/day) for its import contracts¹⁶². This situation is not expected to change in the medium term as Already Allocated Capacity has priority under the cross-border capacity allocation rules. MOL WMT requires in any case a significant part of the Western entry point capacity to perform its obligations under its gas import contracts and their related TOP obligations.
- (379) Finally, according to the parties, MOL WMT is also planning to conclude a [5-15]*-year cross-border capacity reservation agreement with MOL Transmission. Such long-term capacity bookings will have priority over new requests for capacity, and could prevent access by other market players to the necessary entry capacity on HAG.
- (380) In view of the above, the Commission concludes that only limited transmission capacities are available on the HAG pipeline and at the Hungarian Western entry point. It would therefore be difficult (and even impossible for large quantities) for a new entrant to obtain sufficient transmission capacities to import gas from Baumgarten into Hungary and become active on the Hungarian gas markets.

iii) Price and regulatory changes in Hungary

- (381) The expert report submitted by the parties introduces the concept of "*marginal entry point*" to explain that gas imported through the Baumgarten entry point would become competitive in Hungary when current price regulations are lifted. According to the expert report, Hungary has in any case to import gas from Baumgarten (as total demand is higher than the Eastern entry point capacity) and this gas will set gas prices in Hungary as the "*marginal gas*". According to the parties¹⁶³, current gas regulated prices in Hungary lead to a significant price differential between price

¹⁶¹ E-control, Press-briefing on the investigation of the Austrian gas industry under the Competition Act 2002, Vienna, 27 September 2005, page 6, "Access to interconnector capacity into Austria".

¹⁶² Paragraph 25 of the SO; see also response of E.ON to question 9 raised in the Commission's e-mail of 14 October 2005 which shows that MOL WMT has booked [5-15]* million m³/day at the HAG entry point for the gas year 2005/2006.

¹⁶³ Reply to the SO, Annex II, p. 2 (comment concerning paragraph 346 of the SO), and E.ON's submission of 21 October 2005, part III and Annex 12.

levels for gas available in Baumgarten and gas supplied within Hungary, which will disappear once regulated gas prices are terminated.

- (382) While the Commission agrees that gas will continue to be imported into Hungary through the Western entry point, it is clear that competitors that would import gas only from the Western entry point would be at a competitive disadvantage compared to MOL WMT, which would have a lower average cost of gas over its portfolio (due to its imports of Russian/Turkmen gas at cheap prices, and principally through the Eastern entry point). The Commission also refers to its previous analysis of transmission cost through Slovakia and on the HAG pipeline for gas imported through the Western entry point. Therefore, the fact that Baumgarten will constitute a “marginal entry point” does not mean that competitors having only access to this gas resource can compete effectively with MOL WMT in Hungary given their higher sourcing cost.
- (383) With respect to cross-border transmission tariffs, the parties claim that the current regulatory framework (equalised entry/exit tariff at the Western and Eastern entry points) penalizes imports of gas through the Western entry point as compared to imports through the Eastern entry point. According to the parties, this situation will change once a differentiated entry/exit tariff is introduced by the HEO. Such new entry/exit tariff would equalise gas prices (import prices plus entry/exit tariffs) at the Western and Eastern entry points. However, it would be difficult to equalise gas prices at the two entry points through differentiated tariffs given the significant price differential between import prices. In addition, there are currently no clear plans of the HEO to introduce differentiated entry/exit tariffs and this would in any event not take place before 2008¹⁶⁴.
- (384) In view of the above, the Commission believes that the price differential between gas imported through Hungary’s Western and Eastern entry point is essentially structural (cost of transmission through Slovakia and Austria) and it is not expected to be removed by upcoming changes in the regulatory framework in the medium term. As a consequence, even if Baumgarten were to act as “marginal entry point”, MOL WMT will continue to benefit from a significantly lower cost of gas as compared to any potential competitor importing gas from Baumgarten.

Existence of independent importers in the Hungarian wholesale gas market

- (385) In their reply to the SO¹⁶⁵ the parties argue that the Commission “*tries to belittle*” the “*significant entry*” of “*independent*” companies like EMFESZ and CENTREX.
- (386) To do so, the parties on the one hand contest the Commission’s argument that both companies are not truly “independent” from Gazprom and on the other hand claim that their market entry demonstrates that Gazprom has no intention to prevent “*at all cost independent market entry which reduces the margin earned by Panrusgáz*”.

¹⁶⁴ E-mail of the HEO of 20 October 2005.

¹⁶⁵ Parties’ reply to the SO, II.3.2, pages 13-16

- (387) However, the parties' argument as regards the entry of EMFESZ and CENTREX on the Hungarian market is not new to the Commission and has been factored in its assessment of the proposed transaction. As a matter of fact, the whole range of arguments and quotations put forward by the parties is rebutted by in paragraph 342 of the SO, where the Commission states that *"no competitor of MOL WMT can enter the Hungarian gas market without the approval and support of Gazprom and E.ON/MOL and at most only for limited quantities corresponding to the future "supply gap" in Hungary"* (emphasis added). As a matter of fact, the parties fail to acknowledge that the long term plans of expansion for both EMFESZ and CENTREX match very closely the figures as regards the "supply gap" highlighted by the Commission. If one adds the [0-3]* bcm, representing CENTREX' long-term sales plans¹⁶⁶, and the [0-3]* bcm of long-term forecast sales by EMFESZ¹⁶⁷, the result is approximately the long-term "supply gap" as elaborated by the parties.
- (388) Moreover, as regards EMFESZ, the parties fail to acknowledge that [0-3]* bcm of EMFESZ current sales are destined to MOL, as indicated in paragraph 339 of the SO. It therefore appears groundless for the parties to emphasize that EMFESZ *"was able to independently import more than [0-3]* bcm"*, that it has built up a *"significant position"* in less than 2 years and that this volumes represent *"20% of the Hungarian gas demand by industrial and commercial customers as well as power plants"*. The Commission also refers to the swap agreement between MOL and EMFESZ and the other elements (see above in recital 343) that call in question the *"independent"* character of EMFESZ's entry. As regards CENTREX, the Commission underline that the company is not active on the Hungarian gas market yet and that its 2-2.5 bcm long term sales plans should be taken for granted.
- (389) To conclude, the Commission estimates that the parties' remarks on Gazprom incentives, the availability of competitive gas in Baumgarten and the existence of independent new entrants are insufficiently supported by evidence and do not reflect accurately the current and future competitive situation of the gas sector in Hungary. Based on the information provided by the market investigation and its assessment thereof, the Commission therefore concludes that MOL WMT controls competitive import sources in Hungary prior to the transaction.
- (iii) *MOL WMT enjoys further significant incumbency advantages*
- (390) In addition to a privileged access to competitive gas sources, MOL WMT enjoys significant incumbency advantages in terms of security of supply, cost of transmission and storage of gas.
- (391) The market investigation has shown that to compete in Hungary, it is necessary to have access to gas and transmission capacity at both entry points, which only MOL WMT, the incumbent, has. This is necessary to ensure the security of supply of the clients. According to a third party active in gas, *"having only one point of importation is not enough to secure a satisfactory supply to clients in case of reduction or force majeure at [HAG], as it happened in 2004 for example"*. *"The*

¹⁶⁶ See report of teleconference with Centrex of August 2005, page 2

¹⁶⁷ See response of EMFESZ to Question 13 k) of the Commission's request for information of 19 July 2005

consequence of Force Majeure (i.e. any unpredictable event that makes the gas flow impossible or reduced) at [HAG] for a newcomer who is not allowed to contract through Beregovo because of saturation are important: (i) financial, as the newcomer will not be able to supply the gas quantities for its clients through another delivery point, he could be under strong penalties with MOL Transmission; (ii) commercial image will be deteriorated in front of the clients who will lose confidence.”¹⁶⁸

- (392) The expert report provided by the parties in their reply to the SO disputes the fact that simultaneous access to gas at both entry points is required for successful competition. According to the report, the Hungarian gas network code permits reliable participation in the market from just one entry point. In case of technical problem at the entry point, a gas supplier would not be penalised as “firm” transmission capacity implies that it is the TSO’s responsibility to deliver the gas injected at the Western entry point for example. If the TSO fails to do so, the Hungarian network code waives any imbalance penalties and it puts all customers on an equal footing with respect to potential curtailments of consumption in the event of a network failure. A supplier with access to gas from different sources would have the same likelihood of interruption as a competitor operating exclusively from Baumgarten in case of a problem on the transmission network.
- (393) The Commission agrees that the provisions of the Hungarian network code described in the expert report ensure that a supplier with access to only one entry point is not penalized in case of network failure. However, that supplier’s liability is not protected in case of problems with access to gas upstream of the Hungarian transmission network, which would not be the responsibility of the Hungarian TSO. It thus remains important for reliability and safety of supply to have access to gas at more than one entry point in the country (Hungary has only two entry points for gas, most countries have several entry points for gas). It remains true that a supplier which is not able to ensure back-up gas from an alternative entry point would face high imbalance penalties and damage to its reputation. Therefore, a supplier having access to gas at the two entry points benefits from a strong competitive advantage in term of security of supply, one of the most important criteria customers consider to select their gas supplier.
- (394) Similarly, due to its position as gas incumbent, MOL WMT is the only gas operator that has several gas supply contracts with delivery points at the Hungarian borders. This means that only MOL WMT can fully benefit from the advantages resulting from a diversified gas supply portfolio and optimize its sourcing in terms of prices and flexibility provisions notably.
- (395) Furthermore, as a direct result of its large size in Hungary and its incumbency position, the new entity has a competitive advantage in terms of costs of transmission and storage of gas vis-à-vis new entrants on the Hungarian gas markets. This constitute an additional barrier to entry on these markets. For example, it appears that balancing rules are biased in favour of the incumbent in Hungary: a gas

¹⁶⁸ Response of OMV to Question 17 of the request for information of 19 July 2005: “Due to the fact that E.ON/Ruhrgas will have gas and import capacity available at the Ukrainian and Austrian borders, it will be in the best position to use the 80-20 percent division of capacity stipulated in the grid and commercial code (cf. point 5.1.2.). This might at least put it in a favourable position to an outside competitor.”

trader licensee that can provide the TSO daily gas options can avoid paying a nomination penalty for deviations of up to +/- 8% from daily nominations. At this stage, only MOL WMT can provide such flexibility, thanks to its huge source portfolio. Other gas traders, which cannot offer such daily flexibility, have only a tolerance of +/- 2% for deviations and thus have to pay high imbalance penalties for any deviation exceeding 2%¹⁶⁹.

- (396) Similarly, MOL WMT benefits from a synchronicity effect for its transmission and storage capacity bookings due to its large portfolio of customers¹⁷⁰. A supplier with a large and diversified customer base needs lower transmission and storage capacities per customer than a supplier with a limited number of customers as the overall variation in demand of a large number of customers is lower on average than the sum of the variation in demand of each individual customer¹⁷¹. According to the HEO *“for daily balancing, it is necessary to have flexibility of sources and to be able to take import sources as needed. MOL WMT has a larger flexibility due to its huge customer base and because it has all the imports. The other traders have to buy their flexibility from MOL WMT in order to serve the specific needs of their new customers. (...) The Public Utility Wholesaler is well equipped to offer flexibility schemes for the remaining players, but this is done in a way in the least possible advantageous way for the small players.”*¹⁷²

Conclusion on the new entity’s dominant position in the wholesale supply of gas in Hungary

- (397) For the reasons set out above, already before the transaction, MOL WMT is dominant on the different Hungarian wholesale gas markets identified in the market definition section (the market for gas supply to RDCs, the market for gas supply to traders and the market for gas supply to large power plants). According to the Commission, MOL WMT’s dominance does not result from the transaction. However, the Commission disagrees with the parties’ view that *“the proposed transaction does not bring about any relevant change to this situation”*¹⁷³.

¹⁶⁹ See also minutes of the meeting of 26 July 2005 with the HEO (comments on slide 17 of the presentation entitled “The Hungarian Natural Gas Market: Storage and miscellaneous questions”): *“Furthermore the penalty for imbalance imposed by the TSO (MOL Transmission) is high. Although the penalty is lessened if the player can offer another flexibility tool, this system works obviously against the small players who cannot offer flexibility schemes for the TSO.”*

¹⁷⁰ A third party active in gas has stated that *“Being able to gain market share means not only to have competitive prices for importation, but also to be able to import enough quantities of gas to benefit from scale effects, and also to lower transportation and balancing costs by access to multiple delivery points.”*

¹⁷¹ This results directly from the fact that, in a large pool of customers, not every customer has its peak demand at the same point in time. The peak in demand of the aggregate demand of the pools (which is relevant for the transmission and storage capacity booking) is hence lower than the sum of the peak demands of each customer in the pool. More generally, the larger the number of customers in the pool, the lower is the relative fluctuation of the aggregate demand.

¹⁷² Minutes of the meeting of 26 July 2005 with the HEO (comments on slide 17 of the presentation entitled “The Hungarian Natural Gas Market: Storage and miscellaneous questions”).

¹⁷³ Reply to the SO, page 2.

B. Impact of the transaction on the gas markets

(398) The following recitals will focus on the effects of the proposed transaction on competition on the Hungarian gas markets.

(i) Supply of gas

(399) The new entity, like MOL WMT prior to the transaction, will enjoy a dominant position in the upstream markets for the supply of gas to RDCs and to traders. MOL WMT controls, through long-term procurement contracts and structural links the two existing competitive sources of gas, namely domestic production and imports from Gazprom. The essential change brought by the transaction is that E.ON, unlike MOL, is active in the retail supply of gas, through the two RDCs it controls and its participation in a third one.. Thus, the proposed merger will result in a vertically integrated company active across all stages of the gas supply chain and controlling access to gas volumes and part of the infrastructure.

(400) While, prior to the transaction, MOL WMT had the ability to act, to an appreciable extent, independently of its customers (i.e., RDCs and traders) in the wholesale supply of gas in Hungary, it lacked any economic incentives to act to their detriment as it was not present on the downstream gas retail markets and was not, therefore, competing with them. Conversely, E.ON had no presence in the upstream market and thus no power to act to the detriment of its downstream rivals. For the reasons stated below, the Commission considers that the vertical integration created by the transaction is likely to result in the new entity having the ability *and* the incentive to foreclose its actual and potential competitors on the downstream markets for the supply of gas so as to significantly impede competition thereon.

a. The new entity will have the ability and incentive to foreclose access to wholesale gas to its competitors (RDCs and traders) in gas retail on the market for the supply of gas to small industrial and commercial customers

(401) The Commission's analysis indicates that, as a result of and immediately after the transaction, the new entity will have the ability and incentive to foreclose access to gas to its current downstream competitors supplying retail gas to small industrial and commercial customers¹⁷⁴, thereby significantly impeding effective competition on these markets. Emerging entrants in the open segment of the market, including the trading arm of independent RDCs, would be obliged to rely on their strongest competitor to procure their wholesale gas, thus placing them at a competitive disadvantage. Further, the Commission is concerned that by deterring or delaying entry, the transaction will also prevent the effective opening of the market to competition despite its full liberalisation since 1 July 2004¹⁷⁵.

¹⁷⁴ Owing to different competitive and regulatory circumstances input foreclosure to gas-fired power plants is analysed separately.

¹⁷⁵ Pursuant to Directive 2003/55/EC and to the implementing provisions under Hungarian law (Article 36 of the HGA and Article 1(1) of the Eligibility Decree), all non-residential customers have become eligible and, accordingly, are free to choose their supplier.

- (402) Several market participants have pointed out the likelihood and the negative effects of such input foreclosure on effective competition and potential new entries. As stated by a third party active in the gas sector, as a result of the merger, “*E.ON would become monopoly wholesaler*” and “*through its vertical integration, would be able to control the upstream gas market and – thanks to its existing position on the retail gas market would be in a unique position to control the whole gas supply chain*”.

Ability to foreclose access to wholesale gas thereby raising the costs of competitors in the market for the supply of gas to small industrial and commercial customers

- (403) Input foreclosure here refers to the strategy of raising the costs of wholesale gas procurement to rival RDCs in the regulated segment and traders in the open segment of the market for the supply of gas to small industrial and commercial customers. Higher costs will reduce rivals’ profit margins and tend to reduce their ability to compete effectively in this retail market with the new entity. As a result, the new entity’s downstream rivals are likely to be marginalised and effective competition to be significantly impeded, allowing the new entity to gain increased market power and raise retail prices to the detriment of final small industrial and commercial customers.
- (404) Following the merger, the merged entity will have the ability to foreclose access to gas and raise its rivals’ costs in various ways. According to the Commission’s market investigation post-merger the new entity will first have the ability to deny access to gas resources and infrastructures to its downstream competitors on the market for the supply of gas to small industrial and commercial customers. A third party active in the gas sector points out for example that “*E.ON will be the only gas retailer who will have access to the TOP import contracts of MOL WMT and the domestic production of MOL E&P, so they will be able to control the gas resources in Hungary*”.
- (405) The dependence of gas traders affiliated with the RDCs on MOL WMT for their access to gas is evidenced by [...] ¹⁷⁶. This table (extracted from a table presented above in recital 347) shows that these traders have already asked for a bid of MOL WMT trader for their access to gas for the liberalised segment of the market (on the regulated segment of the market, MOL WMT Public Utility Wholesaler has for the time being the obligation to supply them):

[...]*

- (406) In the open segment of the market, the new entity could directly increase the wholesale price of gas to traders and/or engage in non-price discrimination. Non-price discrimination includes a whole range of actions intended to increase the costs of wholesale gas procurement to rivals, such as intentional delays in supply and in processing orders, reductions in the quality of service, lack of flexibility, reduced

¹⁷⁶ [...]*

transparency, unwillingness to renegotiate, etc. Non-price discrimination provides ways to raise rivals' costs even in the regulated segment of the market, where prices are regulated.

(407) The Commission's investigation has indeed revealed that safety of supply, flexibility and service guarantees are of significant importance for a small industrial and commercial customer in choosing its gas supplier. In turn retailers must ensure that they can receive the corresponding quality of service and supply guarantees from their respective wholesaler. Nomination penalty risk is also important for gas retailers.

(408) A number of market players have outlined the risk of non-price discrimination and have indicated the broad range of parameters on which the new entity would have the ability to discriminate its competitors. A third party active in the gas sector stated for instance:

“Besides the prices set in the supply contracts other contractual conditions may provide room for discrimination (e.g. terms of payments, capacity booking, synchronicity of customers' capacity needs, etc)”¹⁷⁷.

(409) E.ON would thus have the ability post-merger to influence the above-mentioned parameters of competition and to limit the ability of targeted retailers to compete on the downstream market for the supply of gas to small industrial and commercial customers.

Incentive to foreclose access to wholesale gas thereby raising the costs of competitors in gas retail markets

(410) Prior to the transaction, MOL WMT has no economic motive to discriminate among downstream gas players (i.e. RDCs and traders) active on the market for gas supply to small industrial and commercial customers as it has no gas retail activities. However, as a result of its vertical integration into gas retailing, the new entity will have the incentive, post-merger, to engage in input foreclosure strategies on the downstream market for the supply of gas to small industrial and commercial customers where E.ON is present, so as to favour its downstream affiliates and marginalise its rivals.

(411) The table below summarizes the current market shares of the existing RDCs on the market for gas supply to small industrial and commercial customers. No trader is active on this market so far.

¹⁷⁷ Submission of [...] dated [...].

Suppliers	Supply of gas to small commercial and industrial customers in 2004	
	In million m ³	In %
KÖGÁZ	[0-500]*	[10-15%]
DDGÁZ	[0-500]*	[5-10%]
Total E.ON	[0-500]*	[15-20%]
FÖGÁZ	[500-1000]	[20-30%]
ÉGÁZ	[0-500]	[0-10%]
DÉGÁZ	[0-500]	[10-20%]
TIGÁZ	[500-1000]	[30-40%]
MOL WMT	0	0%
Total Market	[2000-3000]	100%

- (412) E.ON has sole control of two RDCs (KÖGÁZ and DDGÁZ), which together represented nearly [15-25%]* of the sales on the market for the supply of gas to small commercial and industrial customers (< 500 m³/h) in 2004. Such market presence already gives the new entity a strong incentive to raise its current competitors' costs.
- (413) In addition, E.ON holds a 16.4% participation in FÖGÁZ, an RDC exclusively controlled by the municipality of Budapest, which represents more than 20% of the sales of gas on the market for the supply of gas to small commercial and industrial customers. If one also takes into account FÖGÁZ's sales, because of E.ON's financial interest therein, the merged entity's position on the retail market for gas supply to small commercial and industrial customers is even stronger (around [35-45%]*).
- (414) It is likely that, by pursuing an input foreclosure strategy as a result of which competing RDCs and traders will be marginalised because of higher gas costs, the merged entity will enhance its market position and gain increased market power on the market for the supply of gas to small commercial and industrial customers.
- (415) The market investigation has confirmed that the transaction would change MOL WMT's incentives in this way. In that respect, EDF has stated that: "*We believe that MOL/E.ON, in a quasi-monopoly sourcing situation, could easily provide a wide and tailor-made range of products (blocks, peak, off peak...) favourable to their own downstream subsidiaries, for instance especially during peak hours*"¹⁷⁸.
- (416) The new entity's incentives to foreclose are all the more likely in view of the specificities of the Hungarian gas retail market for the supply of gas to small industrial and commercial customers. As described above in recitals 55 to 59, the Hungarian gas sector is characterized by a hybrid model, with the coexistence of a regulated segment of the market and a liberalized market (or "open segment of the market"). Eligible customers have the right but not the obligation to switch suppliers to enter the open segment of the market. Customers who have switched to the open segment of the market are allowed to switch back to the regulated segment of the market (albeit this takes one year instead of 4 months).

¹⁷⁸ Response of EDF of 10 August 2005 to Question 27 of the request for information of 19 July 2005.

- (417) Customers that choose to stay under the regulated regime are supplied by their local RDC at regulated prices. In turn the RDC has an exclusive right and obligation to purchase gas from MOL WMT also at regulated prices. MOL WMT is the sole public utility wholesaler licensee. It has the obligation, by law, to cover the full natural gas demand for public utility purposes of the RDCs. To fulfil this obligation, the gas RDCs and MOL WMT have entered into long-term framework supply contracts, with duration from [...]* years. In contrast with the public utility contracts, the relationship between the eligible customers who switched suppliers and traders is largely subject to the principle of contractual freedom.
- (418) According to the parties, switching does not entail any significant costs or time investment on the side of the eligible customer. A customer that switches to the open segment of the market remains entitled to the cross-border, transmission, distribution and storage capacities allocated to him under the regulated regime. Therefore retail competition for eligible customers is based largely on price. This in turn implies that access to wholesale gas at competitive prices is the only way to attract customers from the regulated segment and increase market share. The integration with MOL WMT will give E.ON's downstream affiliates such competitive advantage over all other emerging and potential rivals on the market for the supply of gas to small industrial and commercial customers.
- (419) The Commission's analysis indicates that E.ON/MOL WMT's incentives to raise the costs of rivals on the market for the supply of gas to small industrial and commercial customers and its optimal foreclosure strategy is likely to evolve with the regulatory environment. One can distinguish two stages:
- i) Immediately after the transaction: as long as both retail prices to small industrial and commercial customers and wholesale gas prices are regulated, the new entity will have an incentive to raise the costs to rivals RDCs through non-price discrimination. Simultaneously, it is likely to increase the price of wholesale gas to independent traders to capture customers that switch to the open segment of the market.
 - ii) In July 2007: regulated prices are expected to be suppressed. At that point all eligible customers will have to switch to the open segment of the market. It is then likely that the new entity will have an incentive to foreclose all its downstream rivals on the market for the supply of gas to small industrial and commercial customers either by increasing the cost of gas or by reducing the quality of supply, whatever is optimal.

Current regulatory framework

- (420) Immediately after the transaction, the new entity will be in a position to increase the wholesale price to rival traders in the open segment of the market for the supply of supply to small industrial and commercial customers. This would tend to reduce their demand for wholesale gas but also it would reduce their ability to supply gas at competitive prices in the open segment of the market, thus losing market share to E.ON's trading affiliates. Given that the retail margin is high due to limited and

incipient competition, the lost profits upstream from reduced sales would likely be more than offset by increase profits in the open segment of the market¹⁷⁹.

- (421) In contrast, under the current framework, the merged entity cannot raise the costs of rival gas RDCs by unilaterally increasing the wholesale price, at least in the short-run¹⁸⁰. However, as the sole wholesale public utility supplier, MOL WMT has the ability to influence the profitability of RDCs. At the same time it increases wholesale gas prices to rival traders on the free segment of the market for the supply of gas to small industrial and commercial customers, the merged entity will have an incentive to raise the costs of rival gas RDCs by deteriorating the quality or flexibility of wholesale supply. It is also likely to deliberately reallocate costs associated with the supply to traders in the open segment of the market to the public utility segment¹⁸¹. In either case this would negatively affect the overall cost structure of RDCs, discouraging their expansion and limiting their ability to refinance their operations. This reduction in profitability would also affect the ability and incentive of rival RDCs to create and support trading arms to compete in the open segment of the market. As a result, competition would be significantly impeded to the detriment of consumer choice and the success of the ongoing liberalisation process.
- (422) Furthermore, a strategy of raising rivals' costs through non-price discrimination can be reflected in higher regulated prices.
- (423) Pursuant to Article 48(2) of the HGA the regulated price is based on the so-called cost-plus principle. The regulated purchase price that has to be paid to the public wholesaler contains both the gas fee and the fee for using the facilities (transport network and storage). The regulated price also includes the costs of the justified investments, as well as the profit necessary for long-term operation. The principle is that maximum prices shall be set so as to cover the costs of an efficient entrepreneur and the necessary profits for operation. Within the four-year revision cycle there are two built-in price correction elements: a regular price correction, proposed by the HEO with respect to annual changes e.g. in the import prices of natural gas, and an extraordinary price correction proposed in case events on the natural gas market make it obviously necessary.

¹⁷⁹ E.ON's strong presence in the downstream market for the supply of gas to small industrial and commercial customers through its control of DDGÁZ and KÖGÁZ and participation in FÖGÁZ would raise no concerns if these markets were intensely competitive. This is because the merged entity could appropriate all monopoly rents through its choice of the input price. Hence, in these circumstances it would not matter whether the upstream monopolist participates downstream. However, in the present case this retail market is oligopolistic and in the process of liberalisation. As a result, in a free market, the downstream equilibrium price will likely exceed marginal cost.

¹⁸⁰ But note that in the regulated segment the merger will not lead to the elimination of the double margin, even if that is possible in practice. Double marginalization occurs when downstream firms mark up over their marginal cost, which because of market power upstream exceeds the marginal cost of the upstream producer. Hence there is a mark-up on a mark-up or double marginalization.

¹⁸¹ According to economic analysis it is likely the merged entity will have an incentive to raise its rivals' costs all the way up to the point that revenues at regulated prices fail to cover costs thus forcing the rival RDC to push for an increase in the retail price, sell the company to the merged entity, or give up its own customers and focus on protecting its distribution profits.

- (424) Pursuant to Article 49 (3) of the HGA the HEO is obliged to undertake a price revision procedure on the basis of the request of any interested party, and shall publish the result thereof. The merged entity and independent RDCs have the right for such a price revision. Thus, if increased gas procurement costs lead to reduced margins, RDCs may choose to request a revision of the retail gas prices in order to maintain their profit margins¹⁸². Unfortunately, higher regulated retail prices would also have negative consequences on the liberalisation process since they would induce end-customers to switch to the open segment of the market, most likely to E.ON's trading arm given that its rival traders would pay a higher price for wholesale gas to MOL WMT and would not be competitive at the retail level. Not only would RDCs lose customers but may be unable to meet their TOP obligations (due to lower sales than expected), which would entail an additional cost.

Future regulatory framework

- (425) With respect to the medium term (after 2007), if customers were obliged to switch to the open segment of the market, this would only further strengthen the new entity's ability and incentive to foreclose access to wholesale gas. First, the new entity could increase prices in a fully open market unconstrained by the regulated price. Second, it could raise rivals' costs by increasing the wholesale gas price, which is likely to result in higher revenues than a reduction in the quality of supply – for an equivalent revenue loss from reduced demand for wholesale gas.
- (426) All market participants consulted by the Commission expect the hybrid model to disappear shortly after July 2007, when all residential customers will become eligible. Small industrial and commercial customers that have not yet switched to the open segment of the market will be forced to do so. According to current HEO plans, a USP appointed through an open competitive tender shall supply the small industrial and commercial customers¹⁸³ that have not concluded a supply contract with a specific supplier.
- (427) The market investigation has also revealed that most market players active in gas retail consider that the anti-competitive effects of input foreclosure are likely to be more immediate in such case. In particular, they have expressed the concern that *“post-transaction, E.ON's complete vertical integration on the gas supply chain will discourage new entries at the gas retail level, as it is likely to make it significantly harder for new operators to have access to competitive supplies and possibly storage service”*. Respondents also point to the mutually reinforcing effect of controlling access to wholesale gas and storage of gas, by arguing that, as a result of the merger *“E.ON would become de facto the exclusive supplier of its competitors in the Hungarian retail market. In addition through the control of storages, it could make significantly harder for third parties to supply fluctuating retail demand”*, and that *“there is significant space for E.ON as supplier (or storage service provider) to*

¹⁸² It is unlikely the regulator can monitor and oblige WMT to increase its efficiency with respect to supply to RDCs.

¹⁸³ The proposal for a new electricity market model foresees this for small industrial customers with fewer than 50 employees (see minutes of the meeting of 26 July 2005 with the HEO). It could be expected that the future proposal for a new gas market model will use the same reference.

apply to its competitors terms and conditions de facto different from those utilised by E.ON itself for its downstream activities in the Hungarian market”.

Factors relevant for raising rivals' costs strategies

- (428) In addition, several empirical factors relevant to determine the magnitude of the incentives to raise rivals' costs are present in this case.
- (429) First, there is little differentiation in the retail supply of gas. Despite small differences in calorific content, natural gas can be regarded as largely homogenous. When the downstream products are viewed by consumers as very similar, then the vertically integrated firm can readily supplant the sales its rivals lose due to discrimination with its own sales, thereby mitigating the effects of lost input sales.
- (430) Second, given contractual completeness, non-price discrimination may not only increase the costs of downstream rivals on the market for the supply of gas to small industrial and commercial customers but also reduce the costs of MOL WMT. By depressing quality and flexibility of supply and reducing customer service, MOL WMT avoids additional costs. When it is inexpensive for the upstream firm to non-price discriminate vis-à-vis its rivals then, other things equal, the upstream firm will have greater incentive to pursue non-price discrimination. Thus the merged entity benefits not only from the increased market share in the retail market for gas supply to small industrial and commercial customers but also from increased margins in the supply of wholesale gas to rival RDCs and traders.
- (431) Third, when the marginal cost of downstream gas supply is increasing, then it becomes progressively more costly for the integrated firm to replace its rivals' sales with its own. Hence the integrated firm may find it profitable to engage in some non-price discrimination, but not to raise its rivals' costs so high that they exit the market. An extreme form of this occurs when the integrated firm has a capacity constraint on its downstream production. In contrast, in this case, it appears that there exist economies of scale in the retail supply of gas to small industrial and commercial customers. This is due to fixed costs in developing a sales network able to induce consumers under the regulated segment to switch to the open segment of the market. Furthermore the integrated firm faces no capacity constraint in its ability to procure gas from upstream sources to supply.
- (432) Fourth, the incentive to raise rivals' costs also depends on the existence of a positive margin (price above cost) in the downstream market. If there is a high margin downstream the merged entity benefits from expanding market share at the expense of its foreclosed rivals. Profit margins are in general positively related to the intensity of competition. If competition is weak, margins are likely to be high. In this case, competition in the retail gas markets is limited. In part, this is because the open segment of the market is still incipient and RDCs have a strong incumbency position in their respective regions. It follows that, other things being equal, the new entity would have an incentive to raise its rivals' costs so as to obtain the profit margin from acquiring its rivals' customers on the market for the supply of gas to small industrial and commercial customers¹⁸⁴.

¹⁸⁴ The relative efficiency of downstream producers can also affect the incentive to raise rivals' costs. When the integrated firm has lower downstream production costs than its rivals, then the profit it can generate by

(433) It should be recognised that such discriminatory conduct is unlikely to be detected or penalised by the regulator. First, neither supply contracts nor the relevant regulation cover all scenarios and contingencies that may arise. As a result, MOL WMT enjoys certain discretion to worsen conditions of supply in ways that are difficult to verify by third parties. E.ON would enjoy the same discretion following the merger. Second, market players would not be likely to submit complaints to the regulator or competition authority in view of the dependence from the new entity for their gas supply. The likelihood of such input foreclosure strategy against downstream competitors would thus be increased, in the absence of sufficiently strong “regulatory” deterrence.

The parties’ reply to the SO

(434) In their reply to the SO, the parties generally argue that the Commission’s competition concerns do not go beyond the expression of “doubts” and, therefore, fail to meet the relevant standard of proof¹⁸⁵.

(435) However, the Commission’s competition concerns identified in its SO and in the present decision rely, as required by the case-law¹⁸⁶, on a prospective analysis of the events which, in its view, “*are the most likely*” to occur in the future, should the merger as notified take place. Contrary to the parties’ assertion, the Commission’s competition concerns set out in its SO are not based on mere speculations, but on a close examination of all the relevant evidence available as well as on a thorough economic analysis thereof, showing that the development envisaged is particularly “*plausible*”¹⁸⁷ and thus, likely to occur post-merger. In particular, the Commission examined whether, in view of both the ability and the likely incentives of the merged entity, the merger would be likely to result in an input foreclosure strategy and, thereby, significantly impede effective competition on the downstream gas markets in the foreseeable future. Consequently, the Commission did not limit itself to consider possible strategies, but also considered whether such outcome would be more likely than not to take place.

(436) As to the competition concerns identified by the Commission, the parties, in their reply to the SO, do not specifically dispute that effective competition would indeed be significantly impeded on the market for the supply of gas to small industrial and commercial customers, should an input foreclosure strategy take place as a result of the merger. Nor do they dispute the timing envisaged by the Commission as regards the likely effects of the merger on the market. However, they argue that, in any event, input foreclosure of downstream gas competitors would not be likely to occur post-merger.

(437) In the parties’ opinion, the new entity would not have the *ability* and the *incentive* to discriminate its downstream rivals because significant gas surpluses could be

selling retail gas downstream is greater than the profit (gross of input charges) its rivals can generate by selling that quantity of gas.

¹⁸⁵ Reply to the SO, I.2, pages 4-5.

¹⁸⁶ See Case 12/03 P, Commission / Tetra Laval, paragraphs 42-43.

¹⁸⁷ See Case 12/03 P, Commission / Tetra Laval, paragraph 44.

diverted to the Baumgarten entry point for onward supply into Hungary, following the removal of price regulation¹⁸⁸.

- (438) However, this argument ignores that the Commission's competition concern is essentially based on the fact that, should gas supplies be available in sufficient quantities at the Western entry point, such supplies would not be made, in any event, at competitive prices. In that regard, the parties do not dispute that a substantial price difference exists with the cost of gas imported by MOL WMT, which purchases most of its gas from Gazprom and other operators at the Eastern entry point, and that, as a consequence, foreclosed competitors would not be in a position to rely on competitive gas should their input costs increase post-merger.
- (439) The parties also dispute the likelihood of foreclosure by E.ON of its downstream competitors, arguing that the Commission's analysis is too pessimistic as it ignores the high level and effectiveness of Hungarian energy regulation and the sophistication of other market participants.
- (440) While the Commission does not dispute the existence of regulations, it should be pointed out that the regulation mostly concerns the activities of transmission and storage rather than gas supply (with the exception of the hybrid model until July 2007). In addition, as pointed out by the HEO itself, regulations may not consider and address all possible scenarios of discrimination:

*“There is an ongoing polishing of the existing rules in the Grid Code, which is modified every year to give more chance to the free market. There are no stable rules in the market.”*¹⁸⁹

- (441) The parties also submit that the Commission's analysis relies on a purely speculative analysis of which type of “*abusive behaviour*” the merged entity might adopt in the future, which fails to satisfy a test of “high probability”¹⁹⁰. In that respect, the parties essentially argue that the merged entity would have no *incentive* to adopt an abusive behaviour because, in light of the relative simplicity of gas market contracts, such a conduct would be detected by competitors and by the regulator, and would be penalised accordingly following complaints¹⁹¹. In addition, according to the parties, the various discrimination scenarios have not been identified by market respondents and are not typical of E.ON's conduct (or of other energy companies)¹⁹².
- (442) The parties' suggestion that the Commission's competition concerns rely on a list of “*abusive behaviour*” is based on a wrong reading of the SO. Contrary to what is argued by the parties, the Commission did not take a position as to whether the various strategies likely to be adopted by the merged entity as a result of the merger

¹⁸⁸ Reply to the SO, II.1.1, page 6.

¹⁸⁹ Minutes of the meeting with the HEO on 26 July 2005, p. 5 (comments on slide 25 of the Presentation entitled “Introduction of the Hungarian Natural Gas Market”).

¹⁹⁰ Reply to the SO, II.1.2 and II.1.3, pages 6-8.

¹⁹¹ Reply to the SO, II.1.3, II.1.4 and II.1.5, pages 9-10. and Annex 1 thereto

¹⁹² Reply to the SO, II.1.2 and II.1.3, pages 7-9.

would necessarily fall within the scope of Article 82 EC and would be penalised as such. As recently held by the Court of Justice, it is not necessary for the Commission, when assessing the likely effects of a merger, to determine whether a specific conduct likely to be adopted by the merged entity would constitute an infringement of Article 82 EC and would be sanctioned as such in the relevant national order. Indeed, an exhaustive and detailed examination of the rules of the various legal orders which might be applicable and of the enforcement policy practised in them would call for a high probability of the occurrence of the acts envisaged as capable of giving rise to objections on the ground that they are part of anti-competitive conduct.¹⁹³ However, it would run counter to the Regulation's purpose of prevention to require the Commission to examine, for each proposed merger, the extent to which the incentives to adopt anti-competitive conduct would be reduced, or even eliminated, as a result of the unlawfulness of the conduct in question, the likelihood of its detection, the action taken by the competent authorities, both at Community and national level, and the financial penalties which could ensue¹⁹⁴. Moreover, as stated by the Court of Justice, "*at the stage of assessing a proposed merger, an assessment intended to establish whether an infringement of Article 82 EC is likely and to ascertain that it will be penalised in several legal orders would be too speculative and would not allow the Commission to base its assessment on all of the relevant facts with a view to establishing whether they support an economic scenario in which a development such as leveraging will occur*"¹⁹⁵. In that context, the Court of First Instance recently concluded, citing paragraph 74 of the Court of Justice's judgment in *Tetra Laval*, that "*where the Commission, without undertaking a specific and detailed investigation into the matter, can identify the unlawful nature of the conduct in question, in the light of Article 82 EC or of other provisions of Community law which it is competent to enforce, it is its responsibility to make a finding to that effect and take account of it in its assessment of the likelihood that the merged entity will engage in such conduct*".¹⁹⁶

- (443) In the present case, it would be all the more difficult to consider *ab initio* that the various foreclosure strategies likely to be adopted post-merger would necessarily be considered by the national authorities as discriminatory practices within the meaning of Article 82 EC given that, contrary to what the parties claim, gas supply contracts with traders are generally complex and contain specific clauses adapted to the needs of each negotiating party.
- (444) Even if such discriminatory practices were ultimately considered as an abuse of a dominant position, it is nonetheless highly likely that, in the future market context, the merged entity would have strong incentives to act in such a manner. Indeed, there is generally no transparency as regards the price formulae applicable in gas supply contracts since such information is crucial for the competitive operation of

¹⁹³ Case C-12/03 P, *Commission v Tetra Laval* [2005] ECR I-987, paragraph 76.

¹⁹⁴ Case C-12/03 P, *Commission v Tetra Laval* [2005] ECR I-987, paragraph 75.

¹⁹⁵ See Case 12/03 P, *Commission / Tetra Laval*, para.77.

¹⁹⁶ Case T-210/01, *General Electric v Commission*, judgment of 14 December 2005, not yet recorded, paragraph 74.

traders. For these reasons, it is very unlikely that a rival trader would be in a position, at any given time, to effectively compare the terms of its contract with those applicable in E.ON's affiliates' contracts.

(445) This is also true as regards the energy regulator, since it may not detect such differences in due time. In that regard, the HEO itself acknowledged, with respect to possible discriminative practices in access to storage (which is even more regulated than the market for the supply of gas to RDCs and traders) that they are “*very hard to prove using administrative methods (as it is indicated from time to time, the market player which is at a disadvantage fears for its future position on the market, and will rather not submit a complaint at the regulatory or competition authority)*”¹⁹⁷.

(446) As regards gas supply contracts, although the HEO has indicated that it has the right to control and to force market players to act without discrimination¹⁹⁸, it has also indicated several times, concerning different issues, that it did not have good information on the commercial contracts concluded by operators, nor could it request access to this information:

*“The HEO is not familiar with the free market prices, as few players provide information to the HEO on the prices on the free market (and only average prices).”*¹⁹⁹

*“In the Hungarian regulatory framework, confirmed customer demand is required to book capacity. Every year, every market player is required to show the demand of its customers for the next ten years (the demand relating to the 9 years after is based on their hopes, not on facts!). The problem is that it is not clear who is responsible for checking this, as the law does not say how it is checked. The HEO takes the view that this should be checked by the TSO, but the TSO claims that they have no tools to do so, because the agreements signed between third parties are confidential. (...) The HEO can check the licensees and their books, but not the commercial contracts.”*²⁰⁰

*“The HEO does not know which companies were offered such a long-term contract and which have signed a long-term contract and for which volumes of gas.”*²⁰¹

¹⁹⁷ Document received by the Commission from the HEO on 9 May 2005 entitled “Answers to the questions raised by GVH related to the share transfer transaction between E.ON and MOL”, page 4, dated 11 April 2005.

¹⁹⁸ Minutes of the meeting of 26 July 2005 with the HEO, p. 10 (slide 16 of the Presentation entitled “Hungarian Natural Gas Market: Storage and miscellaneous questions”).

¹⁹⁹ Minutes of the meeting of 26 July 2005 with the HEO, p. 6 (comments on slide 27 of the Presentation entitled “Introduction of the Hungarian Natural Gas Market”).

²⁰⁰ Minutes of the meeting of 26 July 2005 with the HEO, p. 7 (comments on slide 18 of the Presentation entitled “Hungarian Natural Gas Market: Transmission and Distribution”).

²⁰¹ Minutes of the meeting of 26 July 2005 with the HEO, p. 10 (comments on slide 20 of the Presentation entitled “Hungarian Natural Gas Market: Storage and miscellaneous questions”).

- (447) As to the argument that the various ways in which input foreclosure strategies may take place have not been precisely identified by market respondents, it ignores the fact that, nevertheless, market players have clearly identified the risk of input foreclosure as a likely effect of the merger. Similarly, the argument that discriminatory practices are not typical of E.ON's conduct in other jurisdictions does not demonstrate that such outcome is unlikely in Hungary as it relies on the wrong assumption that comparable market conditions exist in other jurisdictions and/or that such practices could have been easily detected and penalised under Article 82 of the Treaty.
- (448) Last, the parties argue that it is pure speculation for the Commission to consider that market players would not be likely to submit complaints in view of their dependence on the new entity for their gas supply other market participants. According to the parties, this did not prevent Hungarian energy companies from expressing their opinion freely on the merger in the course of the Commission's market investigation. The parties disregard the fact that many respondents requested a confidential treatment of their responses, precisely to avoid possible future retaliation by the new entity on which they depend for their operations in the Hungarian energy markets.

Conclusion

- (449) On the basis of the evidence available and the analysis developed above, the Commission considers that, as a result of the merger, the new entity is likely to have the ability and the incentive to foreclose access to gas resources to its downstream competitors on the market for the supply of gas to small industrial and commercial customers, starting immediately after the transaction.
- (450) In view of the new entity's dominant position on the upstream markets for the wholesale supply, and the storage, of gas in Hungary and because of its presence in the downstream gas market for the supply of gas to small industrial and commercial customers (owing to its controlled RDCs) the merged entity will have, already in the current regulatory scenario and at the current stage of market liberalisation, the ability and the incentive to foreclose access to gas to a) its competitors in the current free market, thereby reducing the scope for the development of a competitive free market; and b) its competitors in the regulated market by engaging in non-price discrimination with a view to raising their input costs. As a result, actual competitors are likely to be marginalised, thereby allowing the new entity to gain increased market power on the downstream gas market for the supply of gas to small industrial and commercial customers.
- (451) Furthermore, this vertical effect of the transaction (i.e. input foreclosure) will, in all likelihood, discourage new entries in the market as potential entrants will not expect to be in a position to contract gas supplies with the new entity under terms and conditions similar to those applicable to E.ON's affiliates.
- (452) Furthermore, the Commission considers that the above-described foreclosure strategy will be all the more effective and easier to implement in the framework of an increasingly liberalised market, whose next developments are expected to occur in the near future (as from 1 July 2007).
- (453) For all these reasons, the Commission is of the view that, by allowing the merged entity to raise its rivals' costs and deter new entry on the retail market for the supply

of gas to small industrial and commercial customers, the merger as notified will significantly impede effective competition in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation.

b. The new entity will have the ability and incentive to foreclose its competitors in gas retail on the market for the supply of gas to residential customers

(454) Currently, the market positions of the various retailers (RDCs and traders) on the Hungarian market for the supply of gas to residential customers are as follows:

Suppliers	Supply of gas to residential customers in 2004	
	In million m ³	In %
KÖGÁZ	[0-500]*	[5-10%]
DDGÁZ	[0-500]*	[5-10%]
Total E.ON	[0-500]*	[15-20%]
FŐGÁZ	[500-1000]	[20-30%]
ÉGÁZ	[0-500]	[0-10%]
DÉGÁZ	[500-1000]	[10-20%]
TIGÁZ	[1000-2000]	[30-40%]
MOL WMT	0	0%
Total Market	[4000-5000]	100%

(455) As for the supply of gas to small industrial and commercial customers, the fundamental change brought about by the transaction is that E.ON, unlike MOL, is active on the market for the supply of gas to residential customers through its solely controlled affiliates, KÖGÁZ and DDGÁZ, and through FŐGÁZ, in which it holds a minority shareholding. Thus, whereas prior to the transaction MOL WMT had no incentives to act to the detriment of its customers as it was not competing with them downstream, the merger is likely to result in the new entity now having the ability *and* the incentive to foreclose competitors on the downstream market for the supply of gas to residential customers, so as to significantly impede competition thereon.

(456) In that regard, the analysis developed in section a) above (recitals 401 to 453) with regard to the likely effects of the merger on the market for the supply of gas to small industrial and commercial customers applies to the effects of the merger on the market for the supply of gas to residential customers. However, with respect to the timing of such effects, the Commission considers that a distinction should be drawn due to the different regulatory situations of both markets.

(457) Indeed, by contrast with the market for the supply of gas to small industrial and commercial customers, the market for the supply of gas to residential customers is not yet open to competition as, pursuant to Directive 2003/55/EC, residential customers will only become eligible as of July 2007. For the time being, residential customers are supplied within a public utility contract by their local RDC, which in turn is supplied by the public utility wholesaler, MOL WMT.

- (458) When the market is open to competition, i.e. at the latest in July 2007, Hungarian players expect that the current system of public utility supply will be replaced with a Universal Service Provider (“USP”) concept for residential customers which have not concluded a supply contract with a specific supplier. Such USP shall be a gas trader licensee appointed through a competitive tender and shall be entrusted with the supply of residential customers throughout Hungary at regulated prices.
- (459) Although the parties have not raised any specific argument with respect to the impact of the regulatory situation on the competitive assessment²⁰², the Commission has carefully considered whether the absence of competition on the market for residential customers on the expected date of the decision could, by itself, dispel the concern that the merger will significantly impede effective competition within the meaning of Article 2(3) of the Merger Regulation.
- (460) It follows from the case-law that, where markets are due to be open to competition in the future by virtue of Community legislation, the Commission must not limit itself to assessing only the future effects of the concentration as from the date of their opening to competition, but should also take into account the immediate effects of the concentration on these markets²⁰³. Indeed, according to the Court of First Instance, although the Commission “*may, where appropriate, take into account the effects of a concentration in the near future...or indeed base its prohibition decision of a concentration on such future effects...that does not allow it to refrain from analysing the immediate effects of such a transaction if they exist and from taking them into account in its overall assessment of the transaction*”²⁰⁴. On the other hand, it would run counter to the “*Regulation’s purpose of prevention*”²⁰⁵ and to the prospective analysis of the kind necessary in merger control²⁰⁶ to focus exclusively on such immediate effects (if they exist) as it would lead the Commission to ignore that a merger may have the effect of pre-empting the introduction of effective competition - and thus significantly impede it - in markets not yet liberalized, contrary to the intention of the Community legislature.
- (461) In the present case, since residential customers will become eligible in July 2007, i.e. only 18 months after the adoption of the present decision, the Commission considers that the main anticompetitive effects resulting from the merger will occur as from that date. Indeed, in view of the new entity’s dominant position on the upstream markets for the wholesale supply, and the storage, of gas in Hungary and because of its presence in the downstream market for the supply of gas to residential customers (owing to its controlled RDCs), the merged entity will have – for the same

²⁰² It is not argued, in particular, that the Commission is not entitled to assess the effects of the merger on that market, due to be opened to competition shortly.

²⁰³ Case T-87/05, *EDP – Energias de Portugal / Commission*, [2005] ECR II-0000 para. 123.

²⁰⁴ Case T-87/05, *EDP – Energias de Portugal / Commission*, [2005] ECR II-0000 para. 124.

²⁰⁵ Case 12/03 P, *P Commission v Tetra Laval* [2005] ECR I-0000, para. 75.

²⁰⁶ According to the Court of Justice, such a prospective analysis entails “*a prediction of events which are more or less likely to occur in future if a decision prohibiting the planned concentration or laying down the conditions for it is not adopted*” (Case 12/03 P, *P Commission v Tetra Laval* [2005] ECR I-0000, paragraph 42).

reasons as for the market for the supply of gas to small industrial and commercial customers - the ability and the incentive to foreclose access to gas to its actual and potential competitors in the market for the supply of gas to residential customers, thereby a) reducing the scope for the development of a competitive free segment of the market for the supply of gas to residential customers (where residential customers would conclude a gas supply contract with the supplier of their choice); and/or b) its actual and potential competitors in the regulated segment of the market for the supply of gas to residential customers (USPs) which are in competition with E.ON's affiliates to be appointed as USPs in a competitive tender while having to source their gas from the new entity (at prices and conditions freely negotiated). As a result of this likely behaviour, actual competitors are likely to be marginalised, thereby allowing the new entity to gain increased market power on the downstream gas market for the supply of gas to residential customers when they become eligible in July 2007.

- (462) Furthermore, the Commission considers that, in addition to these future anticompetitive effects, the merger is also likely to produce immediate effects. First, given that the merger is likely to immediately and significantly impede effective competition on the neighbouring and closely related market for the supply of gas to small industrial and commercial customers, existing rival retailers will be weakened. Since those retailers are the same as those likely to compete for residential customers when they become eligible, the merger will therefore produce an immediate spill-over effect. Secondly, the likely vertical effects of the transaction (i.e. input foreclosure) is likely to already discourage potential new entrants to prepare their entry on the market for the supply of gas to residential customers as they will not expect to be in a position to contract gas supplies with the new entity under terms and conditions similar to those applicable to E.ON's affiliates. In particular, it is worth recalling that gas supply contracts for the gas sourcing of the suppliers are often concluded well in advance and that market entry has to be planned well before the actual opening of the market. From that perspective, the merger will thus also produce immediate effects by further deterring possible entries on the market.
- (463) Finally, it should be noted that the Commission's competitive assessment would be the same, should the markets for gas supply to residential customers and for gas supply to small industrial and commercial customers become one same market immediately after July 2007. The only change in July 2007 in that case would then be the size of the market of gas supply to small customers (residential and non-residential), which would increase from 2-3 bcm to 6-8 bcm (when residential customers are added).

Conclusion

- (464) On the basis of the evidence available and the analysis developed above, the Commission considers that, as a result of the merger, the new entity will have the ability and the incentive to foreclose access to gas resources to its downstream competitors on the market for the supply of gas to residential customers.
- (465) In their reply to the SO, the parties raise the same arguments with regard to both the market for the supply of gas to small industrial and commercial customers and the market for the supply of gas to residential customers, without putting forward considerations specific to the latter market. Consequently, it is sufficient to refer, in

that respect, to the Commission's analysis already set out in the previous section relating to the market for the supply of gas to small industrial and commercial customers.

- (466) For all these reasons, the Commission is of the view that, by allowing the merged entity to raise its rivals' costs and deter new entry on the retail market for the supply of gas to residential customers, the merger as notified will significantly impede effective competition in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation.

c. The new entity will acquire a dominant position in the supply of gas to large industrial customers

- (467) On the market for the supply of gas to large industrial customers, MOL WMT directly supplies natural gas to approximately [10-20]* industrial customers connected to the high pressure pipeline and, therefore, competes - to some extent - with the RDCs which also supply some large industrial customers through the distribution network. The customers supplied by MOL WMT (both as public utility wholesaler on the regulated segment of the market and as a trader on the open segment of the market) accounted for approximately [0-2]* bcm in 2004, that is [30-40%] of the market. The table below summarizes the market shares of the various suppliers of large industrial customers (both on the regulated segment of the market through RDCs and MOL WMT public utility wholesaler and on the open segment of the market through MOL WMT and the only new entrant so far, EMFESZ).

Suppliers	Supply of gas to large industrial customers in 2004	
	In million m ³	In %
KÖGÁZ	[0-500]*	[5-10%]
DDGÁZ	[0-500]*	[5-10%]
Total E.ON	[0-500]*	[10-15%]
MOL WMT	[500-1000]*	[30-35%]
FÖGÁZ	[0-500]	[10-20%]
ÉGÁZ	[0-500]	[10-20%]
DÉGÁZ	[0-500]	[0-10%]
TIGÁZ	[500-1000]	[10-20%]
EMFESZ	[0-500]	[0-10%]
New entity	[1000-2000]*	[45-50%]
Total Market	[3000-4000]	100%

- (468) It should be underlined that, up to now, MOL WMT and RDCs have only been indirect competitors on that market. On the regulated segment of the market, MOL WMT can only supply customers directly connected to the transmission network that are listed in its license as public utility wholesaler, whereas customers connected to the distribution network can only purchase gas from their local RDCs. In addition, despite being both supplying large industrial customers, MOL WMT and RDCs are in a vertical relationship as RDCs are obliged to source their gas from MOL WMT on the regulated segment of the market.
- (469) Up to now, few customers have been able to obtain better offers on the open segment of the market from traders such as EMFESZ because regulated prices have so far remained quite low.

- (470) As of July 2007, the hybrid model and regulated prices will disappear for large industrial customers. It is likely that, absent the merger, MOL WMT would have been able, in its position of gas trader licensee, to gain more customers connected to a distribution network by proposing to supply them directly. Therefore, the Commission acknowledges that, irrespective of the merger, MOL WMT would already have the ability and the incentive to increase its position on the market for gas supply to large industrial customers.
- (471) Nevertheless, the change brought about by the merger results from the addition of E.ON's significant customer portfolio of its controlled RDCs (KÖGÁZ, DDGÁZ) and, arguably, of FŐGÁZ, about which it has privileged information. This overlap will grant an additional competitive advantage to the merged entity by enabling it, as opposed to its current competitor EMFESZ and to potential entrants, to immediately gain access to a significant customer base.
- (472) In addition, the Commission believes that, for the same reasons as in section a) above (recitals 401 to 453), the new entity will have the ability and incentive to foreclose access to its competitors downstream in the market for the supply of gas to large industrial customers in Hungary. Moreover, such foreclosure strategy would likely be reinforced as MOL Transmission would have an incentive to discriminate vis-à-vis MOL WMT's rivals for the supply of gas to large industrial customers, with a view to increase MOL WMT's profits.
- (473) In their reply to the SO²⁰⁷, the parties argue that the Commission has not sufficiently developed its reasoning as regards the creation of a dominant position in this market and "*has not engaged into an analysis of the countervailing competitive forces emanating from the other five significant*" competitors.
- (474) It appears that four out of the "*other five significant competitors*" referred to by the parties are RDCs not connected to E.ON. However, as explained in the SO, on the market for the supply of gas to large industrial customers, MOL WMT competes with RDCs, whilst, at the same time, the latter are obliged to source their gas from MOL WMT for their supply activities on the regulated segment of the market, and do not have any alternatives to sourcing from MOL WMT on the liberalised segment of the market. The parties have not even attempted to explain how RDCs would be in a position to exert a "significant" competitive constraint on the new entity while, at the same time, sourcing their gas from the latter, and have limited their rebuttal to alleging that the Commission has not developed its analysis in full. Consequently, in addition to the significant horizontal effects brought about by the merger, the new entity will have the ability and the incentive to foreclose these competitors on the market for gas supply to large industrial customers in the same manner as in other retail gas markets. Hence, the foreclosure scenario described in detail in the previous sections applies, mutatis mutandis, to this market as well.
- (475) As to the parties' argument that the Commission has not made up its mind on whether the competition concerns on this market would be of horizontal or vertical nature, it is worth recalling, as indicated in the SO, that the concerns arising on this market are due mainly to the horizontal effects of the merger, which result not only from the overlap leading to a combined market share indicative of dominance ([40-

²⁰⁷ Page 11

50%]* market share resulting from the combination of the market shares of MOL WMT and of E.ON's RDCs KÖGÁZ and DDGÁZ), but also from the addition of the significant customer portfolio of E.ON's RDCs, and arguably, of FÖGÁZ, about which the new entity will have privileged information.

(476) For these reasons, the Commission is of the view that the merger will significantly impede effective competition in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation, through the creation of a dominant position on the market for gas supply to large industrial customers.

(ii) Storage of gas

(477) Any gas supplier needs to have access to storage facilities to be active on the gas retail markets, essentially in order to manage the seasonal fluctuations in the demand of its customers. Depending on the type and the number of customers, a gas supplier has to deal with daily, weekly and seasonal fluctuations so that access to efficient storage facilities at good economic conditions is an absolutely necessary condition for any supplier.

(478) It is interesting to note that suppliers with a very large and diversified customer base may need to reserve lower storage capacities as the overall variation of demand of their customers is lower due to synchronicity (when using storage for balancing) than suppliers with a limited number of customers with a fluctuating demand. This provides large gas suppliers and other gas suppliers whose customers have a stable demand with a competitive advantage over smaller competitors.

a. MOL Storage holds a dominant position in the storage of gas in Hungary

(479) MOL Storage is the only company owning gas storage facilities in Hungary and therefore the only one able to offer gas storage services.

(480) MOL Storage will be acquired by E.ON as part of the transaction. The Share Purchase Agreement also foresees that MOL will retain a 25%+1 shareholding in MOL Storage. A structural link between MOL and MOL Storage will thus be maintained. An additional commercial link arises from the Supply Agreement concluded between MOL (MOL E&P) and MOL WMT for the sale of domestic gas.

(481) All Hungarian gas storage capacities are currently fully booked, essentially by MOL WMT as public utility supplier ([2-4]* bcm or [40-50]* million m³/day, accounting for [90-100%]* of storage capacities). The rest of the storage capacity is booked by EMFESZ for [0-1]* bcm and by MOL WMT as trader (MOL's trading licensee on the open segment of the market) for [0-1]* bcm.

(482) It is worth noting that, similarly as for the access to the transmission network, as the public utility wholesaler and supplier, MOL WMT has privileged access to storage facilities (for residential and "communal" customers), as specified in Article 30(2) of the HGA. Like any other operator, MOL WMT is entitled to book capacity only on the basis of confirmed customer demand.

(483) The remaining capacity can be allocated to operators on the open segment of the market (i.e. serving customers in the open segment of the market). Pursuant to the

HGA, access to storage in the open segment of the market is negotiated and not regulated (i.e. tariffs are not set by the regulator but through commercial negotiations with the storage operator). It is however foreseen that the system will change and become fully regulated for all operators (regardless of the status of their customers), pursuant to the conditions attached to the HEO resolution approving the E.ON/MOL transaction.

- (484) As mentioned on 27 June 2005, the HEO adopted a resolution approving the E.ON/MOL transaction, subject to legally binding conditions.
- (485) Some of these conditions are related to Storage, most notably Condition 5 (Implementation of a gas storage development scheme for 2005-2009 approved by the HEO); and Condition 6 (MOL Storage commit to apply a regulated access for all system users, i.e. also in the open segment of the market, until real competitive market situation between natural gas storages takes place, and to comply with the GGPSSO).

b. The new entity will have the ability and incentive to discriminate against its competitors in granting access to storage

Discriminatory behaviour in granting access to storage

- (486) The Commission believes that, as the result of the merger, E.ON will have the ability and the incentive to adopt discriminatory behaviour with respect to access to storage with a view to reinforce the gas input foreclosure strategy as described above to the detriment of E.ON's competitors downstream.
- (487) In their reply to the SO the parties argue that, as regards storage, "*MOL currently has the same power and incentive to discriminate*" and claim that "*the change in ownership in MOL Storage will not result in the emergence of a new discriminatory element or increase the chance or willingness for such discrimination*"²⁰⁸.
- (488) The Commission disagrees with the parties' argument that the incentive to discriminate will remain unchanged further to the transaction. As a matter of fact, the vertical integration of E.ON downstream (notably through its majority and minority participation in three gas RDCs) represents the fundamental difference vis-à-vis the situation pre-transaction, as MOL is not active in the downstream gas markets, and will create the incentive for the new entity to exploit its dominant position in storage to reinforce its strategy of foreclosure of competing operators in the gas downstream markets, by raising (directly or indirectly) the cost of storage services for those competitors.
- (489) While the incentive to discriminate would change with the transaction, the ability to discriminate would not in spite of the conditions attached to the HEO resolution. The parties have stressed in particular the importance of condition 6 of the resolution, by emphasising that MOL Storage will be forced to apply the regulated segment of the market conditions also to all operators in the open segment of the market, thereby eliminating the possibility of discriminating against E.ON's competitors with the aim of raising rivals' costs.

²⁰⁸ Reply to the SO, p. 18.

- (490) However, the Commission understands that MOL Storage will have to submit a proposal for the new “fully” regulated regime by 31 May 2006. The HEO would then review and possibly approve MOL Storage’s proposal. This approval process may take some time, as the HEO may request certain amendments to the proposal.
- (491) This means that the fully regulated regime may enter into force well into the second semester 2006 if not later. Whilst the Commission acknowledges that the coming into force of a fully regulated storage regime may at least alleviate concerns regarding the discriminatory behaviour on the part of MOL Storage against E.ON’ competitors, and that therefore the full and timely implementation of the conditions attached to the resolution of the HEO may reduce the ability to discriminate, it has to be stressed that during the period running up to the final approval by the HEO of the new fully regulated regime, MOL Storage would still have margin for manoeuvre for applying discriminatory pricing terms and conditions. In a scenario of growing liberalised market (as also stressed by the parties), the scope and the incentive for potential discrimination should be taken into account, as such discriminatory behaviour could be particularly harmful at the beginning of the liberalisation process.
- (492) The parties argue in their reply to the SO that the Commission has not duly taken into account that “*under the approval decision of the HEO, the present transaction can only be consummated if E.ON/ERI submitted an irrevocable guarantee in respect of the fulfilment of the conditions*”.
- (493) The Commission however stresses that the new entity’s obligation is, in this respect, limited to elaborating “*the conditions of regulated storage access in its General Terms of Business*” by 31 May 2006 and applying for the HEO’s approval. It is only following the HEO’s approval – which may take some time – that “*MOL Storage obeys the amended provisions thereof in the c[o]urse of applying regulated storage access*”.
- (494) Moreover, the parties also argue that the Commission “*should not be worried about the interim period of the first half year of 2006*” as “*this represents the second half of the current gas year for which all agreements relevant to storage access have already been concluded and those agreement cannot be changed post closing*”.
- (495) The Commission considers that this argument fails to acknowledge the possibility that other third parties may need access to storage services during the second half of 2006, for which new contracts would have to be negotiated during the first half of 2006. The storage injection season does not correspond to the gas year, as it runs from 1 April until 30 September, and the withdrawal season starts from mid-October after a few weeks of maintenance. Furthermore, the parties may also engage in non-price discriminatory behaviour even in the framework of existing contracts, as further explained below. Finally, the parties put forward their argument as regards the first semester of 2006, while not contesting the Commission’s assessment that “*the fully regulated regime may enter into force well into the second semester 2006 if not later*.”
- (496) Moreover, since the regulated prices are established by the HEO on the basis of inputs, estimates and information provided by the operator of the storage facilities, E.ON may have the ability and the incentive to cross-subsidise its activities in the gas downstream open segment of the markets through its near-monopolistic

activities (in gas storage) by providing information according to which the HEO would set regulated prices above real costs.

- (497) The parties argue in their reply to the SO (Annex 2, page 3) that the HEO is currently reviewing the “*storage costs*” with the objective of “*calculating the new regulated storage tariffs, which will be in effect from 1 January 2006 for four years*”. This review should be finalised before the expected completion of the transaction. The parties conclude, on this basis, that “*E.ON can have no effect on the newly accepted cost regime for the period 2006-2009*”.
- (498) However, the parties fail to mention that price reviews are possible, at the request of the storage operator. The HEO foresees a specific procedure for such reviews, to be concluded with HEO resolutions. In this light, the argument of the parties appears to be moot.
- (499) Secondly, MOL WMT may still exploit its priority position for the allocation of storage capacity by over-nominating its capacity needs of storage. This appears to be a concrete possibility, in spite of the requirement that capacity only be booked on the basis of confirmed consumption/customer demand. As a matter of fact a third party indicated that the system’s “*technical capacity*” is 20-30% higher than “*regulatory capacity*”²⁰⁹, meaning that most if not all operators tend to book more capacity than actually needed. This has the effect of congesting the system and the objective/effect of raising barriers to entry for new suppliers.
- (500) By overbooking its priority storage capacity, MOL WMT would increase the system’s congestion. As a result, the “*lower priority*” capacity would become scarcer, thus raising, in the period up to the full implementation of the HEO resolution, the non-regulated price of storage services and creating an additional barrier to entry on the open segment of the market.
- (501) The parties have argued²¹⁰ that it would not be “*in the interest of the owner of MOL WMT to overbook storage capacities as this would be costly*”. However, the Commission considers that the cost of overbooking incurred by MOL WMT may well be (more than) compensated by the extra revenues accruing to MOL Storage due to the higher price of storage services, now become scarcer due to their reduced availability, and by the revenues accruing to MOL WMT through preventing and/or raising barriers to the entry of competitors.
- (502) Thirdly, as already indicated, the HGA provides for Third Party Access to storage, whose principles are the same as for the booking of transmission capacities. Once a new supplier has acquired an eligible customer, the Already Allocated Capacity required to supply this customer should be automatically transferred to the new supplier.
- (503) However, the customer-based capacity allocation regime may leave some margin for discriminatory behaviour. As a matter of fact, MOL Storage may engage in a whole

²⁰⁹ Minutes of meeting with EMFESZ of 28 July 2005: “Better control of compliance with the rules should be secured, e.g. regarding the customer-based capacity allocation regime”.

²¹⁰ Reply to the SO, annex 2, pp. 3-4.

range of actions intended to increase the costs to E.ON's downstream competitors, such as designing storage services that are more suited to the needs of an incumbent than those of new entrants (as regards injection and withdrawal rates and volumes of gas stored), delays in allocation of storage capacity, reductions in the quality of service, mistakes in processing orders, lack of flexibility and so on, thereby significantly increasing the operational costs of competitors of the merged entity in the downstream markets.

- (504) Finally, even in the scenario of fully regulated prices for storage services, MOL Storage may have the ability and the incentive to discriminate against E.ON competitors by means of more onerous/less flexible contractual terms as compared to those negotiated with intra-group companies (e.g. the trading branch of MOL WMT active on the open segment of the market).
- (505) Moreover, it may be argued, as an aggravating factor, that any discriminatory behaviour may also prove difficult to detect considering that market players would not be likely to submit complaints to the regulator or competition authority in view of the monopolistic position of E.ON in the market for storage. In addition, as MOL WMT will remain by far the biggest client of MOL Storage, E.ON may argue that contractual terms and conditions would differ for "objective" reasons. The likelihood of the anticompetitive behaviour aimed at reinforcing the gas foreclosing strategy vis-à-vis downstream competitors would thus be increased, in the absence of sufficiently strong "regulatory" deterrence.
- (506) In their reply to the SO²¹¹ the parties argue that *"there is no reason to believe that in the future, the customers of MOL Storage would be deterred from submitting complaints against the business conduct of MOL Storage"*.
- (507) Nonetheless, the Commission stresses that even the HEO, the body which is responsible for overseeing the fair, transparent and non discriminatory functioning of the gas sector in Hungary, has stated that *"[p]ossible discriminative rules applied regarding storage access is a behaviour that is very hard to prove using administrative methods. (...) The market player which is at a disadvantage fears for its future position on the market, and will rather not submit a complaint at the regulatory or competition authority"*²¹². In this light, the argument of the parties appears to be moot.

The development of storage capacity and the possibility of increased competition

- (508) Finally, E.ON will be able to control the development of new storage capacities in Hungary. This is due to the combination of two elements: a) the call option foreseen in paragraph 10.10 of the Share Purchase Agreement for MOL Storage to purchase depleted fields from MOL E&P; and b) the 25%+1 shareholding to be retained by MOL into MOL Storage.

²¹¹ Page 18

²¹² Reply of the HEO to the Hungarian Competition Authority's questions regarding the E.ON/MOL transaction, 11 April 2005, page 4.

- (509) There are around 50 empty underground reservoirs in Hungary, owned by MOL E&P, which have the potential to be converted into storage facilities. The parties have stated that [...] of these 50 depleted fields can be converted into storage facilities within a 3 to 10 years period. The capacity of these potential storage facilities is between 100 million m³ and 3 bcm each.
- (510) Out of these ten “best” depleted fields, three may be converted within a period of 2 years for a total capacity of 350 million m³²¹³. Another two may be converted within 3-4 years for a total capacity of 850 million m³.
- (511) Paragraph [...] of the Storage Shareholder Agreement (“SSA”) between MOL and E.ON grants the [...]. The call option has a validity of [...] years. Schedule 7 attached to the SSA foresees that [...].
- (512) As mentioned, the call option grants MOL Storage the right to purchase depleted fields for a total capacity of up to 1 bcm. As a result, by exercising the call option E.ON will be in a position to prevent new entry into the storage market for a number of years, as the most readily available fields (i.e. convertible in a period of [0-5]* years) amount to a capacity of only [1-2]* bcm, thus leaving no scope for entry for at least [0-5]* years and only marginal scope, if any, for [2-5]* years.
- (513) Furthermore, in view of the minority shareholding of MOL into MOL Storage and the commercial relationship between MOL (MOL E&P) and the new entity as regards the sale of domestic gas, MOL will have an economic interest to discourage potential new entrants into the storage market by refusing to sell depleted fields or by applying unfavourable terms and conditions as compared to those applied to MOL Storage. MOL’s financial interest arises from the possibility to receive dividends from MOL Storage’s profits corresponding to its shareholding and to obtain capital gain on the increase in value of its shareholding resulting from the company’s greater profitability (even if no dividends are distributed). Such discrimination strategy is not expected to induce a decrease in MOL E&P’s revenues deriving from the sale of depleted gas fields (as it would favour MOL Storage to the detriment of its potential competitors) and would strengthen MOL Storage’s gas storage services input foreclosure strategy mentioned above.
- (514) In addition, due to the structural links between MOL and MOL Storage, MOL Transmission will have the incentive to favour the development of MOL Storage’s new storage facilities as compared to its competitors, in terms of connection to its gas transmission network. In their reply to the SO²¹⁴, the parties argue that “*the transaction reduces the incentive of MOL E&P to sell sites exclusively to MOL Storage, because the transaction weakens the relationship between MOL E&P and MOL Storage*”.
- (515) While the Commission acknowledges that the ownership unbundling of gas supply activities (MOL WMT) on the one hand, and gas production activities (MOL E&P), future storage sites (MOL E&P) and transmission activities (MOL Transmission) on

²¹³ See the MOL Plc document “Opportunities for UGS capacity expansion”, submitted by the parties in reply to question 71 in the Commission’s request for information.

²¹⁴ Annex 1 page 26.

the other hand brings, in principle, positive effects, the Commission nonetheless is of the opinion that that the cross-shareholdings, the existence of the put option for MOL Transmission, the Supply Agreement with MOL E&P and the call option for MOL Storage to purchase depleted fields from MOL E&P impair the “effectiveness” of the unbundling of those activities and, by maintaining a structural link between MOL and the new entity, significantly limit the scope of the positive effects described by the parties.

- (516) At any rate, even in the absence of this structural link, the Commission stresses that the parties have, as a matter of fact, negotiated a call option which grants MOL Storage a right of “first choice” on the best fields to be developed into storage facilities and which will, in all likelihood, act as a barrier to entry into the gas storage market for the foreseeable future.
- (517) To conclude, the Commission believes that, following the transaction, the new entity will have the ability and the incentive to discriminate against its competitors in the downstream gas markets for their access to storage capacity. MOL Storage already had the ability to exploit its dominance on the market for the storage of gas in Hungary prior to the transaction, but the transaction strengthens its incentives to do so by creating a fully vertically-integrated undertaking along the gas supply chain.
- (518) Moreover, owing to the call option foreseen in the SSA, E.ON will have the ability and the incentive to make new entry into the storage market impossible, at least in the short-medium term.
- (519) Finally, owing to the structural link between MOL and MOL Storage, MOL will have the ability and the incentive to contribute to raising barriers to entry into the storage market.
- (520) For these reasons, the Commission is of the view that the merger will significantly impede effective competition in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation, as the new entity is likely to discriminate against its competitors in the downstream gas markets for their access to storage capacity and is likely to make new entry into the storage market impossible.

(iii) Transmission of gas

- (521) MOL Transmission owns and manages the gas high pressure grid in Hungary including the two entry points for imports. MOL Transmission also acts as system operator, in charge of the continuous and transparent operation and balance of the integrated natural gas system.
- (522) MOL Transmission is not part of the proposed transaction. However, as already mentioned, the parties have concluded an agreement whereby MOL is granted a “put option” under which MOL may sell to E.ON either a 25 % plus 1 share or a 75 % minus 1 share interest in MOL Transmission during the next two years. E.ON has stressed that it has no influence to request MOL to exercise this put option.

a. Nabucco pipeline

- (523) Respondents to the Commission's investigation have argued that the mere existence of this put option may provide E.ON with a strong influence over MOL Transmission, which means that the market for the transmission of gas may also be affected by the merger, even prior to the exercise of the put option.
- (524) In particular, respondents to the market investigation have expressed the concern that the new entity may be able to influence MOL Transmission's strategy post-merger and to have an impact on the transit options to other European countries. Market participants have reported to the Commission that E.ON already had de facto a decisive influence on new pipeline projects going through Hungary.
- (525) Serious concerns have been raised in relation to the Nabucco project dealing with a new pipeline going from Turkey to Austria, crossing Bulgaria, Romania, and Hungary to bring Caspian and Middle Eastern gas to European markets. The pipeline's operation phase is expected to start in 2011/2012 and its yearly capacity will be either [25-30] bcm (base case scenario) or [30-35] bcm (high case scenario). Around [10-20] bcm are expected to be available at the Baumgarten Austrian hub for further transmission and distribution in Europe. The project has received the support of the European Union (TEN Programme) and plays a key role in diversifying the European Union's gas sourcing.
- (526) Two respondents to the market investigation directly involved in the project have claimed that the project had already been delayed by the proposed transaction. According to these third parties, while all other partners were about to sign the JV agreement in March 2005, MOL Transmission indicated that it would first need to obtain the approval of E.ON Ruhrgas.
- (527) More importantly, these companies have also raised the concern that MOL Transmission could be unwilling or unable to contribute to the development of the project over the duration of the put option. Any such development could have an impact not only on the availability of alternative sources of gas for new entrants in Hungary but also on the security of supply and sourcing policy of Hungary and the rest of the European Union.
- (528) E.ON's incentives would be two-fold. First, according to these third parties, the Nabucco pipeline, which offers a chance to bring significant quantities of non-Russian gas to Europe, could interfere with Gazprom's commercial strategy in Europe. In the opinion of the parties involved in Nabucco, this gas could even be competitive on the Polish, Czech, Ukrainian and Belarusian markets, which are currently essentially supplied by Gazprom. In view of the strategic relationship between Gazprom and E.ON, Gazprom may therefore influence E.ON's position in order to delay or impede the success of the project. Secondly, E.ON would also have an incentive not to favour new pipelines entering Hungary to prevent new competitors from entering the Hungarian gas markets.
- (529) The Commission has carefully assessed the concerns raised by these third parties but could however not come to the conclusion that the proposed transaction was likely to impede or delay significantly the construction of the Nabucco pipeline.

- (530) The Commission first notes the company involved in the Nabucco joint venture is no longer MOL Transmission but its parent company MOL (MOL Rt.)²¹⁵. The joint venture agreement was signed by the five Nabucco partners in July 2005. E.ON is thus not in a position to have a decisive influence on the project development and MOL is likely to continue to support the construction pipeline if the further economic analysis and the project financing confirm that it will be profitable for its joint owners.
- (531) Moreover, the Commission's investigation did not provide indications that E.ON had strong incentives to oppose the new pipeline project. While the strategic relationship with Gazprom may have a bearing on E.ON's position²¹⁶, E.ON is also certainly interested in diversifying its gas sourcing portfolio in Europe and the Nabucco project could bring E.ON significant advantages in this respect.
- (532) For these reasons, the Commission has concluded that the proposed transaction is not likely to impede or significantly delay the Nabucco pipeline project, as the result of which competition could be significantly impeded in a substantial part of the common market.

b. Transmission of gas in Hungary

- (533) With respect to the impact of the proposed transaction on gas transmission within Hungary, respondents to the market investigation have argued that MOL Transmission will be in a position to favour E.ON in the allocation of cross-border or national capacities, although such behaviour would be subject to monitoring by the HEO. Moreover, it has been argued by some respondents that the existence of the put option may lead MOL Transmission to "freeze" the development of its network (e.g. new entry capacity) during the period up to the deadline for the put option, while waiting to decide whether the option will be exercised or not.
- (534) As MOL Transmission is not part of the notified transaction, the full effect of the contemplated put option, which would further strengthen the vertical integration of E.ON, is not assessed in this document. However, the Commission acknowledges that the mere existence of the put option is likely to have an impact on the functioning of the markets and the management of the gas infrastructure in Hungary.
- (535) Furthermore, as already indicated, according to the Share Purchase Agreement signed by the parties, MOL (which will continue to control MOL Transmission) will retain a 25%+1 shareholding in MOL WMT, which will be controlled by E.ON, thereby creating a structural link between MOL and the merged entity. An additional commercial link arises from the Supply Agreement concluded between MOL (MOL E&P) and MOL WMT for the sale of domestic gas. This commercial relationship between MOL and MOL WMT is likely to reinforce the structural link.
- (536) The 25%+1 minority shareholding that MOL would retain in MOL WMT and the above-mentioned commercial relationship give MOL Transmission an incentive to discriminate against E.ON's downstream competitors when granting access to the

²¹⁵ Parties' reply to the Commission request for information dated 19 July 2005 – Question 101.

²¹⁶ In particular in light of E.ON's participation in the Baltic pipeline project led by Gazprom.

transmission network. MOL's financial interest arises from the possibility to receive dividends from MOL WMT's profits corresponding to its shareholding and to obtain capital gain on the increase in value of its shareholding resulting from the integrated new entity and MOL WMT's greater profitability (even if no dividends are distributed) owing to MOL Transmission granting it a favourable treatment. As for the gas input foreclosure, such non-price discrimination strategy is not expected to induce a decrease in MOL Transmission's revenues (as it would favour MOL WMT to the detriment of its competitors) and would strengthen MOL WMT's gas input foreclosure mentioned above.

- (537) As a matter of fact the vertical integration of E.ON downstream (notably through its majority and minority participation in three gas RDCs) represents the fundamental difference vis-à-vis the situation pre-transaction, as MOL is/was not active in the downstream gas market. The incentive therefore exists to reinforce the gas input foreclosure strategy to the detriment of E.ON's competitors downstream through discriminatory behaviour in granting access to the transmission network.
- (538) Whilst it has to be stressed and acknowledged that the operation of the transmission grid is highly regulated by the HEO, MOL Transmission is still likely to have the ability and incentive to favour MOL WMT for the access to the transmission network.
- (539) Moreover, as already mentioned, the Network Code contains the detailed technical rules for the operation of the gas system. The Network Code is drafted by the Network Code Committee.
- (540) It has to be highlighted that E.ON may, post transaction, directly or indirectly control the majority of the 9 members of the Committee, who are either representatives of or elected by the various licensees active in the gas sector²¹⁷. Since changes to the Network Code are decided by simple majority, E.ON is therefore likely to be in a position to influence the way in which the Network Code may be re-drafted/updated in the future with the objective/effects of discriminating against E.ON's competitors in the allocation of capacity along the grid and to favour MOL WMT over new entrants.
- (541) Furthermore, as described, capacities along the transmission (and storage) chain are crucially divided into Already Allocated Capacity (AAC) and Free Capacity (FC) in accordance with Article 1(30) of the Executive Decree.
- (542) Generally, MOL WMT will be in a position to exploit its priority position for the allocation of transmission capacity by over-nominating its capacity needs, in spite of the requirement that capacity only be booked on the basis of confirmed consumption/customer demand. As a matter of fact a third party indicated that the system's "*technical capacity*" is 20-30% higher than "*regulatory capacity*"²¹⁸, meaning that most if not all operators tend to book more capacity than actually needed. This has the effect of congesting the system and the objective/effect of raising barriers to entry for new suppliers.

²¹⁷ See Chapter 3.1 of the Network Code.

²¹⁸ See minutes of meeting with EMFESZ of 28 July 2005.

- (543) By overbooking its priority transmission capacity, MOL WMT would increase the system's congestion. As a result, the "lower priority" capacity would become scarcer, thus raising additional barrier to entry on the open segment of the market.
- (544) Moreover, Free Capacities ("FC") are measured by the TSO (i.e. MOL Transmission) according to a methodology which has to be approved by the HEO. Capacities are allocated by the TSO to market players within a maximum of three months subsequent to their application.
- (545) In case of "overbooking" of FC, the procedure for allocation foresees an "auction", pursuant to point 5.1.3.1(g) of the Network Code. The Network Code however does not specify how these auctions should take place and within which timeframe. The parties have argued that this auction process "*usually takes two weeks to complete*".
- (546) Arguably, in the presence of the MOL Transmission's incentive to discriminate in favour of the new entity, this auction processes could be managed in a non-transparent, discriminatory manner, or with undue delay, to the detriment of third parties. In the expectation that the liberalised market may grow after 2007, instances of discriminatory behaviour are still likely to occur in the allocation of FC to market operators. This discriminatory behaviour would be particularly harmful during the initial phase of liberalisation.
- (547) In their reply to the SO, the parties underline that the transaction will bring about the ownership unbundling between gas wholesale and gas transmission. Although the ownership unbundling of gas wholesale and transmission activities brings in principle positive effects, the Commission notes that the cross-shareholdings, the existence of the put option for MOL Transmission and the Supply Agreement with MOL E&P do not achieve a full unbundling of those activities and significantly limit the scope of the positive effects described by the parties.
- (548) In their reply to the SO, the parties contest that the "*timing and degree of [the transmission network] development*" may be negatively impacted by the transaction. On the contrary, the parties claim that it "*depends totally on consumer demand and the approval of the Hungarian regulator*"²¹⁹. While this assertion may be verified in normal business conditions, the Commission estimates that the uncertainties about MOL Transmission's ownership are likely to negatively impact the company's ability to carry out and plan long term projects.
- (549) To conclude, the Commission believes that MOL Transmission is likely to have the ability and the incentive to discriminate against E.ON's competitors in granting access to the gas transmission network, owing to the structural link resulting from the 25%+1 minority shareholding of MOL into MOL WMT. MOL Transmission already had the ability to exploit its dominance on the gas transmission market in Hungary prior to the transaction. The structural link created by the transaction will strengthen its incentives to do so in view of the vertical integration of the new entity along the gas supply chain.
- (550) Moreover, the Commission is also concerned that, pending the exercise of the put option, the development of the network (for instance additional entry point capacity)

²¹⁹ Reply to the SO, Page 22.

may be put on hold while waiting to see who the “final” owner of such projects would be.

- (551) For these reasons, the Commission is of the view that the merger will significantly impede effective competition in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation, as the new entity is likely to discriminate against its competitors in the downstream gas markets for their access to transmission capacity.

C. Impact of the transaction on the electricity markets

- (552) In addition to the concerns related to the gas sector presented in section B above, the Commission’s market investigation has identified competition concerns on various electricity markets, as a result of the vertical integration of MOL WMT’s activities in the upstream market of gas supply to large power plants with E.ON’s activities in the downstream markets of electricity generation/wholesale and electricity retail.
- (553) Prior to the transaction, MOL WMT is dominant on the market for the supply of gas to large power plants, whereas it is not active in the electricity markets. On the contrary, E.ON already has a strong position on the electricity retail markets in Hungary and is likely to become significantly active on the generation/wholesale electricity markets.
- (554) The Commission’s market investigation has revealed that, following the merger, the new entity will have the ability and the incentive to raise the costs of future and existing gas-fired power plants in Hungary. The Commission is also concerned that the new entity will have the ability and the incentive to supply competitive gas to future and existing gas-fired power plants under the condition that they sell their electricity production to E.ON’s RDCs or trading subsidiary at favourable conditions (“tolling strategy”).
- (555) The economic interest to pursue these strategies will increase with the further liberalization of the electricity sector in Hungary and the increase in E.ON’s share in electricity generation. These two likely strategies would also prevent existing and future rival electricity generators/wholesalers from competing effectively in the markets for the wholesale supply of electricity to traders²²⁰.
- (556) The new entity’s strategy in electricity generation / wholesale would lead to a restriction of new electricity generation capacities in Hungary and would therefore have an impact on electricity wholesale prices in the country. The “tolling agreements” strategy would restrict E.ON’s electricity retail competitors’ ability to get competitive supplies of electricity, thereby significantly impeding effective competition on electricity retail markets. In addition, the transaction will give E.ON the ability and incentive to prevent its electricity retail competitors from developing dual offers (electricity and gas) in Hungary. This would further increase E.ON’s market power on the electricity retail markets in Hungary.

²²⁰ In addition, third parties have indicated that, since 80% of heat production in Hungary is gas-fired, E.ON will have the same ability and incentive as regards heat production as for electricity. Therefore the transaction will lead to similar anticompetitive effect in the district heating sector.

(557) The Commission's assessment of the effects of the transaction on the electricity markets in Hungary has been carried out both under current market conditions and within the foreseeable future, taking account of the most likely scenario following the implementation of the New Electricity Model in Hungary.

(558) The position of E.ON and other market players in the electricity sector is first presented before setting out in detail the competition concerns resulting from the transaction at the electricity generation / wholesale and electricity retail level.

(i) *Market players in the electricity sector in Hungary*²²¹

(559) Besides E.ON, MVM and several large European electricity groups are active in Hungary at the generation, the wholesale or the retail level. Smaller electricity trading companies have also developed more recently.

a. E.ON

(560) E.ON has made significant investment in the electricity sector in Hungary since 1995/96. The group is currently active at the generation level with a gas-fired power plant in Debrecen, and at the wholesale and retail supply level with ownership of three out of the six electricity RDCs and the electricity trading company E.ON EK. In addition, E.ON controls various companies involved in electricity retail supply in Hungary's neighbouring countries.

Electricity generation

(561) E.ON owns a medium size gas-fired power plant and several smaller generation facilities in Hungary which produce both electricity and heat (for district heating purposes). These facilities had a total production of [0-2]* TWh in 2004, accounting for [5-15]*% of Hungarian gas-fired electricity and [0-5]* % of Hungarian electricity generation. It should be noted that E.ON has plans to expand significantly its generation capacity.

(562) In 2004, E.ON's largest power plant (Debrecen) sold almost²²² its entire electricity production ([500-1,000]* GWh) on the regulated segment of the market, in the frame of a long-term PPA with TITÁSZ²²³. Most of E.ON's plants are also used for heat production. E.ON is the sole heat generator/supplier for the district heating of two large cities (Debrecen and Nyíregyháza). However, at the national level, E.ON's share in heat production amounts to [5-10]*%.

(563) The assessment of E.ON's position in electricity generation in Hungary should also take into account the importance of gas-fired power plants in the Hungarian electricity markets, as explained by most market players. For instance, a third party active in the electricity sector has highlighted that:

221 None of the companies controlled by MOL is active in the production or supply of electricity in Hungary. MOL only indirectly owns minority interests in TVK-Erőmű, a 50 MW gas-fired cogeneration plant.

222 DKCE sold in 2004 minor quantities of electricity to [...] on the free market ([0-500]* MWh).

223 TITÁSZ is wholly owned by E.ON.

“The fact that E.ON currently only owns 2.8% of electricity generation capacity may be misleading. First, as regards electricity produced from gas for system balancing, suppliers with even a small percentage have market power because it is not possible to live without this electricity.”

- (564) Finally, E.ON is also active in power generation in Austria, through its interests in Donau Kraftwerk Jochensten AG (“DKJ”) and Österreichisch-Bayerischen Kraftwerk AG (“OBK”). DKJ and OBK have respectively power generation capacity of [0-200]* MW and [200-500]* MW and produced [500-1,000]* GWh and [1,000-2,000]* GWh in 2003.

Electricity wholesale

- (565) E.ON EK started its activities as electricity trader in Hungary in March 2003. In 2003, E.ON EK traded [0-5]* TWh of electricity and this quantity increased to [0-5]* TWh in 2004. The company sells electricity exclusively to MLCs and not to electricity traders. E.ON EK is one of the three major Hungarian electricity traders, with the ATEL group and MVM.
- (566) In 2004, the company sourced the large majority of its electricity from imports ([0-5]* GWh), essentially from the group’s German electricity trading subsidiary (“EST”) ([35-45]*% of E.ON EK’s imports) and through the Slovak interconnection ([85-95]*% of E.ON EK’s imports). Domestic sources ([0-2]* GWh) were MVM auctions ([0-500]* MWh) and Electrabel ([0-500]* MWh).

Electricity RDCs

- (567) E.ON has sole control of three of the six RDCs: TITÁSZ, ÉDÁSZ and DÉDÁSZ. In 2004, those three RDCs supplied respectively [0-5]* TWh, [5-10]* TWh and [0-5]* TWh of electricity to residential customers, SCs and MLCs in their respective regions and in the public utility segment.

Electricity retail in neighbouring countries

- (568) E.ON is also active on the electricity retail markets in Hungary’s neighbouring countries. In Slovakia, the group has a 49% interest in Zapadoslovenska Energetika a.s. (“ZSE”), active in retail supply of electricity. In 2003, ZSE had total electricity sales of [5-10]* TWh, accounting for [30-40]*% of the overall Slovak market. In Romania, E.ON acquired recently 51% in Electrica Moldova S.A (“Moldova”), also active in the retail supply of electricity. In 2003, Moldova had total electricity sales of [0-5]* TWh, accounting for [0-10]*% of the overall Romanian market.
- (569) E.ON acquired in 2003 the control of three Czech electricity regional distribution companies, ZCE, JCE and JME. Together, these three companies supplied [10-15]* TWh in 2003, accounting for [20-30]*% of the overall Czech electricity market. It is worth mentioning that ZCE’s, JCE’s and JME’s in the Czech Republic, ZSE’s in Slovakia and ÉDÁSZ’s and DÉDÁSZ’s geographic areas in Hungary have contiguous borders. Finally, E.ON also has a majority interest in the electricity distribution companies Varna and Gorna in Bulgaria, which together accounted for [15-25]*% of total Bulgarian electricity market in 2003 with sales of [0-5]* TWh.

(570) Although there is currently no relationship between E.ON's electricity retail assets in Eastern Europe, E.ON's presence in several of Hungary's neighbouring countries allows E.ON to import electricity into Hungary. In addition, E.ON may enjoy an additional competitive advantage in terms of brand recognition, reputation and ability to supply large chain customers with branches in several countries.

b. MVM

(571) MVM is the former monopoly electricity wholesaler and electricity transmission grid operator in Hungary. During the energy sector privatization in 1995/1996, Hungarian power plants and RDCs were sold to private investors while MVM remained a state owned company, owning the electricity transmission network and retaining the ownership of the Paks nuclear power plant and other power plants. Since the opening of the market to competition in 2003, MVM has maintained a leading role in electricity wholesale, as public utility wholesaler and as trader on the open segment of the market.

- Generation

(572) MVM owns the Paks nuclear power plant, the Hungarian largest power plant, and several medium-size gas-fired or coal-fired power plants. The Paks nuclear power plant produced [10-12.5] TWh in 2004, entirely sold in the public utility segment. The company owns a 25% stake in the gas-fired Dunamenti power plant, the second largest power producer in Hungary.

- Electricity wholesale

(573) As the licensee for public utility wholesale, MVM has long-term contractual relationships with the majority of large electricity generators on the one hand and the electricity RDCs on the other hand. In 2004, the company sold [25-27.5] TWh in the public utility segment, to be compared to a total electricity consumption of [37.5-40] TWh in Hungary. The company organises auctions every six months to sell its surplus power to traders.

- Electricity retail

(574) MVM fully owns MVM Partner Rt. ("MVM Partner"), active in the Hungarian free electricity market. In 2004, the company sold [2.5-5] TWh on the open segment of the market and was the second largest electricity trader.

c. MAVIR

(575) MAVIR is the current transmission system operator in Hungary. The company started its operations in January 2001 according to a "Base contract" with MVM. Initially, MAVIR was part of the MVM group, but after the adoption of the HEA in December 2001, MAVIR's ownership was transferred to the MET in December 2002. MAVIR obtained the licence for System Operation in January 2003.

- (576) Following a recent government decree²²⁴ of July 2005, the ownership of MAVIR has been transferred to MVM. The ownership of the Hungarian electricity transmission grid has been transferred from MVM (parent company) to MAVIR.
- (577) Due to the long-term PPAs contracted by MVM, MAVIR procures the electricity needed for system balancing mainly from MVM.

d. International groups

RWE

- (578) RWE is active at the generation level, with a majority stake in the Mátra lignite power plant²²⁵, at the retail supply level (public utility segment), with majority stakes in two electricity RDCs (ELMŰ and ÉMÁSZ) and at the wholesale and retail level with the electricity trader MÁSZ, a 50/50% joint venture between ELMŰ and ÉMÁSZ. In 2004, ELMŰ, ÉMÁSZ and MÁSZ had respective electricity sales of [7.5-10] TWh, [2.5-5] TWh and [0-2.5] TWh.

EDF

- (579) In Hungary, EDF is present through its subsidiaries BERT, active in cogeneration and the electricity RDC DÉMÁSZ. BERT owns three medium size CCGTs with a total generation capacity of [250-500] MW. BERT's electricity production amounted to [0-2.5] TWh in 2004 and was entirely sold in the public utility segment.
- (580) DÉMÁSZ supplies electricity in the public utility segment and sold [2.5-5] TWh in 2004. The company has established an electricity trading subsidiary named D-Energia. The latter sold [0-250] GWh and [250-500] GWh on the liberalized market in 2003 and 2004 respectively.

Electrabel

- (581) Electrabel-Suez is a French/Belgian group active on several European electricity and gas markets. The group owns the second largest electricity production facility in the country, Dunamenti Erőmű (gas-fired), with a total capacity of [1,500-1,750] MW²²⁶. In 2004, the power plant produced [2.5-5] TWh and [...] of this capacity was sold to MVM in the public utility segment. Electrabel-Suez is not active in electricity retail in Hungary.

ATEL

- (582) The Swiss group ATEL owns the gas-fired Csepeli power plant. It has a [250-500] MW generation capacity and produced [0-2.5] TWh in 2004, which were entirely sold in the public utility segment. The Csepeli power plant is the most recent large power plant in Hungary and started its operations in November 2000.

²²⁴ Government decision 1070/2005 of 8 July 2005

²²⁵ RWE holds a 50.9% stake in Mátra. Lignite is produced in Mátra-owned mines.

²²⁶ Additional generation units installed in the 60's (530 MW capacity) are currently being mothballed.

(583) The group is also active at the retail level through the two electricity traders ATEL Energia Kft. (“ATEL Energia”) and Entrade Hungary Kereskedelmi Kft.²²⁷ (“Entrade Hungary”), which respectively sold [0-2.5] TWh and [0-2.5] TWh on the open segment of the market in 2004. Combined, the two trading companies constitute the largest electricity trader in Hungary. The Csepeli plant does not have commercial relationship with ATEL Energia nor with Entrade Kft.

Others

(584) The other major market players in electricity generation are the AES group, which owns the AES Tisza gas-fired power plant and the Borsod coal power plant, and the group PannonPower Holding Rt. (“Pannon Power”) which owns the Pannon Hőerőmű gas power plant in Pécs.

(585) Several electricity traders are active on the open electricity markets in Hungary, the largest being System Consulting²²⁸, Sempra Energy Europe and Energy Financing Team Budapest. Elektra Energia and ETC Hungary started their activity more recently and the trading company Energy Capital is planning to enter in the short term.

(586) The table below provides an overview of the main market player’ position in electricity generation²²⁹ and retail supply level in Hungary.

	MVM	E.ON	RWE	EDF	Electrabel	ATEL	Others	TOTAL
Electricity generated in 2004 (GWh)	[10000-12500]	[0-2500]*	[5000-7500]	[0-2500]	[2500-5000]	[0-2500]	[5000-7500]	[30000-35000]
2004 - %	[30-40%]	[0-5%]	[10-20%]	[0-10%]	[10-20%]	[0-10%]	[20-30%]	100%
Electricity sales to final users in 2004 (GWh)	[2500-5000]	[12500-15000]*	[12500 - 15000]	[2500-5000]	0	[2500-5000]	[0-2500]	[35000-40000]
2004 - %	[0-10%]	[40-45%]	[30-40%]	[10-20%]	[0-10%]	[0-10%]	[0-10%]	100%

²²⁷ ATEL acquired at the beginning of 2005 the company Entrade GmbH, the owner of Entrade Hungary.

²²⁸ System Consulting is an independent company that imports electricity from Ukraine to Hungary for resale to traders in Hungary and for exports. System Consulting is only active at the wholesale level and does not sell electricity to any final customer.

²²⁹ As explained above, electricity generation does not constitute a relevant product market for the assessment of this transaction but is part of the generation/wholesale product market. “Electricity sales to final users” include sales in all retail electricity markets.

(587) As reflected in the above table, E.ON is the main player in the Hungarian electricity retail markets, with a market share in excess of 40%, due to its strong position both in the public utility segment and as an electricity trader.

(ii) *Electricity generation/wholesale*

(588) MOL already has the ability to exploit its position of gatekeeper of gas resources in Hungary prior to the transaction. The fundamental change brought about by the transaction is that the new entity will now also have the incentive to do so owing to the creation of a fully vertically-integrated undertaking along the gas and electricity supply chain.

(589) The Commission believes that, as the result of the proposed transaction, E.ON will have the ability and the incentive to foreclose access to gas to its competitors in electricity generation due its dominant position in the wholesale supply of gas to power plants. E.ON will also have the ability and incentive to discriminate against gas-fired power plant that do not supply its subsidiaries active in electricity retail and to engage in “tolling agreements” with new gas-fired power plants.

(590) E.ON is likely to pursue these strategies in view of its strategic plans to significantly develop its electricity generation capacity and its economic interest in obtaining competitive electricity supplies. These strategies would result in a restriction of new electricity generation capacities by other / independent market players and would strengthen E.ON’s market power and lead to an increase in electricity wholesale prices.

(591) In their reply to the SO, the parties claim that the proposed transaction will not bring about any change in MOL WMT’s strategy vis-à-vis power plants and contest the new entity’s economic interest in engaging in foreclosure strategies. The Expert Report submitted by the parties states²³⁰ that this “*would be equally likely in the absence of the proposed transaction, because the existing power stations of E.ON/ERI do not provide any head-start in the long road to monopolizing the power market*”. On the contrary, the Commission believes that the proposed transaction brings about significant changes in MOL WMT’s incentives in view of E.ON’s strategic focus on building/acquiring additional generation capacity in Hungary and of its strong position in the electricity retail supply markets.

(592) The parties also insist on E.ON’s currently limited generation capacities and argue that “*E.ON will remain a small player [in the market for electricity generation] without significant market power*”.²³¹ However, post transaction, E.ON will be dominant upstream from electricity generation / wholesale (wholesale supply of gas to power plants) and will have a very strong position in the downstream markets (electricity retail). This position will confer E.ON with unrivalled advantages to further increase its market power along the electricity supply chain.

(593) The following recitals will first present the current structure of electricity generation in Hungary and its likely evolution. The new entity’s ability to foreclose access to

²³⁰ Expert Report, Page 22/23.

²³¹ Reply to the SO, Page 24.

gas to its competitors in electricity generation will then be assessed and E.ON's focus on developing new generation capacities will be presented. The new entity's incentives to engage in the strategies mentioned above in recital 589 both in the current and in the future regulatory framework will finally be analysed.

a. The structure of electricity generation in Hungary

(594) The following recitals will present the current structure of electricity generation in Hungary and its likely evolution, based on information on new power plants and power plants decommissioning gathered by the Commission in its in-depth market investigation. The importance of gas-fired power plants in the current regulatory framework as well as in new generation capacities will be underlined.

Current generation structure

(595) Total generation capacity in Hungary is approximately 8,000 MW in 2005, to be compared with the country's peak load of 6,350 MW (in 2004). The Hungarian electricity generation is split between nuclear energy (1,800 MW installed capacity) and lignite, gas and coal power plants (5,700 MW installed capacity). Almost 40% of electricity consumed in Hungary is generated by the Paks nuclear power plant, the remaining 60% is mainly generated by power plants burning hydrocarbons (lignite, gas and coal) and by imports.

(596) In 2005, 19 power plants had a generation capacity exceeding 50 MW:

Large power plants in Hungary²³²:

Name of power plant	Owner	Fuel	Official production capacity in 2003 (MW)	Official production in 2003 (GWh)	Market investigation: current production capacity (MW)	Market investigation: production in 2004 (GWh)
Paksi Atomerőmű	MVM	Nuclear	1,866	10,297	[...]	[...]
Dunamenti	Electrabel	Gas/oil	2,126	5,053	[...]	[...]
Tisza II	AES	Gas/oil	860	2,426	[...]	[...]
Mátra	RWE	Lignite	836	5,032	[...]	[...]
Csepeli GT	ATEL	Gas	389	1,860	[...]	[...]
Oroszlány	MVM	Coal	240	1,033	[...]	[...]
Tiszapalkonya	AES	Coal/Gas	200	477	[...]	[...]

²³² The differences between the official production capacity in 2003 and the current production capacity in the table are due to capacity extension / decommissioning in 2004 and 2005.

Pécs	PannonPower	Gas	190	514	[...]	[...]
Lőrinci	MVM	Oil	170	5	[...]	[...]
Borsodi	AES	Coal/Gas/Wood	137	282	[...]	[...]
Kelenföld GT II	EDF	Gas	136	602	[...]	[...]
Sajószöged	MVM	Gas	120	3	[...]	[...]
Litér	MVM	Gas	120	1	[...]	[...]
Újpest	EDF	Gas	110	423	[...]	[...]
Bánhida	MVM	Coal	100	462	[...]	[...]
Debrecen	E.ON	Gas	95	731	95	627
Ajka	Transelectro	Coal	71	205	[...]	[...]
Kispest	EDF	Gas			[...]	[...]
EMA Power	EPIC Energy Hungary	Gas			[...]	[...]
Small power plants			280	4,084	[...]	[...]
TOTAL			8,046	31,632	[...]	[...]

PPAs

(597) The major part of the large power plants' capacity is booked under long-term PPA with MVM. The market investigation has established that the total capacity booked under those PPAs amounted to [4,000-5,000 MW] in 2005, compared to the total national generation capacity of approximately 8,000 MW. The table below indicates the existing long term PPAs with MVM and their end-date.

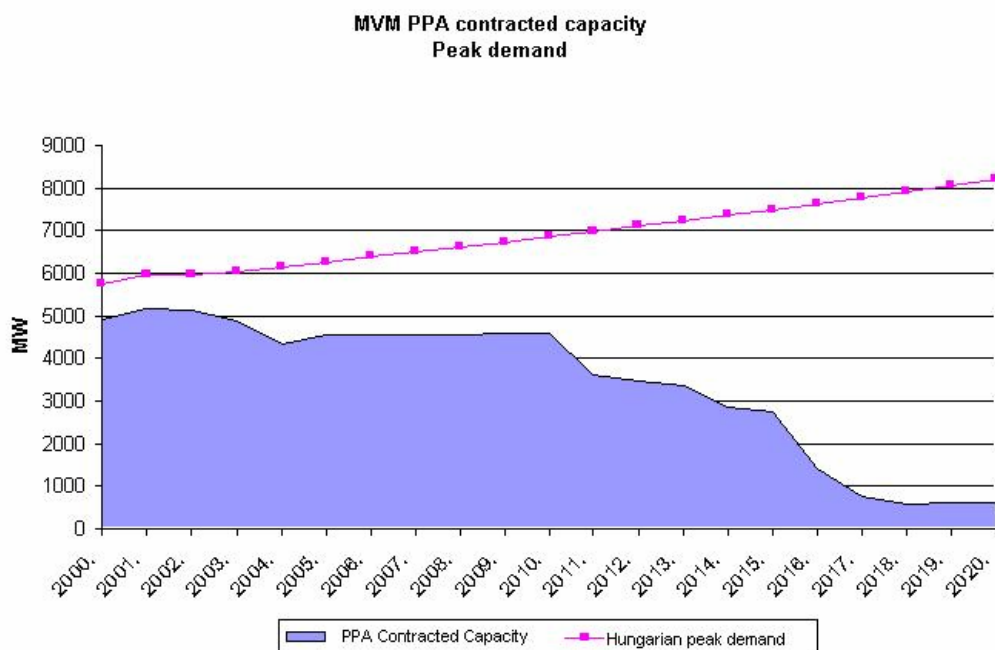
Existing long-term PPAs:²³³

Power plant	Owner	Fuel	Official production capacity in 2003 (MW)	Official production in 2003 (GWh)	PPA: Reserved capacity	PPA: End date
Paksi Atomerőmű	MVM	Nuclear	1,866	10,297	[...]	[...]
Dunamenti	Electrabel	Gas/oil	2,126	5,053	[...]	[...]
Tisza II	AES	Gas/oil	860	2,426	[...]	[...]
Mátra	RWE	Lignite	836	5,032	[...]	[...]
Csepeli GT	ATEL	Gas	389	1,860	[...]	[...]
Oroszlány	MVM	Coal	240	1,033	[...]	[...]
Tiszapalkonya	AES	Coal/Gas	200	477	[...]	[...]
Pécs	Pannon Power	Gas	190	514	[...]	[...]
Lőrinci	MVM	Oil	170	5	[...]	[...]
Borsodi	AES	Coal/Gas/Wood	137	282	[...]	[...]
Kelenföld GT II	EDF	Gas	136	602	[...]	[...]
Sajószöged	MVM	Gas	120	3	[...]	[...]
Litér	MVM	Gas	120	1	[...]	[...]
Újpest	EDF	Gas	110	423	[...]	[...]
Bánhida	MVM	Coal	100	462	[...]	[...]
Debrecen	E.ON	Gas	95	731		
Ajka	Transelektro	Coal	71	205	[...]	[...]
Kispest	EDF	Gas			[...]	[...]
EMA Power	EPIC Energy Hungary	Gas			[...]	[...]
TOTAL			8,046	31,632	[4,000-5,000]	

²³³ Source: MVM, Submissions of 31 August 2005 and 6 October 2005.

(598) Competition on the market for the wholesale supply of electricity to traders is therefore limited to large power plants to the extent of their non-reserved capacity and smaller power plants. Generation capacities booked under those long-term PPAs are expected to decrease progressively as PPAs are renegotiated or come to expiry. In addition, new power plant are, in principle, not expected to enter into such long-term PPAs with MVM and will therefore play a significant role on the market for the wholesale supply of electricity to traders. The table below illustrates the progressive reduction in the scope of the PPAs.

Evolution of the capacity reserved under long term PPAs:



Source: HEO

New power plants projects

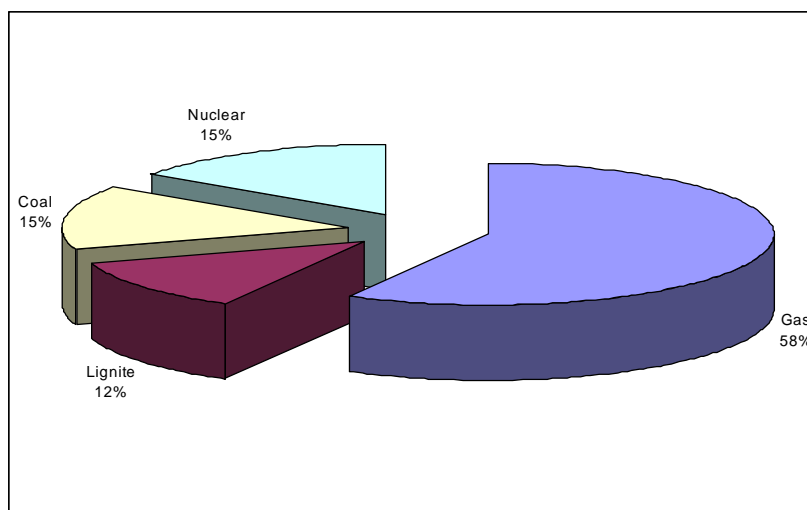
(599) As mentioned above in recitals 150 and 151, it is estimated that large electricity generation capacities will be needed in Hungary in the coming years. New generation capacity of approximately 5,000 MW has to be built until 2020 to replace old power plants²³⁴ (3,500 MW) and to satisfy the increase in demand. This figure accounts for roughly 60% of the total production capacity currently installed in Hungary. Accordingly, the Hungarian electricity generation capacity should increase from 8,000 MW to approximately 10,500 MW.

(600) The market investigation has indicated that, as of December 2005, around [1,000-1,500] MW of new generation capacity is planned to be constructed by 2010, both in new power plants and in capacity replacement / expansion in existing power plants. All these projects relate to gas-fired power plants or units, which will play an

²³⁴ The old coal-fired power plants are expected to be closed down for environmental reasons. Another possibility is to use new technologies, with lower impact on the environment and higher efficiency.

important role in the market for the supply of gas to traders, in particular in view of their ranking in the Hungarian electricity generation merit curve²³⁵. As regards the 2010-2015 period, the market investigation has shown that approximately 2,000 MW of additional generation capacity is envisaged although the degree of uncertainty is higher. The majority of projects are gas-fired, as evidenced by the following pie chart:

Breakdown of new capacity generation by type of fuel (new projects and capacity extensions until 2015):



- (601) According to this investigation, the main projects to build new large power plants in Hungary will be carried out by E.ON. All other new power plant projects which are considered with a sufficient degree of certainty by other market players are of smaller size than those of E.ON.
- (602) According to the HEO, power plant construction licenses have been granted for a total generation capacity of [0-500] MW until now. In addition, the HEO has received informal information about additional plans to build [1,000-1,500] MW generation capacity. Among those new power plant projects, [500-1,000]* MW are planned by E.ON. According to MAVIR²³⁶, E.ON intends to build either a 500 MW coal-fired power plant or a 2 x 400 MW gas-fired power plant.
- (603) E.ON has confirmed that it is considering [...] but noted that these [...] power plant projects are at an early planning stage and have not yet received all the required internal approvals. E.ON's internal documents submitted to the Commission²³⁷ [...]*. In addition, while MAVIR and another market player mentions a 2x400 MW power plant project in Gönyű, E.ON's internal documents [...]*.

²³⁵ See section above on the Electricity sector in Hungary and the graph of the Hungarian electricity generation merit curve.

²³⁶ MAVIR network planning realized in the spring of 2005. E.ON contributed to the realization of this analysis and requested MAVIR to take the two power plant projects into consideration.

²³⁷ E.ON internal documents submitted in the Reply to the Commission's questionnaires dated 18/07/2005 (Question 122).

- (604) As regards other market players, [Confidential: Overview of E.ON's competitors new power plants projects].
- (605) [Confidential: Overview of E.ON's competitors new power plants projects]
- (606) [Confidential: Overview of E.ON's competitors new power plants projects]
- (607) The tables below summarize the new power plants or power plant capacity expansions planned by 2015, with a capacity above 50 MW. Only projects that were confirmed by the relevant companies have been reported.

New power plants projects (gas-fired):

Location	Company / Group	Fuel	Capacity (MW)	Schedule
[...]*	E.ON	Gas	[250-500]* ²³⁸ - [500-1,000]* ²³⁹	Planned – [...]*
[...]	[...]	Gas	[0-250]	[...]
[...]	[...]	Gas	[0-250]	[...]
[...]	[...]	Gas	[0-250]	[...]

New power plants projects (other fuels):

Location	Company / Group	Fuel	Capacity (MW)	Schedule
[...]*	E.ON	Coal	[250-500]*	Planned – [...]*
[...]	[...]	[...]	[250-500]	[...]

Capacity expansion (gas-fired):

Location	Company / Group	Fuel	Capacity (MW)	Schedule
[...]	[...]	Gas	[0-250]	[...]

²³⁸ According to E.ON internal documents submitted in reply to the Commission's questionnaire dated 18 July 2005 (Question 121).

²³⁹ According to various market players.

[...]	[...]	Gas	[250-500]	[...]
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Capacity expansion (other fuels):

Location	Company / Group	Fuel	Capacity (MW)	Schedule
[...]	[...]	Nuclear	[0-250]	[...]

- (608) E.ON is also currently refurbishing its power plant in Nyíregyháza with a 49 MW CCGT, which should be commissioned in [...]*.
- (609) As regard other market players, MVM currently conducts a programme to increase the Paksi nuclear power plant lifetime by 10-15 years and to increase the reactors efficiency (from 430 MW to 460 MW). Several old gas or coal power plants are also undergoing modernization and efficiency improvement programmes.

Limited potential for non gas-fired power plants

- (610) The Expert Report submitted by the parties explains that the new entity's gas foreclosure strategies' would not be successful²⁴⁰ as competitors may invest in non-gas fired power plants. Although the parties claim that competitors could develop non gas-fired power plants, they fail to indicate on which alternative fuel new power plants would rely and do not provide any analysis on the competitiveness of those alternative fuels.
- (611) The Commission refers to the above market investigation on existing new power plants projects in Hungary and on the statements made by all the major market players in the electricity sector related to the predominance of gas as fuel for new power plants. The market investigation has clearly indicated that gas-fired power plants would represent the largest part of new generation capacities in Hungary. For example, the HEO considers that the proportion of gas-fired power plant in new generation capacity could reach 60%.
- (612) As a matter of fact, this analysis is not disputed by the parties. In a presentation held by MOL gas division²⁴¹, the strong increase in new gas-fired electricity generation capacity is also cited as a key driver of the Hungarian gas demand:

MOL: "[...]."*

- (613) The Commission and market players estimate that none of the alternative fuels (nuclear, lignite, coal, hydro, etc.) does offer the same advantages as gas for power generation.

²⁴⁰ Expert Report, Page 4.

²⁴¹ "MOL Gas, Management presentation", March 2004. Annex 27 to Form CO.

- (614) Nuclear power plants require a very large upfront investment compared to any other type of power plant and the process to expand or build a new nuclear reactor is subject to extremely long studies and involves political considerations. There is currently no indication that a new nuclear reactor could be built and become operational before 2015.
- (615) There is only one lignite power plant in Hungary, the Mátra power plant, and it is closely linked to the exploitation of Hungary's only lignite mine. While lignite may be an efficient fuel for new power plants, [...].
- (616) Coal production is marginal in Hungary and is decreasing. Coal has to be imported with high transportation costs. In addition, old coal power plants have the highest variable generation cost in Hungary and require substantial investment to meet the stringent Community environmental standards. As evidenced by the market investigation, the large majority of power plants expected to be decommissioned by 2015 are old coal-fired power plants.
- (617) While new coal power plants may have a higher efficiency, they still emit carbon dioxide and need expensive carbon dioxide emission permits. The only project to build a new coal-fired power plant is [...]*.
- (618) A strong increase in renewable (biomass, wind, solar, etc.) generation capacities in Hungary is projected due to the favourable feed-in tariffs set by the regulation. However, these new capacities are usually not competitive and subsidized by these high tariffs. They are not expected to account for a significant part of Hungary's generation capacity before 2015.

Power plants decommissioning

- (619) The market investigation carried out by the Commission has identified projected power plants decommissioning and capacity reductions. According to the investigation, around [0-500] MW of generation capacity should be decommissioned by 2010. As regards the 2010-2015 period, approximately 1,500 MW of additional generation capacity should be decommissioned. The vast majority of power plants that are expected to close or to reduce their capacity are coal-fired; some of the oldest gas-fired units are also expected to be shut down and/or replaced.

Power plant decommissioning:

Location	Company / Group	Fuel	Capacity (MW)	Schedule
[...]	[...]	Gas	[0-250]	[...]
[...]	[...]	Gas	[500-750]	[...]
[...]	[...]	Gas	[0-250]	[...]
[...]	[...]	Coal	[0-250]	[...]
[...]	[...]	Coal	[0-250]	[...]
[...]	[...]	Coal	[0-250]	[...]

[...]	[...]	Coal	[0-250]	[...]
[...]	[...]	Coal	[0-250]	[...]
[...]	[...]	Coal	[0-250]	[...]
[...]	[...]	Coal	[0-250]	[...]

Importance of gas-fired power plants

- (620) Gas-fired power plants account for 40% of the total generation capacity installed in Hungary but represent only 25% of the total electricity produced in Hungary²⁴². The large gas-fired power plants are supplied either by MOL WMT directly through the gas transmission network or by the RDCs through their gas distribution network. The total gas consumption of gas-fired power plants amounted to approximately [3-3.5] bcm in 2004.

Name of power plant	Owner	Official capacity in 2003 (MW)	Gas supplier	Gas consumption in 2004 (million m ³)
Dunamenti	Electrabel	2,126	MOL WMT	[1,000-1,500]
Tisza II	AES	860	MOL WMT	[0-500] ²⁴³
Csepeli GT	ATEL	389	MOL WMT	[0-500]
Kispest	EDF	116	FŐGÁZ	[500-1,000]
Újpest	EDF	110	FŐGÁZ	
Kelenföld GT II	EDF	136	FŐGÁZ	
Sajószöged	MVM	120	TIGÁZ	[0-500]
Lítér	MVM	120	KÖGÁZ	[0-500]
Debrecen	E.ON	95	TIGÁZ	[0-500]*
Others				[500-1,000]
TOTAL		4,072		[3,000-3,500]

- (621) According to the parties, a 500 MW gas-fired power plant (CCGT) with a 56% thermal efficiency factor has an annual electricity output of approximately 3.5 TWh and an annual gas consumption of approximately 600 million m³, **based on a 80%**

²⁴² It is MVM that decides which power plants should produce electricity based on the marginal costs of production of the respective plants. Gas-fired power plants have a higher marginal cost of production than the nuclear and lignite plants and are therefore used to satisfy peak demand.

²⁴³ Excluding [0-250]* million m³ of inert gas. (E.ON's reply dated 29 August 2005 to various request for information from the Commission).

load factor²⁴⁴. Accordingly, the gas consumption of new gas-fired power plants planned until 2010 could be in the range of [1-2] bcm, depending on their efficiency and their load factor.

- (622) As indicated by the market investigation, gas-fired power plants play a critical role in the functioning of electricity markets as they usually provide balancing energy and set electricity wholesale prices due their ranking in the national merit order. This is also the case in Hungary.
- (623) First, due to their technical characteristics and load profile, gas-fired power plants play an essential role in the provision of balancing electricity in Hungary (mainly the Electrabel, AES and ATEL power plants). This is because Hungary has practically no hydro-power capacity, all the system balancing must be provided either by gas-fired or coal-fired power plants.
- (624) Second, gas power plants are at [...] of the merit order ranking in Hungary, after the nuclear and [...]*. This means that they are used partially for base load and for peak load and supply the fluctuation of the total demand. In countries where an organized day-ahead market²⁴⁵ (or a pool structure) exists, an essential consequence is that gas power plants determine the electricity prices as they balance supply and demand. Any change in the costs of gas-fired power plants, such as an increase in the price of gas, therefore has an impact on the price of all electricity sold on the organized market.

b. The structure of electricity imports in Hungary

Current electricity imports

- (625) Imports are essentially made by electricity traders for transit or to supply medium and large customers in Hungary²⁴⁶. MVM, the public utility wholesaler, accounted for 35% of electricity imports in 2003, while E.ON was the second importer, ahead of other electricity traders, with [10-20]*% of imports. Under interconnection capacity allocation rules, it is not possible to know the country of origin of the electricity imported (only the cross-border entry point is known) nor whether market players import electricity for their own needs or for resale.

Evolution of electricity imports

- (626) A recent and in depth study on the evolution of Hungarian electricity imports has been carried out by MAVIR in 2005²⁴⁷. According to this study, Hungarian electricity imports are expected to decline over the next ten years compared to the

²⁴⁴ E.ON's submission dated 28 October 2005.

²⁴⁵ Such a market is expected to be introduced in 2007 in Hungary.

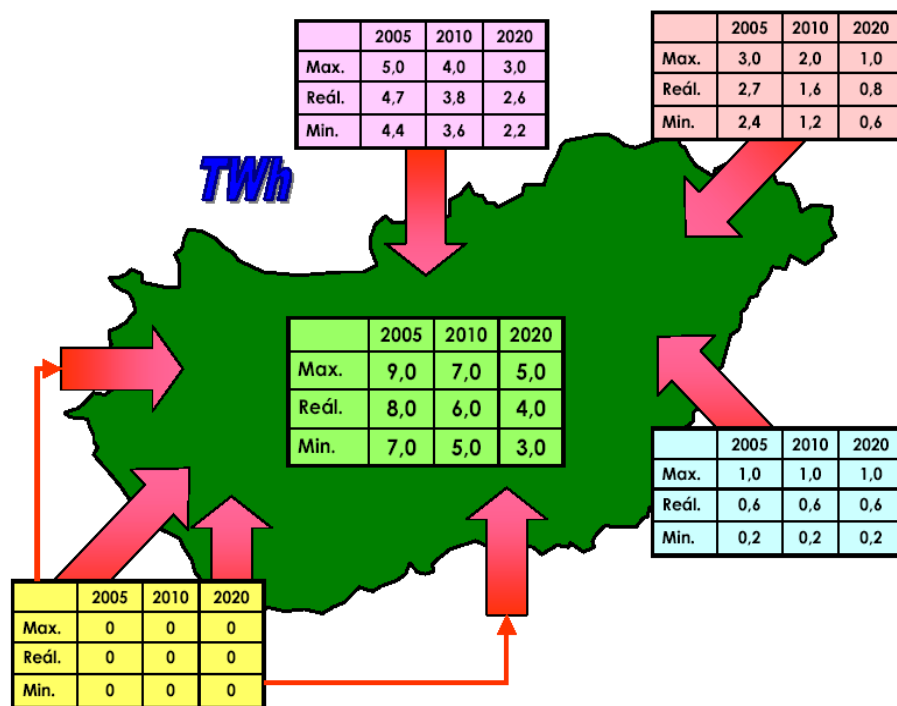
²⁴⁶ E.ON's reply to the Commission's request for information dated 18 July 2005. Electricity binder.

²⁴⁷ See:
[http://www.mavir.hu/domino/html/www/mavirwww.nsf/vAllPages/78D623653362C24FC1256FFF003D9E22/\\$FILE/korzeti_forraselemzes20050512.pdf](http://www.mavir.hu/domino/html/www/mavirwww.nsf/vAllPages/78D623653362C24FC1256FFF003D9E22/$FILE/korzeti_forraselemzes20050512.pdf)

current level, while the total electricity demand will continue to increase in Hungary. The share of electricity imports in the total electricity demand would therefore decline while the share of domestic production would increase.

- (627) The MAVIR study adopts a two-step approach; the countries which may export electricity to Hungary are first defined and then the evolution of electricity production is analyzed for each of these countries.
- (628) As a result of this study, MAVIR estimates that the current surplus in electricity generation capacities in countries that may export to Hungary will gradually decrease until 2010. As a consequence, Hungary's net electricity import balance will certainly decrease from 1200-1300 MW today to around 700-800 MW (daily peak). The chart below clearly shows that even in the best case scenario, Hungarian net electricity imports will decrease in 2010 and 2020.

Net electricity import flows and forecasts in 2005, 2010 and 2020 by country of origin:



c. The new entity will have the ability to foreclose access to gas to its competitors' gas-fired power plants

- (629) Prior to the merger, MOL WMT has a dominant position in the market for the supply of gas to large power plants. As a consequence, the Commission considers that post-merger, the new entity will have the ability to determine its competitors' power plants gas supply conditions (prices, rules for nomination, take-or-pay penalties, interruptibility, etc.) and to discriminate power generators in several ways.
- (630) Pre-transaction, as demonstrated above in section A, MOL WMT is dominant on the market for the supply of gas to large power plants, with a market share of almost 70%. Furthermore, large power plants connected to a distribution network may only be supplied by the RDCs on the regulated segment of the market (as MOL WMT can

only supply customers directly connected to the transmission network on the regulated segment of the market). RDCs are in turn obliged to procure gas for their public utility needs from MOL WMT. No trader is active on this market, as reflected in the table below:

Suppliers	Supply of gas to power plants in 2004	
	In million m ³	In %
KÖGÁZ	[0-500]*	[0-5%]
DDGÁZ	[0-500]*	[0-5%]
Total E.ON	[0-500]*	[0-5%]
MOL WMT	[2000-3000]*	[65-70%]
New entity	[2000-3000]*	[70-75%]
FÖGÁZ	[500-1000]	[10-20%]
ÉGÁZ	[0-500]	[0-10%]
DÉGÁZ	[0-500]	[0-10%]
TIGÁZ	[0-500]	[10-20%]
EMFESZ	[0-500]	[0-10%]
Total Market	[3000-4000]	100%

- (631) The market investigation has also confirmed the current and expected lack of alternative sources of supply for power plants. No other gas supplier (except the gas RDCs, which are dependent upon MOL WMT for their gas sourcing) is able to supply large power plants in view of their large consumption volume and of their requirements for high flexibility²⁴⁸ and security of supply.
- (632) The market investigation has shown that the new entity may discriminate against power plants: (i) by altering gas delivery conditions even without having to change the gas supply contracts, (ii) by increasing gas prices in July 2007 (iii) by altering gas delivery conditions in the context of a price renegotiation in 2007, (iv) by deteriorating gas supply conditions and prices at the expiry of the supply contracts and /or (v) by not offering more favourable gas supply conditions and prices on the open segment of the market.
- (633) As a direct supplier of gas-fired power plants supplied through the gas transmission network, MOL WMT has long-term gas supply agreements with those power plants. These contracts are generally long-term contracts (20 year duration for instance) that were established at the power plant construction. Therefore, the new entity is not able to unilaterally change the conditions of the contracts immediately after the merger.
- (634) As regards gas prices, at the moment, these supply contracts are public utility contracts subject to regulated prices, defined by governmental decrees. Therefore, the MOL WMT does not have the ability to increase prices under these contracts. However, as of July 1st 2007, it is expected that gas prices will be deregulated for all non residential customers. This means that the prices of public utility gas supply contracts will have to be renegotiated by the new entity and the power plants. Due to the lack of alternative supplier and the incipient stage of competition on the market for the supply of gas to power plants, the new entity will hence be able to increase gas supply prices to the power plants it will directly supply in 2007.

²⁴⁸ Because the operation of power plants depends on decisions by MVM, the single buyer, their gas consumption is extremely variable.

- (635) This risk of price increases has been highlighted by the market investigation. In particular, a third party has stated that:

“Although we have a long-term gas supply agreement with MOL WMT, the price is not defined in this contract, instead it contains a reference to the public utility prices set out in the applicable regulation. In 2007, when the market has to be fully opened, large customers will probably be forced on to the free market, and they will have to have a serious negotiation on prices with their gas supplier (the reference to public utility prices in the long-term gas supply agreement will not be relevant any more once the market is totally liberalized).”

- (636) Current prices paid by power plants for gas can also to some extent be renegotiated each year. As explained by a third party, gas prices do not always cover the entire gas quantities actually needed by power plants, leaving additional room for negotiation:

“Although the power plants have long-term contracts with MOL, their contracts only cover minimum quantities, and a new contract is signed each year to cover the needs of the coming year, in which the prices are renegotiated each time.”

- (637) As regards other supply conditions, no unilateral contractual changes are in principle possible before the contract expiry. However, following the merger, the new entity may have an influence over gas supply conditions in at least three ways.

- (638) First, the new entity could alter the gas supply conditions of power plants it directly supplies without any change in the contractual supply conditions. As explained in the gas section, the gas supplier may alter the power plants gas supply conditions in various ways. The vast majority of market players confirm the new entity’s ability to play with a broad range of supply conditions to discriminate power plants:

“E.ON can influence not only the pricing, but also the various conditions under which the plants take their gas in terms of minimum and maximum off take, balancing, nomination, cost of scheduling nominations (which is very important for “balancing” power plants)”

“E.ON/MOL can discriminate against its competitors not only through prices, but also by interrupting more competing power plants (even though the contracts with E.ON power plants and with competing power plants would formally provide for the same amount of firm and interruptible supplies), thereby forcing them to resort to alternative fuels and raising their costs. This behaviour cannot be regulated.”

“There are many possibilities for E.ON to discriminate between customers, not only as regards prices, but also as regards other important supply conditions such as gas nominations, penalties for breaching nominations, take-or-pay limits, interruption of gas supply, etc.”

“The gas supply to power plants can be influenced (legally and within the terms of the existing contracts) in such a way to support the energy market interests of E.ON and in a way that may damage the interests of non E.ON market players”.

- (639) As a concrete example (brought to the Commission’s attention by a power generator during the market investigation), in a scenario in which the new entity is contractually allowed to interrupt the gas supply to gas-fired power plants, the new

entity will have the possibility to arbitrarily decide to which power plant to interrupt supply, thereby increasing its cost of operation.

- (640) In their reply to the SO, the parties argue that “*possible interruptions of supply by MOL WMT to its customers would be contained and possibly penalized by the transmission operator*”.²⁴⁹ As evidenced by the market investigation, the Commission underlines that MOL WMT has the ability to foreclose gas-fired power plants in the various ways presented above in recitals 630 to 637, in particular as regards the interruptible gas supply to power plants.
- (641) It is worth noting that such behaviour (alteration of gas supply conditions) would not be costly for the new entity as it would not result in lower gas sales. As it would not be reflected in a contractual increase in gas prices, it would simply result in higher generation costs for these power generators and therefore lower margins as their electricity sales prices are fixed in the PPAs.
- (642) Second, the new entity could renegotiate part or all of the supply conditions in 2007 at the same time as the gas prices are renegotiated with power plants. The rules for setting the yearly, monthly and daily gas consumptions, their adjustment and the penalties for deviating for the fixed amounts also play an important role in a power plant’s gas supply contract and are relatively complex. The new entity would thus have the possibility to influence various parameters to reduce the competitiveness of its competitors’ gas-fired power plants: minimum and maximum yearly and monthly tolerance rate, maximum percentage of the yearly gas amount than can be nominated for one month, dates for providing gas nominations, penalties in case of over / under usage, rules for billing and payments, planning of maintenance operations, quantities of interruptible and uninterruptible gas, etc. The new entity could for instance impose higher penalties in case of non respect of the power plants’ daily gas nominations for instance or lower tolerance ranges for daily nominations
- (643) Finally, another way to discriminate power plants would be to offer more favourable gas supply contracts on the open segment of the market to certain gas-fired power plants. As large power plants are already eligible customers (although none of them has switched so far), they may change supplier and revert to the new entity as gas trader on the open segment of the market. Again, due to the absence of competition on the open segment of the gas market, power plants would not be able to switch to another market player on the open segment of the market.
- (644) The new entity’s ability to discriminate against the remaining power plants it does not supply directly with gas is more limited before 2007. While E.ON will not be in a position to modify the gas supply conditions to those power plants, it will still have the ability to discriminate amongst them by not offering them more favourable gas supply conditions and prices on the open segment of the market. As an example, E.ON may wish to offer more (or less) advantageous gas supply conditions to certain gas-fired power plants depending on their commercial relationships (or lack thereof) with E.ON electricity retail subsidiaries²⁵⁰.

²⁴⁹ Reply to the SO, Page 9.

²⁵⁰ E.ON’s incentives to engage in such input foreclosure / discrimination is discussed in sections d) and e) below.

d. E.ON plans to expand significantly its electricity generation capacities in Hungary

- (645) The essential change brought about by the transaction is that, contrary to MOL, E.ON has a strong presence in electricity retail in Hungary and has therefore a strategic interest in developing new electricity generation capacities.
- (646) The Commission's investigation has established that E.ON's strategy is to expand its electricity generation capacity with a view to balance its strong existing position in electricity retail. This point is essential as it constitutes the essential change brought about by the proposed transaction in the electricity sector and it modifies MOL WMT's set of incentives vis-à-vis existing and future gas-fired power plants.
- (647) As explained in recitals 150-151 and 599, due to the growth of domestic consumption and the closure of old power plants, a substantial part of the Hungarian electricity generation capacity will need to be renewed in the coming years. This large nation-wide need for additional generation capacity offers market players the opportunity to significantly increase their generation capacity in Hungary.
- (648) E.ON is strongly focused on the electricity markets at the European level and in particular in Central Europe.

*E.ON*²⁵¹: “[...]”.

*E.ON*²⁵²: “[...]”.

- (649) In Hungary, E.ON's currently generation capacity is limited but the company is the leading player at the wholesale and retail level. According to the market investigation, E.ON's current limited generation capacity in Hungary will develop significantly in the next years. Internal documents from E.ON [...] ²⁵³.

*E.ON*²⁵⁴: “[...]”.

- (650) The Commission's market investigation, based on data provided by MAVIR, the HEO and all major market players, has shown that E.ON was the only group planning to build large new power plants in Hungary in the next 5 years.
- (651) Based on the information available to the Commission, although E.ON's projects are at an early stage, the likelihood that the power plants will actually be built is very high. E.ON has already purchased two sites to build the new power plants ([...])^{*} and the projects have been extensively discussed within the group. Although new

²⁵¹ E.ON's reply to the Commission request for information dated 18 July 2005 – Binder Supplement I – Various presentations.

²⁵² E.ON's reply to the Commission request for information dated 18 July 2005 – Binder Supplement I – Various presentations.

²⁵³ E.ON's reply to the Commission's request for information dated 18 July 2005. Binder Supplement I. Presentation « E.ON Energie – Capital Market Day – Munich, September 6, 2004 ».

²⁵⁴ E.ON's reply to the Commission' request for information date 18 July 2005. Binder Electricity, Reply to Question 122, Document: « Greenfield power generation assets for the Hungarian market ».

power plant projects require a long time before commissioning, this will lead to an increase in E.ON's share of total and gas-fired power generation around [...]*

On the [...] project, E.ON²⁵⁵: “[...]”.

- (652) New power plants will play a decisive role on the Hungarian electricity markets as they are not obliged to sell the bulk of their electricity production to MVM under long-term PPAs. This means that the share E.ON will acquire in electricity generation capacity available for the wholesale supply of electricity to traders will be much more important than its share of the total national generation capacity.
- (653) Finally, due to its presence in neighbouring countries at the retail level, E.ON could seek to import competitive electricity into Hungary. Moreover, in view of its financial strength and its focus on Eastern European energy markets, E.ON is likely to further expand this position. Although the Commission acknowledges the apparent current lack of relationship between E.ON's owned companies in Eastern Europe, E.ON's position as a large vertically integrated company in the energy sector in several of Hungary's neighbouring countries provide the group with additional strengths in Hungary.
- (654) To conclude, through its new power plants and its role in electricity imports, E.ON will acquire a critical role on the open segment of the wholesale electricity market in Hungary, as it will own new and competitive gas-fired power plant available for the wholesale supply of electricity to traders (as opposed to other generators with capacity booked under the PPAs) and will be in a position to play a major role in electricity imports through its presence in neighbouring countries. In view of the combination of these strengths, even before the proposed transaction, E.ON is set to become a major player in the market for the wholesale supply of electricity to traders in Hungary.

e. The new entity will have the incentive to foreclose its competitors in electricity generation/wholesale

- (655) According to the Commission's assessment, the new entity is likely to engage in two types of foreclosure strategies to strengthen its position both in electricity generation / wholesale and retail supply in Hungary. The new entity has a substantial economic interest in carrying these foreclosure strategies against new or existing gas-fired power plants immediately after the transaction, either alternatively or simultaneously.
- (656) As regards new power plants, the new entity is likely to increase the total cost of gas to its competitors' new gas-fired power plants immediately after the transaction, with the aim to deter these rivals from building new gas-fired power plants and to favour its own new power plants projects²⁵⁶. This strategy would be attractive for E.ON's in view of its strong interest in expanding significantly its power generation capacity in Hungary.

²⁵⁵ E.ON's reply to the Commission request for information dated 18 July 2005. Binder Electricity, Reply to Question 122.

²⁵⁶ E.ON's focus and plans in new electricity generation capacities in Hungary is discussed in section d) above.

- (657) The new entity may also immediately after the transaction discriminate against new gas-fired power plants that do not supply its downstream electricity retail affiliates. This strategy would be economically rationale as it would provide the new entity a certain degree of control over the market for the wholesale supply of electricity to traders and additional competitive advantage on all electricity retail markets. The new entity's ability and incentive to carry out this strategy would increase with the progressive reduction of the scope of the PPAs.
- (658) The merger is therefore likely to limit the development of new electricity generation capacities in Hungary and to significantly impede effective competition on the market for the wholesale supply of electricity to traders. As explained below, the Commission stresses that this effect will materialize immediately after the transaction and will increase over time.
- (659) The following recitals will present the new entity's incentives to carry out these foreclosure strategies and discuss the likelihood and potential combination thereof in the current regulatory framework.

Foreclosure of access to gas

- (660) The new entity could first increase / threaten to increase the total cost of gas supply to its competitors' new gas-fired power plants through the various ways presented above in section c). The objective of such input foreclosure strategy would be to deter new gas-fired power plants projects from E.ON's competitors in Hungary.
- (661) In to favour its own plans to build new gas-fired power plants, E.ON would offer worse conditions of gas supply to its competitors planning to build new gas-fired power plants than to its own power plants. Considering the risk to be foreclosed for their gas supply, E.ON's competitors with plans to invest in new gas-fired power plants (accounting for the large majority of new power generation capacities), would most likely to abandon / delay their projects. This strategy would lead to a reduction / slow down of new generation capacity projects compared to the situation where E.ON's competitors would have also invested in new power plants and it would therefore strengthen E.ON's position as the major investor in new generation capacity in Hungary.
- (662) The new entity would not even need to actually carry out this strategy since the mere possibility that it will do so post-merger is sufficient to create a strong deterrence effect for E.ON's competitors.
- (663) In order to plan large investments, private companies evaluate the return / risk ratio and require a certain level of return on investment with limited risks. These requirements are all the more stringent (and difficult to evaluate) than the return on investment is planned to be achieved over a long period, as it is the case for power plants projects. The simple fact that E.ON will be at the same time the unique significant gas supplier and a major player on the electricity markets hence suffice to deteriorate the return / risk ratio (by increasing the risk level of the project) and as a consequence to limit non-E.ON investments in new power plants.
- (664) The cost of gas supply accounts for approximately 60-70% of gas-fired power plants operating costs and has therefore a major impact on their profitability. E.ON's

internal documents related to the heat and power plant in Nyíregyháza²⁵⁷ confirm that [...]*. E.ON estimates that the power plant modernization project has an Internal Return Rate (“IRR”) of [5-10]*%, which would decrease by [0-5]*% as a result of a hypothetical [5-15]*% increase in the price of gas. The sensitivity of a gas-fired power plant’s IRR on gas prices is obviously higher if the power plant does not produce heat.

(665) E.ON’s competitors planning to invest in new gas-fired power plants also evaluate the IRR of their projects, which may be largely influenced by E.ON’s gas supply policy. In view of these elements, the return / risk ratio of new gas-fired power plants projects is likely to fall below the threshold required by new electricity producers to invest in new generation capacity.

(666) All potentially affected competitors have expressed their serious concerns about the transaction. Some of them also compete with E.ON at the electricity retail supply level. The following are examples of concerns expressed by third parties:

“E.ON having privileged access to gas and capacities, it will obtain a competitive advantage over the other power generation companies. The merger may thus lead to discrimination of competitors on the Hungarian power market and may ultimately cause serious investment problems. (...) We strongly fear that the Parties will gain a considerable competitive advantage over our personal investment plans in electricity generation”.

“We are uncertain what gas prices E.ON will offer to its competitors and this is a potential risk for new power plants projects. As a consequence, the transaction creates significant uncertainties for non-E.ON market players and deters new gas-fired power plant projects.”

“As we don’t see any new interconnection project on the medium term, locally, there will be no investments in power plants because no private investor will take the risk to be downstream under E.ON gas monopoly which, in the same time, is its electricity competitor. In the medium run, it will increase electricity price.”

(667) Based on its knowledge of the energy sector and its contacts with market players in the electricity sector, the HEO’s assessment confirms these concerns²⁵⁸:

“It is possible that in the case of E.ON dominating the natural gas sector supply side, power plant investors under different ownership will abandon their plans to build natural gas fuelled power plants (...). If electricity generation investors withdraw from creating new capacity - as they have already indicated in advance - E.ON may appear as a dominant power plant investor”

(668) The HEO also reported to the Commission that *“Several investors are hesitating to build new gas-fired power plants.”*²⁵⁹

²⁵⁷ E.ON’s reply to the Commission’s request for information of 18 July 2005. Binder Supplement 2, Reply to Question 121. “Errichtung eines GuD-Heizwerk in Nyíregyháza (Ungarn)”, 16 June 2005.

²⁵⁸ “Answers to the questions raised by the GVH related to the Share Transfer Transaction between E.ON and MOL” - HEO

- (669) The deterring effect on new gas-fired power generation would have a significant impact on the development of new generation capacity in Hungary. It should be recalled that, according to the Commission's market investigation, approximately [1,000-1,500] MW of gas-fired generation capacity is expected to be added / renewed until 2010 by several market players, accounting for the very large majority of new power plants projects in Hungary. Based on the concerns expressed by several market participants and its own assessment, the Commission estimates that the proposed transaction significantly puts at risk those projects. Furthermore, as discussed above²⁶⁰, alternative fuels are less competitive than gas for new power plants to be built in Hungary and electricity producers would thus not be in a position to build non gas-fired power plants to counter the new entity's strategy to foreclose access to gas.
- (670) In their reply to the SO and the accompanying Expert Report, the parties however claim that the new entity has no incentive to impede the development of new gas-fired power plant and, on the contrary, has rather an interest in supporting their development to increase its gas sales²⁶¹.
- (671) The Commission acknowledges that the new entity, as a supplier of gas, has an obvious interest in increasing its gas sales over the long term. Deterring investments in new electricity generation capacities will therefore have a cost for the new entity if its results in less new gas-fired power plants in Hungary. The Commission however estimates that the new entity is likely to incur this cost in view of the substantial additional profit that this strategy would bring to the new entity in the electricity wholesale and retail markets, where it would strongly strengthen the new entity's market position. The new entity would also in any case revise and increase its own new power generation plans in order to partly replace the new power generation projects abandoned by its rivals.
- (672) Finally, the foreclosure strategy may be combined with a "tolling strategy", whereby the new entity would only partially limit the development of new generation capacity by its competitors but would supply gas under competitive conditions only to the power plants that supply its electricity retail subsidiaries. This approach would effectively limit the new entity's "lost gas sales" to future gas-fired power plants. It would also enable the new entity to increase its share in new power generation projects, to limit its competitors' gas-fired power plants market power and to ensure competitive electricity supply to the new entity's electricity retail subsidiaries.

Tolling agreements

- (673) During the market investigation, several market players expressed the concern that E.ON could provide competitive gas supply conditions only to the power plants that would sell electricity to E.ON's USPs and electricity traders ("friend" power plants):

²⁵⁹ Minutes of meeting with HEO on 26 July 2005.

²⁶⁰ See section a) on the Limited potential for non gas-fired power plants.

²⁶¹ Reply to the SO, Page 23

Enpol2000²⁶²: “The transaction will have an effect on the electricity markets even if E.ON has a small presence in generation since E.ON may connect its gas supply contracts with its electricity purchase contracts”

Other third parties have expressed similar concerns, as reflected in the following statements: *“One of the main threats of the merger is that E.ON will award advantageous gas contracts to its own power plants or to the power plants that are not related to a company with supply activities.”*

“Although E.ON does not have large electricity generation capacities itself, it could grant more favourable natural gas supply conditions to the power plants that supply E.ON and its subsidiaries with electricity and discriminate against the power plants supplying other traders than E.ON.”

“Following the merger, E.ON will have the opportunity to favour itself as trader on the electricity wholesale market and its RDCs on the electricity retail market. Secondly, E.ON/MOL may sell gas at better conditions to power generators on the conditions that they supply its RDCs at better prices (and thus would gain an advantage over its competitors).”

- (674) The Commission takes the view that the new entity will have an economic interest, (and is therefore likely to) adopt this discriminatory behaviour immediately after the transaction. This strategy could be implemented for new gas-fired plants in various ways: (i) tacit understanding between the new entity and the power generators, (ii) explicit link between gas supply and electricity purchase contracts and (iii) “tolling agreement”, where the conversion of gas into power is simply “outsourced” by the new entity.
- (675) The objectives of such gas foreclosure strategy vis-à-vis new power plants would be twofold: (i) to gain a significant control over the development of new generation capacity and (ii) to secure competitive electricity supply for the new entity’s electricity retail subsidiaries. The new entity would also seek to prevent the cost of lost gas sales to new gas-fired power plants as the reduction in total new generation capacity addition would be more limited than in the previous foreclosure scenario. Such strategy would in addition provide E.ON with more flexibility as regards the level of its own investment in new generation capacity and the investment risk will be shared to some extent with other electricity producers. E.ON could therefore decide which amount of new generation capacity it wants to build in Hungary and establish tolling arrangements for the additional increase in generation capacity.
- (676) The new entity will have the choice of various contractual arrangements to achieve this objective. The first solution would consist in maintaining the link between the gas supply and the electricity purchase conditions tacit and absent from the two supply contracts (which constitute anyway business secrets). In a second solution, the two supply contracts could be linked and the electricity supply contract could mention the price of gas set in the gas supply contract or other supply conditions thereof. Finally, in a third solution, the new entity could also present it as the outsourcing of the electricity generation process in its integrated activities along the

²⁶² Energiapolitika 2000’s reply dated 28 July 2005 on the Commission’s second phase questionnaire. Energiapolitika 2000 is a group of independent energy experts in Hungary.

gas and supply chain. The competitor's power plant would be supplied with gas and would sell electricity under conditions defined by the new entity against a fee based on the reserved capacity or the quantity produced. Given the wide array of potential contractual arrangements, the Commission estimates that the new entity would be in a position to select the most advantageous way and in particular the procedure the less likely to give rise to complaints or legal concerns.

- (677) The parties contest the new entity's ability to carry out these two foreclosure strategies. They first argue that competitors planning to build new gas-fired power plants would revert to alternative gas suppliers should they be confronted to such foreclosure strategies from the new entity. The Expert Report submitted by the parties also argues that Gazprom could sell gas directly to E.ON's competitors in power generation²⁶³.
- (678) The Commission refers to its assessment of the new entity's control over all gas resources available in Hungary and on its current dominant position on the market for the supply of gas to power plants, which clearly contradicts the parties' arguments. All major market players in electricity generation reported to the Commission their inability to find alternative gas suppliers to MOL WMT. It should be recalled that, as of December 2005, the only suppliers of gas to power plants are MOL WMT (market share in excess of 65%) and the gas RDCs, sourcing gas from the latter and that neither EMFESZ nor CENTREX (nor other traders) supply power plants in Hungary.
- (679) With respect to Gazprom, the Commission notes that Gazprom has never engaged in the direct supply of gas to power plants (nor in any other gas supply activities), in competition with its gas wholesale customers. Although Gazprom has already publicly stated its interest in being active in the Hungarian gas supply markets, it is not expected to enter the market on its own but through acquisition of stakes in existing businesses or assets.
- (680) The parties also claim that the manipulation of gas supplies would be easily identified by the regulator²⁶⁴ and that the new entity would therefore be deterred from carrying out this strategy. The Commission disagrees with the parties on this point as gas supply contracts with power plants constitute business secrets and are not available to third parties or to the HEO. Therefore, the Commission believes that it is actually very difficult for power generators to detect whether they are foreclosed for their gas supply or to complain to the HEO with a sufficient degree of confidence (see comments in the gas section). In view of the specificity of power plants' gas supply needs, it would anyway be difficult to establish that differences in gas supply prices between two power plants result directly from a discriminatory behaviour rather than from differing gas supply conditions. In addition, neither Directive 2003/55/EC nor the HGA explicitly prohibit discrimination in gas supply²⁶⁵.

²⁶³ Expert Report, Page 4.

²⁶⁴ Expert Report, Page 21/22

²⁶⁵ Such discrimination could be prohibited by the provision of the European Community Treaty on abuse of dominant position (Article 82).

Existing power plants

- (681) The Commission that the new entity may also carry out the above-described foreclosure strategies against existing gas-fired power plants immediately after the transaction, with a view to marginalize existing gas-fired power plants and eventually induce some power producers to exit the market.
- (682) The new entity may seek to marginalize existing gas-fired power plants to ultimately acquire the assets of exiting players. E.ON's interest in acquiring existing gas-fired power plant has been confirmed by the market investigation. For instance, a third party has stated that E.ON has started negotiations to acquire privately owned existing power plants:
- “In addition, E.ON may be able to overtake easily one of the private electricity generators (according to this third party there would be currently negotiations with Dunamenti, AES and ATEL; EDF is also currently negotiating the sale of its Budapest plant).”*
- (683) [...] discussed in E.ON's internal documents. In the presentation “New Energy for Central Europe”²⁶⁶, “[...]” are discussed, in particular “[...]”.
- (684) To conclude, the Commission considers that, post-merger, the new entity has strong incentives to increase the total cost of gas supply to its competitors' new and existing gas-fired power plants or to supply competitive gas to those power plants only under the condition that they supply E.ON's electricity retail subsidiaries with competitive electricity supplies. These strategies would result immediately after the transaction in deterring new entries in electricity generation and restricting competitors' gas-fired power plant's ability to obtain competitive gas supply.
- (685) For these reasons, the Commission considers that the merger will increase the new entity's market power and will already significantly impede effective competition on the market for the wholesale supply of electricity to traders under the current market conditions.

f. The new entity's incentives to foreclose its competitors in electricity generation/wholesale will increase with the further liberalization of the electricity sector and the increase in E.ON's generation capacity

- (686) The Commission believes that the new entity's incentives to foreclose its competitors' gas-fired power plants and to implement a “tolling strategy” will increase in the future regulatory framework due to the conjunction of three factors: (i) the increase in E.ON's generation capacity, (ii) the progress in the liberalization of the gas and electricity sectors and the (iii) progressive reduction in the scope of the long term PPAs in Hungary. These three factors imply that the total cost of the gas supply will become even more crucial for gas-fired power plants to compete on the market for the wholesale supply of electricity to traders.

²⁶⁶ E.ON's reply to the Commission's request for information dated 18 July 2005. Binder Supplement I – Presentation « E.ON Energie – Capital Market Day – Munich, September 6, 2004 ».

- (687) The increase in E.ON's generation capacity has already been discussed above in section d). It is expected to start in [...]*, except if E.ON speeds up its existing power plant projects or acquires existing power plants before that date.
- (688) The greater E.ON's share in gas-fired generation capacity in Hungary is, the greater are the group's incentives to foreclose its competitors' gas-fired power plants. An increase in the share of gas-fired generation capacity both increases the benefits resulting for higher electricity sales and decreases the cost of lost gas sales for the new entity.
- (689) The new step in the gas and electricity market liberalization in Hungary in July 2007 will also create additional opportunities and strengthen the new entity's ability and incentives to engage in foreclosure behaviours.
- (690) The end of regulated gas prices for power plants will allow the new entity to increase contractual gas prices to its competitors' gas-fired power plants (and possibly to deteriorate gas-fired power plants' gas supply conditions). At the same time, the end of electricity regulated prices for non residential end-users and the eligibility of residential customers should increase competition among electricity traders on all electricity markets and their interest in procuring electricity at the lowest price.
- (691) The potential renegotiation or even termination of the PPAs has also been discussed previously in this document. While the scope and the timing of these changes is still unclear, it may be assumed for the purpose of this assessment – as this is a very likely development - that their duration and the booked capacities may be progressively reduced. In any case, the proportion of generation capacity available for the wholesale supply of electricity to traders will necessarily increase as newly built power plants' capacities are generally not bound by long term PPAs.
- (692) In this regulatory framework, gas-fired power plants will compete on the market for the supply of electricity to traders and the total cost of the gas supply will be a crucial competitive factor. The market investigation has also indicated that competition is largely price-driven for electricity wholesale and that gas-fired power plants have similar technologies in Hungary, and thus similar cost structure.
- (693) Finally, the scope of the PPAs for the non gas-fired power plants, in particular the nuclear power plant, is less likely to be reduced , resulting in increased competition between gas-fired power plants on the market for the wholesale supply of electricity to traders. As indicated by the HEO, one of the essential objectives set by the Hungarian government for the New Electricity Model is to preserve the security of supply and the affordability of electricity supply for residential customers. In this respect, the government may decide to preserve cheap electricity generation resources for MVM for resale to USP and residential customers.
- (694) Moreover, in this future regulatory framework, a significant part of electricity wholesale will be achieved through bilateral transaction (“OTC”) between power plants (to the extent of their capacity available on the open segment of the market) and electricity traders. The news entity may therefore not only favour itself as an electricity trader but also replicate this mechanism with its competitors' gas-fired power plants and implement in a larger scale the “tolling strategy” described above. This concern has been expressed by several market players in the electricity sector:

“Such discrimination would be more accentuated once the “single buyer” framework ends after 2007 and once E.ON has built additional power generation capacities.”

“As soon as this system (“single buyer” scheme) disappears (according to the last draft of the Hungarian Electricity Act issued by the Hungarian regulator in June 2005), E.ON will be in a favourable position to provide cheap gas either to its own power plants (existing + [...]) project) or to contract with existing power plants with low gas price in order to buy cheap electricity for its own needs to supply their electricity RDCs.”*

- (695) This strategy would benefit E.ON to the detriment of its competitors in two ways as it would strengthen its position both at the power generation level and at the retail supply level. First, gas-fired power plants that would not benefit from advantageous gas supply conditions (“non friend” power plants) would become less competitive on the market for the wholesale supply of electricity to traders. These power plants would become marginalized thereby inducing them to eventually exit the power generation activity.
- (696) Secondly, USPs and electricity traders that would not have the ability to source electricity from gas-fired power plants supplied by the new entity under competitive conditions would have a significant competitive disadvantage vis-à-vis E.ON’s electricity retail subsidiaries and would have to rely on other less competitive gas-fired power plants and other electricity sources²⁶⁷.
- (697) To conclude, the Commission considers that E.ON’s ability and incentives to engage in the above-described foreclosure strategies will increase in the future liberalized regulatory framework. The significant impediment to competition on the market for the wholesale supply of electricity to traders will therefore become more severe in the long term, when the immediate “dampening effect” of the transaction on new generation capacities will materialize.

²⁶⁷ This strategy will not imply significant costs for E.ON as the electricity production lost by “non-friend” power plants being captured by E.ON’s or “friends” power plants.

(iii) *Electricity retail*

- (698) The impediment to the development of new power generation in Hungary and the impediment to competition on the market for the wholesale supply of electricity to traders would lead to price increases in electricity wholesale and retail and would limit E.ON's rivals ability to procure competitive electricity.
- (699) In addition, the Commission estimates that the proposed transaction will provide the new entity with the ability and incentive to prevent its competitors from developing dual offers²⁶⁸, which are expected to play a significant role in electricity retail markets. This would further contribute to increase E.ON's market power and would significantly impede effective competition on all electricity retail markets.
- (700) The following recitals will first present the structure of electricity retail in Hungary. The impact of the various foreclosure strategies at the level of electricity generation / wholesale on competition in the electricity retail markets and the new entity's ability and incentives to prevent its electricity retail competitors from developing dual offers will be analysed. The Commission's assessment has been carried out both in the current and in the future regulatory framework.

a. Market structure

- (701) Both RDCs (public utility segment) and traders (open segment) are active in the markets for the retail supply of electricity. As regards the various categories of customers, MLCs are supplied both by RDCs and traders; SCs are supplied essentially through RDCs and residential customers are only supplied through RDCs.
- (702) E.ON is active in the retail supply of electricity both in the public utility segment, through its three RDCs and in the open segment, through E.ON EK.

RDCs

- (703) The table below provides the sales of RDCs in each of the relevant product market for the retail supply of electricity²⁶⁹. While the figures reflect market shares for residential customers and SCs, sales of traders to MLCs are not taken into account and RDCs' actual market share are thus lower than those indicated in the table. It should be noted that E.ON's actual market share for the supply of electricity to MLCs should be approximately the same as the one estimated in the table below, in view of E.ON's strong position as electricity trader.

²⁶⁸ Dual offers combine the retail supply of gas and electricity in one « package » with clear advantages for customers such as « one stop shop » service (e.g. single billing).

Suppliers	Supply of electricity to residential customers in 2004		Supply of electricity to small commercial and industrial customers in 2004		Supply of electricity to medium and large commercial and industrial customers in 2004	
	In GWh	In %	In GWh	In %	In GWh	In %
ÉDÁSZ	[1000-2000]*	[15-20%]	[1000-2000]*	[15-20%]	[2000-3000]*	[20-25%]
DÉDÁSZ	[1000-2000]*	[10-15%]	[0-1000]*	[10-15%]	[0-1000]*	[5-10%]
TITÁSZ	[1000-2000]*	[10-15%]	[1000-2000]*	[15-20%]	[0-1000]*	[5-10%]
Total E.ON	[4000-5000]*	[45-50%]	[3000-4000]*	[50-55%]	[3000-4000]*	[30-40%]
ÉMÁSZ	[1000-2000]	[10-20%]	[0-1000]	[10-20%]	[1000-2000]	[10-20%]
ELMŰ	[3000-4000]	[20-30%]	[1000-2000]	[20-30%]	[3000-4000]	[30-40%]
DÉMÁSZ	[1000-2000]	[10-20%]	[0-1000]	[0-10%]	[1000-2000]	[10-20%]
Total Market	[10000-12500]	100%	[5000-7500]	100%	[7500-10000]	100%

Electricity traders

(704) Electricity customers that have switched to the open segment of the market are supplied by electricity traders. The main electricity traders active on the Hungarian market in 2003 and 2004 were:

Name	Group	2003 (GWh)	2004 (GWh)	% (2004)
Entrade	ATEL	[0-1000]	[1000-2000]	[10-20%]
ATEL Energia	ATEL	[0-1000]	[1000-2000]	[10-20%]
Total ATEL	ATEL	[1000-2000]	[3000-4000]	[20-30%]
MVM Partner	MVM	[1,000-2,000]	[2000-3000]	[20-30%]
E.ON EK	E.ON	[1000-2000]*	[2000-3000]*	[20-30%]
MÁSZ	RWE	[0-1000]	[1000-2000]	[0-10%]
System Consulting		[0-1000]	[0-1000]	[0-10%]
Sempre Energy Europe	Sempre Trading	[0-500]	[0-500]	[0-10%]
D-Energia	EDF	[0-500]	[0-500]	[0-10%]
Energy Financing Team	Energy Financing Team	[0-500]	[0-500]	[0-10%]
Others		[0-500]	[0-500]	[0-10%]
TOTAL		[5000-10000]	[10000-15000]	100%

(705) Electricity sales figures in the table above include both sales to traders and sales to final customers²⁷⁰. Total sales thus represent the total volume of electricity supplied by traders in Hungary and do not correspond to the total consumption of electricity end users that have switched to the open segment of the market.

(706) Based on the above, E.ON is clearly the leading player in the retail supply of electricity in Hungary and is the only group with strong positions both in the regulated and the open segments of those markets.

b. The new entity's strategies in electricity generation and wholesale would significantly impede effective competition in all the markets for the retail supply of electricity

(707) The deterring effect on new generation capacities and the impediment to competition brought about by the transaction on the market for the wholesale supply of electricity to traders would directly affect competition on all electricity retail markets. The proposed transaction would thus lead to higher prices on all electricity retail markets.

(708) In addition, the new entity's "tolling strategy" as regards competitors' gas-fired power plants would directly restrict E.ON's competitors' ability to compete effectively and increase E.ON's market power on all electricity retail markets.

(709) The Commission's projections on generation capacities available for the wholesale supply of electricity to traders indicate that E.ON could account for a substantial share of these capacities in 2010-2015. It should be stressed that these projections do not take into account the impact of the foreclosure strategies described above, which would deter new entries and favour E.ON's new power plants projects.

(710) The Commission estimates that the electricity generation capacities available on open segment of the wholesale market in 2010-2015 will reach approximately [4,000-5,000] MW. Gas-fired power plants will account for around [60-75%] of these capacities and E.ON for around 25%. The new entity's foreclosure strategies would therefore have an impact on at least 60% of total generation capacities available in Hungary for the wholesale supply of electricity to traders.

(711) In the reply to the SO, the parties argue that such strategies would be unsuccessful as "*electricity wholesalers and retailers have abundant alternative in buying electricity*"²⁷¹. They further identify the following four electricity sources: (i) nuclear power, (ii) coal-fired power plants, (iii) other gas-fired power plants and (iv) imports ("*for which sufficient interconnection capacity is available*"). The Expert Report also mentions²⁷² the "*ability of electricity retail competitors to obtain electricity supplies from non gas-fired power sources at competitive rates*".

(712) The Commission acknowledges the existence of alternative electricity sources in Hungary, in particular those listed by the parties. However, each of these sources is

²⁷⁰ There is no breakdown of electricity traders' sales according to the various categories of customers.

²⁷¹ Reply to the SO, Page 24.

²⁷² Expert Report, Page 26.

subject to major limitations, be it in terms of price-competitiveness, availability or flexibility. Procurement from non-gas-fired power plant may prove difficult as a large share of the cheapest power plants' capacity (nuclear and lignite) may not be available on the free market while coal power plants have much higher generation costs. This would be all the more difficult for peak-load electricity which in any event, cannot be procured from the nuclear and the lignite power plants.

- (713) The scope of the PPA is not expected be reduced for the nuclear power plant (and potentially the lignite power plant) and the electricity produced by this power plant is therefore not expected to be available on the open segment for the market. As indicated by the HEO, one of the essential objectives set by the Hungarian government for the New Electricity Model is to preserve the security of supply and the affordability of electricity supply for residential customers. In this respect, the government may decide to preserve cheap electricity generation resources for MVM for resale to USPs and residential customers. Other market players confirmed this view:

“The nuclear power plant will be operated as a national company at a regulated cost for the benefit of residential customers in Hungary.”

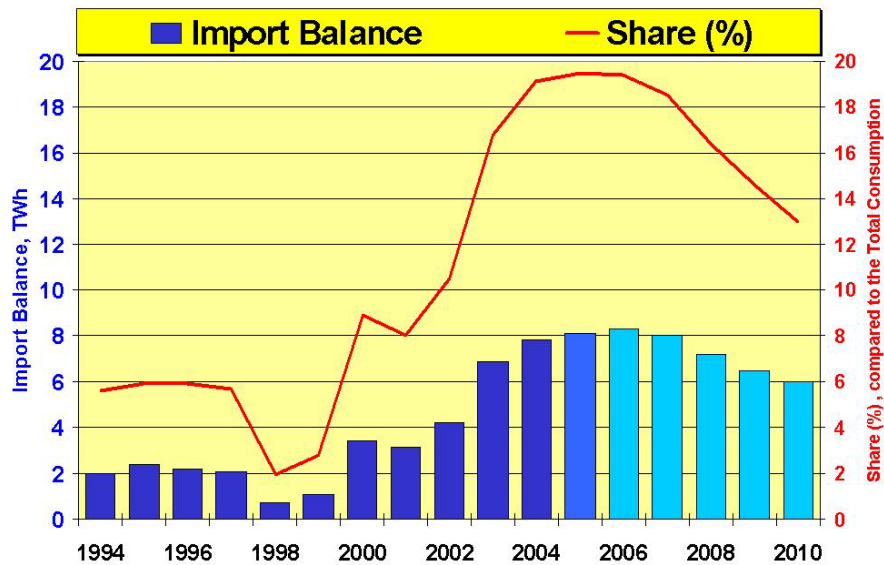
- (714) According to the market investigation, the nuclear power plant's electricity production may be reserved for the USPs, which will take over the public service functions of the RDCs. The USP could purchase this competitive electricity to the extent of the quantities they supply to small customers at low regulated tariffs. In 2004, the quantity of electricity produced by the Paksi nuclear power plant ([10-12.5] TWh) was approximately the same as the quantity of electricity consumed by Hungarian households ([10-12.5] TWh).
- (715) In addition, the nuclear power plant and the lignite power plant ([2,500-3,000] MW capacity together) are essentially used for base-load electricity in Hungary, while gas-fired power plants are both used for base-load and peak demand due to their ranking in the national merit order²⁷³. Electricity retailers are therefore not able to revert to those power plants to match the fluctuations of demand or to satisfy a peak in demand.
- (716) The Commission notes that the Expert Report submitted by the parties also excludes the nuclear power plants to calculate the non gas-fired power capacity in Hungary as²⁷⁴ *“it sells directly onto the public utility market”*.
- (717) As regards electricity imports, the market investigation has clearly shown that interconnectors with countries where electricity is competitive are already congested, which strongly limits the possibilities to increase electricity imports into Hungary. In addition, according to MAVIR projections, net Hungarian electricity imports are expected to decrease in the next five years due to lower availability of electricity generation capacities in neighbouring countries. Through its extensive

²⁷³ See section V.B.(i).e on Electricity generation in Hungary for a graphic representation of the Hungarian power plants' merit curve.

²⁷⁴ Expert Report, Page 26

presence in Hungary's neighbouring countries in electricity retail, in particular in Slovakia, E.ON would anyway play a significant role in electricity imports.

Expected evolution of Hungarian electricity net imports:



Source: MAVIR presentation, May 2005

(718) To conclude, the Commission considers that E.ON will have the ability and incentive to restrict its competitors' ability to obtain competitive electricity supplies and to distort competition on all electricity retail markets. For those reasons, the Commission considers that the merger would increase E.ON's market power on all the electricity retail supply markets in Hungary and would significantly in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation.

c. The new entity will have the ability and incentive to foreclose access to gas to its electricity retail competitors

(719) The Commission's market investigation has also revealed that access to gas resources is also crucial for electricity retail activities as dual offers are expected to play an important role in electricity retail markets. Following the transaction, the new entity will be in a position to foreclose access to gas to its electricity retail competitors with the objective to prevent them from developing dual offers²⁷⁵. The new entity will have an economic interest in denying access to competitive gas to its competitors in order to retain its current gas and electricity customers and to acquire new customers.

²⁷⁵ "Dual offers are a good opportunity, but at present there are no accessible gas resources for electricity traders to get into the gas trading business."

"Although [we] could also team up with gas resellers (RDCs for instance), [we] could certainly not obtain gas in very competitive conditions. This gas would anyway be sourced from E.ON"

(720) In their reply to the SO, the parties state that “*whether dual offers will become important in the Hungarian gas market is a matter of pure speculation*” and allege that “*third parties have not expressed any more clear views than to say that dual offers might be possible in the future*”²⁷⁶. These statements do not reflect the result of the market investigation and the assessment carried out by the Commission.

(721) First, most of the respondents to the market investigation in the present case (both electricity and gas suppliers and customers) reported to the Commission that dual offers will play a significant role on the Hungarian energy retail markets. Although some large industrial customers concurred with this statement in their reply to the Commission, most market players indicated that this type of offer would be more attractive for residential customers and small industrial and commercial customers (together “small customers”). These small customers do not devote a large part of their budget to gas and electricity and do not make much effort to compare the offers from various suppliers (in countries where they may do so). From their view point, having only one bill (this also valid for IT services providers for instance or banks and insurance, etc.) is quite convenient and “makes life easier”.

(722) The following are statements by third parties as regards the future importance of dual offers:

“The main advantages of a dual offer, from the client’s perspective, are its simplicity (one bill, one call centre, etc.), the benefits of a customized commercial approach, the access to a unique qualified interlocutor and through him to advices and energy services and the impression of saving money”

“The electricity-gas (multi-utility) offers may become widespread after the full market opening (while the efficiency gains in the supply of the residential customers may become possible).”

“Dual offers could be very competitive at the retail market, especially if the service provider caters for energy efficiency, optimization, scheduling issues as well.”

(723) Dual offers also represent significant advantages for gas and electricity suppliers. For incumbent operators, dual offers are a tool to limit customer switching by offering new services meeting customers’ expectations and enhancing customers’ commercial relationship. Dual offers also enable suppliers to enter into new energy markets and to benefit from economies of scale (purchasing, infrastructures, commercial network, etc.).

(724) Second, some respondents to the market investigation have pointed out examples of dual offers in other European countries, which have proved to be relatively successful. Dual offers have already been developed in the United Kingdom, in Spain and in Germany by energy suppliers and are currently advertised in France²⁷⁷.

²⁷⁶ Reply to the SO, Page 25.

²⁷⁷ See:

http://ecx.gazdefrance.fr/ecx/redirect.jsp?repertoire=/Espace_Entreprises/Offre_Elec/offre_elec_professionnel_s&caller_a_webc_url=temp_EEN/accueil_professionnel.htm

<http://www.edfpro.fr/61033i/Accueilfr/EDFPro/Offres/GammeProenergies/EssentielProenergies.html>

As an example, Centrica in the United Kingdom, a historical gas operator, entered the electricity market by introducing dual offers for all customers segments and has gained a significant share of the United Kingdom electricity retail market.

- (725) The various acquisitions involving companies active both at the gas and electricity retail level show that there is a convergence of the gas and electricity retail markets in Europe. This trend is even [...] strategy by [...]*:

*E.ON*²⁷⁸: “[...]”

- (726) Third, according to a survey conducted by a market player among its residential customers in Hungary, [50-100%] of the clients would be interested in dual fuel offers and they would expect such offers from their local energy supplier. The Commission notes that this result indicate without any doubt that dual offers are likely to play an important (if not essential) role, in Hungary’s gas and electricity retail markets.
- (727) In view of its dominance on the markets for the supply of gas to RDCs and to traders and the interest of small customers in dual offers, the Commission believes that the merged entity will have the ability and the incentive to foreclose access to gas resources for its downstream competitors in the markets for the retail supply of electricity to SCs and residential customers, thereby increasing its market power on these markets. As a result, effective competition would be significantly impeded in a substantial part of the common market within the meaning of Article 2 of the Merger Regulation.
- (728) Although the parties have not raised any specific argument with respect to the impact of the regulatory situation on the competitive assessment²⁷⁹, the Commission has carefully considered whether the fact that residential customers will only become eligible in July 2007, and thus the market for the supply of electricity to residential customers is not open on the date of the decision, could, by itself, dispel the concern that the merger will significantly impede effective competition within the meaning of Article 2(3) of the Merger Regulation. For the same reasons as those developed as regards the market for the supply of gas to residential customers, the Commission has concluded that the transaction is likely to have immediate effects on the market for the retail supply of electricity to residential customers by restricting the ability of potential suppliers to compete with the new entity on neighbouring markets and thus further discouraging potential entries.

Conclusion on the impact of the proposed transaction in the electricity sector

- (729) In view of the merged entity’s near monopoly in the access to competitive gas resources and its strategic focus on building new power generation capacities, the merged entity will have, already in the current regulatory scenario and at the current stage of market liberalisation, the ability and the incentive to foreclose access to gas to its competitors’ new gas-fired power plants and /or to discriminate in its supply to

²⁷⁸ E.ON’s reply to the Commission’s request for information dated 18 July 2005. Binder Supplement I. Presentation « E.ON Energie – Capital Market Day – Munich September 6, 2004 ».

²⁷⁹ It is not argued, in particular, that the Commission is not entitled to assess the effects of the merger on that market, due to be opened to competition shortly.

competitors' new gas-fired power plants, thereby deterring competition from any of its rivals as regards the foreseen replacement and expansion of generation capacity in Hungary.

- (730) E.ON's strategy would lead to a slower and less competitive development of new generation capacity in Hungary starting immediately after the transaction (compared to a situation where several market players would have built new power plants) and ultimately lead to higher electricity wholesale prices. It would thus impede effective competition on the market for the wholesale supply of electricity to traders.
- (731) In the future liberalized regulatory framework characterized by a larger share of power generation capacities available on the open segment of the market (new power plants and potential renegotiation of the existing PPAs) and by E.ON's larger share in power generation (resulting from E.ON's current capacity extension projects and the foreclosure strategy described above), the above described foreclosure strategies will be all the more effective and therefore damaging. They would reduce E.ON's competitors' gas-fired power plants' ability to compete and limit the scope for the development of a competitive open segment of the electricity wholesale market.
- (732) This would have a direct impact on competition in all the markets for the retail supply of electricity, due to the restriction in new generation capacity and higher wholesale prices. As a result of the strategy to link the gas supply and electricity purchase of gas-fired power plants, the new entity would reduce its electricity retail competitors' ability to source competitive electricity and would increase its already strong market power in electricity retail, thereby significantly impeding competition on all electricity retail markets.
- (733) Finally, immediately after the transaction, E.ON will have the ability and incentive to prevent any other company active in electricity retail from developing dual offers (gas and electricity) by foreclosing access to gas resources to those competitors willing to pursue this marketing strategy, thereby significantly impeding competition on the markets for the supply of electricity to SCs and residential customers.

VII. ASSESSMENT OF THE REMEDIES PROPOSED BY THE PARTIES

(734) In order to remove the competition concerns described above in section VI on the gas and electricity markets, on 20 October 2005 E.ON submitted a package of commitments. On 15 November 2005, following the market test, E.ON submitted revised commitments. E.ON submitted final commitments on 8 December 2005. The commitments are set out in the Annex. The recitals below describe the main features of the commitments, as submitted by the parties and modified/improved following the results and the suggestions of the market test.

A. Description of the remedies

(i) Ownership unbundling

(735) Under the agreements concluded between MOL and E.ON, MOL would remain a minority shareholder in MOL WMT and MOL Storage (25% + 1 share in each) and enjoy a 5-year put option under which it can require E.ON to purchase these minority interests.

(736) Pursuant to the undertakings, MOL will divest its remaining shareholdings of 25% + 1 share in MOL Storage and MOL WMT within six months following the transaction. The buyer of the shares will be subject to the Commission's approval. In addition, MOL will not acquire direct or indirect minority stakes in MOL WMT and MOL Storage for a period of 10 years as long as E.ON is a majority shareholder of those companies.

(737) The objective of the ownership unbundling remedy is to alleviate the competition concerns raised by the Commission as regards MOL's incentives (in particular through its subsidiary MOL Transmission and its branch MOL E&P) to favour MOL WMT (for access to the transmission network) and MOL Storage (for access to future storage sites).

(ii) Put option related to MOL Transmission

(738) Under the agreements concluded between MOL and E.ON, MOL would be granted a 2-year put option under which it can require E.ON to purchase a 25% + 1 share or a 75% - 1 share interest in MOL Transmission.

(739) Pursuant to the undertakings, MOL will not exercise the put option for the 25% + 1 share interest in MOL Transmission. In addition, MOL will not sell to E.ON or any of its affiliates, for a period of 10 years as long as E.ON is a majority shareholder of MOL WMT and MOL Storage, a share interest in MOL Transmission that would not result in the acquisition of sole control over MOL Transmission by E.ON or of joint control over MOL Transmission by E.ON and MOL.

(740) The objective of the undertaking related to the put option for MOL Transmission is to ensure that any acquisition of a share interest in MOL Transmission by E.ON will be subject to merger control review by the relevant competition authority.

(iii) Gas Release Programme

(741) E.ON undertakes to implement a gas release programme in Hungary by way of business-to-business internet auctions. The programme will start in 2006 and have a duration of 8 years. Auctions will be held in 2006, 2007, 2008, 2009, 2010, 2011, 2012 and 2013. The necessity of continuing the programme for the last three years can be reassessed upon request by the parties at the end of 2010. 1 billion m³ of gas will be released at each annual auction. The annual quantities to be released will be divided in 5 lots of 100 million m³, 5 lots of 50 million m³ and 10 lots of 25 million m³ each. E.ON's affiliates will be excluded from participating, directly or indirectly, in the auctions.

(742) The successful bidders will enter into gas supply contracts with E.ON under the following terms and conditions. The contracted gas will be equally split over two years and delivered at the two Hungarian entry points (80% at the Eastern entry point and 20% at the Western entry point). The gas supply contracts will provide for the same flexibility as MOL WMT's upstream gas supply contracts, namely an annual flexibility of 85% to the effect that the purchaser will have to purchase and pay only 85% of the annually contracted gas quantity ("TOP obligation"). In addition, the daily and quarterly flexibility shall not be lower than the weighted average daily and quarterly flexibility of all purchase contracts of MOL WMT. In any event, the daily flexibility shall be at least 50% of the daily contracted quantity.

(743) The auctions will be carried out by an international IT service provider, and the auction procedure will be handled so as to ensure that MOL WMT does not gain knowledge of the intermediary bids placed by participants to the auction.

(744) The starting price for each annual auction will be 95% of the weighted average cost of gas of MOL WMT ("WACOG"). The calculation of the WACOG will be verified by the HEO. Quantities that are not sold in a given auction shall be reoffered with one third of the quantities each in the following three auctions, but no auction for unsold quantities will take place after 2014.

(745) The Hungarian Energy Office (HEO) and a Monitoring Trustee will supervise the auctions and the implementation of the gas release programme. In particular, the HEO will comment on and review E.ON's proposal for the technical implementation of the auction and the details of the supply contracts with the successful bidders, before it is submitted to the Commission for its approval.

(746) In addition, E.ON undertakes to grant the existing direct customers of MOL WMT and E.ON (KÖGÁZ and DDGÁZ) who participate in the auction or who purchase gas from a trader/wholesaler participating in the auction the right to reduce their obligation to purchase natural gas from MOL WMT and E.ON by the amount of gas that they will purchase directly or indirectly from the gas release programme. E.ON also undertakes to grant to those purchasers access to storage at regulated prices and conditions (See Storage undertaking).

(747) E.ON undertakes to modify and/or improve the implementing regime on the basis of the experience gained from the yearly auctions with a view to improving the effectiveness of the gas release programme.

(748) The objective of the gas release programme is to ensure sufficient competitive alternatives for access to gas on the Hungarian gas and electricity markets (independently of the parties and at competitive conditions) so as to prevent the new entity from foreclosing the access to gas resources for its downstream competitors in the gas and electricity markets.

(iv) Contract release

(749) ERI undertakes to assign to a third party (the “Third Party”) half of the contract between MOL WMT and MOL E&P for the supply of domestic gas (“Supply Contract”) within 6 months. Once the contract assignment becomes effective, the Third Party will take over all the rights and obligations of MOL WMT under the Supply Agreement for the part assigned to it. The assignment will become effective at the beginning of the gas year 2007 (July 2007) and will be valid for the whole duration of the Supply Contract, until 2016.

(750) According to the parties, the part of the Supply Contract to be assigned represents approximately 7.6-10 bcm of gas in total, with the volumes to be released in the first year amounting to 1.2 bcm.

(751) ERI will procure MOL to approve the partial transfer of the Supply Agreement. In addition, MOL will grant equal treatment to MOL WMT and the Third Party as regards the Supply Contract flexibility provisions.

(752) The assignment to the Third Party of half of the contract will be subject to the HEO’s and the Commission’s approval. The Third Party must not be the purchaser of MOL’s minority interests in MOL WMT and MOL Storage.

(753) In case E.ON (and subsequently the Divestiture Trustee) does not succeed in finding a Third Party for the partial assignment of the Supply Contract for the start of the gas year 2007 (or for a subsequent year), the gas quantities that would have been released in that given gas year will be added to the gas release programme for that year. In this case, E.ON (and the Divestiture Trustee) shall seek again to find a third party interested in the partial contract transfer until 50% of the Supply Contract has been effectively assigned.

(754) As for the gas release programme, the objective of the contract release programme is to ensure sufficient availability of gas on the Hungarian gas and electricity markets (independently of the parties and at competitive conditions) so as to prevent the new entity from foreclosing the access to gas resources for its competitors in the gas and electricity markets.

(v) Access to storage

(755) E.ON undertakes to grant access to storage capacities at regulated price and conditions to end users and wholesalers that purchase gas directly through the gas release programme or the contract release. In particular, E.ON undertakes to offer access to

sufficient storage capacities for those end users and wholesalers even if they purchase gas for the first time or develop an increased demand for storage when buying gas quantities through the gas release programme or the contract release.

- (756) E.ON undertakes to report any issue related to storage capacity constraints to the HEO. In any event, in accordance with the HEO resolution, E.ON is under an obligation to implement a storage development plan.
- (757) The objective of the access to storage capacities at regulated price and conditions is to ensure that successful bidders in the gas release programme and the Third Party assignee of the contract release will be able to structure the purchased gas quantities according to their own or their customers' needs.

B. Assessment of the concentration as modified by the remedies

- (758) In the framework of the market test on the proposed undertakings, the Commission contacted approximately 100 third parties, including gas and electricity operators (both Hungarian and international companies) and participants in other gas release programmes (notably in Germany). Moreover, the Commission contacted a number of national energy regulators in Member States with a view to benefiting from their expertise and knowledge of similar programmes.
- (759) Many respondents put forward concrete and substantial suggestions for amendments to the package proposed by the parties with a view to improving the overall package and making the commitments more effective. The most substantial suggestions related to the gas release programme and in particular to its overall duration, to the volumes of gas to be auctioned, to the minimum price of the auctions and to the flexibility rules as to the delivery of gas to the successful bidders.
- (760) The final package of undertakings, submitted on 8 December 2005 and described in Section A above, incorporates the bulk of the suggestions and comments made by third parties in the context of the market test. The undertakings in their final form, substantially improved compared to the parties' initial offer, thus meet the concerns expressed by third parties as regards the need to ensure sufficient liquidity of gas on the Hungarian wholesale gas market at price and conditions which will allow third parties to compete effectively with the new entity on the downstream Hungarian gas and electricity markets.
- (761) As described, the undertakings proposed by the parties aim essentially at (i) strengthening the positive unbundling of MOL E&P (gas production) and MOL Transmission (gas transmission) on the one hand and MOL WMT (gas wholesale) and MOL Storage (gas storage) on the other hand and at (ii) releasing volumes of gas on the Hungarian wholesale markets through a gas release and a contract release.

(i) Unbundling

- (762) The Commission has found that the 25% + 1 minority shareholdings which MOL would retain in MOL WMT and MOL Storage and the existence of the "put option" for the shareholdings of MOL Transmission to E.ON (even though the sale of MOL Transmission is not part of the present transaction), would create structural links between ERI and MOL which would provide the ability and the incentive for MOL

to discriminate against the parties' competitors for access to domestic gas, gas transmission services and new gas storage facilities.

- (763) The Commission is of the opinion that the divestment by MOL of its 25% + 1 interest in MOL Storage and MOL WMT within 6 months after the transaction remedies the concerns stemming from the structural links between MOL and E.ON. The market test has, to a very large extent, welcomed the severing of the structural link between the parties.
- (764) In particular, the sale of MOL's minority share in MOL Storage and MOL WMT would eliminate the incentive for MOL E&P to engage in discriminatory behaviour vis-à-vis potential future gas storage operators as regards the sale of depleted gas fields and the incentive of MOL Transmission to engage in discriminatory behaviour vis-à-vis traders and rival RDCs with a view to increase MOL WMT profits²⁸⁰.
- (765) Moreover, the Commission is also of the opinion that the fact that MOL will not exercise the put option vis-à-vis E.ON for the 25% of MOL Transmission (and not to sell E.ON a shareholding that would not result in the acquisition of joint control over MOL Transmission by E.ON and MOL or of sole control by E.ON) can contribute to alleviate the concerns that may stem from E.ON's becoming further integrated also in the gas transmission market. What is essential for the assessment is that the exercise of the put option by MOL for the 75% stake (or the sale of another shareholding) would result in a change of control of MOL Transmission and would be subject to the review and require the approval of the competent competition authorities (the Commission or the Hungarian Competition Authority).
- (766) By contrast, the exercise of the 25 % put option would not bring about a change in control of MOL Transmission, hence it would not be subject to any approval procedure, in spite of its creating a structural link between E.ON and MOL Transmission. The remedy at stake seeks precisely to avoid this situation, and, should the put option be exercised, will provide the competent competition authorities²⁸¹ with the opportunity to review the new transaction in the framework of the market situations prevailing at the time of the exercise of the put option.
- (767) A large number of respondents to the market test, while highlighting their concerns as regards the possibility that the new entity may also acquire control of the transmission network, have confirmed that the commitment at stake contributes to alleviate the concerns that may arise from such transaction, should the put option be exercised.

(ii) *Gas release programme and contract release*

a. European experience on gas release programmes

- (768) To be in a position to assess properly whether the gas release and the contract release commitments submitted by the parties are suitable to remove the competition concerns identified during the procedure, the Commission has carried out an

²⁸⁰ See section on the Impact of the transaction on the gas sector.

²⁸¹ The Commission or the Hungarian Competition Authority.

additional investigation focusing on existing similar programmes in various European countries.

(769) The main results of this investigation are set out here below.

General features

- (770) Gas release programmes and contract release programmes aim at making gas available to wholesalers and end users at the wholesale level. In this type of programmes, the gas incumbent company undertakes to offer certain quantities of gas for sale to its competitors/customers. The undertakings proposed by the parties in the present case comprise both a gas release and a contract release.
- (771) In a gas release programme, the gas incumbent offers for sale certain quantities of gas from its overall gas sourcing portfolio. Purchasers enter into supply contracts with the gas incumbent for these quantities. In a contract release programme, the gas incumbent transfers (assigns) part of its gas supply contracts with gas producers. Purchasers enter into a supply contract directly with the gas producers (without the intermediary of the incumbent) and the transferred gas supply contract(s) of the incumbent is terminated, or the gas quantities in the transferred supply contracts are reduced accordingly. Both types of programmes are designed to improve the liquidity of gas markets and enable competing traders and customers to acquire gas for their own use or for resale. The essential difference between contract and gas release is that the incumbent's supply portfolio remains the same in a volume release programme, while it is partly transferred to competitors/customers in a contract release programme.
- (772) The sale of the gas or the transfer of the gas supply contract may be achieved in two ways: (i) auctions, or (ii) bilateral contracts. The gas quantities may be sold through public auctions where companies with the highest bid are selected. In case of bilateral negotiations, the incumbent negotiates with interested companies and gas sales/contract transfers are concluded based on mutual agreement. The undertakings proposed by the parties in the present case comprise both a gas release through auctions and a contract release through bilateral negotiations.

Specific features

- (773) Gas release programmes have been and are being implemented in several European countries; experience is more limited for contract release programmes. Gas release programmes are either part of a broader action plan required under national law and/or designed by the national energy regulators to open the gas wholesale markets to competition (UK, Spain, Italy) or are implemented as undertakings in merger or antitrust procedures (France, Germany, Austria).
- (774) In order to assess whether the remedies proposed by the parties are suitable to remove the competition concerns identified, the Commission has contacted the energy regulators in each of the countries where a gas release programme has been implemented with a view to understanding whether the programme has actually fulfilled its objectives and to establishing which elements are crucial for a gas release programme to be effective. The recitals below describe the most important features for successful gas release programmes according to the Commission's assessment and based on the experience of the energy regulators.

- (775) The Commission has also drawn useful guidance and suggestions from the paper “Implementation of Gas Release Programmes for European Gas Market Development” published by the European Federation of Energy Traders²⁸² (EFET) to which the parties have widely referred.

Volumes

- (776) The quantities of gas to be released depend on the objectives of the gas release programme and of the regulatory framework. More specifically, in a merger case, the volumes should be sufficient to remove the competition concerns and thus depend on the number and the size of markets in which competition concerns arise. The released volumes need to be sufficient to exclude that the incumbent supplier can foresee that all or most of the released volumes will be acquired by certain customer categories. Only if the volumes released are sufficient to allow eligible customers in all affected markets to benefit from the programme (as direct purchasers or indirectly as customers of traders buying gas through the gas release programme) can a gas release programme offset the incumbent’s ability and incentives to engage in anticompetitive behaviour and thus remove the negative impact on competition.
- (777) A gas release programme should in addition foresee that gas quantities that were offered for sale but did not find a buyer a given year should be added to the quantities to be released the following years.

Duration of the programme

- (778) A gas release programme generally aims at increasing the liquidity on gas wholesale markets and facilitating new entries. In the context of a merger case, a gas release programme may seek to reduce or eliminate the merging parties’ ability and incentives to engage in behaviour that would significantly impede effective competition. To achieve these objectives, the gas release programme should remain in place for a sufficiently long time as to ensure that the market structure and the competitive conditions have changed significantly, and that the level of competition achieved through the programme is sustainable.

Price and costs

- (779) The price at which gas is available through the gas release programme should enable wholesalers to compete with the supplier of gas under the gas release on the gas wholesale and retail markets. The auction mechanism is a convenient way to allocate efficiently the gas quantities to be released. As the final price results from competitive bids, it is the price that bidders are willing to pay for the gas made available under the programme, given prevailing market conditions.

EFET: “The release programme will only be successful if the price of the gas or capacity made available to new entrants is low enough for the competition to compete. As a guide, the price must not be higher than the average price paid by the incumbent (including contractual discounts), nor must it be higher than the average netback from the incumbent’s eligible customers. If a release programme is also

²⁸² <http://www.efet.org>

used as a remedy to balance the incumbents' market power, the price must not be higher than that offered in the wholesale market, even if this implies a financial loss to the incumbent."

- (780) The WACOG is recognised in the EFET paper as one of the benchmarks for the definition of price mechanisms in auctions for gas release programmes.
- (781) As regards additional costs, all costs incurred by participants to the auctions and by successful bidders should be clearly defined. As a principle, the additional costs should be avoided unless there are specific reasons.

Gas supply duration and lot size

- (782) The duration of the gas supply contract and the size of the lots in a gas release programme should be designed so as to meet the needs of the various categories of bidders in the relevant markets.

Flexibility

- (783) The daily, quarterly and yearly flexibility provisions for the gas supplied through the gas release programme are essential. Wholesalers and industrial customers should have the ability to structure the gas quantities they purchase according to their own or their customers' consumption profiles. Depending on the conditions of access to storage, the requirements for the flexibility of the gas supplied through a gas release programme differ.
- (784) The annual flexibility (swing and TOP levels) should reflect the incumbent's average annual flexibility. As quarterly flexibility needs may be provided by the storage of gas, the flexibility provided by the seller in the gas release programme depends on access to storage.

EFET: "The swing and take-or-pay levels of the release gas programme should reflect the overall portfolio of the incumbent. If only flat gas is available, and access to storage or other flexibility tools is still difficult or at punitive prices, then competition in supply will not arise from the release programme."

- (785) Finally as regards daily flexibility, it is clear that wholesalers, especially small ones, and end users have higher flexibility requirements than large importers (such as the seller generally). Therefore, it is clear that a base-load gas supply or even a daily flexibility similar to the seller's gas portfolio's average daily flexibility may be insufficient.

German Ministry: "In our decision, only a base load supply was foreseen. Such a product has no flexibility and is not attractive for potential purchasers. Ruhrgas has voluntarily offered a certain degree of flexibility (...). For potential purchasers minimum gas deliveries in summer are an issue."

- (786) Experiences in European countries, particularly in Germany, show that the attractiveness of a gas release programme for small wholesalers and industrial customers strongly depends on the flexibility provisions of the gas supply.

Gas delivery points

- (787) The gas should be delivered at a delivery point from which wholesalers can easily transport and store the gas. A gas hub or cross-border entry points are therefore generally appropriate delivery points. A certain degree of flexibility for the choice of the delivery point (as is often the case for the seller) increases the attractiveness of the programme.
- (788) The delivery point location is in particular relevant when gas transmission network are split among various owners, when the level of free capacity is low in the transmission or storage system and when entry-exit tariffs (and not post stamp tariffs) are applicable. Availability of gas at more than one delivery point reduces the risk that the transmission regime constrains competition in any market area and ensures that purchasers face the same physical and operational risks as the seller.

EFET: "Gas should be made available at more than one entry point, in principle using the same entry points as where the incumbent brings in most of its gas. This reduces the possibility that the transportation regime constrains competition in any specific area or market segment. It also ensures that new entrants face the same physical and operational risks as the incumbent by sharing the same entry points. In deciding delivery locations, consideration must also be given to the ease and cost to participants of onward transportation and/or trading."

- (789) In a merger case, the delivery point of a gas release programme should be selected so as to enable wholesalers and end users to source gas from the gas release programme for resale or for their own use in the geographical market where competition concerns have been identified.

Security of supply

- (790) The gas supply conditions should include standard provisions on security of supply issues (maintenance, force majeure, off-spec, interruptibility, etc.) following the common practices in the relevant markets. The rights and obligations of the purchasers and the seller should be balanced.

Auction design and guarantees

- (791) The "ascending clock auction" has been used in several countries and is apparently an appropriate procedure to allocate the gas quantities. The organization of the auction should also ensure that the seller does not gain information on its competitors.
- (792) The amount of the deposits and guarantees should not be disproportionate and should not constitute a disincentive for potential bidders. Payment terms should reflect standard market practices and in particular those of the seller's upstream supply contracts.

EFET: "Credit terms must not unduly restrict participation of new entrants, especially smaller companies".

Access to transmission

- (793) Access to sufficient gas transmission capacities is necessary to ensure that wholesalers and end users purchasing gas through the gas release programme can transport gas to the place where the programme is intended to solve competition concerns. Thus, access to transmission capacities is essential and a gas release programme is not expected to be successful if little free capacity is available in the gas transmission network. If transmission capacity is booked by the company that organizes the gas release programme, it should be released to the transmission system operator to the extent of the gas quantities released.

EFET: “For gas release to be effective there needs to be properly implemented, regulated third party access downstream of the delivery point”.

- (794) Responses from market operators indicate that difficulties to obtain sufficient capacity to transport the acquired gas were one of the main issues explaining the lack of success of the first auctions in the German gas release programme of E.ON/Ruhrgas.

Access to storage

- (795) If the flexibility conditions foreseen in the gas release programme are not sufficient to meet the flexibility needs of wholesalers and end user, access to sufficient gas storage capacities is necessary to ensure that wholesalers and end users purchasing gas through the gas release programme can structure the acquired gas according to their own or their customers’ needs. Thus, access to storage capacities is essential and a gas release programme is not expected to be successful if marginal free capacity is available in the gas storage system. If storage capacity is booked by the company that organizes the gas release programme, it should be released to the storage system operator to the extent of the gas quantities released.

Access to customers

- (796) A gas release programme has little chance to be successful if the majority of customers are bound to their gas suppliers under long-term supply contracts. In these conditions, a gas release programme is not expected to introduce much competition on the gas markets as customers are not able to switch suppliers. Therefore, it is essential that customers purchasing gas in the gas release programme or indirectly from a trader purchasing gas in the gas release programme have the opportunity to terminate their existing gas supply contracts or to reduce their obligation to purchase gas.

Monitoring and review provision

- (797) Experience has shown that it was important for an effective gas release programme to be able to review the conditions of implementation to address the difficulties encountered with the practical implementation of the programme. Given the high complexity and the specificities of the various market conditions, it is essential to provide for a close monitoring by the competent national authorities and for sufficient flexibility to modify the auction and gas supply rules so as to take duly into account the needs of third parties.
- (798) While gas release programmes imposed by energy regulators may be easily reviewed and improved on an on-going basis, this is more difficult for gas release programme

constituting undertakings in merger cases. Therefore the degree of freedom of the parties to set the terms and conditions of the programme should be restricted to ensure the effectiveness of the remedy and most practical/technical rules for the implementation of the programme should not be part of the undertakings attached to a decision, but rather defined at a later stage under the supervision of the relevant competition authority.

b. Assessment of the gas release programme and on the contract release proposed by the parties

(799) The Commission has concluded that the gas release programme and the contract release as offered by the parties, incorporating the amendments and improvements proposed by third party respondents to the market test, are sufficient to remove all the competition concerns identified by the Commission as resulting from the transaction. In particular, the Commission considers that the combination of the gas release programme and the contract release will ensure that gas end users and wholesalers will have the ability to source their gas needs under competitive and non-discriminatory conditions and, for at least a significant part, independently from the merged entity.

Volumes

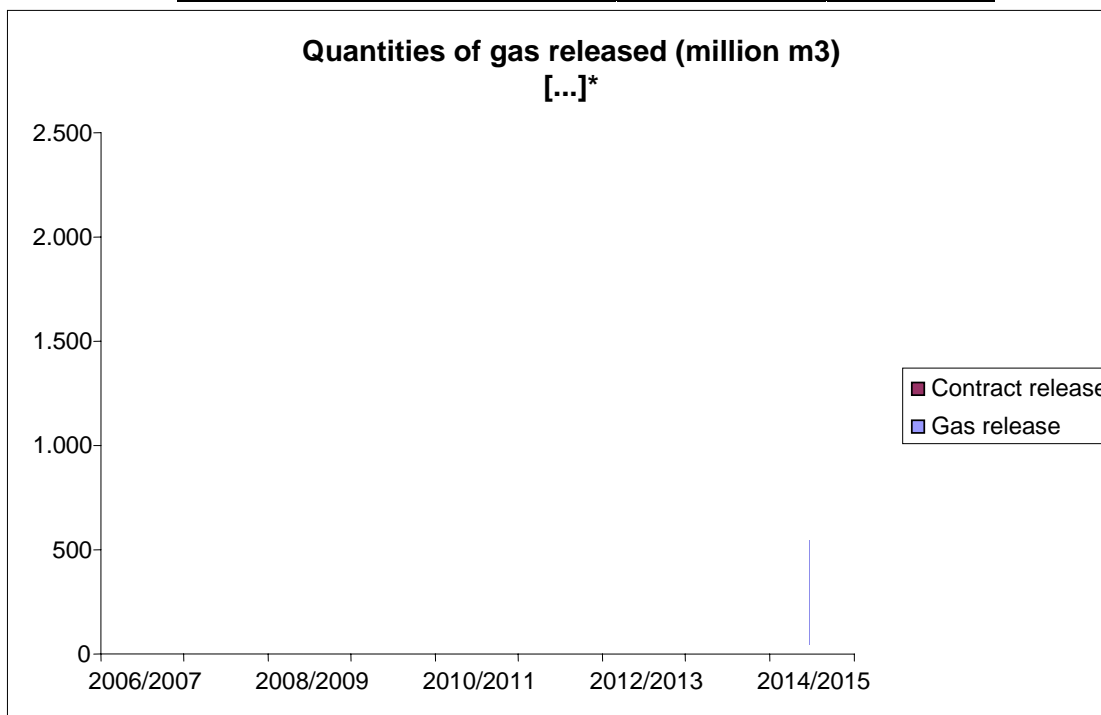
(800) In particular, the Commission considers that the volumes offered in the gas release programme (in conjunction with the volumes made available by the contract release for MOL E&P's production) are suitable to create sufficient liquidity of gas on the gas and electricity markets so as to ensure that effective competition can develop and remain sustainable. The total quantities of gas to be released through both remedies are significant in comparison to other existing gas release programmes.

(801) Based on MOL E&P current production forecasts (as included in Annex to the Supply Agreement), the Commission has estimated the quantities of gas that the parties undertake to release on a yearly basis until the gas year 2014/2015.

Quantities of gas released under the proposed commitments:

Gas Year	Quantities of gas released (in millions m ³)		
	Gas release	Contract release	TOTAL
2006/2007	500	[700-1300]*	[0-1000]*
2007/2008	1000	[700-1300]*	[2000-2500]*
2008/2009	1000	[700-1300]*	[2000-2500]*
2009/2010	1000	[700-1300]*	[2000-2500]*
2010/2011	1000	[500-1000]*	[1500-2000]*
2011/2012	1000	[500-1000]*	[1500-2000]*
2012/2013	1000	[500-1000]*	[1500-

			2000]*
2013/2014	1000	[0-500]*	[1000-1500]*
2014/2015	500	[0-500]*	[500-1000]*
TOTAL	8,000	[5000-10000]*	[13000-18000]*



(802) The table and chart in recital 799 above show that, at least until 2013/2014, substantial quantities of gas (around 2 bcm) will be released and the programmes will last until 2014/2015 (expiry of MOL WMT upstream procurement contracts and of MOL E&P's supply contract). The quantities released by the parties account for up to 14% of the total Hungarian demand and represent 21% of total third parties' gas sales (i.e., excluding sales of E.ON's RDCs and of MOL WMT). This means that third parties will have the ability to purchase a significant share of their gas from the gas release and/or the contract release.

(in million m ³)	Quantities of gas released	Hungarian gas consumption	%
2006/2007	[0-1000]*	[15000-20000]*	[0-10]*%
2007/2008	[2000-2500]*	[15000-20000]*	[10-20]*%
2008/2009	[2000-2500]*	[15000-20000]*	[10-20]*%
2009/2010	[2000-2500]*	[15000-20000]*	[10-20]*%
2010/2011	[1500-2000]*	[15000-20000]*	[10-20]*%
2011/2012	[1500-2000]*	[15000-20000]*	[10-20]*%
2012/2013	[1500-2000]*	[15000-20000]*	[5-15]*%
2013/2014	[1500-2000]*	[15000-20000]*	[5-15]*%
2014/2015	[0-1000]*	[15000-20000]*	[0-10]*%
TOTAL	[10000-20000]*	[140000-150000]*	[5-15]*%

- (803) The commitments do not foresee any restriction on the quality of participants to the gas release programme and the gas released may thus be purchased by commercial and industrial customers and power generators to meet their own needs or by gas traders. It is therefore not possible to estimate which quantities of gas released will be used in each of the relevant market where the Commission has identified competition concerns.
- (804) However, the total quantities of gas released over the gas years 2007/2008 to 2013/2014 represent approximately 60% of the size of the market for the supply of gas to power plants and 55% of the size of the market for the supply of gas to large industrial customers. The Commission therefore estimates that the released gas quantities will significantly increase liquidity and hence limit the likelihood of anticompetitive behaviour by the new entity.
- (805) The total quantities of gas to be released through both remedies are significant in terms of international benchmark. In this regard, the volumes of gas to be released are significantly higher (in percentage value) than in the similar programmes implemented in other European countries. For example, the gas release programme organized by Eongas in Austria amounts to 2.9% of the total Austrian gas market, the programme by E.ON Ruhrgas in Germany corresponds to 2.5% and ENI's programme in Italy represents 3.1% of total demand.

Gas release programme

- (806) The Commission believes that the gas release programme offered by the parties is designed, as regards its main features (volumes, duration, price mechanism) and in its more technical features (size of lots, duration of contracts, flexibility rules) largely in line with the criteria described in recitals 766 to 796 above, which are widely considered to be most relevant for the successful implementation of gas release programmes. The gas release programme was improved to take into account comments and suggestions made by respondents in the market test. The detailed rules for the effective implementation of the auction and the gas supply contracts will be elaborated by the parties under the scrutiny of the HEO, and submitted to the Commission for its approval.
- (807) The duration of the gas release programme will ensure that sufficient liquidity will be available for a sufficiently long time as to ensure that the market structure and competitive conditions have changed. It has to be highlighted that all of the parties' current supply agreements, including those with Gazprom / Panrusgáz, will have terminated by 2015. The new entity's gas supply contracts with Gazprom and the privileged access to gas resources (which confer to new entity the ability to foreclose access to gas to its downstream competitors and to significantly impede effective competition on the gas supply markets) will be open for competition at this date.
- (808) While the market investigation has revealed that Gazprom had no incentive to supply other traders competing with MOL WMT as long as it supplied the latter with gas quantities covering the bulk of the Hungarian gas consumption, at the expiry of the contract with MOL WMT, Gazprom will obviously have an economic interest in selecting its "Hungarian partner(s)" based on a competitive process. Large international market players already present in Hungary through ownership in the gas RDCs (ENI, RWE and GDF) will indeed have an interest in bidding for this

(these) new gas supply agreements with Gazprom and the Commission believes that the new entity and the largest gas traders active in Hungary will be in the same position to negotiate such supply agreement(s) in 2015.

- (809) Furthermore, the price mechanism foreseen for the programme will ensure that successful bidders will obtain gas at the same competitive conditions as the parties, and possibly cheaper, owing to the fact that the starting bidding price foresees a 5% discount off the WACOG. The Commission considers this pricing mechanism as enshrined in the remedies is attractive for third parties and will provide good incentives to participate actively in the programme's auctions. The remedy package also foresees that potential financial losses resulting from the price mechanism will be incurred by the parties for a considerable amount.
- (810) As regards the implementation of the gas release programme, it is important to ensure that all participants are admitted at transparent and non-discriminatory terms and that the sale is made at competitive conditions.
- (811) To this end, various parameters of the gas release programme have been modified by the parties following the market test in order to cater for the needs of potential buyers. For example, the size of the lots has been adjusted to meet the specificities of the Hungarian markets: three lots sizes are now offered to better meet the needs of the various categories of market players. The period between the auction and the delivery period has been extended by two months to give more time to successful bidders to find new customers if they intend to resell the gas they have acquired.
- (812) Access to customers is also granted under the proposed remedies as the parties undertake to amend the existing contracts of their existing customers intending to purchase gas from the gas release programme, either directly or through a wholesaler.
- (813) The Commission believes that the Hungarian regulatory framework (in particular "capacity-follows-the-customer" principle) should ensure that sufficient transmission and distribution capacities are made available to the successful bidders to transport the acquired gas within Hungary.

Contract release

- (814) The Commission believes that the assignee of the contract release will constitute a sizeable and sustainable competitive force in the Hungarian gas markets. The assignee will purchase significant quantities of gas from MOL E&P starting in July 2007 (expected date of the further liberalization of the Hungarian gas markets) until 2013/2014, independently from the new entity. It will also have to ability to combine the contract release with the purchase of gas quantities through the gas release programme until 2013/2014. The assignee of the contract release will therefore have sufficient long term gas resources to develop its position on the Hungarian gas markets and introduce liquidity on these markets.
- (815) The fact that the terms and conditions of the contract will be similar for the new entity and the assignee ensures that the latter will have the ability to compete with the new entity. In particular, MOL will grant equal treatment to WMT and the third party in exercising its put options concerning production quantities.

- (816) Access to customers is also granted under the proposed remedies as the parties undertake to entitle to amend the existing contracts of their existing customers from the Third Party assignee of the contract release.
- (817) The Hungarian regulatory framework (in particular “capacity-follows-the-customer” principle) should ensure that sufficient transmission and distribution capacities are made available to the Third Party assignee to transport the acquired gas within Hungary.

Storage

- (818) Additionally, the commitments of the parties to grant access to storage for the successful bidders of the gas release programme and the assignee of the contract release at regulated prices are sufficient to grant an effective and non-discriminatory access to the storage capacities for the relevant gas quantities. The Commission believes that this commitment will enable traders and customers to structure the acquired gas according to their own or their customers’ needs.

Monitoring

- (819) Finally, the effective monitoring by the HEO, with the assistance of the Commission’s Trustee, will help the Commission ensure that the parties will fully comply with their commitments for their full duration.

C. Conditions and obligations

- (820) Under the first sentence of the second subparagraph of Article 8(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.
- (821) Where a condition is not fulfilled, the Commission decision declaring the merger to be compatible with the common market no longer stands. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(5)(b) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2)(d) and 15(2)(c) of the Merger Regulation.
- (822) In accordance with the basic distinction described above, this Decision should be subject to compliance with the conditions set out in Section B, subsection I and II of the Annex.
- (823) In accordance with the basic distinction described above, this Decision should be subject to compliance with the obligations set out in Section B, subsection III, IV and V and in Section C of the Annex.

VIII. CONCLUSION

- (824) It is concluded that the commitments submitted by the notifying party are sufficient to address the competition concerns raised by this concentration. Accordingly, subject to compliance with the commitments submitted by the notifying party, the notified operation should be declared compatible with the common market and the functioning of the EEA Agreement.

HAS ADOPTED THIS DECISION:

Article 1

The notified operation whereby E.ON Ruhrgas AG acquires sole control of MOL Földgázellátó Rt. and MOL Földgáztároló Rt. within the meaning of Article 3(1)(b) of the Regulation (EC) No 139/2004 is hereby declared compatible with the common market and the functioning of the EEA Agreement.

Article 2

Article 1 is subject to compliance with the conditions set out in Section B, subsection I of the Annex.

Article 3

Article 1 is subject to compliance with the obligations set out in Section B, subsection III, IV and V of the Annex.

Article 4

This decision is addressed to:

E.ON Ruhrgas International AG

E.ON Ruhrgas AG
Huttropstrasse 60
D - 45138 Essen
Germany

Done at Brussels, 21/XII/2005

For the Commission
(signed)
Neelie KROES
Member of the Commission

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DATE: 8.12.2005 (REVISION OF THE COMMITMENTS 15. NOVEMBER 2005)

By e-mail and by fax: 00 32 2 296 4301

European Commission
DG Competition
Rue Joseph II 70 Jozef-II straat
B-1000 Brussels

Case M.3696 E.ON/MOL

COMMITMENTS TO THE EUROPEAN COMMISSION

submitted by E.ON Ruhrgas International AG

Pursuant to Article 8(2) of Council Regulation (EC) No. 139/2004 (the "Merger Regulation"), E.ON Ruhrgas International AG ("ERI") hereby provides the following Commitments (the "Commitments") in order to enable the European Commission (the "Commission") to declare the acquisition of control of ERI over MOL Földgázellátó Rt. ("WMT") and MOL Földgáztároló Rt. ("MOL Storage") compatible with the common market by its decision pursuant to Article 8(2) of the Merger Regulation (the "Decision"). The Commitments shall take effect upon the date of adoption of the Decision.

This text shall be interpreted in the light of the Decision to the extent that the Commitments are attached as conditions and obligations, in the general framework of Community law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies and under Commission Regulation (EC) No 802/2004.

Section A. Definitions

Affiliated Undertakings: Undertakings controlled by the Parties and/or by the ultimate parents of the Parties, whereby the notion of control shall be interpreted pursuant to Article 3 Merger Regulation and in the light of the Commission Notice on the concept of concentration under Council Regulation (EEC) No 4046/89.

Date of Closing: The day on which ERI will have taken over sole control of WMT and MOL Storage.

Divestment Business: The businesses as defined in section B. I.

Divestiture Trustee: One or more natural or legal person(s), independent from the parties, who is (are) approved by the Commission and appointed by ERI or MOL and who has (have) received from ERI or MOL the exclusive trustee mandate to sell the Divestment Business (in case of MOL) or the transferred business according to section IV (in case of ERI).

Effective Date: The day of adoption of the Decision.

ERI: Throughout this document the term ERI shall also apply to WMT and MOL Storage in the sense that after the Date of Closing ERI will cause WMT and MOL Storage to comply with their obligations as identified in this document.

First Divestiture Period: The period of six months from the Date of Closing.

HEO: The Hungarian Energy Office.

MOL: MOL Hungarian Oil and Gas Company Rt., including its gas exploration and production division (MOL E&P)

MOL Transmission: MOL Földgázszállító Rt.

Monitoring Trustee: One or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by ERI and MOL (as procured by ERI), and who has the duty to monitor ERI's and MOL's compliance (as procured by ERI) with the conditions and obligations attached to the Decision.

Trustee(s): The Monitoring Trustee and the Divestiture Trustee.

Trustee Divestiture Period: Period of three months from the end of the First Divestiture Period.

Section B. The proposed remedies

(i) I. Ownership Unbundling

1. Under the agreements concluded between MOL and ERI, MOL remains a shareholder of WMT and MOL Storage and it enjoys put-option rights under which MOL can require ERI to purchase the remaining 25 % plus one share interests which MOL will have in WMT and MOL Storage following the date of closing of the transaction. The put-options have a term of 5 years.
2. ERI undertakes to procure MOL to dispose of its remaining 25 % plus one share interest in WMT and MOL Storage (the “Divestment Business”) within six months following the Date of Closing. The disposal and acquisition of the Divestment Business will be subject to the approval of the HEO.
3. The disposal of the Divestment Business to a third party is subject to the Commission’s approval. The Commission shall grant its prior approval if the disposal to the third party does not, in the light of the information available to the Commission, create competition concerns in the Hungarian energy markets or does not give rise to a risk that the implementation of the Commitments will be delayed. ERI is not a third party within the meaning of this subsection.
4. Should MOL, in spite of its best efforts, encounter difficulties arising from regulatory or other government-induced proceedings, such as a possible clearance procedure before the HEO, in the disposal of the Divestment Business, ERI shall immediately inform the Commission and then rely on the review-clause mechanism set out under section D. of this document below.
5. A Monitoring Trustee will supervise the divestiture of the Divestment Business in WMT and MOL Storage. ERI shall procure MOL to submit written reports in English on potential transferees of the Divestment Business and developments in the negotiations with such potential transferees to the Commission and the Monitoring Trustee no later than ten days after the end of every month following the Date of Closing.

ERI shall procure MOL to inform the Commission and the Monitoring Trustee on the preparation of the data room documentation and the due diligence procedure and shall submit a copy of an information memorandum, if any, to the Commission and the Monitoring Trustee before sending the memorandum out to potential transferee.

6. If MOL has not entered into a final agreement with a third party or exercised its put-option vis-à-vis ERI at the end of the First Divestiture Period, ERI shall procure MOL to grant the Divestiture Trustee an exclusive mandate to sell the Divestment Business to a purchaser at no minimum price within the Trustee Divestiture Period. ERI shall be deemed to have complied with this Commitment if, by the end of the

Trustee Divestiture Period, MOL has entered into a final binding agreement on the disposal, if the Commission approves the transferee and the terms in accordance with subsection I.3 and if the closing of the disposal of the Divestment Business takes place within a period not exceeding three months after the approval of the transferee and the terms of disposal by the Commission.

7. The final binding agreement shall be conditional on the Commission's prior approval. When MOL has reached an agreement with a transferee, ERI shall procure MOL to submit fully documented and reasoned proposal, including a copy of the final agreement, to the Commission and the Monitoring Trustee. ERI must be able to demonstrate to the Commission that the transferee meets the requirements according to subsection I.3 and that the Divestment Business is being sold in a manner consistent with the Commitments. For the approval, the Commission shall verify that the transferee fulfils the transferee's requirements according to subsection I.3 and then the Divestment Business is being disposed of in a manner consistent with the Commitments.
8. In order to maintain the structural effect of the Commitments, ERI shall procure MOL, for a period of 10 years after the Effective Date, not to acquire direct or indirect minority stakes in WMT or MOL Storage as long as ERI is a majority shareholder, unless the Commission has previously found that the structure of the market has changed to such an extent that the absence of influence of MOL over WMT or MOL Storage is no longer necessary to render the proposed concentration compatible with the common market.

II. Put Option Mol Transmission

Under the Transmission Put Option Agreement concluded between MOL and ERI, MOL is granted a put option under which MOL can require ERI to purchase a 25 % plus one share or a 75 % minus one share interest in MOL Transmission. ERI hereby undertakes to the Commission that it shall procure MOL not to exercise the put option for the sale of 25 % plus one share interest in MOL Transmission. Also, ERI shall procure MOL, within the time period defined in section I.8., not to sell to ERI or any of its Affiliated Undertakings a share interest in MOL Transmission which would not result in the acquisition of sole control over MOL Transmission by ERI or of joint control over MOL Transmission by ERI and MOL. The terms "sole and joint control" are to be interpreted in compliance with the Merger Regulation.

III. Gas Release Programme

1. ERI undertakes to organize and implement a gas release programme to become effective on the Hungarian market. Under the gas release programme, ERI will offer for sale (release) natural gas on a non-discriminatory and transparent basis under the following terms and conditions:

1.1. The amount of gas to be auctioned each year will be 1 billion m³. The amount of 1 billion m³ will be auctioned in the years 2006, 2007, 2008, 2009, 2010, 2011, 2012 and 2013 respectively. However, by the end of 2010, ERI will have the possibility to apply for a termination of the gas release programme at the end of the initial five-year period if it can demonstrate to the Commission, on the basis of data available from the HEO and other public and reliable sources, that the market conditions have significantly changed.

The first auction and its envisaged date of commencement for the gas year 2006/2007 (July 1st) will be announced to the Hungarian market and be published on the websites of ERI and WMT no later than one month after the Date of Closing. The subsequent first auction will take place in the first week of May. In the next years, the auctions will take place in the first week of March. The above-mentioned gas volumes refer to gas suitable for public utility services according to the prevailing Hungarian national standard or in case there will be no public utility service always to the prevailing Hungarian national standard.

1.2. The sale will be organized by way of a business-to-business internet auction. Participants will be invited at an appropriate point of time before the beginning of the gas year to place their bids remotely via the internet. In 2006, the bidders will be invited in April; in the next years, they will be invited in February. Each auction shall comprise 5 tranches of 100 million m³, 5 tranches of 50 million m³ and 10 tranches of 25 million m³ each with a duration of two years to be delivered to the successful bidders according to the flexibility provisions foreseen in paragraph 1.7. below. The quantity of the tranches will be equally split over two years. It will be possible to bid for more than one tranche at the discretion of the participant.

The execution of the auctions will be carried out by an international IT-service provider. The auction procedure shall be handled so as to ensure that WMT will not gain knowledge of the intermediary bids placed by participants to the auction. Only the number of lots awarded to each successful bidder and the final auction price shall be communicated to WMT. The auction process shall be documented including the intermediary bids and name of the bidders. The documentation shall be made available to WMT after the auction has been terminated in order to enable WMT and/or ERI to discuss with the Monitoring Trustee and the HEO any comments or

representations which may have been made by companies which have participated in the gas release programme

ERI shall submit, within two months after the Effective Date, a proposal for the technical implementation of the auctions and the details of the supply contracts for gas delivered to successful bidders to the HEO for its comments and review. At the same time the proposal will also be submitted to the Commission. The review by the HEO shall be concluded within one month after the submission of the proposal by ERI. Further to the review by the HEO, the proposal of ERI shall be subject to the approval of the Commission.

The procedure of the auction (e.g. auction mechanism, bidding stages) should be designed so as to ensure a transparent and non-discriminatory allocation of the offered gas quantities in a competitive way. ERI undertakes to fully abide by the procedure for the technical implementation of the auctions as approved by the Commission and as possibly modified according to paragraph 2.2. hereunder.

The terms and conditions of the supply contracts for gas delivered to successful bidders to the auctions (e.g. nomination procedure, payment periods, price indexation etc) and in particular as regards the security of supply and penalties (e.g. situation of maintenance, force majeure, off-spec gas, interruptibility, etc.) should be in line with standard practices of the Hungarian gas markets.

- 1.3. Each auction process will start at a minimum price as defined in subsection 1.4. below and shall be based on the weighted average cost of gas (WACOG) of WMT. The WACOG shall be calculated as the weighted average cost of gas under all gas purchase contracts of WMT and shall closely reflect WMT's actual net cost of procurement of gas (both domestic and imported) at the time of each auction. The respective calculations are subject to a verification procedure carried out by the Monitoring Trustee who will report to the Commission pursuant to Section C II 2. (d) (2) of the Commitments. The general methodology of the WACOG calculation shall be submitted to the Commission two months after the Effective Date for its prior review and timely approval.
- 1.4. WMT will carry out the auction at a discounted minimum price which will be 95% of WACOG provided that the aggregate loss WMT may incur as a result of the final auction price being set below WACOG does not exceed EUR 26 million. The loss in a given auction is the negative difference between the final auction price minus the respective WACOG multiplied with the volumes of gas sold under this auction. After each auction, WMT will communicate any such loss WMT has incurred as the case may be to the Monitoring Trustee who is entitled to verify this information if required.

- 1.5. Quantities that are not sold in the auction shall be carried forward to the following years. Unsold quantities of a specific year's gas release programme shall be reoffered with one third of the quantities each in the following three auctions. Such final auctions for unsold quantities will not take place after 2014.
- 1.6. Potential bidders must register for the auction process and will be admitted to the auction process upon payment of a deposit (per tranche they intend to bid for) for the participation. The amount of the deposit shall be in line with standard practices of the European gas market and shall be established in consultation with the HEO. This deposit can also be made by providing a bank guarantee. This deposit will be returned to the bidders after the end of the auction. Successful bidders will have to place an additional deposit as guarantee for the payment of the purchase price. The amount of such payment guarantee will be fixed in consultation with the HEO depending on the amount the successful bidder will have to pay for gas volumes acquired in the auction.
- 1.7. The sales contract will provide for an annual minimum offtake obligation of 85 % to the effect that the purchaser will only have to purchase and pay 85 % of the annually contracted quantity. The daily minimum offtake obligation for successful bidders shall not exceed the weighted average daily minimum offtake obligation of all purchase contracts of WMT (currently being 50%). The quarterly minimum offtake obligation shall be 85 % of the quarterly contracted quantities. In case the respective daily and quarterly minimum offtake obligations of the import contracts change, the weighted average daily and the quarterly minimum offtake obligations shall be adapted accordingly. WMT shall submit its calculations of the weighted average daily and of the quarterly minimum offtake obligations (including the methodology used for these calculations) to the HEO for its review (see subsection 2.2. below) and shall publish the results on WMT's webpage.
- 1.8. In the auction process, each tranche will be offered for 80% gas delivery at the Hungarian side of the Eastern entry point into Hungary and 20% at the Hungarian side of the Western entry point into Hungary.

The successful bidders shall bear the (regulated) cross-border transmission fees for the acquired gas and, for the volumes to be offered at the Hungarian side of the Western entry point into Hungary also the transportation fee on the HAG pipeline from Baumgarten to the Hungarian border. These fees shall be separately identified and added by WMT to the price of the gas sold under the gas release program.

In case the Hungarian grid code is changed and the 80%/20% ratio is amended, WMT undertakes to correspondingly change its Commitments under this subsection.

- 1.9. Transport capacity booked by WMT with MOL Transmission shall be returned to MOL Transmission by WMT in the amount and to the extent that gas is sold to the successful bidders. ERI shall procure MOL Transmission in turn, to ensure that the necessary transmission capacities are available for the successful bidders.
- 1.10. Existing direct customers of WMT or ERI which participate in the auction processes or which purchase gas from a trader/wholesaler, who participates in the auction processes, are entitled to ask WMT or ERI for an extraordinary contractual modification in order to reduce their obligation to purchase natural gas from WMT or ERI by the amount of gas they will have purchased as a result of the gas release programme. The other terms and conditions of the gas supply contracts between these direct customers and WMT or ERI shall not be modified. The total amount of reductions must not be higher than the quantities sold in the auction processes.
- 1.11. ERI and all of its Affiliated Undertakings are excluded from placing bids in the auction processes, be it directly or indirectly through an agent. Furthermore, ERI and all of its Affiliated Undertakings shall be excluded from purchasing gas from the successful bidders, be it directly or indirectly through an agent.
2. A Monitoring Trustee and the HEO will supervise the auction processes under the gas release programme.
 - 2.1. Within a period of two months after the conclusion of each annual auction process up until the year 2010, ERI or WMT will inform the Monitoring Trustee and the HEO about the implementation of the yearly gas release programme and will make the respective tender and bidding documents, correspondence and contracts available to the Monitoring Trustee and the HEO for onward reporting to the Commission.
 - 2.2. ERI undertakes to modify and/or improve the implementing regime established for the implementation of the gas release programme on the basis of the experience gained from the yearly auctions with a view to solve issues raised by participants to the previous auctions and to improve the effectiveness of the program in achieving greater liquidity on the Hungarian wholesale gas markets. The Monitoring Trustee and the HEO shall therefore receive and hear comments or representations from companies which have participated or which intend to participate in the gas release auctions. The Monitoring Trustee will evaluate such comments or representations and afford WMT the opportunity to reply to the comments or representation and to adduce factual evidence to the extent necessary. Should the findings of the Monitoring Trustee in his opinion give reasons for concern as to the implementation of the remedy, the Monitoring Trustee will prepare a written report to the Commission which will also be provided to WMT and to the company which had initially made the comments or representations, provided however, that business

secrets of WMT must not be revealed to this company and that business secrets of this company must not be revealed to WMT. The proposal for the amendment and/or improvement of the implementing regime established for the implementation of the gas release programme will be submitted to the HEO for its comments and review. At the same time the proposal will also be submitted to the Commission. The review by the HEO shall be concluded within one month after the submission of the proposal by ERI. Further to the review by the HEO, the proposal of ERI shall be subject to the approval of the Commission.

IV. Contract release

1. In addition to its gas release programme, ERI undertakes to partially transfer and assign WMT's rights and obligations in and to its gas supply agreement with MOL (MOL E&P) to a third party gas trader in Hungary in respect of a 50 % portion of the gas volumes, including also the proportional volumes to be sold at the option of MOL contracted to be delivered and received under the terms of the said agreement. (**Note:** In view of the domestic production forecast indication as of today, this 50 % represent app. 7.6 – 10 billion m³, whereas the amount to be released in the first year will correspond to app. 1.18 billion m³.) The above-mentioned gas volumes refer to gas suitable for public utility services according to the prevailing Hungarian national standard or in case there will be no public utility service always to the prevailing Hungarian national standard.
 - 1.1. This transfer shall become effective at the beginning of the gas year 2007 (July 1st) and shall remain in force through to the end of said gas supply agreement (June 30th 2015).
 - 1.2. Under the terms of the transfer agreement, the third party gas dealer shall assume all of the rights and obligations of WMT under the supply agreement in respect of said 50 % portion of the gas volumes contracted under said agreement, and ERI shall procure MOL to agree to fulfil its delivery obligations stipulated under the supply agreement towards such third party in respect of said 50 % portion of the gas volumes. ERI shall procure MOL, in exercising its put options concerning production quantities, to grant equal treatment to WMT and the third party, respectively, according to the percentages of their contracted volumes and to acknowledge and agree that, in respect of this 50 % portion of gas volumes, MOL has established a direct contractual relationship with the third party whereby each of them shall be liable to the other for the rights and obligations assumed, without any recourse to ERI or WMT.

- 1.3. ERI shall procure MOL to approve the partial transfer of the supply agreement.
- 1.4. Within the First Divestiture Period, ERI undertakes to use its best efforts to transfer said portion of the gas supply agreement to a third party gas trader acceptable to MOL and to the Commission. The third party must be (a) independent of and unconnected to ERI and (b) have the financial resources, proven expertise and incentive to maintain and develop the transferred business as a viable and active competitive force in competition with ERI and other competitors. Moreover, this third party must not be identical to a possible purchaser of the Divestment Business.

The final transfer agreement shall be conditional on the Commission's prior approval. When WMT has reached an agreement with a purchaser, it shall submit a fully documented and reasoned proposal, including a copy of the final agreement, to the Commission and the Monitoring Trustee. ERI must be able to demonstrate to the Commission that the purchaser meets the above mentioned purchaser requirements and that the transferred business is being sold in a manner consistent with the Commitments. For the approval, the Commission shall verify that the purchaser fulfils said requirements and that the transferred business is being sold in a manner consistent with the Commitments.

In case that ERI has not entered into such an agreement within the six months period, ERI shall grant the Divestiture Trustee an exclusive mandate to transfer the portion of the supply agreement according to the terms and conditions of that agreement within the Trustee Divestiture Period, even without any additional consideration paid by the third party to WMT.

Should the Divestiture Trustee not be able to enter into such an agreement with a third party, it shall submit a report to the Commission which sets out and explains why ERI and the Divestiture Trustee have been unsuccessful in transferring said portion of the supply agreement. The annual volume of gas for that given gas year and, as the case may be, subsequent years, shall then be added to the gas release programme of that year in accordance with section III. For the following gas year, ERI shall then again seek to identify a third party gas trader in accordance with sections 1.1. to 1.4. above. In such a case the First Divestiture Period shall start on May 1st of the respective next year before the next gas year (e.g. for the gas year 2008 in June 2007). The same applies accordingly to the Trustee Divestiture Period which shall start on November 1st. The rights and obligations of the Divestiture Trustee apply accordingly for these subsequent years. The same is true for WMT's obligation to add the respective gas to the gas release programme of the following year. As a result, the gas release programme could continue to run for a longer term as described under section III, i.e. until the end of the gas supply agreement between WMT and MOL.

Existing direct customers of WMT or ERI which participate in the auction processes or which purchase gas from a trader/wholesaler, who participates in the auction processes, are entitled to ask WMT or ERI for an extraordinary contractual modification in order to reduce their obligation to purchase natural gas from WMT or ERI by the amount of gas they will have purchased as a result of the gas release programme. The other terms and conditions of the gas supply contracts between these direct customers and WMT or ERI shall not be modified. The total amount of reductions must not be higher than the quantities assigned to the third party trader in the contract release.

2. The Monitoring Trustee and the HEO shall be empowered to supervise that MOL is fully cooperative in bringing about the Contract Release and does not refuse to accept the transfer of the 50 % portion of the gas supply agreement to a suitable third party, which is eligible under this section IV and which is prepared to agree to the transfer of the agreement. The Monitoring Trustee and the HEO will have the power to review all relevant documents and correspondence. Should they see reasons for concern, they will immediately report these concerns to the Commission and give their opinion as to whether MOL has shown good cause for its behaviour. MOL and ERI will be provided with an opportunity to be heard.
3. Neither ERI nor any of its Affiliated Undertakings shall directly or through an agent purchase gas from the third party gas trader in Hungary.

V. Storage Capacity

1. ERI undertakes to make available storage capacities in Hungary under the terms and conditions as described in the following:

ERI undertakes to transfer under the applicable regulated prices and conditions, as approved by the HEO, storage capacities required by successful bidders which purchase gas quantities in the gas release programme as described under section III. and/or gas quantities in the MOL E&P contract release as described under section IV above in order to structure the acquired gas quantities for their own or their customers' needs.

In this respect, the current regulatory conditions provide that existing customers that switch from the regulated to the open market take their storage capacity into the open market. This will also apply to such customers being supplied with volumes from the gas release programme and/or the MOL E&P contract release. For customers and/or wholesalers that purchase gas for the first time, or develop an increased storage demand when buying gas quantities from the gas release programme and/or the MOL E&P contract release, ERI undertakes to offer them

sufficient access to storage capacities to structure the acquired gas quantities for their own or their customers' needs. Access to storage capacity shall be granted under the applicable regulated prices and conditions.

2. A Monitoring Trustee and the HEO will supervise that MOL Storage makes available storage capacities in Hungary under the terms and conditions defined in subsection 1. They will have the power to review all relevant documents and correspondence. Should the Monitoring Trustee or the HEO see reasons for concern, they will immediately report these concerns to the Commission and give their opinion as to whether MOL Storage has shown good cause for its behaviour. MOL Storage will be provided with an opportunity to be heard.

In case MOL Storage is unable to give access to the storage capacities requested by the successful bidders to the gas release programme and the third party trader of the contract release due to contractual or technical constraints in storage capacities, MOL Storage shall submit within 15 days from the date of the unfulfilled demand for access to storage, to the Monitoring Trustee and the HEO a report explaining the constraints in storage capacities. Furthermore, MOL Storage will comply with the decision of the HEO under which it is obliged to complete the development of gas storage capacity provided in the respective plan of MOL Storage covering the years 2005 until 2009 by the end of such period.

Section C. Trustees

I. Appointment Procedure

1. ERI shall procure MOL to appoint a Monitoring Trustee in relation to the Divestment Business to carry out the functions specified in the Commitments for a Monitoring Trustee.

ERI shall appoint a Monitoring Trustee concerning the gas release programme, the contract release and the storage capacity to carry out the functions specified in the Commitments for a Monitoring Trustee. ERI may appoint only one person as a Monitoring Trustee for the above mentioned tasks.

2. If MOL has not entered into a binding agreement regarding the disposal of the Divestment Business one month before the end of the First Divestiture Period or if the Commission has rejected a transferee proposed by MOL at that time or thereafter, ERI shall procure MOL to appoint a Divestiture Trustee to carry out the functions specified in the Commitments for the Divestiture Trustee.

If ERI has not entered into a transfer agreement one month before the end of the First Divestiture Period or if the Commission has rejected a purchaser proposed by ERI at that time or thereafter, ERI shall appoint a Divestiture Trustee to carry out the functions specified in the Commitments for the Divestiture Trustee. The appointment of the Divestiture Trustees shall take effect upon the commencement of the Trustee Divestiture Period.

3. The Trustees shall be independent of MOL and ERI, possess the necessary qualifications to carry out their mandate, for example as an investment bank or consultant or auditor, and shall neither have nor become exposed to a conflict of interest. The Trustees shall be remunerated in a way that does not impede the independent and effective fulfilment of its mandate.
4. No later than one month after the Effective Date, ERI shall submit (and shall procure MOL to submit) a list of one or more persons whom MOL or ERI propose to appoint as the Monitoring Trustee to the Commission for approval. No later than one month before the end of the First Divestiture Period, ERI (in case of the Contract Release Programme) shall submit and shall procure MOL (in case of the Divestment Business) to submit a list of one or more persons whom MOL and ERI, respectively, propose to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the proposed Trustee fulfils the requirements set out above and shall include:
 - a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;
 - b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks;
 - c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether different Trustees are proposed for the two functions.
5. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modification it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, ERI, shall appoint and procure MOL to appoint, the individual or institution concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, MOL or ERI, respectively, shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.
6. If all the proposed Trustees are rejected, ERI, shall submit and, as the case may be, procure MOL to submit the names of at least two more individuals or institutions

within one week of being informed of the rejection, in accordance with the requirements and the procedure set out above.

7. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom ERI shall appoint and shall procure MOL to appoint, in accordance with a Trustee mandate approved by the Commission.

II. Functions of the Trustees

1. Each Trustee shall assume its specified duties in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustees, MOL or ERI give any orders or instructions to the Trustee(s) in order to ensure compliance with the conditions and obligations attached to the Decision.

MOL and ERI will only have the power to request such orders and will only be involved in the monitoring procedure according to the following procedural steps as far as their particular obligations under the Commitments are concerned, i.e. MOL in respect of the divestiture of its minority stakes in WMT and MOL Storage and ERI in respect of the gas release programme, contract release and storage capacity.

2. The Monitoring Trustees shall:
 - a) propose in their first report to the Commission a detailed work plan describing how they intend to monitor compliance with the obligations and conditions attached to the Decision.
 - b) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision;
 - c) propose to MOL or ERI such measures as the Monitoring Trustees consider necessary to ensure MOL's or ERI's compliance with the conditions and obligations attached to the Decision;
 - d) provide to the Commission, sending MOL or ERI a non-confidential copy at the same time, a written report
 - (1) in case of the disposal of the Divestment Business within 15 days after the expiry date according to section B. I. 2.;
 - (2) in case of the gas release programme for each auction by the end of July;
 - (3) and in case of the contract release for each transfer agreement, as the case may be one month after the expiry date of the First Divestiture Period and the Trustee Divestiture Period, respectively.

In addition to these reports, the Monitoring Trustees shall promptly report in writing to the Commission, sending MOL or ERI a non-confidential copy at the same time, if it

concludes on reasonable grounds that MOL or ERI is failing to comply with these Commitments.

3. As far as MOL is concerned, the Divestiture Trustee shall within the Trustee Divestiture Period sell at no minimum price the Divestment Business to a transferee, provided that the Commission has approved both the transferee and the final binding agreement in accordance with the procedure laid down in section B. I. 1.3. The Divestiture Trustee shall include in the agreement such terms and conditions as it considers appropriate for an expedience sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the agreement such customary representations and warranties and indemnities as are reasonably required to effect the disposal. The Divestiture Trustee shall protect the legitimate financial interests of MOL, subject to the parties' unconditional obligations to divest at no minimum price in the Trustee Divestiture Period.
4. As far as ERI is concerned, the function of the Divestiture Trustee is defined in section IV. 1.4.
5. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the end of every month with a simultaneous copy for the Monitoring Trustee and a non-confidential copy to the Parties.

III. Duties and obligations of the Parties

1. ERI shall provide and shall cause its advisors and MOL's advisors to provide the Trustees with all such cooperation, assistance and information as the Trustees may reasonably require to perform their tasks. The Trustees shall have full and complete access to any of ERI's or MOL's or the Divestment Business' books, records, documents, Management or other personnel, facilities, sites and technical information necessary for fulfilling their duties under the Commitments, and MOL and ERI shall provide the Trustees upon request with copies of any document. MOL or ERI shall make available to the Trustees one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of their tasks.
2. ERI shall cause MOL's advisors to provide the Monitoring Trustee, on request, with the information submitted to potential transferees, in particular give the Monitoring Trustee access to the data room documentation and all other information granted to potential transferees in the due diligence procedure. MOL shall inform the

- Monitoring Trustee on possible transferees, submit a list of potential transferees, and keep the Monitoring Trustee informed of all developments in the divestiture process.
3. MOL and ERI, respectively, shall grant or procure Affiliated Undertakings to grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee to effect the disposal/transfer, the Closing and all actions and declarations which the Divestiture Trustee considers necessary or appropriate to achieve the disposal/transfer and the Closing, including the appointment of advisors to assist with the disposal/transfer process. Upon request of the Divestiture Trustee, MOL and ERI shall cause the documents required for effecting the disposal/transfer and the Closing to be duly executed.
 4. MOL and ERI shall indemnify the Trustees and their employees and agents (each an "Indemnified Party") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to MOL or ERI for any liabilities arising out of the performance of the Trustees' duties under the Commitments, except to the extent that such liabilities result from the willful default, recklessness, gross negligence or bad faith of the Trustees, their employees, agents or advisors.
 5. At the expense of MOL or ERI, the Trustees may appoint advisors (in particular for corporate finance or legal advice), subject to MOL's or ERI's approval (this approval may not be unreasonably withheld or delayed) if the Trustees consider the appointment of such advisors necessary or appropriate for the performance of their duties and obligations under the mandate, provided that any fees and other expenses incurred by the Trustees are reasonable. Should MOL or ERI refuse to approve the advisors proposed by the Trustees, the Commission may approve the appointment of such advisors instead, after having heard MOL or ERI. Only the Trustee shall be entitled to issue instructions to the advisors. Subsection 4. shall apply mutatis mutandis.

IV. Replacement, discharge and reappointment of the Trustees

1. If a Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a conflict of interest:
 - (a) the Commission may, after hearing the Trustee, require MOL or ERI to replace the Trustee; or
 - (b) MOL or ERI, with the prior approval of the Commission, may replace the Trustee.

2. If a Trustee is removed, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in section I.
3. Beside the removal, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section D. Mediation

1. In the event that a third party, notably but not exclusively a bidder in an auction under the gas release program, has reasons to believe that ERI is failing to comply with the requirements of the Commitments, the Monitoring Trustee may be instructed by the Commission to act as mediator to attempt to settle the dispute amicably. The Monitoring Trustee shall be allowed to appoint further professionals to assist him in the mediation process. The appointment of such professionals must be acceptable to ERI and the third party.
2. The procedure of the Mediation process under the Monitoring Trustee stewardship shall be proposed by the Monitoring Trustee and agreed to by ERI and the third party. The Monitoring Trustee shall also set forward a proposal as to who bears the costs of the mediation procedure which shall take into account general mediation standards. The procedure shall correspond to the European Code of Conduct for Mediators as developed by the European Commission and launched on 2 July 2004 in as far as appropriately applicable under the stewardship of the Monitoring Trustee. The procedure shall comprise a first phase of exchange of written observations between the parties. It is envisaged that the deadlines to reply to the observations shall be set by the Monitoring Trustee in a timely manner in order to accelerate the mediation process.
3. Following the exchange of written observations the Monitoring Trustee shall arrange for negotiations between ERI and the third party under his stewardship with a view to reaching an amicable solution of the dispute. Should such negotiations not produce an amicable solution, the Monitoring Trustee is then empowered to recommend a solution which shall become binding upon ERI and the third party unless ERI and / or the third party have lodged its / their opposition to this recommendation within one month from receiving a fully reasoned version of the recommended solution in the English language. In the latter case the Monitoring Trustee shall prepare a report for the Commission on the outcome of the Mediation

process. A copy of this report shall also be provided to the HEO and to ERI and the third party. Nothing in the mediation procedure shall affect the powers of the Commission to take decisions in relation to the Commitments in accordance with its powers under the Merger Regulation and the EC Treaty.

Section E. The Review Clause

The Commission may, where appropriate, in response to a request from ERI showing good cause and accompanied by a report from the Monitoring Trustee:

- (i) Grant an extension of the time periods foreseen in the Commitments, or
- (ii) Waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments.

Where ERI seeks an extension of a time period, it shall submit a request to the Commission no later than one month before the expiry of that period, showing good cause. Only in exceptional circumstances shall ERI be entitled to request an extension within the last month of any period. An appropriate extension of the time periods foreseen in this document for the implementation of the gas release programme shall be granted in case the Date of Closing will be after 28 February 2006.

Section F. ERI's full responsibility regarding conditions and obligations involving MOL

ERI shall be fully responsible for procuring MOL to act so as to ensure ERI's full and effective compliance with and implementation of these Commitments.

Duly authorized for and on behalf of ERI

Berlin/Düsseldorf, 8 December 2005

for ERI

.....
Dr. Gerhard Wiedemann

.....
Dr. Thomas Lübbig



OPINION

**of the ADVISORY COMMITTEE on CONCENTRATIONS
given at its 135th meeting on 6 December 2005
concerning a draft decision relating to
Case COMP/M.3696 – E.ON/MOL**

1. The Advisory Committee agrees with the Commission that the notified operation constitutes a concentration within the meaning of Article 1(3) and 3(1)(b) of the Merger Regulation and that it has a Community dimension as defined by the Merger Regulation.
2. The Advisory Committee agrees with the Commission that for the purpose of assessing the present operation, the **relevant product markets** are in the gas sector:
 - a) Transmission of gas
 - b) Distribution of gas
 - c) Storage of gas
 - d) Supply of gas to traders
 - e) Supply of gas to Regional Distribution Companies (“RDCs”)
 - f) Supply of gas to large power plants
 - g) Supply of gas to large industrial customers (with an hourly consumption exceeding 500 m³/hour)
 - h) Supply of gas to small commercial and industrial customers (with an hourly consumption below 500 m³/hour)
 - i) Supply of gas to residential customers

in the electricity sector:

 - j) Transmission of electricity
 - k) Distribution of electricity
 - l) Provision of balancing power
 - m) Wholesale supply of electricity to traders
 - n) Wholesale supply of electricity to the public utility wholesaler
 - o) Wholesale supply of electricity to RDCs
 - p) Retail supply of electricity to medium and large commercial and industrial customers
 - q) Retail supply of electricity to small commercial and industrial customers
 - r) Retail supply of electricity to residential customers
3. The Advisory Committee agrees with the Commission that for the purpose of assessing the present operation, the **relevant geographic markets** are **national** for the following markets
in the gas sector:
 - a) Transmission of gas
 - b) Storage of gas

- c) Supply of gas to traders
- d) Supply of gas to RDCs
- e) Supply of gas to large power plants
- f) Supply of gas to large industrial customers (with an hourly consumption exceeding 500 m³/hour)
- g) Supply of gas to small commercial and industrial customers (with an hourly consumption below 500 m³/hour)
- h) Supply of gas to residential customers (after July 2007 when residential customers become eligible)

in the electricity sector:

- i) Transmission of electricity
- j) Provision of balancing power
- k) Wholesale supply of electricity to traders
- l) Wholesale supply of electricity to the public utility wholesaler
- m) Wholesale supply of electricity to RDCs
- n) Retail supply of electricity to medium and large commercial and industrial customers
- o) Retail supply of electricity to small commercial and industrial customers
- p) Retail supply of electricity to residential customers (after July 2007 when residential customers become eligible)

4. The Advisory Committee agrees with the Commission that for the purpose of assessing the present operation, the **relevant geographic markets** are at present **sub-national** for the following markets

in the gas sector:

- a) Distribution of gas
- b) Supply of gas to residential customers until July 2007

in the electricity sector:

- c) Distribution of electricity
- d) Retail supply of electricity to residential customers until July 2007

5. The Advisory Committee agrees with the Commission that the proposed transaction will create a fully vertically integrated entity along the gas and electricity supply chains by combining MOL's almost exclusive control over gas resources and storage and E.ON's strong market positions in the retail supply of gas through its ownership of regional distribution companies in both gas and electricity, and E.ON's activities in electricity generation/wholesale.

6. The Advisory Committee agrees with the Commission that therefore after the transaction, the new entity will have both the ability and incentive to foreclose access to gas for its competitors in the downstream gas and electricity markets.

7. The Advisory Committee agrees with the Commission that the merged entity has a **dominant position** in the following markets in the gas sector:

- a) Supply of gas to traders in Hungary
- b) Supply of gas to RDCs in Hungary
- c) Supply of gas to large power plants in Hungary
- d) Storage of gas in Hungary

-
8. The Advisory Committee agrees with the Commission that the proposed concentration is likely to result in a **significant impediment to effective competition** in the common market or in a substantial part of it and the EEA for the following markets
- in the gas sector:
- a) Supply of gas to large industrial customers in Hungary through the creation of the dominant position
 - b) Supply of gas to small commercial and industrial customers in Hungary
 - c) Supply of gas to residential customers in Hungary (in each of the RDCs' areas separately before July 2007)
- in the electricity sector:
- d) Wholesale supply of electricity to traders in Hungary
 - e) Retail supply of electricity to medium and large commercial and industrial customers in Hungary
 - f) Retail supply of electricity to small commercial and industrial customers in Hungary
 - g) Retail supply of electricity to residential customers in Hungary (in each of the RDCs' areas separately before July 2007)
9. The Advisory Committee agrees with the Commission that the maintenance of cross-shareholdings between MOL and the new entity will allow the new entity to reinforce its foreclosure strategy through its position in the gas storage market and MOL's position in the transmission market.
10. The Advisory Committee agrees with the Commission that the **undertakings** are sufficient to remove the significant impediment to competition in the following markets
- in the gas sector:
- a) Supply of gas to large industrial customers in Hungary
 - b) Supply of gas to small commercial and industrial customers in Hungary
 - c) Supply of gas to residential customers in the Hungarian RDCs' areas (in Hungary after 2007)
 - d) Storage of gas in Hungary
- in the electricity sector:
- e) Wholesale supply of electricity to traders in Hungary
 - f) Retail supply of electricity to medium and large commercial and industrial customers in Hungary
 - g) Retail supply of electricity to small commercial and industrial customers in Hungary
 - h) Retail supply of electricity to residential customers in the Hungarian RDCs' areas (in Hungary after July 2007)
11. The Advisory Committee agrees with the Commission that, subject to full compliance with the undertakings offered by the parties, and considered all undertakings together, the proposed concentration does not significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, within the meaning of Article 2(2) of the Merger Regulation and that the proposed concentration is therefore to be declared compatible with Article 2(2) and 8(2) of the Merger Regulation and Article 57 of the EEA Agreement.

12. The Advisory Committee asks the Commission to take into account all the other points raised during the discussion.

<u>BELGIË/BELGIQUE</u>	<u>ČESKÁ REPUBLIKA</u>	<u>DANMARK</u>	<u>DEUTSCHLAND</u>	<u>EESTI</u>
J. MUTAMBA	---	---	K. WEIDNER	---
<u>ELLADA</u>	<u>ESPAÑA</u>	<u>FRANCE</u>	<u>IRELAND</u>	<u>ITALIA</u>
---	---	B. ALOMAR	---	G. CALABRO
<u>KYPROS/KIBRIS</u>	<u>LATVIJA</u>	<u>LIETUVA</u>	<u>LUXEMBOURG</u>	<u>MAGYARORSZÁG</u>
---	---	I. KUDZINSKIENE	---	I. NAGYHAZI
<u>MALTA</u>	<u>NEDERLAND</u>	<u>ÖSTERREICH</u>	<u>POLSKA</u>	<u>PORTUGAL</u>
---	Mr VAN GEMERT	A. LUKASCHEK	---	S. MOURA
<u>SLOVENIJA</u>	<u>SLOVENSKO</u>	<u>SUOMI-FINLAND</u>	<u>SVERIGE</u>	<u>UNITED KINGDOM</u>
---	---	J. BOËLIUS	C. BERGER	T. KRAJEWSKA



EUROPEAN COMMISSION

The Hearing Officer

FINAL REPORT OF THE HEARING OFFICER
IN CASE COMP/ M.3696 – E.ON/MOL

**(pursuant to Articles 15 and 16 of Commission Decision (2001/462/EC, ECSC)
of 23 May 2001 on the terms of reference of Hearing Officers
in certain competition proceedings – OJ L162, 19.06.2001, p.21)**

On 2 June 2005, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004 of 20 January 2004 (“the Merger Regulation”) whereby the German group E.ON intends to acquire sole control over the gas wholesale, marketing and trading activities as well as gas storage activities of MOL Hungarian Oil and Gas Company Rt. (“MOL”, Hungary). Furthermore, E.ON intends to acquire MOL’s 50% shareholding in Panrusgáz, a joint venture between MOL and Gazexport (a subsidiary of Gazprom).

At the end of the first phase of the investigation, the Commission concluded that the concentration raised serious doubts as to its compatibility with the common market and with the EEA Agreement. In particular, the transaction was found to have significant impact on the gas and electricity sector in Hungary, given that MOL has an almost exclusive control over the procurement of gas (imports and domestic production) and therefore enjoys a gatekeeper position for access to gas resources and to the gas infrastructures in Hungary.

On 7 July 2005, the Commission therefore initiated proceedings in accordance with Article 6(1)(c) of the Merger Regulation.

On 20 July and 2 August 2005, E.ON was provided with access to the “key documents” in the Commission file in accordance with chapter 7.2. of the “Best Practices on the conduct of EC merger control proceedings”.

On 2 August 2005, the procedure was suspended for eight days pursuant to Article 10(4) of the Merger Regulation owing to the fact that E.ON did not respond in a comprehensive and timely manner to a decision requiring information pursuant to 11(3) of the Merger Regulation.

A statement of objections was sent to E.ON on 19 September 2005. As agreed between E.ON and MOL, a version of the SO without E.ON's business secrets was transmitted to MOL by E.ON's legal representatives. In the following days, access to the Commission’s file was granted. E.ON and MOL were given the opportunity to comment on the Commission’s preliminary findings as set out in the statement of objections by 3 October 2005. This deadline was subsequently extended to 6 October 2005 at the parties’ request. E.ON’s reply was received on 5 October 2005.

The parties did not request to develop their arguments in a formal oral hearing.

On 21 October 2005, I granted the request of Energie Baden-Württemberg AG to be admitted as an interested third party. The same day, the Commission sent them a non-confidential summary of the statement of objections.

On 20 October 2005, E.ON offered commitments which were amended on 11 November and on 16 November 2005 respectively. Further to the market testing of the proposed undertakings, E.ON substantially improved their draft commitments, in particular as regards the duration of the gas release program and the price mechanism of the gas release auctions.

I have not been asked to verify the objectivity of the enquiry.

In agreement with and following an express request by the parties, the Commission issued a decision on 10 November 2005 pursuant to article 10(3) second paragraph of the Merger Regulation in order to extend the procedure by 11 working days.

In the light of the commitments eventually proposed and having analysed the results of the market test, the draft decision concludes that the proposed concentration is compatible with the common market and with the EEA Agreement.

In the light of the above, I consider that the rights to be heard of all participants to the present proceeding have been respected.

Brussels, 7 December 2005

(signed)
Serge DURANDE

EN

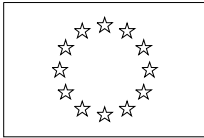
This text is made available for information purposes only.
A summary of this decision is published in all Community languages in the Official Journal of the European Union.

Case No
COMP/M.4404 –
Universal/BMG Music
Publishing

Only the English text is authentic.

REGULATION (EC) No 139/2004
MERGER PROCEDURE

Article 8 (2)
Date: 22/V/2007



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 22/V/2007

C(2007) 2160

PUBLIC VERSION

**COMMISSION DECISION
of 22 May 2007**

**declaring a concentration to be compatible with the common market
and the functioning of the EEA Agreement**

(Case No COMP/M.4404 – Universal/BMG Music Publishing)

**Commission Decision
of 22 May 2007
declaring a concentration to be compatible with the common market
and the functioning of the EEA Agreement**

(Case No COMP/M.4404 – Universal/BMG Music Publishing)

(Only the English text is authentic)

(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings¹, and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 8 December 2006 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations,

Having regard to the final report of the Hearing Officer in this case,

WHEREAS:

I. INTRODUCTION

1. On 3 November 2006, the Commission received a notification of a proposed concentration pursuant to Article 4 of Regulation (EC) No 139/2004 ("the Merger Regulation") by which the undertaking Universal Music Group Inc. ("Universal") acquires within the meaning of Article 3(1)(b) of the Merger Regulation sole control of the whole of the undertaking BMG Music Publishing ("BMG") which currently forms part of the Bertelsmann group, by way of purchase of shares and assets. Universal and BMG are collectively referred to in this decision as "the parties" with Universal alone being the "notifying party".
2. After examination of the notification, the Commission has concluded that the operation falls within the scope of the Merger Regulation and threatens to significantly impede effective competition in the common market. It therefore decided on 8 December 2006 to initiate proceedings pursuant to Article 6(1)(c) of the Merger Regulation.

¹ OJ L 24, 29.1.2004, p. 1

3. On 15 March 2007, Universal offered commitments with a view to rendering the concentration compatible with the common market. These commitments were modified on 26 March 2007 and improved on 30 March 2007. The final version of the commitments was submitted on 23 April 2007.
4. The Commission has concluded that the commitments entered into by Universal remove the serious doubts as to the compatibility of the notified operation with the common market. The concentration is therefore to be declared compatible with the common market and the functioning of the EEA Agreement pursuant to Articles 8(2) and 10(2) of the Merger Regulation and Article 57 of the EEA Agreement.

II. THE PARTIES

5. Universal is a 100% subsidiary of Vivendi SA ("Vivendi"). It is an international media company and its world-wide activities include music recording and publishing. Universal is active in music publishing through Universal Music Publishing Group ("UMPG").
6. BMG is part of the Bertelsmann group ("Bertelsmann") which is an international media company. BMG comprises the worldwide music publishing and production music activities of Bertelsmann.

III. THE CONCENTRATION

7. On 6 September 2006 Vivendi and Universal signed a share purchase agreement with Bertelsmann AG and seven further companies within Bertelsmann for the acquisition of BMG. As a result of the transaction Universal will acquire sole control of BMG. The transaction therefore constitutes a concentration within the meaning of Article 3(1)(b) of the EC Merger Regulation.

IV. COMMUNITY DIMENSION

8. Vivendi and BMG have a combined aggregate worldwide turnover of more than EUR 2 500 million (EUR 19 484 million for Vivendi in 2005 and EUR [...] for BMG in 2005). The aggregate Community wide turnover of each party exceeds EUR 100 million (EUR [...] for Vivendi in 2005 and EUR [...] for BMG in 2005).
9. The aggregate turnover of all the undertakings concerned exceeds 100 million in more than three Member States, namely France (Vivendi: EUR [...]*, BMG: EUR [...]*), Germany (Vivendi: EUR [...]*, BMG: EUR [...]*), Italy (Vivendi: EUR [...]*, BMG: EUR [...]*) and the United Kingdom (Vivendi: EUR [...]*, BMG: EUR [...]*). The aggregate turnover of each of Vivendi and BMG is more than EUR 25 million in all of these Member States.

* Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

10. The Parties do not achieve more than two-thirds of their turnover in one and the same Member State. The notified operation therefore has a Community dimension pursuant to Article 1(3) of the Merger Regulation.

V. RELEVANT MARKETS

1. Relevant product markets

11. Both parties are active in the music publishing business. The Commission identified in the case *Sony/BMG*² that the main activities of a music publisher comprise the discovery and identification of new talented songwriters with a view to acquiring and commercially exploiting their intellectual property rights and the provision of financial and promotional support to authors, arranging for music recordings and supporting their dissemination.
12. Music publishing is the exploitation of intellectual property rights of song writers (in this decision the term "authors" will be used to cover both lyricists (text) and composers (music)). Generally, authors transfer copyright of their works (referred to in this Decision as "publishing rights") to music publishers and receive from the latter payments of advances and a share of the royalties generated by the commercial exploitation of their works. The term "transfer of rights" refers both to the assignment and licensing of copyright.³
13. While the Commission in past merger cases mainly focussed on the music publishing market on which publishers grant licences to right-users, such as to producers of movies, record companies or radio stations, it appears that another market level to be taken into consideration would be the one covering the supply of publishing services to authors.
14. The activities of a publisher are thus twofold: on the one hand, the downstream activity of exploiting the works of authors under contract, inter alia by means of licensing the rights through the collecting societies, and on the other hand an upstream activity of signing authors and providing them with financial and marketing support as a counterpart to the transfer of their musical works. It appears that these two activities relate to separate markets as each one implies a distinct supply and demand relationship (between publishers and final users downstream, and between authors and publishers upstream).

² Case No COMP / M.3333 – Sony/BMG, 19 July 2004.

³ An assignment of copyright is the absolute (except for moral rights) transfer of the copyright ownership from one person (an "assignor") to another (an "assignee"). Usually, an assignment contains no restrictions as to the subsequent exploitation of the work by the assignee. A licence of copyright is a contractual right or permission whereby the copyright owner (the "licensor") allows another person (the "licensee") to exercise particular rights under copyright for a specified term. Unlike an assignment, a licence is not an absolute grant of rights and legal title does not pass to the licensee. It is a contractual right that usually ends on expiry of the term or upon termination of the licence. On expiry or termination of the licence, all rights granted under it, including under any sub-licences, revert to the licensor. The precise conditions under which copyright is transferred may differ in each country. In the Decision, the term "transfer" will be used encompassing both the assignment and the licensing of rights by authors to publishers / collecting societies while "licensing" will mainly refer to the exploitation of these transferred rights by publishers / collecting societies granting licences to users.

1.1 Markets for the exploitation of music publishing rights (downstream market level: publisher - user)

15. Music publishers exploit the rights received from authors by granting licences to right-users. The right-users encompass all sectors where music is required (CDs, films, advertising, radio, TV, internet and mobile communications)⁴. The users pay royalties for the use of these musical works. Depending on the specific types of rights, the licences are granted to right-users either by the publishers directly or via collecting societies.

Combination of recording and publishing

16. Publishing rights (i.e. the rights originally held by authors) need to be distinguished from so-called "neighbouring rights" or "recording rights" which mainly protect the individual interpretation of a song by a performing artist. While the publishing rights of a song are with the authors and their publishers, the recording rights are with the recording companies and the singers who normally transfer them to their record companies.
17. In order to legally use a song, for example on the radio, or for downloading services on the internet, a music user in most cases has to acquire a licence for both the publishing right and the recording right. The lack of either of these prevents legal use of the song.

Types of publishing rights

18. The following different types of rights⁵ exist, each of which might constitute a distinct product market as they are commercialised through distinct channels, address different needs and apply for different uses:
 - i. **mechanical rights**: for reproduction of a work in a sound recording (e.g. CDs);
 - ii. **performance rights**: for commercial users such as broadcasters (TV or radio stations), concert halls, theatres, night clubs, restaurants etc.;
 - iii. **synchronisation rights**: for commercial users such as advertising agencies or film companies (i.e. when the music is synchronised with the visual image);
 - iv. **print rights**: for the reproduction of work in sheet music.

⁴ The publishing business has no direct relationship with final/end consumers and can therefore be considered as a wholesale market.

⁵ This categorization broadly covers the rights indicated in the Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyrights and related rights in the information society (Official Journal L 167, 22/06/2001). The "reproduction right" covers mechanical and synchronization rights, the "right of communication to the public" includes also a "making available right" which relates to communication to the public where the public may access the works from a place and at a time individually chosen. This makes particular reference to downloading and streaming.

19. **Online rights** are a fifth category of rights to be considered. They constitute a specific combination of mechanical and performance rights for online applications, such as music downloading services.
20. The parties are of the view that a segmentation of the market by categories of rights is not necessary as it would not reflect the commercial realities of the music publishing industry. According to the parties, music publishers do not distinguish for operational purposes between separate categories of rights but administer all the different categories in respect of a particular song or composition and authors generally contract with a publisher to exploit *all* their rights rather than one category of rights.
21. In its decision in *Sony/BMG* (as in *Seagram/Polygram*⁶), the Commission stated that the exploitation according to the different types of rights may lead to the definition of separate product markets for each categories of rights, although the precise market definition was left open in that regard. Both demand-side (different characteristics of rights relating to different customer needs) and supply-side considerations (existence of different exploitation systems, application of dissimilar licensing rates) backed this statement.
22. From a demand-side perspective there is clearly no substitutability between the different categories of rights. A radio station needing a licence to play music on the radio (performance right) will not be able to take a licence for reproduction on CDs (mechanical right) instead.
23. The assumption of one overall market for publishing rights does not seem to be appropriate from a supply-side perspective either. While publishers often administer not only specific rights but several or even all of the authors' rights, the market investigation in this case has nevertheless shown that the market conditions differ significantly as to the different rights, which points to separate markets.
24. The main differences relate to the role of the collecting societies. It is worthwhile noting that licensing of mechanical and performance rights (which generate the largest share of revenues) are generally carried out by collecting societies⁷ on behalf of publishers and/or authors while synchronization and print rights are generally licensed and administered directly by the publishers without involvement of collecting societies. There are also differences in the way royalties are paid by users to the relevant collecting societies; for example, in the case of mechanical rights for Continental Europe, there is a standard rate whereas for performance rights rates are negotiated by each collecting society. In some countries, there are even separate collecting societies for mechanical and performance rights (e.g. Austria, United Kingdom and Sweden). The market investigation has confirmed that the licensing conditions differ per category of rights.
25. Therefore the product markets for publishing rights need to be defined according to the specific fields of application (mechanical, performance, synchronisation, print and online)

⁶ Case No IV/M.1219 – Seagram/Polygram, dated 21 September 1998.

⁷ The collecting societies generally sign agreements with all publishing companies, which allow the collecting society to grant a blanket licence (including repertoires from all publishing companies) on a non-discriminatory basis. Therefore all end users have a full and non-discriminatory access to musical works.

for which the rights are used since the prices as well as the overall economic conditions differ significantly.

Online rights

26. Among the five right categories mentioned above, specific considerations apply to online rights. The notifying party submits that there is no separate right for the online distribution of music but that these digital rights are merely a combination of mechanical and performance rights. Although the market investigation has shown that in most national laws online rights are not defined as a distinct legal right, it also demonstrated that competitive conditions for online applications differ from the other categories of rights. Online rights therefore constitute a distinct product market.
27. Online rights apply to a wide range of applications. All these online and mobile applications have in common that they require a licence combining both mechanical and performance rights.⁸ At present, the most important online and mobile music services, in terms of revenues generated, are (in systematic order):
- *On-line (audio) download:*
recording of music on the user's computer and the possibility (potentially limited by Digital Rights Management ("DRM")) to transfer it on other devices and to make copies;
 - *On-line (audio and video) streaming:*
temporary listening or viewing of music on the user's computer without recording;
 - *Mobile (audio) download:*
recording of music on the user's mobile device by wireless transmission, in particular a mobile phone;
 - *Mobile (audio and video) streaming*
temporary listening or viewing of music, without recording, on the user's mobile device by wireless transmission, in particular a mobile phone;
 - *Ringtones*
melodies, i.e. without lyrics, which are played as ringing signal of a mobile phone, in particular for incoming calls; ringtones may be monophonic or polyphonic melodies;
 - *Mastertones*
ringtones embodying sound recording excerpts, i.e. songs (melody and lyrics) used as ringing signal of a mobile phone, in particular for incoming calls;
 - *Ringbacktones*
songs or melodies played for the call initiator until the phone is answered.

⁸ Cf. paragraph 105 of the form CO.

28. There are many different business models for these music services: Some are advertisement-financed and thus free of charge for users; publishing royalties for these services are usually calculated as a percentage of the advertising revenues. Other services are integrated into a subscription model with the publishing royalties being calculated on the basis of the subscription revenues. Finally, many services are billed on the basis of the number of titles or tones downloaded; for these services publishing royalties are calculated as a percentage of the retail price or as a minimum fee per track. The importance of the various music services for the individual provider depends on its main business areas, e.g. for a pure mobile phone operator ringtones, mastertones and other mobile applications are most important whereas other providers such as Apple i-tunes focus on online downloads. However, it is also noteworthy that the convergence of online and mobile technologies increasingly blurs any clear borderline between online and mobile applications. This convergence applies in particular to downloading and streaming applications whereas mastertones, ringtones and ringbacktones are mobile-specific.⁹
29. Despite this convergence trend, a further distinction within the online rights category between online and mobile applications could be argued as from the demand side there is a limited substitutability. However, for the purpose of this case, such a further distinction would not be necessary as the competition analysis would remain unchanged under any distinction considered.
30. The delineation of online rights as a distinct market is furthermore supported by the following elements.
31. The Commission Recommendation of 18 May 2005 on collective cross-border management of copyright and related rights for legitimate online music services¹⁰ (the "Recommendation") singles out online rights in order to foster effective structures for the cross-border management of these rights. It defines online rights as: "(i) the exclusive right of reproduction provided for under Directive 2001/29/EC in the form of intangible copies, made in the process of online distribution of musical works; (ii) the right of communication to the public of a musical work, either in the form of a right to authorise or prohibit pursuant to Directive 2001/29/EC or a right to equitable remuneration in accordance with Directive 92/100/EEC, which includes webcasting, internet radio and simulcasting or near-on-demand services received either on a personal computer or on a mobile telephone; (iii) the exclusive right of making available a musical work pursuant to Directive 2001/29/EC, which includes on-demand or other interactive services".¹¹

⁹ In some countries (e.g. Germany), mastertones, ringtones and ringbacktones require an additional licence for so-called adaptation rights, a kind of moral right of the author. These adaptation rights are currently licensed directly by the publishers without involvement of the collecting societies.

¹⁰ OJ L 276, 21.10.2005, p. 54.

¹¹ Commission Recommendation of 18 October 2005 on collective cross-border management of copyright and related rights for legitimate online music services (2005/737/EC), point 1(f) (i) to (ii). See also Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society, [2001] OJ L 167/10 and Council Directive 92/100/EEC of 19 November 1992 on rental right and lending right and on certain rights related to copyright in the field of intellectual property [1992] OJ L346/67.

32. Universal itself considers¹² that online rights include telephone and online usage rights including reproduction, distribution and moral rights (synchronisation rights are excluded), telephone and online usage meaning mainly exploitation of musical works through downloading¹³ and streaming (simulcasting¹⁴ excluded). As far as BMG is concerned, online usage means online and mobile usage including ringtones and web casting (simulcasting excluded)¹⁵.
33. From a demand-side perspective there is no substitutability between online rights and traditional mechanical and performance rights since licences are granted for a specific application. The prices are defined according to different rules from the traditional mechanical and performance rights.
34. Since online applications are a comparably new development, there has been some uncertainty about the rules which apply to these rights on the part of the market participants. For instance some collecting societies have established specific rules as to online rights which were inserted into the collecting societies' statutes and thereby define distinct rules.
35. The market conditions under which online rights are licensed are, moreover, currently changing which further widens the gap between them and the traditional mechanical and performance rights. Thus, since the beginning of 2006, there have been some attempts (see in more detail further below) to turn the current system of collective management of rights (where all collecting societies, each enjoying a dominant position on its own territory, are dealing with equivalent rights through reciprocal agreements) into a system where a limited number of collecting societies are granted exclusivity in the management of online rights belonging to some publishers. This will distinguish online rights even more clearly from other rights since very specific rules will apply to online rights. So far, such a change mainly relates to the management of online mechanical rights (see below). Without it being necessary to determine whether the management of online mechanical rights constitutes a separate market from the wider online right market, the competitive assessment will focus on this segment as the conclusion will remain unchanged irrespective of whether the relevant product market is considered to be the overall online rights market or the online mechanical rights segment.

¹² This definition of the online right was provided by Universal to the Collecting Societies [...]*

¹³ It is often considered that downloading involves to 75% mechanical rights due to the storage of the song on a hard-disk which is comparable to a CD and to 25% performance rights since the online music provider normally offers to the end-customers the possibility to listen to parts of the songs before buying them.

¹⁴ Contraction of "simultaneous broadcast", and refers to programs or events broadcast across more than one medium at the same time.

¹⁵ In the same way, it can be also observed that the mechanical rights British collecting Society MCPS indicates on its website that "*online rights shall include online and mobile usage rights including, as regards the performing right, any right to communication to the public and as regards the mechanical right, to the extent possible, reproduction, distribution [...]*".

Anglo-American and Continental Europe repertoires

36. Apart from the categories of rights, the notifying party considers as a theoretically possible product market a segmentation of national and international¹⁶ repertoires for music publishing. A "repertoire" is the entirety of a number of titles, i.e. songs which may also be called works. However, the notifying party submits that a distinction between separate markets for national and international repertoires would not be justified.
37. The market investigation indicated that "Anglo-American" repertoire (i.e. titles registered with the collecting societies mainly in the U.S. (BMI and ASCAP) and the United Kingdom (MCPS and PRS)) may be distinguished from "Continental European" repertoire¹⁷ (i.e. titles registered with collecting societies in Continental Europe such as GEMA in Germany or SACEM in France). Anglo-American and Continental European repertoire differ for historical reasons (as explained in detail below). In addition, Continental European repertoire is largely commercialised on a national basis whereas Anglo-American repertoire relates to works acquired and exploited on a multi-national basis.
38. However, as will be explained in more detail later-on, the main difference between the Anglo-American and Continental European repertoire is the fact that publishers do not share the same level of control over the mechanical rights concerned: for Anglo-American repertoire, the publisher holds full control of the mechanical rights (which are transferred by the author to the publisher) whereas for Continental European repertoire a share is kept by the author. Hence, the management of the Anglo-American repertoire will in the future (after the reorganisation of the online rights market as discussed in more detail below) follow different rules from Continental European repertoire. For instance the mechanical British collecting society (MCPS) notably pays 100% of the royalties collected to publishers whereas Continental European collecting societies pay only a share of collected royalties to publishers, the other share being directly paid to authors.
39. On the other hand, both Continental European and Anglo-American repertoires address similar customers and follow the same market rationale. Major publishers generally have a strong position for Anglo-American repertoire compared to independent publishers who often appear to focus rather on specific genres and/or territories.
40. It is however not necessary to assess whether Anglo-American mechanical rights for online use could in the future constitute a separate market since the competitive assessment would not change. The current assessment is based on Universal's future market strength in Anglo-American repertoire on the overall online rights market (including Anglo-American and other titles). Even under the assumption of a separate market for Anglo-American titles (for online use) the market analysis would not be different.

¹⁶ The international repertoire corresponds mainly with the Anglo-American repertoire (i.e. US/Canada, United Kingdom/Ireland, Australia/New Zealand) whereas the national repertoire will refer to the Continental European repertoire.

¹⁷ As a synonym also the term BIEM repertoire is used.

Musical genres

41. In its previous cases the Commission also considered that the market might be delineated by different genres/categories of music. The basic segmentation generally referred to applies to pop versus classical music. However, in *Seagram/Polygram* and *Thorn EMI/Virgin* the Commission held that within pop music a large number of different categories could be identified (e.g. jazz, soul, heavy metal and techno). So far, however, the Commission has left the precise scope of the relevant product market open¹⁸.
42. The parties submit that music publishers usually acquire and commercialize rights for several types of music, while users will generally license rights covering a wide variety of genres. For this reason the parties consider that no distinction should be made between genres with regard to the product market definition. Even if a number of independent publishers specialize in one specific genre (niche strategy), this view is generally confirmed by the market investigation, with a possible exception for classical music.
43. However the question whether different genres may lead to the definition of separate product markets can be left open as the competitive analysis will remain unchanged under any envisaged definition.

Conclusion

44. For the reasons explained above, a definition of the market along the lines of different categories of rights is appropriate since the economic conditions seem to differ mostly between these categories. The precise definition of the market for music publishing rights for online applications with respect to a potential further sub-division into "mobile" and "online (excluding mobile)" can be left open as the effects of the transaction will be the same under both market delineations. The market for music publishing rights for online and mobile applications will hereinafter be referred to *pars pro toto* as the "market for online rights".

1.2 Market for music publishing services to authors (market level: author - publisher)

45. The author-publisher market level refers to the market on which publishers provide the authors with various services such as advances, management and administration of copyrights. Apart from this, publishers provide services to authors which serve the promotion and further development of the author. The parties describe those as "A&R" (Artist and Repertoire) services, which include for example the finding of producers, the provision of creative guidance and career development and suggestions of suitable writing partnerships with other authors. In return the authors transfer the rights connected to their own works to the publishers for exploitation. The business relation between authors and publishers is therefore partially characterised by a form of barter trade. Authors receive services for transferring their rights to publishers (either by assignment or by licence). While from the perspective of publishers this market level constitutes a market for the acquisition of rights, from the viewpoint of authors it constitutes a market for publishing services.

¹⁸ Case No IV/M.202 – Thorn EMI/Virgin, dated 27.04.1992 ; Case No IV/M.1219 – Seagram/Polygram, dated 21.09.1998.

46. Generally, authors license copyrights of their works to music publishers and receive from the latter payments of advances and a share of the royalties generated by the commercial exploitation of their works. The advances usually have the character of a loan since all royalties which are earned by licences to users go to the publisher until the advances are amortised. The publisher carries the risks if the advances are not fully amortised. Only then does the author receive the share of royalties as agreed with the publisher. A minority of authors do not rely on publishers' services and publish their works themselves. This can in particular be viable for established authors thanks to the existence of collecting societies who collect mechanical and performance royalties on behalf of the author.
47. For those working with a publisher, the licensing is based on an individual contract between the parties, where the publisher will administer the copyright of the author for a duration which varies between several years to the lifetime of the copyright (70 years after the death of the author). The most frequent situation is lifetime of copyrights with however some shorter term contracts signed in the recent past (e.g.: contract of 5 years plus a retention period of 10 years – meaning that the publisher will administer all rights for works created during the 5-year contract for a period ending 10 years after termination of the contract).
48. Authors should therefore not only be considered as suppliers of songs, but also as customers receiving various publishing services. For new authors principally, a publisher usually provides strategic support to start a career as it gives the author initial financial support and access to its established network of artists and record companies. More generally the administrative support of publishers allows authors to focus on creative activities. The market investigation confirms that many authors would not envisage working without a publisher.
49. It is relatively common for authors to work with different publishers who each administer different works. It is generally observed that one author can work with different publishers during different periods, each publisher administering the rights of the works created during the period in respect of which he had a contract with the author. However, authors do not seem to use different publishers for the different categories of rights. Therefore, in contrast to the considerations for the market for publishing rights (downstream level) no further segmentation of this market appears to be appropriate. In this Decision, a market for music publishing services for authors will be assumed.

2. Relevant geographic markets

2.1 Markets for the exploitation of music publishing rights (downstream market level: publisher - user)

50. The notifying party considers the geographic scope of the market for the exploitation of music publishing rights granted to right-users to be essentially national in scope and refer to the Commission's considerations concerning the geographic market in music publishing in the *Sony/BMG* decision.
51. In *Thorn EMI/Virgin Music* and *Seagram/PolyGram*, the Commission left open the question as to whether the geographical scope of the music publishing market(s) was

national or broader, in particular EEA-wide. In *Bertelsmann/Zomba*¹⁹ and *Sony/BMG* the Commission concluded that there were indications that the markets for mechanical and performance rights were national as these rights were generally administered and collected by national collecting societies on behalf of the publishers and/or authors. In addition, it was found that all publishers who wish to diffuse their repertoire outside their home country rely on local agencies implanted in the target country or sub-publish their repertoire to a publisher established in the target country. However the exact geographic scope of the market was left open.

52. The concept of national markets might be mitigated by major recording companies having signed so-called central licensing agreements for mechanical rights. This type of licensing agreement is signed with a selected collecting society who then grants licences for the European territory by negotiating itself with the individual national collecting societies.
53. However although this central licensing allows for a one-stop-shop for record companies, it is basically a centralised system of reporting of national sales and still involves activities of all national collecting societies in their respective territories.
54. As regards print and synchronisation rights, the scope of the licences obtained by the customers is usually national even if this could depend on the use foreseen (for instance a TV advertisement broadcast in several countries).
55. Moreover the market investigation confirms that publishers are generally active on their national market, or work with a local partner on foreign markets. Mostly, publishers work in different countries by having either own representations there or agreements with local sub-publishers to exploit their catalogues in the foreign countries.
56. There is no need to strictly define the geographic scope of the markets for mechanical, performance, synchronisation or print rights as the competitive assessment will remain unchanged, irrespective of whether the market was considered to have a national or EEA-wide dimension.
57. As regards more particularly online rights, and as mentioned above, the administration of online rights has so far been done by the collecting societies which in the traditional system work on a strictly national basis granting licences only for their respective national territory to national users. Therefore, currently the market is national.
58. A significant restructuring of online rights administration is currently taking place (this will be explained in more detail below) which may lead to an EEA-wide licensing of online rights. Where these restructuring initiatives have advanced already, they currently simply replicate the national licensing system on the basis of so-called "country of destination" tariffs. Even in this case, the market would therefore still be considered as a national market.
59. However, some of the current initiatives, where publishers appoint one (or more) collecting societies to manage and administer the online rights for mobile and online uses as the publisher's agent, aim at developing this activity throughout Europe, applying a foreseen single tariff. It is therefore possible that the market may eventually develop an EEA-wide scope.

¹⁹ Case No COMP / M.2883 Bertelsmann/Zomba.

60. The relevant geographic dimension of the online rights markets assessed will therefore mainly relate to the national markets where the transaction raises competition concerns. However, in order to take into account the developing restructuring initiatives and their likely impact on competition, a complementary assessment at the EEA-wide level will be undertaken. The conclusions remain unchanged under both geographical scopes.

2.2 Market for music publishing services for authors (upstream market level: author-publisher)

61. The geographic scope of the market for publishing services provided to authors appears to be national as authors mainly seem to turn to publishers with local presence and are members of the national collecting societies. The exact geographic scope may, however, be left open since the conclusions of the analysis will be the same, irrespective of the geographic dimension of the market.

2.3 Conclusion on market definitions

62. The competitive assessment will therefore examine the impact of the merger on the following markets:
- markets for publishing services for authors (on a national level)
 - market for synchronization rights (on national and EEA level)
 - market for print rights (on national and EEA level)
 - market for mechanical rights (on national and EEA level)
 - market for performance rights (on national and EEA level)
 - market for online rights (on national and EEA level)

VI. COMPETITION ASSESSMENT

A. MARKET FOR MUSIC PUBLISHING SERVICES FOR AUTHORS

1. Market structure

63. The market structure of the market for music publishing services is mirrored in the market for the exploitation of publishing rights. The authors choose a publisher for the provision of music publishing services which cover the promotion and exploitation of their songs. The revenues received by exploiting these rights (directly or via collecting societies) are shared between the publishers and the authors.
64. While some deviations are possible due to different splits between authors and publishers, it is likely that the market shares of the music publishing services are similar to their market shares on the downstream market(s) for the exploitation of publishing rights vis-à-vis the users. Basically the same market structure prevails in this market as for the overall market for music publishing rights (including mechanical, performance, print, synchronization and online rights) as summarized in the following table (source: parties' estimates):

Market share estimates for a market covering all publishing rights (2005)

All rights	Universal	BMG	Merged	EMI	Warner	Sony	Others
	%	%	%	%	%	%	%
Austria	[10-20]*	[0-10]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
Belgium	[10-20]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
Czech Rep.	[0-10]*	[0-10]*	[10-20]*	[30-40]*	[20-30]*	[0-10]*	[10-20]*
France	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Germany	[0-10]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Greece	[10-20]*	[10-20]*	[30-40]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*
Hungary	[20-30]*	[20-30]*	[40-50]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*
Italy	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
Netherlands	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[10-20]*
Poland	[10-20]*	[10-20]*	[30-40]*	[10-20]*	[10-20]*	[10-20]*	[10-20]*
Spain	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[20-30]*
United Kingdom	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
EEA	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*

Source: Parties' estimates

65. The operation would thus give rise to horizontally affected markets on an EEA-wide level and in the EEA-countries Austria, Belgium, Czech Republic, France, Germany, Greece, Hungary, Italy, the Netherlands, Poland, Spain and the United Kingdom.

2. Non-coordinated effects

66. The parties submit that there is strong competition between publishers to sign and develop new artists since the large, vertically integrated major publishers ("majors": Universal, BMG, EMI, Warner, Sony) equally compete against each other and against the smaller independent publishers ("independents"). However, during the market investigation some concerns were raised by authors in respect of the merger which mainly pointed at potential non-coordinated effects resulting from the merger.

Impact of size of catalogue on the quality of services to authors

67. Some market participants raised the concern, that the larger the catalogue, the more difficult it is for the publisher to have detailed knowledge of each work, its characteristics and its potential. Majors who have much larger catalogues than independents are therefore reputed to bring more attention to a limited number of successful works and authors to the detriment of less successful ones. The independents generally have the reputation of better supporting authors and paying more attention to the development and commercial exploitation of their works.
68. Several market players submitted that, like previous mergers in the music publishing industry, the proposed merger is likely to result in a reduction of staff if compared with current Universal and BMG staff in charge of promotion of publishing rights. As a consequence, the same number of works would be managed by less people, therefore

ensuring a lower quality of service to authors. As a result, authors expect that the number of authors/works actively supported by Universal/BMG after the merger will decrease²⁰.

69. However, the investigation has ultimately not confirmed that the merger will lead to competition concerns on these grounds. Competition between the publishers for authors takes place when an author is looking for a publisher. Competition therefore becomes relevant at the time when an author signs a contract. At that time, the author can choose between the different publishers – he is, however, "locked in" after having signed for the duration of the contract according to the terms he agreed upon when signing. Promotional services of lower quality are therefore not a lack of effective competition since the author may choose between different publishers only at the time when a contract is signed, whilst the concern indicated in the market investigation mainly relates to business relations between authors and publishers once the author is "locked in" and may not be able to sufficiently influence the quality of the services provided by the publisher.
70. Authors have claimed that the contractual obligations of the publisher are rather vague. A "best effort" is often required to promote the works concerned, which does not lead to clear actions to be undertaken by the publishers with respect to the contract. The consequence is that it is difficult for an author to challenge the publisher with regard to its effective support for his works. The merger would, however, only raise competition concerns if the authors would be left with significantly reduced possibilities to switch to a different publisher after the expiry of the contract as a consequence of the deterioration in the promotional services. The market investigation has, however also not supported this second claim.²¹

Impact on the choice of authors to sign publishers

71. During the market investigation the concern was raised that the merger could reduce the authors' choice to an extent which would lead to a significant impediment of competition. It was argued that majors and independents have a different business focus which limits their substitutability.
72. Majors and independents have different characteristics with regard to their relationship with authors. Majors have the reputation of focusing more on renowned authors. They have a capacity to provide larger advances and promote international hits. Independents have the reputation to focus more on new authors to whom they propose tailor-made support. They also pay higher royalty rates. Independents often explore new trends and styles, which once successful are further developed and exploited by majors.

²⁰ Questionnaire to authors associations – phase 2. **Q 11a**

²¹ A proxy to measure how a catalogue is exploited is to calculate the average revenue per work. This analysis does not show any evidence that smaller catalogues enjoy a better exploitation as measured in terms of revenue per work. Majors even enjoy larger average revenue per work, which might however be explained by the larger proportion of international hits in their catalogues. (The average revenue per work is 3 to 4 times higher for the major publishers (EUR 300-600 per work) than for independents (EUR 50-200 per work). A few large and international independents reach the level of revenue of the majors.) The same analysis conducted only on independents' catalogues does not either provide evidence of a better exploitation of smaller catalogues. (When considering independents only, the revenue per work varies from EUR 50 to EUR 200 per work and is not correlated to the size of catalogue.)

73. Authors claimed that after the merger of Universal and BMG, their choices to sign a major will decrease and raise competition concerns. However these concerns are not confirmed by the market investigation. The competition to sign authors appears to be fully effective. Majors and independents actively seek to sign new authors through participation in concerts, music conferences, networking, contacting record companies, developing links with the artistic community, etc.
74. As explained above, majors tend to focus on renowned authors. It is mainly those established authors who will be eligible for large advances whereas the new authors (who are more risky for the publishers) will often not receive such an up-front investment into their future songs. The market investigation has shown indications that the large publishers compete with each other in particular with regard to established authors, generally through direct negotiation or, in the case of the very successful authors, even through bidding contests.²²
75. After the merger, the authors seeking large advances will still have a choice between four majors (Universal/BMG, EMI, Warner, Sony). In terms of market shares, Universal will be in a leading position after the merger but will be closely followed by EMI and Warner. The existence of at least two comparable publishers leaves sufficient room for switching possibilities should Universal/BMG decide to deteriorate the terms offered to authors following the merger. Apart from the fourth major Sony there are moreover, a few larger independents (e.g. Chrysalis) who are in an intermediary position and can also compete for renowned authors through the payment of large advances. The market investigation has also not shown any tight capacity constraints which would prevent Universal's competitors from signing additional authors who want to leave Universal following the merger when signing a new contract.
76. The market investigation confirms that publishers need to permanently renew their catalogue to maintain its value. This is highlighted by the table below where the active deals are deals where the author is still under contract and continues to produce new works. The percentage of turnover achieved through the exploitation of the works produced under these active deals is significantly higher than the share represented by works produced under active deals. In simplified terms, most recent works generate more revenue than oldest ones. This has been confirmed by majors and independents.

	Active deals		
	Number	%of total number of works	% of total publisher turnover
Universal	[...]*	[<10]*%	[>25]*%
BMG	[...]*	[<30]*%	[>50]*%

Source: Universal/BMG

77. This reflects the necessity for publishers to permanently renew their catalogue. This occurs in two ways: issuing of new works by signed authors and signing of new authors. Publishers, notably majors, therefore have a strong incentive to attract the most promising new authors or established ones, resulting in a competitive market for the signing of

²² Cf. Warner Chappell Music: "[...] it is rare that WCM signs someone who has not also received an offer from at least one other publisher" Questionnaire competitors (majors)1 – Q24.

authors. Independents confirm that they also actively compete to sign authors, even if majors have an advantage in terms of financial capacity and support to develop international hits.

78. The market investigation has moreover shown indications that the retention periods are becoming shorter. The retention period is the time period in which a publisher can exploit a song which was written by the author while under a contract with the publisher. All the majors and about half of the independents who responded to the market investigation indicated that they sign contracts for a shorter period than the life-time of copyright (70 years after death of the author). Half of the independents continue to sign contracts for the life of copyright. This appears to be a significant evolution compared with the situation in the past when, according to the profession, the majority of rights were transferred for the life-time of the copyright. Consequently, the authors' possibilities to switch will not only affect new songs to be written in the future but also, to an increasing extent, older songs for which the retention period expires.
79. The switching possibilities are even greater for those authors who are not seeking large advances. Those authors will still have the possibility to sign a publisher among the majors or all independents, where attractive offers can be found.

Sister companies (publishing & record)

80. The majority of independent competitors indicate that it is common practice for major companies to encourage singer-songwriters to sign with both the record and the publishing branches of the major. This also applies to authors who are not singers, who can be encouraged to sign with the publishing branch of the major recording their works.
81. Universal appears to integrate its publishing and recording business more closely than other music companies. [30-40]*% of its top 500 authors are also signed with (for singer-songwriters) or recorded by Universal, whereas Universal has a market share in the record industry of only [20-30]*%. This deviation is also observed within other major music companies. More generally, the majors do not confirm this practice and at best acknowledge that exchanges of information take place between their record and publishing branches. However EMI recently stated in a press release (12 January 2007 - where the company highlights the key elements of its strategy for the next period) that it aimed at "*Extracting revenue and cost synergies between recorded music and music publishing*".
82. The market investigation indicates that when authors are encouraged to sign with a publishing sister company, it is more commonly the record company that provides this "encouragement". However, it might happen that the publisher takes the initiative.
83. Many independents claim that this practice is detrimental to their business, as they cannot compete with the majors on this ground. However, this practice is also common within the independent publishers who also control a record company.
84. Authors have a mixed view on this issue, with half considering that it is common practice and the other half not reporting it²³. Several authors stress that this practice is a means to

²³ Questionnaire to authors– phase 1. Q 17 – 45% of authors considers it is common practice to be "encouraged" to sign with sister record company versus 55% who do not report it.

increase the margin within the music company, and that it is more common with the majors than with the independents. Others state that authors, notably new singer-songwriters, might have a direct interest in signing with the publishing and the recording branch of the same company as it is a guarantee to release an album. With regard to established singer-songwriters, they have enough negotiation leverage to impose their conditions.

85. However, the merger only concerns the publishing activities of Universal and BMG. The merger will not have an effect on the recording branch of Universal. Generally, the latter will not have a greater possibility to require authors to sign with its publishing branch than before the merger. The merger will therefore not strengthen the parties' market position in the market for publishing services to authors on the basis of Universal's (unchanged) recording activities.
86. Universal might after the merger have an increased capacity to influence singer-songwriters currently signed with BMG to sign a recording deal with Universal's recording arm. However, the current market situation shows that doing so is not a condition for signing a deal. It is therefore not likely, that Universal's influence on these BMG singer-songwriters would actually translate into additional recording contracts. Considering, moreover, that only a portion of all BMG authors are singer-songwriters, this effect cannot be considered as significant and would – if at all – take place only in the long-term with the successive expiry of the existing recording contracts of those singer-songwriters. With regard to authors who are not singers and who are signed with BMG, the merger will be neutral as they are already under contract.

3. Coordinated effects

87. The market investigation has, moreover, not shown any indications which would suggest potential coordinated effects as a result of the merger. Every major publisher has a large number of authors under contract (several hundred). There was no indication that the exact terms on which a publisher signs these authors could be transparent to the competitors. Also the unpredictability of the different authors' success appears to render coordination on prices or other conditions difficult. It is, moreover, likely that competition from those larger independents which are in an intermediary position between majors and independents (e.g. Chrysalis,) would be able to counteract any coordinated strategy by Universal/BMG, EMI and Warner (and potentially Sony).

4. Conclusion

88. For all the above reasons, the Commission therefore concludes that it is not likely that the proposed concentration would lead to competition concerns due to non-coordinated or coordinated effects on the markets for publishing services to authors. The merger therefore does not impede effective competition on the market for publishing services to authors.

B. MARKETS FOR THE EXPLOITATION OF MUSIC PUBLISHING RIGHTS

89. The analysis of the affected markets for the exploitation of music publishing rights differs according to the role taken by the collecting societies in the exploitation of the specific right. As already indicated in the market definition, the collecting societies' role varies

across the different publishing rights. While print and synchronisation rights are generally managed by the publishers directly without any involvement of the collecting societies, mechanical and performance rights are normally administered via the collecting societies, without any direct licensing on part of the publishers.

90. A particular situation applies to online rights as a mixture of mechanical and performance rights. Online rights have so far been administered in the same way as the mechanical and performance rights for traditional applications, i.e. via collecting societies. However, recently, this market has been undergoing significant changes. These changes will lead to a form of rights administration which is comparable to direct licensing while, at the same time, collecting societies will remain involved, albeit in a different role from mechanical and performance rights for traditional applications.
91. This leads to differing results in the assessment of this case:
- *Synchronization and print*: As will be shown in the following analysis, the merger does not raise any competition concerns in the synchronization and print rights markets. The market investigation has shown that in the synchronization rights market sufficient alternatives will remain available for the customers of synchronization rights after the merger. As already found in the decision addressed to the parties pursuant to Article 6(1)c of the Merger Regulation, there is no significant overlap in the market for print rights as Universal has only marginal activities in this field.
 - *Mechanical and performance*: In the markets for mechanical and performance rights the merger results in a substantive overlap. Nevertheless, the merger does not lead to competition concerns due to the strong role of the collecting societies in the administration of these rights which limits the publishers' independence in pricing.
 - *Online*: The limitation in the publishers' independence in pricing, as it applies for mechanical and performance rights in traditional applications, is, however, currently being removed for the mechanical part of online rights in Anglo-American repertoire due to the on-going withdrawal initiatives. As will be shown, the significant overlap of the parties' activities leads to serious doubts, which are, however, removed by the commitments offered by the parties.
92. In this Decision, the analysis of the rights administered directly by the publishers will precede the assessment of those markets in which the collecting societies are involved. With regard to the latter assessment, the collecting societies' role will first be described in general terms in order to then differentiate between the effects of the merger according to the extent of the collecting societies' involvement in the exploitation of mechanical, performance and online rights and in particular the impact of the publishers' withdrawals from the traditional system with respect to online rights.

1. Rights administered directly: Synchronization and print

1.1 Synchronisation rights

93. In the following analysis the concept of synchronisation rights must be understood in the following sense:

- a. rights that are purchased in order to synchronize a musical work with a visual image for incorporation in an audio-visual work such as a film, TV program or TV advertisement,

and

- b. only when those rights are directly commercialised by the publishers.

94. For the purpose of this analysis, licences commercialised by the collecting societies to synchronise musical work with videos are not considered, because they are subject to similar competition conditions as those prevailing for traditional mechanical and performance rights. Notably, the blanket licences granted by collecting societies to TV channels in certain countries, for synchronisation of video and musical works, are therefore not considered in the following analysis. According to the market investigation, these synchronisation blanket licences account for less than 5% of the total synchronisation turnover of publishers.

1.1.1 Market structure

95. Following the proposed transaction, Universal would become the largest music publisher for synchronisation rights on an EEA-wide level as well as in seven Member States as the following table shows:

Market shares for synchronization rights (2005)

Synchronization	Universal	BMG	Merged	EMI	Warner	Sony	Others
	%	%	%	%	%	%	%
Austria	[10-20]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Belgium	[0-10]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Czech Republic	[0-10]*	[0-10]*	[10-20]*	[30-40]*	[20-30]*	[0-10]*	[10-20]*
France	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Germany	[0-10]*	[0-10]*	[10-20]*	[20-30]*	[20-30]*	[0-10]*	[30-40]*
Greece	[0-10]*	[10-20]*	[20-30]*	[30-40]*	[20-30]*	[0-10]*	[0-10]*
Hungary	[20-30]*	[0-10]*	[20-30]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*
Italy	[10-20]*	[10-20]*	[30-40]*	[20-30]*	[10-20]*	[0-10]*	[0-10]*
Netherlands	[0-10]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Poland	[10-20]*	[30-40]*	[50-60]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*
Spain	[10-20]*	[30-40]*	[50-60]*	[10-20]*	[10-20]*	[0-10]*	[0-10]*
Sweden	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
United Kingdom	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
EEA	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*

Source: Parties' estimates

96. The combined market share of Universal and BMG would exceed 30% in Italy as well as in Poland and Spain. In the latter two countries, the parties would according to their own

estimates even reach market share of slightly more than 50%. In those countries where the merged entity would take the lead, EMI or Warner would follow as second strongest competitors. In a number of countries (Austria, Belgium, Czech Republic, Greece, Netherlands), EMI would remain the leading player even after the merger.

97. The market investigation has broadly confirmed that the merged entity will obtain a strong position on the market for synchronization rights but is very unlikely to reach more than 30%. The market share estimations provided by the parties may, in some instances, even have overstated the merged entity's position, e.g. in Spain (10-20% in Spain/Portugal instead of [50-60]*% as estimated by the parties). According to estimates derived from the market investigation, EMI will remain the market leader on the market for synchronisation rights in the EEA following the merger between Universal and BMG. Universal/BMG and Warner will be on a pair.
98. The share of the independents was derived from their market share in the synchronisation market as described by the parties. According to the market investigation, synchronisation deals account for 5 to 15% of independents' turnover. However, it is hardly feasible to estimate the market share of independents in the market for synchronization rights. Therefore the parties' estimates relying on the market share of independents in the global publishing market have been considered. Nevertheless, the position of Universal/BMG cannot be considered as dominant in any market as the other majors enjoy a high share of the market. Even without any independent publisher active on this market, the position of Universal/BMG would therefore not be dominant.

	Universal	BMG	Universal/ BMG	EMI	Warner	Sony/ATV	Independents⁽¹⁾
Austria/Germany	[10-20 %]	[0-10 %]	[10-20 %]	[20-30 %]	[10-20 %]	[10-20 %]	[20-30 %]
Benelux	[0-10 %]	[0-10 %]	[0-10 %]	[20-30 %]	[30-40 %]	[0-10 %]	[20-30 %]
France	[0-10 %]	[10-20 %]	[20-30 %]	[10-20 %]	[10-20 %]	[10-20 %]	[30-40 %]
Greece	[0-10 %]	[10-20 %]	[20-30 %]	[30-40 %]	[20-30 %]	[0-10 %]	[0-10 %]
Italy	[10-20 %]	[10-20 %]	[30-40 %]	[20-30 %]	[10-20 %]	[10-20 %]	[0-10 %]
Nordic countries ⁽²⁾	[10-20 %]	[0-10 %]	[20-30 %]	[10-20 %]	[10-20 %]	[0-10 %]	[30-40 %]
Spain/Portugal	[0-10 %]	[10-20 %]	[10-20 %]	[20-30 %]	[10-20 %]	[10-20 %]	[20-30 %]
United Kingdom/Ireland	[0-10 %]	[10-20 %]	[20-30 %]	[20-30 %]	[20-30 %]	[0-10 %]	[20-30 %]
Poland	[10-20 %]	[20-30 %]	[30-40 %]	[0-10 %]	[0-0 %]	[30-40 %]	[20-30 %]
Czech Republic	incomplete - data not recorded						
Hungary	incomplete - data not recorded						
EEA	[0-10 %]	[10-20 %]	[20-30 %]	[20-30 %]	[10-20 %]	[0-10 %]	[20-30 %]

EEA synchronisation market shares 2005 – source: EC Market investigation – ⁽¹⁾ Independents data have been estimated - ⁽²⁾ Denmark, Finland, Sweden, Norway

99. Following this methodology, Universal/BMG would lead the synchronisation market in France, Italy and in the Nordic countries, not far ahead of EMI. However, the merged entity would not reach market shares far ahead of the other competitors in any affected country. Countries where the parties would reach potentially critical levels of market shares would be (according to the parties' and/or the Commission's estimates) the national markets in Italy, Spain and Poland. Like in the other affected geographic markets, the merger is not likely to lead to competition concerns in those three Member States, as the following analysis demonstrates.

1.1.2 Analysis

(1) Characteristics of the synchronization rights markets

100. Synchronisation rights are purchased for the inclusion of musical works in advertising, movies or TV programs. To a much smaller extent, synchronization rights are also used in computer games and corporate presentations. They can also be purchased for digital applications such as video streaming; however this latter category is not analyzed here, but will be covered within the online/mobile rights since it mostly forms part of those rights.
101. The final customer (company requesting the advertisement, film producer, TV broadcaster) generally relies on an intermediate, such as an advertisement company, to identify musical works of potential interest for the application requested. In most cases, a pre-selection of works is proposed by the intermediate to the final customer, based on the features of the musical work and its suitability for the advertisement, film or TV show. On some rare occasions, the final customer has a specific track in mind. Therefore, in the very large majority of cases, the music is pre-selected by the agency/final customer before contacting the publisher²⁴. The final decision is usually taken either by the final customer or by the final customer together with the agency. Music companies are generally not involved, but in a few cases can make suggestions.
102. Synchronisation deals cover the following items: exclusivity, price, number of advertisement versions, territory, media concerned, and duration. Works are generally licensed to local publishers²⁵ and often concern international music²⁶. The geographical scope of the licence is national in one case out of two. The price is in general a percentage of the advertisement budget (1-5%) or film budget.
103. Synchronisation customers have the specific feature in the music industry that they do not need to have access to the complete music repertoire unlike other customers in the music industry such as record companies, radios, online music providers, etc. They negotiate each contract to have access to the rights related to one unique musical work.
104. Classical music represents a small minority of deals²⁷. Contemporary music is also in slightly greater demand than older works. Back catalogue is nevertheless an important asset in this business as chart relevant and non-chart relevant works are in equivalent demand.

²⁴ Questionnaire to synchronisation customers – phase 2. **Q 7 C** – 75% of respondents submitted that they preferably rely on an intermediate to pre-select a first set of titles.

²⁵ Questionnaire to synchronisation customers – phase 2. **Q 4** – 76% of titles are licensed from local publishers, including local subsidiaries of international publishers.

²⁶ Questionnaire to synchronisation customers – phase 2. **Q 6** – 70% of titles are extracted from international repertoires

²⁷ Questionnaire to synchronisation customers – phase 2. **Q 28** – 7% of titles are part of the classical repertoire.

105. All deals are different and are negotiated on a case by case basis²⁸. Some TV or online providers submitted that they sign blanket licences for specific TV or online applications. They are however in a different situation from usual synchronisation customers as they need the full repertoire for their daily business.

(2) Non-coordinated effects

106. The market investigation has shown that the merger will not lead to a significant impediment of effective competition as a result of non-coordinated effects in any of the affected geographic markets. Following the merger, Universal/BMG will significantly increase their market share on the market for synchronisation rights in the EEA. Universal/BMG will overall be comparable to EMI and on a par with Warner. As indicated above, only in Spain, Italy and Poland might the parties' combined market shares (according to the parties' estimates) reach critical levels. A number of practices revealed by the market investigation indicate, however, that Universal will not be in a position to impose higher prices for synchronization rights in any of the affected geographic markets.

Switching

107. Principally, synchronisation customers generally need to purchase one or a few single musical works, for example for an advertisement spot on TV or a movie. The selection of the work to purchase is done without the support of the publisher in most cases and customers usually contact the publisher via an intermediary (such as media consultants or advertising agencies). The customers therefore clearly do not select a publisher or a publisher's catalogue, but a song. The publisher is therefore in a 'waiting position' and will negotiate the terms and conditions of a synchronization licence on a case by case basis when approached by a customer.
108. Customers confirmed that they do not feel attached to any publisher, whatever its size. In particular, they confirm that the works are largely substitutable and that when the financial conditions offered for one work do not meet their expectations, they do not have problems identifying another musical work for which acceptable conditions can be agreed upon. The vast majority of customers²⁹ consider that it is even realistic to switch from one "genre" of music to another and/or from one music work to another (within the same "genre").
109. After the merger, there will therefore still be a large number of alternatives since all catalogues of the larger publishers contain several thousand different titles. A customer looking for a song for an advertisement spot will still be able to choose among thousands of songs from the other majors' and independents' catalogues even if Universal should take a leading position in terms of market shares in some countries, such as Spain, Italy and Poland.

²⁸ Questionnaire to synchronisation customers – phase 2. **Q 12**– 96% of deals are negotiated on a case-by-case basis

²⁹ Questionnaire to synchronisation customers – phase 2. **Q 27** – 83% of respondents submitted that titles are substitutable.

110. Customers report that it happens occasionally that a publisher does not grant a synchronisation licence. However the explanations varied; e.g. it was the author who refused to licence the song, or the negotiation delays were too long. Even in cases where no agreement on the granting of a licence was reached, customers could find a substitute which confirms that a sufficient number of alternatives is available to the customers.
111. The market investigation has also not confirmed that a large catalogue would be a decisive element for final customers or intermediaries in choosing a specific publisher. Customers have a mixed view on the importance of working with publishers who have a large catalogue³⁰. However, they are not interested by the size as such but rather by the possibility for a publisher to propose alternative songs when conditions cannot be agreed upon for a specific work or when suggestions are requested. However, all majors and the stronger independents, such as Chrysalis and Peer, have large catalogues with a sufficient number of works constituting credible alternatives. The larger catalogue that Universal will have after the merger will therefore not create a dominant position or allow Universal to unilaterally increase prices due to a lack of adequate possibilities for the customers to switch to other publishers in the market for synchronization rights.
112. This was confirmed by the responses of the customers in the market investigation. With regard to the merged catalogue of Universal and BMG, synchronisation customers consider that Universal/BMG would not be in a stronger position than its main competitors³¹.
113. Since synchronization right customers do not need access to a complete catalogue but pick only a few titles, the enhanced size of Universal's catalogue does not give rise to competition concerns because a sufficient number of alternative publishers with a vast number of songs remains available. Synchronisation customers have the possibility to find alternative titles easily across genres.

Volatility of market shares

114. The parties, moreover, submit that the business of synchronization rights is very volatile. The market shares exhibit significant changes from year to year. According to the parties' estimates, the market share for Spain only increased to [50-60]*% in 2005, after having ranged between [20-30]*% in the two preceding years. A similar situation applies to Poland, where the parties' combined market share was [20-30]*% in 2003, [20-30]*% in 2004 and [50-60]*% only in 2005.
115. This volatility results from the revenues achieved with synchronization rights sold for a single film or advertisement spot which are mostly limited to the time period in which the advertisement spot is published or the film is shown. The terms of the contracts for advertisements are, according to the parties' information, mostly 1 year or less (3 – 6 months). Depending on the deals closed in a specific year, the market shares may therefore change significantly.

³⁰ Questionnaire to synchronisation customers – phase 2. **Q 31** – 55% of respondents consider that it is important for a publisher to have a large catalogue, vs 45% who do not consider it to be a key success factor.

³¹ Questionnaire to synchronisation customers – phase 2. **Q 32**– 65% of respondents submitted that Universal/BMG would not be in a stronger position than its competitors thanks to the merger.

116. This also becomes apparent when looking at the total revenues achieved in those countries with the highest estimated market shares (parties' estimates) Italy, Spain and Poland. Only in Italy did the revenues achieved by Universal and BMG exceed EUR 1 million each in 2005 (Universal EUR [...]*; BMG EUR [...]*). In Spain and Poland, the revenue of each of them was below EUR 1 million (Poland: Universal EUR [...]*; BMG EUR [...]*; Spain: Universal EUR [...]*; BMG EUR [...]*). Considering that the revenue for one deal may amount to EUR 0.5 million ([...]*), the potentially leading market position of the merged entity cannot be regarded as stable. It is plausible that, with a few larger deals, the distribution of market shares among the large publishers may change considerably, which reflects that Universal's market position will remain contestable.

No impact of vertical integration

117. The market investigation has also not confirmed that Universal could achieve a leading market position after the merger on the basis of its vertical integration into the recording business.
118. When including music in a video, a synchronisation customer needs to obtain two licences, one from the publisher and the other from the record company. Therefore the unique position of Universal (post-merger) of controlling the largest publisher catalogue and being the largest record company might be theoretically leveraged to impose market conditions in its favour, notably for titles for which Universal/BMG would control both recording and publishing rights.
119. However the market investigation highlights that even if synchronisation customers would appreciate working with a single company to simplify the acquisition of rights, this is not a key element of their decision. They would notably not accept to pay higher fees when working with a company able to grant both record and publishing rights for the work they are interested in³². Customers consider that there is enough choice proposed by other companies to switch.
120. In addition, while the publishing rights are necessary to include a musical work in an audio-visual work, the record rights can be by-passed by recording a new version. This is done in many cases by advertising companies in order to adapt the music to the advertisement and to lower the costs when the record company's demands exceed what the customers are ready to pay. As the music comes in support to an audio-visual work, the artist is not the key element of the final product.
121. Moreover, Universal/BMG would only control both recording rights and complete publishing rights over a minority of the titles in which it has an interest. For instance, in Germany, Universal/BMG completely controls [10-20]*% of the titles in which it has both recording and publishing rights³³. In France, this control is as low as [0-10]* %, and

³² Questionnaire to synchronisation customers – phase 2. **Q 20**– 86% of respondents submitted that they would not accept to pay higher fees to a company for the reason that this company is able to propose a single package of recording and publishing rights.

³³ Based on the 2006 official top 100 charts in affected countries. Numerator: top 100 titles for which Universal/BMG controls both recording rights and 100% publishing rights. Denominator: top 100 titles for which Universal/BG controls either recording rights or a share of publishing rights. Austria – [10-20]*%; Belgium – [0-10]*%; Czech Republic – [10-20]*%; Finland – [0-10]*%; France – [0-10]*%; Germany – [10-

in the United Kingdom as low as [0-10]*%. This implies that focusing specifically on titles for which it has full control, would force Universal/BMG to decrease the commercial exploitation of the very large majority of works in its catalogue (both in recording and publishing).

122. Synchronisation customers are able to find a substitute relatively easily and have the possibility to record a new version of the musical work. Therefore a strong position in the record industry is an asset, but is unlikely to allow for changing the balance of negotiation. It is therefore unlikely that Universal/BMG could leverage any market power stemming from the vertical integration between publishing and recording activities in the market for synchronisation rights.

Conclusion on non-coordinated effects

123. It is very unlikely that the merged entity will achieve a critical market position. Even on the basis of the most critical market share estimates, it is not likely that competition concerns could arise since the merged entity's market position will remain contestable as a result of the fact that a sufficient number of alternatives will remain. Customers can easily switch between songs and publishers. The merger will therefore not lead to a significant impediment of effective competition on the basis of unilateral effects in the market for synchronization rights.

(3) Coordinated effects

124. It is also unlikely that the merger could lead to competition concerns on the basis of coordinated effects on the market for synchronization rights.
125. The market for synchronisation rights is such that two deals are rarely comparable in terms of price, duration, territory, media, and renown of work. For instance, two advertisements generally cover different products, address different target customers and therefore rely on different musical works. Musical works can be acquired for different periods and licences might cover different geographical areas. Therefore synchronization contracts are highly heterogeneous, and do not favor a coordinated approach of the majors.
126. In addition, according to the *Airtours*³⁴ and *Impala*³⁵ judgments, one of the conditions to be met to characterize a collective dominance on a market is sufficient market transparency, so that each member of the dominant oligopoly has the ability to know how the other members are behaving in order to monitor whether or not they are adopting the

20]*%; Greece – [0-10]*%; Hungary – [0-10]*2%; Italy – [10-20]*%; Netherlands – [0-10]*%; Norway – [0-10]*%; Poland – [10-20]*%; Spain – [10-20]*%; Sweden – [0-10]*%; United Kingdom – [0-10]*%.

³⁴ T-342/99 (*Airtours/Commission*), [2002] ECR II-2585.

³⁵ T-464/04 (*Impala/Commission*).

common policy. It can be inferred from the market investigation that such a transparency is not achievable in the synchronization market considering the large spectrum of deals³⁶.

127. Some synchronisation deals include a "Most Favoured Nation Clause"³⁷ with regard to the most preferential conditions and terms of the contracts. However this cannot be regarded as an indication for a degree of overall transparency which would allow to tacitly coordinating. This clause is notably applied in synchronisation deals to ensure that record and publishing company controlling a title obtain an equivalent share of the deal (which is difficult to obtain when the work (publishing) and the performer (recording) do not have the same notoriety).
128. In addition, the market investigation confirmed that customers do not consider that there is transparency on prices³⁸.
129. Synchronisation customers consider that the concentration will not facilitate the coordination between majors³⁹. It can be concluded that conditions for coordination in the market for synchronisation rights are unlikely to be met.

1.1.3 Conclusion

130. For all the above reasons, it is therefore concluded that it is not likely that the proposed concentration would create competition concerns. The merger, therefore, does not lead to a significant impediment of effective competition on the markets for synchronization rights.

1.2 Print rights

131. Print rights are regularly licensed directly by the publishers without any involvement of collecting societies. The print rights market is rather small in size (EEA-market volume EUR [...] million in 2005 according to the parties' estimates) with specialized publishers. Universal is mostly not active in this market. The merger will, therefore only lead to a marginal overlap in the Netherlands and at EEA-wide level as the following table shows:

³⁶ Several publishing companies provided examples of synchronisation deals varying from EUR 1 000 to several hundreds thousand euros, covering different geographical areas, different time periods, etc.

³⁷ The MFN clause stipulates that when purchasing synchronisation rights for several works from different publishers, if one publisher benefit from more advantageous conditions, these conditions will apply to all publishers involved in the deal. The MFN also applies when only one title has to be purchased by a customer, and ensures that the record company and the publisher who commonly control this title will receive an equal share of the deal. Questionnaire to synchronisation customers – phase 2. **Q 14**– 84% of synchronisation customers reported the existence of MFN clause in their contracts.

³⁸ Questionnaire to synchronisation customers – phase 2. **Q 33** – 79% of respondents did not believe that the prices they negotiate are known by competitors.

³⁹ Questionnaire to synchronisation customers – phase 2. **Q 42**– 65% of respondents consider that the merger will not facilitate coordination between the majors.

Print	Universal	BMG	Merged	EMI	Warner	Sony	Others
	%	%	%	%	%	%	%
Hungary	[0-10]*	[70-80]*	[70-80]*	[0-10]*	[0-10]*	[0-10]*	[20-30]*
Italy	[0-10]*	[30-40]*	[30-40]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Netherlands	[0-10]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[0-10]*	[40-50]*
EEA	[0-10]*	[0-10]*	[0-10]*	[0-10]*	[0-10]*	[0-10]*	[70-80]*

132. The market shares in Hungary and Italy also exceed 15%. However, there is no overlap.
133. It is therefore unlikely that the merger could lead to competition concerns in any of the affected national markets or at EEA-wide level.

2. Rights traditionally administered via collecting societies: Mechanical, performance and online

2.1 Background: Collecting societies

2.1.1 The current system of collecting societies

134. Collecting societies are organizations which were established to act on behalf of right owners in order to relieve the administrative burden of licensing publishing rights, monitoring the use of music and collecting royalty income. Collecting societies generally control the licensing of both mechanical and performance rights, including online rights which are composed of the previous two.⁴⁰ They may require an assignment of rights from the right-holders, or an exclusive licence to grant licences to users of music.
135. Authors usually become members of the collecting society in their country of residence. They thereby entitle their collecting society to administer their mechanical and performance rights, including online rights⁴¹. It is then the collecting societies' task to grant licences and collect the royalties from the users. For this, the collecting society retains a percentage of the royalties collected as commission fee. The net royalties collected are shared between the authors and their publishers.
136. The publishers' receive a part of the royalties as compensation for the advances they had paid to the author and the publishing services they provide to the author. In their classical role, the publishers' main service would consist in helping the author to establish a contact with a record company with a view to the author's song being chosen by the record company for one of their performing artists and subsequently recorded. For this, the recording companies need to have licences for the relevant publishing rights. They

⁴⁰ Certain exceptions apply. For example, the performing right societies do not always administer the so-called "grand rights" (performances of dramatico-musical works and ballets). In the United Kingdom, Germany and Scandinavia, for example, these performances are licensed directly. On the other hand, in France, Italy, Greece, Spain and the Netherlands "grand rights" are licensed through societies

⁴¹ Normally, synchronization rights (rights to combine music with pictures, e.g. in movies and advertisements) and print rights (rights to print sheet music) are not licensed via the collecting societies but directly by the publishers.

acquire these as blanket licences from the collecting societies who subsequently collect from them a share of the revenues made by selling the CDs containing the respective song.

137. In the case of online music providers a similar situation exists: In order to be able to offer the song on a downloading platform they have to acquire a licence over the author's publishing right from the collecting society. However, in addition, they also have to acquire a licence from the recording company for the recording rights which protect the individual interpretation of a song and which are originally partly in the hands of the recording company and partly in the performing artist's hands. The performing artist normally transfers them to the record company. As a consequence, a share of the online music provider's revenue made by selling the song as a downloading track will subsequently go as a license fee to the performing artist/record company and another share to the author and his publisher via the collecting societies.
138. In order to grant licenses and collect royalties also from users abroad, the collecting societies co-operate worldwide on the basis of so-called "reciprocal representation agreements". These representation agreements give each one of them the right to license not only the repertoire of their own members but also the repertoire of all associated collecting societies (this complete repertoire will hereinafter be referred to as "world repertoire" even though there might be exceptionally collecting societies which do not participate in this system). However, on the basis of these agreements, these licences are, currently only granted for the use of music within the country where the collecting society in question is located. Each collecting society in principle has the right to license the repertoire of its own members EEA- or even worldwide. On the basis of the reciprocal agreements, however, each collecting society limits the scope of its licences for the complete repertoire administered, including both the works of the own members as well as the other collecting societies' works, to its own country. At the same time each collecting society collects royalties from users in its own country not only for its own members but also for the authors and publishers abroad who are members of the associated collecting societies.
139. Collecting societies are normally considered dominant in their respective countries. They are for this reason bound by non-discrimination obligations and are not allowed to refuse licences. As a consequence, they usually charge a uniform price for the whole repertoire (only differing per category of use).

2.1.2 Commission's Recommendation concerning online rights

140. So far, mechanical, performance and online rights have been all managed in the traditional system of collecting societies. The pricing decisions in this system are made by the collecting societies. However, due to their dominant positions, the collecting societies are regularly obliged to charge non-discriminatory tariffs and are not allowed to refuse licences to customers. Consequently, they are not usually allowed to charge different tariffs to the right-users –differences in tariffs only apply with respect to different forms of exploitation. The music of all member authors and publishers is normally covered by a blanket licence which defines a uniform price for all titles and users of one right category. Publishers can normally only indirectly influence the tariffs for those licences via their representation on the boards of the collecting societies which, however, usually restrict the number of seats available to publishers.

141. In this traditional system, international music users need to get licences over the worldwide repertoire from the respective collecting societies in each of the countries in which they want to operate. The disadvantages of geographically limited licences were considered as particularly harmful for the development of the online music business. To address this problem in the online music business, the Commission has affirmed that right-holders should be able to withdraw their rights from the traditional collecting societies system in order to transfer them to one or more selected collecting societies for their EEA-wide administration. Right-holders may be publishers and authors who control the relevant rights to differing extents due to the specific features of rights management in the Anglo-American repertoire and the Continental European repertoire.
142. The lack of EEA-wide licences for online applications has already been under discussion for some time. The collecting societies themselves have attempted to create a system which allows for multi-territorial licensing. The so-called "Santiago agreement" (signed at a CISAC⁴² Congress in Santiago de Chile) was concluded between a number of collecting societies in 2001 and allowed for global performance right licences for internet broadcasting. However, the agreements contained a customer allocation provision which restricted the broadcasters to acquiring a multi-territorial licence only from the collecting society in the country in which they operated and resided economically (economic residency clause). In 2004, the Commission issued a statement of objections against the Santiago agreement and in particular the economic residency clause. The Santiago Agreement expired at the end of December 2004 and was subsequently not renewed.
143. In parallel to the Santiago agreement dealing with performance rights, the association of collecting societies in charge of mechanical rights, the "Bureau International des Sociétés Gérant des Droits d'Enregistrement et de Reproduction Mécanique" ("BIEM"), adopted a similar standard contract at its general meeting in Barcelona – the "Barcelona agreement" - for the corresponding mechanical rights, in 2001. Following the discussions on the Santiago Agreement, also the Barcelona Agreement was not renewed after its expiry at the end of December 2004.
144. In 2005, the Commission issued its Recommendation with respect to online rights: the Commission Recommendation on collective cross-border management of copyright and related rights for legitimate online music services (the "Recommendation") which addressed the issue of EEA-wide licensing in the online sector. The Recommendation was based on a preceding Commission Staff Working Paper ("the Working Paper") concerning Cross-Border Collective Management of Copyright⁴³ in which the Commission identified several problems with respect to the licensing of online rights.
145. The Working Paper examined the existing structures for cross-border collective management of copyright for the provision of online music services and concluded that the absence of EU-wide copyright licences for online content services makes it difficult for these music services to develop. In order to improve cross-border management of copyright, the Working Paper considered three options: (1) do nothing (Option 1); (2) improve the current system by eliminating territorial restrictions and discriminatory

⁴² Confédération Internationale des Sociétés d'Auteurs et Compositeurs

⁴³ Commission Staff Working Document - Study on a Community Initiative on the cross-border collective management of copyright, 7 July 2005.

provisions in the reciprocal representation agreements concluded between collecting societies (Option 2); or (3) give right-holders the choice to authorise a collecting society of their choice to manage their works across the entire EU (Option 3).

146. The Working Paper concluded that Option 3 would offer the most effective model for cross-border management. With respect to cross-border licensing, allowing right-holders to choose a collecting society outside their national territories for the EU-wide licensing of their works, would create a competitive environment for cross-border management of copyright. The Working Paper found that the right-holders' freedom to choose any collecting society in the EU would be an incentive for these societies to provide optimal services to all their right-holders, irrespective of their location.
147. While Option 3 explicitly referred to competition between collecting societies for right-holders (authors and publishers), Option 2 would – by removing the territorial restrictions in the reciprocal agreements – introduce the possibility for each collecting society to grant multi-territorial licences over the complete world repertoire and thereby focus on competition between collecting societies for right-users, who could choose their access point to this world repertoire. The Working Paper favoured Option 3 since it would not only introduce competition between collecting societies for right-holders, but at the same time would allow collecting societies to build up their own attractive repertoires for users. In the Working Paper it was expected that different prices would develop for these different repertoires.
148. The subsequent Recommendation consequently stated in paragraph 3 that "Right-holders should have the right to entrust the management of any of the online rights necessary to operate legitimate online music services, on a territorial scope of their choice, to a collective rights manager of their choice, irrespective of the Member State of residence or the nationality of either the collective rights manager or the right-holder" which reflects the withdrawal possibility indicated in option 3.⁴⁴ While the exact forms of withdrawal and subsequent licensing in a market following option 3 are still developing, some features are apparent: In a restructured market after a withdrawal of rights by authors and publishers from the traditional collecting societies system, an international music user would receive EEA-wide licences from the collecting society or societies in charge. These licences would no longer cover the world repertoire, but only the repertoire which is represented by the specific collecting society and its member right-holders who selected this collecting society for the EEA-wide administration of their rights.

⁴⁴ It is worth noting, that the possibility for right holders to withdraw and transfer their rights to one collecting society has been established notably by the "GEMA" Decision (case IV/26760 of 2 June 1971, OJ L 134/15 of 20 June 1971). This principle has been reaffirmed by the Recommendation. Apart from this, the Commission has recently taken a preliminary position against territorial restrictions and restrictions of membership in the CISAC-case (COMP/C2/38.698) in which a Statement of Objections has been issued. With respect to public performance rights, collecting societies have concluded reciprocal representation agreements based on a non-mandatory model of CISAC (The International Confederation of Societies of Authors and Composers). The Commission considers that certain aspects of the agreements might infringe Article 81 of the EC Treaty with respect to the membership restrictions which oblige authors to transfer their rights only to their own national collecting society and the territorial restrictions, which oblige commercial users to obtain a licence only from the domestic collecting society and limited to the domestic territory. The territorial restrictions raise competition concerns in particular in view of certain new forms of distribution, such as internet licensing, satellite transmission and cable retransmission.

149. In the framework of this merger assessment, no position is taken on the withdrawal of rights as such. The withdrawal initiatives already undertaken or likely to be started in the near future show the development of the market which needs to be taken into account in the merger analysis since it defines the competitive conditions under which the merger will show its effects. The following assessment therefore analyses the effects of the merger in a restructured market and compares the situation on the restructured market without the merger with the situation with the merger.

2.1.3 Withdrawal of rights from the current collecting societies system

150. Since the Recommendation was issued, several publishers have started to withdraw rights from the traditional system of collecting societies in order to give the rights to one or more selected collecting societies. All initiatives relate to online applications and mostly focus on Anglo-American mechanical rights as part of the affected online rights. The main reasons why publishers focus on mechanical rights for Anglo-American repertoire result from the differences in the administration of rights.

(1) Administration of rights

151. The administration of rights via collecting societies differs with respect to Anglo-American titles on the one hand, i.e. titles which are registered with collecting societies in the United Kingdom, Ireland and in the US⁴⁵, and Continental European titles on the other, even though both are part of the system of reciprocal agreements as described above. While the differences between Anglo-American and Continental European rights administration are not large with respect to *performance* rights they are substantial in the administration of *mechanical* rights.

152. One underlying reason for the differences is the historically different legal concept concerning the protection of works. In the US and in the United Kingdom, the "copyright" relates to a publisher's investment into a work. The publisher is entitled to full protection of his investment by the copyright law. In contrast, according to the originally French concept a creator of a work owns his creation and is protected by the "droit d'auteur". This concept which allocates the original control over a work to the creator spread from France throughout Continental Europe.

153. The administration of publishing rights mainly differs with respect to:

- ownership of rights and
- international contractual relations and transfer of royalties ("international administration").

154. Both aspects are intertwined and have an influence on the power of the publishers and their possibility to withdraw rights from the traditional collecting societies' system which is one pillar of the competition assessment in this case.

a. Continental European repertoire

⁴⁵ Other countries might have a similar system, such as Canada, Australia, New Zealand or South Africa. Accordingly, sometimes the term English-language repertoire is used instead of Anglo-American repertoire. Since the music from authors in the United Kingdom and in the US covers the large majority of non-classical titles, the following description will only refer to the United Kingdom and to the US.

155. *Ownership of rights:* In Continental Europe, most authors transfer their mechanical and performance rights directly to the collecting societies. They therefore do not normally transfer the rights over the works to the publishers, but rather give them a right to obtain a part of the royalties instead. The ultimate control of the mechanical and performance rights over the authors' works therefore usually remains therefore with the authors (or subsequently with their collecting societies if assigned to them) and is not transferred to the publishers. Any change as to the administration of rights would, in this system, normally need the approval of the author.
156. *International administration:* The collecting societies are entitled by the authors to do the administration as well as the international transfer of royalties within the collecting societies' system. On the basis of the reciprocal agreements, an author's collecting society will grant licences and collect royalties only on a national basis. The administration of these rights in other countries is done by the associated collecting societies in their respective countries. All associated collecting societies grant licences on a territorial basis and collect the royalties from the users in their territory.
157. The international transfer of these collected royalties from the countries of the users to the country of the author is done differently for the part of the royalties to be paid to the author and the part payable to the publisher. Generally, all collecting societies define a split of royalties between authors and publishers. This split is determined pursuant to the terms of the collecting societies' rules and reflected in their mandates with authors and publishers. The ultimate division of royalties between the author and the publisher may differ from this pre-defined split, if the publisher pays an extra portion of the royalties received to the author, in addition to the royalties paid directly by the collecting society. The split prescribed by the collecting societies guarantees a certain remuneration for the author and was established to protect the authors.⁴⁶ The shares for the two sides are called the "author's share" and "the publisher's share" respectively.
158. For the author's share, the distribution of royalties is done via the collecting societies. The collecting societies collect all the royalties for the author's work in their countries. They then transfer the author's share to the original collecting society which in turn passes it on to the member author. The publisher's share, however, will not be transferred to the original collecting society but to a local subsidiary or agent (both called "sub-publisher") of the original publisher in the respective countries.⁴⁷ These sub-publishers transfer the publisher's share of royalties to the original publisher.⁴⁸

⁴⁶ These splits vary between collecting societies as well as between the right categories. In Germany, for example, 40% of the collected net royalties for mechanical rights (after deduction of the collecting society's commission fee) will be retained by the publisher while the author retains 60%. For performance rights the publisher will usually retain 33.33% with the author receiving the rest of 66.66%. Also in the other Continental European countries such splits are applied (often 50% - 50% or 25% - 75%) which all have in common that none of the two sides involved – author and publisher – gets 100%.

⁴⁷ The parties indicate that the major music publishers are established in many Member States and as a result, their need to conclude sub-publishing deals in the EU is more limited than for many of the independents. Also the majors, however, use third-party sub-publishers in other parts of the world. Universal also has sub-publishing agreements in [...]*

⁴⁸ Since – as described above - the control over the mechanical and performance rights in Continental Europe is normally not with the publishers, the international distribution of the publisher's share generally does not take place on the basis that the sub-publisher owns the right over a work itself but only a right to the publisher's share of income.

b. Anglo-American repertoire

159. For Anglo-American repertoire different rules apply in respect of mechanical rights and in respect of performance rights.

Mechanical rights

160. *Ownership of rights:* Authors in the United Kingdom normally transfer their mechanical rights to 100% to their publishers who, in the traditional system, subsequently appoint the United Kingdom collecting society MCPS for the administration of these rights. The control over Anglo-mechanical rights is therefore normally fully transferred to the publishers who do not need the authors' approvals for decisions over the administration of these rights.
161. *International administration:* MCPS could, in principle, sell worldwide licences for the rights it administers. However, the publishers also grant territorial mechanical rights to the own sub-publishers abroad in parallel. These sub-publishers are members of their local collecting societies. They subsequently appoint their respective collecting society for the administration of the mechanical rights limited to their territory. As a consequence, the territorial scope of MCPS is restricted accordingly since its licences can only cover those countries in which no sub-publisher has the relevant mechanical rights.⁴⁹
162. Consequently, all royalties from Anglo-mechanical rights are collected internationally by the respective collecting societies in their countries. Since no split into publisher's share and author's share applies here, the complete royalties (after deduction of the collecting societies' commission fees) are transferred to the relevant local sub-publishers who pass it on to the original publisher in the United Kingdom. The original publisher will then pay out the agreed share of the royalties to the author.
163. For mechanical rights in the US a similar system applies with the difference that publishers collect mechanical royalties in the US directly from the users without any involvement from the US collecting societies. As in the United Kingdom, the US-publishers grant territorial rights to their sub-publishers in the different EEA-countries who appoint the national collecting societies for the administration of the rights. In Europe, therefore, effectively the same system applies for US-works as for United Kingdom-works with respect to mechanical rights.

Performance rights

164. For Anglo-performance rights the administration is in essence the same as for Continental European mechanical and performance rights. The United Kingdom-authors normally transfer their performance rights directly to the relevant collecting society in the United Kingdom: PRS. Control over these rights is therefore not transferred to the publishers.

⁴⁹ See MCPS-PRS' reply to Questionnaire to Collecting Societies 1, dated 7 November 2006, question 28: "The MCPS Membership Agreement is one of agency and it is concluded on the same terms regardless of whether the principal is a music publisher or writer. The member (whether writer or publisher) appoints MCPS to act as the member's sole and exclusive agent (clause 1). The appointment is not only for the United Kingdom: please see the definition of "Territory" contained in clause 6 of the Membership Agreement. Under this clause members retain the right subpublish, and be members of organisations similar to MCPS in other countries of the world; such sub-publishing and local collecting society membership overrides the Membership Agreement."

The publisher's share and the author's share are each 50%. Their international administration is managed as described above for Continental European rights.

165. For US-performance rights some specific features apply. American performance rights are typically not assigned to either a collecting society or a publisher but to both. The relevant US collecting societies are ASCAP and BMI. According to the parties, approximately 49% of the US authors are members of ASCAP and 49% are members of BMI.⁵⁰ The US authors licence their rights to the US performance collecting societies BMI or ASCAP and at the same time to a publisher. ASCAP and BMI have reciprocal agreements with the European collecting societies pursuant to which they grant them the right to licence the US performance rights for exploitation in their respective countries. The collecting societies pay the collected revenues to the sub-publishers who are members of the national collecting societies.⁵¹
166. US collecting societies also apply a split of royalties between authors and publishers in the same way as the European collecting societies do for performance rights. Both BMI and ASCAP, collect 100% of performing rights income and pay 50% to the author and 50% to the publisher. The parties confirm that the international flow of royalties is the same for US-performance rights as for Anglo-performance rights: the publisher's share goes via the sub-publishers and the author's share goes via collecting societies.

(2) Resulting withdrawal possibilities for publishers

a. Withdrawal possibility for Anglo-American mechanical rights

167. The main difference between Continental European repertoire and Anglo-American repertoire relates therefore (i) to the fact that, in the Anglo-American world, the authors' mechanical rights are completely transferred to the publishers who therefore have full control over those rights and (ii) to the sub-publishing system which fully applies to Anglo-American mechanical rights and preserves full control for the publishers over the international management of their rights. This system is to a large extent dependent on their agreements with sub-publishers as opposed to agreements with or between collecting societies.
168. While the parties disputed the possibility and scope of a withdrawal of rights by publishers, the market investigation has brought clear results as to Anglo-American mechanical rights. As described above, the Anglo-American authors assign 100% of their mechanical rights to their publishers. The publishers therefore have full control over these rights and may decide to withdraw from the traditional collecting societies system without the need for approval by the authors.

⁵⁰ The remaining 2% or less are members of the third US-collecting society SESAC.

⁵¹ While ASCAP members may grant their full rights in parallel to the publishers who assign those rights to the sub-publishers, BMI members assign their rights to the publishers only for those territories in which BMI has no reciprocal agreement with the national collecting society. The sub-publishers in the countries where BMI has a reciprocal agreement therefore do not own the rights (since the original publisher does not have them for this territory and therefore cannot assign them to the sub-publishers), but they may collect according to the BMI agreement the revenues out of the licensing which are made by the European collecting societies. Ultimately, therefore no major difference occurs between ASCAP and BMI with respect to the flow of royalties.

169. In practical terms, the withdrawal of Anglo-mechanical rights basically requires that the publishers in the United Kingdom terminate the sub-publishing agreements on mechanical rights with their sub-publishers in other countries in order to effectively withdraw these mechanical rights from the collecting societies in the different countries.⁵² With such a termination of sub-publishing contracts, the sub-publishers no longer have the right to represent the original publisher's repertoire in their respective territory for which they had been entitled to sub-publish. This "automatically" withdraws those rights from the local collecting societies since they only may grant licences and collect royalties for the repertoire which these sub-publishers represent. Some collecting societies accordingly indicated that the termination of sub-publishing agreements does not exactly qualify as a "withdrawal" since it does not require the (partial) termination of a membership agreement with the collecting society. The withdrawal effect is, however, the same as with a termination of a membership agreement. The collecting society which previously granted licences for the sub-publisher's repertoire is no longer entitled to do so for those rights which are no longer represented by the sub-publisher.
170. With such a termination of sub-publishing contracts, the original publisher in the United Kingdom gathers the rights for the Anglo-repertoire in all territories in which the sub-publishers previously were in charge. The geographical scope of the licences that MCPS can subsequently grant is – if no sub-publishing agreement is maintained – worldwide. A publisher wishing also to withdraw the rights from MCPS needs to consider the conditions under which such a withdrawal is viable according to the statutes and the membership agreement. MCPS indicates that following entry into the membership agreement a member can exclude MCPS' powers with respect to a number of right categories including online rights by giving MCPS three months notice.⁵³ With respect to American mechanical rights the publishers similarly only need to terminate sub-publishing contracts.
171. Anglo-American titles represent the majority of the non-classical popular music. Looking at the official charts in the affected countries, on average 74% of the titles are Anglo-American repertoire. The exact shares differ per country since the importance of local repertoire varies. The shares range from approximately 50% in Spain and France to virtually 100% in the United Kingdom.

b. Withdrawal possibility for Continental European repertoire

172. Rights in Continental European repertoire (as well as Anglo-American performance rights) are more difficult to withdraw from a publishers' perspective. Unlike for Anglo-American mechanical rights, here the rights are not assigned to the sub-publishers in the different territories, but are administered internationally via the network of collecting societies (only the publishers' share of royalties is transferred via the sub-publishers). A withdrawal would therefore require the (partial) termination of a membership agreement with the original collecting society to which the rights were assigned. As a consequence

⁵² It was largely confirmed by the collecting societies that a withdrawal of Anglo-American mechanical rights is easy for the publishers on the basis of the termination of sub-publishing agreements. See the responses to the Questionnaire to collecting societies 3, dated 5 February, question 8; 12 collecting societies answered to this question: 10 clearly confirmed, 2 confirmed in principle but also indicated that the actual legal effects depend on the specific agreements.

⁵³ See MCPS/PRS' answer to the Questionnaire to collecting societies 1, dated 7 November 2006, question 26.

of such a termination, neither the original collecting society nor the associated collecting societies abroad could continue to exploit these rights.

173. However, in general, it seems that it would be the authors, rather than the publishers, who could withdraw rights from the collecting societies. The parties submit that legally the publishers may not withdraw any rights, since in the Continental European system, the authors normally assign their rights to the collecting societies, whereas the publishers only receive a right to a share of the royalties, but not a right over the work itself. This would effectively prevent publishers from deciding on a withdrawal. According to the parties' submission, in Continental Europe, publishers therefore have no control over the mechanical and performance rights and would need the authors' approvals for a withdrawal. This would equally apply to Anglo-American performance rights.⁵⁴
174. The market investigation has shown, that the precise national conditions differ in this respect mainly due to often complex and intertwined provisions of the relevant national laws, the statutes and membership agreements of the collecting societies as well as the publishers' agreements with the authors. A number of collecting societies also indicate that the precise possibility of a withdrawal initiated by the publishers in the individual countries also depends on the contracts between the authors and the publishers⁵⁵ which might not be fully known to the collecting society.
175. The market investigation has largely confirmed that a withdrawal of Continental European repertoire (as well as Anglo-American performance rights) is substantially more difficult than is the case for Anglo-American mechanical rights. It is very likely that Universal could generally not withdraw the respective Continental European mechanical and performance rights without the authors' approvals. In Germany, for example, authors are regularly members of GEMA and assign their rights to GEMA under their membership agreement. They may only assign their rights to publishers to the extent that they have not been previously assigned to GEMA. This, however, generally only relates to synchronisation rights and print rights. GEMA confirms that the authors usually assign 100% of their rights to GEMA and that control over these rights is therefore with the authors.⁵⁶ The same applies to France: SACEM confirms that the authors regularly transfer 100% of their rights to SACEM, which even leads to the result that SACEM itself

⁵⁴ A specific situation applies to American performance rights. As explained above, US authors licence their rights to the US performance collecting societies BMI or ASCAP and at the same time to a publisher. ASCAP and BMI have reciprocal agreements with the European collecting societies pursuant to which they grant the right to licence the US performance rights for exploitation in their respective countries. While ASCAP members may grant their full rights in parallel to the publishers who assign those rights to the sub-publishers, BMI members assign their rights to the publishers only for those territories in which BMI has no reciprocal agreement with the national collecting society. Consequently, publishers can according to the parties bundle their ASCAP performance rights for EEA-wide administration, but the European collecting societies will nevertheless still be able to grant territorial licences for the ASCAP-repertoire which was assigned to them by the authors on a non-exclusive basis. For BMI, no withdrawal by the publishers appears to be possible where the authors have assigned the rights to BMI and in those territories where BMI has no agreement with any other collecting society.

⁵⁵ This is well reflected by AEPI in its response to the Questionnaire to collecting societies 2, Table 3: "For all rights the approval of the author depends on the agreement that he has entered into with the publisher. The publisher administers whatever the creator has assigned to him."

⁵⁶ See GEMA's reply to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 9c.

has control over the rights.⁵⁷ A withdrawal by a publisher would consequently not be possible.

176. In some other countries, there is significant legal uncertainty as to the publishers' possibilities to withdraw. According to the parties, Austrian authors, for example, assign their rights on an exclusive basis to both the collecting societies AKM (performance collecting society) and Austro Mechana (mechanical collecting society) as well as to the publishers. This would, according to the parties, create legal difficulties in the event that a publisher planned to withdraw. In fact, it would first have to be clarified which exclusive licence was valid. The answers of the two different collecting societies did not provide a clear picture: AKM confirmed that any withdrawal would generally need the author's approval, whereas Austro Mechana stated that it did not have any data on this question⁵⁸.
177. Similarly, for some of the affected countries the complex legal situation often made it impossible to obtain clear answers. This in itself shows the significant degree of legal uncertainty connected to a withdrawal of rights relating to Continental European repertoire. Overall, the market investigation confirmed that the authors as well as the collecting societies have substantially more control over their rights in Continental Europe than in Anglo-American countries and that any withdrawal of Continental European repertoire will – due to the likely legal difficulties - need more time than a withdrawal of Anglo-American mechanical rights. The withdrawal of rights by the publishers without prior approval by the authors is therefore only likely in respect of mechanical rights for Anglo-American repertoire. This is also confirmed by the fact that the current withdrawal initiatives focus on Anglo-American mechanical rights for online applications as described in more detail below. While it cannot be excluded that in the long-term also a withdrawal of Continental European repertoire will be intended by the publishers where legal possibilities for this can be found in the national legal frameworks, it cannot be assumed to be a likely step which could be expected in the foreseeable timeframe.

(3) Current withdrawal initiatives

178. All currently known withdrawal initiatives cover mainly mechanical rights for online use. They do not apply to mechanical or performance rights in their traditional, off-line applications. The withdrawal initiatives moreover generally only cover Anglo-American repertoire.
179. Several publishers are currently re-organising their Anglo-American mechanical rights for online applications according to different models. This trend follows the Recommendation which re-affirms that right holders have the right to authorize a single collecting society to licence and monitor their rights across Europe.
180. Just before the proposed transaction, Universal studied different scenarios [...] which ranged from granting one collecting society with all copyrights to select several collecting societies at the same time in order to withdraw the current collective management of copyrights. These attempts by Universal were formally made known to the Collecting Societies: Universal had initially informed them that it would withdraw its online rights

⁵⁷ See SACEM's reply to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 9c.

⁵⁸ See AKM's and Austro Mechana's replies to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 9d.

[...]*, but afterwards informed them that this process was put on hold. The most advanced projects of Universal involved [...]* dealing with the Anglo-American repertoire. The parties also indicated intentions to explore a co-operation with [...]*. This would, however, require subsequent agreements with other collecting societies due to the difficulties connected with a withdrawal of Continental-European rights by publishers as can be seen from the internal documents provided by Universal [...]*⁵⁹.

181. BMG also studied some withdrawal possibilities in 2006. The main one involved the creation of a joint venture with [...]* and related to online and mobile rights of BMG's non Continental-European repertoire. [...]* However, as Universal, BMG had already informed some collecting societies of these plans.
182. The most advanced model, [...]*, is the EMI initiative "CELAS" under which EMI has selected a new joint venture established by the German and the United Kingdom collecting societies for the EEA-wide administration of the EMI repertoire. At the beginning of 2006 EMI announced its agreement with the MCPS-PRS Alliance and GEMA and the joint venture has become active as of 1 January 2007. The initiative foresees that the EMI Anglo-American⁶⁰ will be offered under a single licence across Europe for mobile and online use. CELAS will be a new entity separate from the parent collecting societies and will represent the EMI rights on an exclusive basis. But CELAS, MCPRS/PRS and GEMA remain entitled to offer similar services individually to other right holders.
183. In February 2006, Warner Chappell Music launched its Pan European Digital Licensing (hereinafter "PEDL") initiative. Negotiations are still ongoing. It concerns Anglo-American online rights (Continental-European repertoire is not included). Warner intends to designate several collecting societies which have to be able to meet the standards Warner requires as its non exclusive licensing agents to grant pan-European online licences. This project therefore differs to some extent from the others, since there will not be one collecting society in charge of the licensing of the Warner repertoire but several.
184. Throughout the market investigation, some independent publishers (e.g. Chrysalis)⁶¹ have also mentioned considering the withdrawal of their online rights from collecting societies. MCPS-PRS has moreover, together with the Music Publishers Association (hereinafter "MPA"), developed a standard agreement which is supposed to allow to smaller independents an easy withdrawal and transfer to MCPS-PRS, respectively to its "Alliance Digital". The online rights are defined as telephone and online usage rights (including reproduction and distribution). Alliance Digital has sole and exclusive power to negotiate and enter into agreements with those who require licences either in the form of blanket or standard agreements, and to determine by negotiation or otherwise the terms and conditions on which licences are granted including the royalty fees. The payment of royalty by licensor is based on tariffs of country of destination.

⁵⁹ See Annex 5 provided by the parties, dated 22 January 2007, page 477.

⁶⁰ The single licence will also cover German repertoire contributed by GEMA. However, GEMA repertoire is not withdrawn in the sense described but only part of the initiative because GEMA is participating in the joint-venture.

⁶¹ See Chrysalis' response to Questionnaire to competitors (independents) 2, dated 21 December 2006, question 38.

(4) Conclusion

185. It can be concluded that the withdrawal of rights and the subsequent transfer of right to one or a few selected collecting societies is clearly a trend which is currently taking place in the industry. Universal is actively pursuing an own withdrawal initiative [...]*. The pause which was created by the merger proceedings before the Commission does not signal an end to this activity.
186. This trend however currently concerns mainly Anglo-American mechanical rights for online applications since all the initiatives described above at present only cover these rights.⁶² The following assessment will, therefore first cover mechanical and performance rights in their traditional applications and will then focus on online rights, in particular on the Anglo-American mechanical rights for online applications considering the current trend to withdraw.

2.2 Mechanical and performance rights (traditional applications)

2.2.1 Affected markets

187. The parties have provided market share estimations which are summarized in the following tables:

⁶² As a consequence of the current withdrawals, music-users will probably have to acquire separate licences for the mechanical part of the online rights and for the performance part of the online rights. Only those initiatives which select the performance right collecting society in the United Kingdom – PRS - will be able to offer a combined online licence for mechanical and performance rights for online applications with respect to the Anglo-repertoire. With respect to the American performance rights being held by ASCAP, even after withdrawal a combined licence will be possible since the authors grant a non-exclusive licence to both ASCAP and the publishers. Any publisher has therefore access to the performance rights of its own repertoire and may offer them (non-exclusively) together with the corresponding mechanical rights. With respect to BMI, the publishers only have the rights in those territories where BMI does not itself exploit the rights or has an agreement with a collecting society to do so. If BMI is not party to a withdrawal initiative, the online services will therefore have to acquire the licences for BMI-American performance rights separately from each of the EEA-collecting societies for their respective territories.

Mechanical	Universal	BMG	Merged	EMI	Warner	Sony	Others
	%	%	%	%	%	%	%
Austria	[10-20]*	[10-20]*	[30-40]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
Belgium	[0-10]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
Finland	[0-10]*	[0-10]*	[10-20]*	[0-10]*	[40-50]*	[0-10]*	[30-40]*
France	[10-20]*	[0-10]*	[10-20]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
Germany	[0-10]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Greece	[10-20]*	[10-20]*	[30-40]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*
Hungary	[20-30]*	[10-20]*	[40-50]*	[20-30]*	[10-20]*	[0-10]*	[0-10]*
Italy	[10-20]*	[20-30]*	[30-40]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Netherlands	[10-20]*	[20-30]*	[40-50]*	[20-30]*	[10-20]*	[0-10]*	[0-10]*
Poland	[10-20]*	[10-20]*	[30-40]*	[20-30]*	[10-20]*	[10-20]*	[10-20]*
Spain	[10-20]*	[0-10]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[20-30]*
Sweden	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
United Kingdom	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Norway	[10-20]*	[0-10]*	[10-20]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
EEA	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*

Performance	Universal	BMG	Merged	EMI	Warner	Sony	Others
	%	%	%	%	%	%	%
Austria	[10-20]*	[0-10]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Belgium	[10-20]*	[0-10]*	[10-20]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Czech Republic	[0-10]*	[0-10]*	[10-20]*	[30-40]*	[20-30]*	[0-10]*	[10-20]*
Germany	[0-10]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Greece	[10-20]*	[0-10]*	[20-30]*	[20-30]*	[20-30]*	[10-20]*	[10-20]*
Hungary	[10-20]*	[20-30]*	[30-40]*	[20-30]*	[10-20]*	[0-10]*	[10-20]*
Italy	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
Netherlands	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Poland	[10-20]*	[0-10]*	[20-30]*	[10-20]*	[20-30]*	[10-20]*	[20-30]*
Spain	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[20-30]*
United Kingdom	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
EEA	[0-10]*	[0-10]*	[10-20]*	[10-20]*	[10-20]*	[0-10]*	[50-60]*

188. According to this information, the horizontally affected markets are those for

- mechanical rights in: Austria, Belgium, Finland, France, Germany, Greece, Hungary, Italy, The Netherlands, Poland, Spain, Sweden, the United Kingdom and Norway;
- performance rights in: Austria, Belgium, Czech Republic, Germany, Greece, Hungary, Italy, The Netherlands, Poland, Spain, and the United Kingdom;

189. After the merger, the parties would acquire a leading position in a number of EEA-countries. They would exceed a combined market share of 30% in Austria, Greece, Hungary, Italy, the Netherlands and Poland for mechanical rights and in Hungary alone for performance rights, followed mostly by EMI. Warner would in most cases be the third strongest competitor with Sony following in some distance as the smallest of the majors.
190. The market investigation has, however, shown that the merger does not lead to competition concerns in the markets for mechanical and performance rights due to the strong position of the collecting societies which prevents independent pricing on the part of the publishers.

2.2.2 Pricing in the system of collecting societies

191. Mechanical and performance rights in their traditional (non-online) applications are managed in the described traditional system of collecting societies. The pricing decisions in this system are made by the collecting societies which the publishers may influence only indirectly via their representation on the boards. However, most collecting societies only grant a limited share of the voting rights to the group of publishers. In the majority of collecting societies, the number of seats open for publishers is limited to one third of the total number of seats or less.⁶³ In addition, some collecting societies further restrict the number of the publishers' seats available to vertically integrated publishers which mainly affects the majors. In the Spanish collecting society SGAE, for example, three out of twelve board members are publishers, one of which may be a major. In the French collecting society SACEM, six out of 19 board members may be publishers. Among these six only two may be vertically integrated.⁶⁴
192. In most collecting societies the decisions by the board are taken by simple majority.⁶⁵ Some collecting societies indicated exceptions to this rule for some important subject matters, such as the dissolution of the collecting society or significant changes of the statutes. Only a few collecting societies reported specific rules which, however, did not create a specific advantage for the group of publishers (e.g. if the group of composers on the GEMA-board has an unanimous view, this group cannot be overruled). Since generally all votes have equal weight, the publishers formally do not have a decisive influence on the collecting societies and even less so one single publisher. Universal's formal influence will also consequently not increase after the merger.
193. A number of collecting societies have however indicated that the economic weight of the majors is significant and the dependence of the collecting societies on Universal will increase after the merger. Some market participants made reference to the so-called "Cannes Agreement", according to which the publishers reached significantly lower commission fees for the collecting societies in the framework of central licensing agreements for mechanical rights. In this respect it has to be noted, however, that with the Cannes Agreement the publishers did not influence the tariffs for users but only the

⁶³ The main exception to this is the collecting society MCPS in the United Kingdom where the majority of seats on the board are open for publishers.

⁶⁴ See Questionnaire to collecting societies 1, dated 7 November 2006, questions 6, 7 and 53: e.g. SABAM: ¼, AKM 1/3, GEMA 1/3, SACEM less than 1/3, Buma ¼, Stemra 1/3, STIM 1/3, SGAE ¼.

⁶⁵ See Questionnaire to collecting societies 1, dated 7 November 2006, question 7.

commission fees retained by the collecting societies for their administration services. The tariffs themselves are set by the collecting societies. This derives mainly from the fact that collecting societies are bound by a number of legal provisions in their pricing which does not only limit the collecting societies but also any publisher's influence on the tariffs. The main provision is the non-discrimination principle which will be described in more detail in the following.

194. While the parties' economic weight will become larger after the merger, this will not allow Universal to price independently. The licensing tariffs may not under the current rules differ per publisher. It is therefore unlikely that the parties could impose price increases for mechanical and performance rights for traditional applications after the merger.
195. Due to their dominant positions, the collecting societies are regularly obliged to charge non-discriminatory tariffs. As a result, under the current system, they normally may not charge different tariffs to the right-users – differences in tariffs only apply (on a non-discriminatory basis) with respect to the different forms of exploitation. The music of all member authors and publishers is normally covered by a blanket licence which defines a uniform price for all titles and users of one right category.
196. The merger will also not give Universal the possibility to influence the collecting societies to change this system in its own favour. In most cases, the non-discrimination obligation is based on competition law as well as on the respective national copyright laws.⁶⁶ Remaining in the traditional system of collecting societies, it can therefore not be expected that Universal could after the merger impose higher prices for the own repertoire regarding mechanical or performance rights (traditional application).

2.2.3 No withdrawals of mechanical and performance rights for traditional applications

197. While significant changes to the rights administration are taking place for online rights, no such developments can currently be observed for mechanical and performance rights for traditional applications. While some collecting societies have mentioned the possibility of a parallel development occurring in the future in respect of mechanical and performance rights for traditional applications as in online rights, the market investigation has not indicated that any withdrawal initiatives are planned with respect to the traditional fields of applications in the near future.
198. It can be assumed that the withdrawal of mechanical and performance rights for traditional applications is more difficult than the withdrawal of online rights. In particular for performance rights, a withdrawal might be difficult due to the monitoring and collection of royalties from the numerous small and geographically widely dispersed customers, such as restaurants, bars and discotheques. The administration of these rights would continue to require a high degree of local presence in the countries where the customers are located whereas online rights can to a significant extent be administered via the internet. For a withdrawal of such rights, the assistance of most collecting societies would still be needed since each collecting society has for its own country the information about the users as well as the necessary monitoring network.

⁶⁶ See Questionnaire to collecting societies 3, dated 5 February 2007, question 3a.

199. It is, moreover, worth noting that in the current system of the mechanical rights management the large record companies have in the past succeeded in significantly decreasing the commission fees which are retained by the collecting societies and in establishing so-called "central licensing agreements" which constitute European-wide licences granted by a selected collecting society. As opposed to the withdrawal initiatives in online rights, these multi-territorial licences are, however, based on agreements between the relevant collecting societies and are thereby integrated into the traditional collecting societies' system. Due to the better terms and the easier European-wide administration of mechanical rights, the incentives for the vertically integrated music companies to withdraw those rights have to be considered as lower than it is the case for online rights.
200. As described above, the publishers could in essence only withdraw Anglo-American mechanical rights on their own initiative, since only those are regularly assigned to them by the authors. All other rights (performance rights, mechanical rights for Continental European repertoire) are normally assigned by the authors to the collecting societies. Any withdrawal of those rights by the publishers would normally require the authors' approval. Given that the approval of thousands of authors would be necessary a withdrawal of performance rights and Continental-European mechanical rights does not seem likely.
201. But even for Anglo-American mechanical rights for traditional applications a withdrawal cannot be expected in the foreseeable timeframe. All current initiatives focus on online rights. According to one major publisher, the online initiative has already required a huge amount of preparation over the past year. No publisher indicated to currently pursue any such plans for the "offline" rights (mainly Anglo-American mechanical rights). It can be assumed that any potential initiative to withdraw "offline" rights (mainly Anglo-American mechanical rights) in the future would require again a significant amount of time for planning and preparation. Several independents have indicated that a withdrawal of mechanical rights (in their traditional applications) could be in principle feasible for Universal. However, they also mention that mechanical rights account for approximately half of the publishers' turnover, and that any such move would if at all only be decided upon when the currently initiated change for online rights is firmly established. Given these indications, any such step therefore does not appear likely.
202. It can also not be assumed that the merger increases the incentives for Universal to withdraw mechanical rights for traditional applications where it is possible. Both Universal and BMG had indicated already before the merger that they would withdraw their online rights. Equally, a number of independents are currently withdrawing. Consequently, the size of the publisher does not seem to be essential to the decision to withdraw and transfer the rights to a selected collecting society. In any case, any potential minimum size is apparently already reached by the larger independents. The merger therefore cannot be considered to have a decisive effect in this respect.
203. While the possibility of a withdrawal of at least mechanical rights for traditional applications (Anglo-American repertoire) cannot be completely excluded in the long-term, it cannot be assumed as a probable development in the foreseeable timeframe.

2.2.4 Effects of the merger on mechanical and performance rights

204. Against this background, it is not likely that the merger could lead to competition concerns and to an increase in prices for licences for mechanical and performance rights

(traditional applications). The control over the pricing is to a large extent in the hands of the collecting societies and not in the hands of the publishers. No change to this system can currently be expected in the near future. The merger therefore does not lead to a significant impediment of effective competition in the markets for mechanical and performance rights.

2.3 Online rights

2.3.1. Scope of the analysis

(1) Serious doubts in the market for online rights

205. The merger raises serious doubts in the market for online rights, which are composed of mechanical and performance rights for online applications (including mobile). The concerns mainly relate to the mechanical rights part of the online rights and to Anglo-American repertoire. However, a price increase in this segment will have an appreciable effect on the overall market for online rights. The role of performance rights would be neutral since they are likely to remain in the traditional system of collecting societies who have an obligation to license at non-discriminatory terms.
206. Online rights have so far been administered by the collecting societies. The recent major restructuring of the market in which publishers withdraw online rights from the traditional collecting societies' system affects in particular the mechanical rights part of these online rights. Due to the specificities of the rights administration in the Anglo-American countries as described above, such withdrawal is currently easier with respect to Anglo-American repertoire. The current withdrawal initiatives are subsequently focused on Anglo-American mechanical rights for online use.
207. In the traditional collecting societies system the collecting societies are responsible for the pricing of licences which the publishers can influence only via their representation on the collecting societies' boards. The withdrawal shifts pricing power to the publishers who gain pricing independence with respect to the withdrawn rights. In this restructured market, the merger may lead to a significant impediment of competition due to unilateral effects leading to an increase in prices as compared to the situation in the restructured market without the merger.
208. The following analysis therefore assesses the effects of the merger on competition in the new licensing environment envisaged. It does not assess any effects of the withdrawal of rights from the traditional collecting societies' system as such, but neutrally considers the current developments as facts determining the relevant competitive situation in which the merger takes place. The withdrawal from the collecting societies system is the framework which allows the publishers to price independently. After the withdrawal, the collecting societies system and the corresponding regulatory framework cannot prevent a price increase resulting from the merger in this restructured market environment.

(2) Development of the online music market

209. Online rights are an input for the provision of online music services to end-customers. Online music providers, such as downloading services, need to acquire the licences for the necessary online rights in order to be able to offer the respective music titles on their platforms. The licensing of online rights to online music providers is therefore an

upstream (wholesale) market to the (retail) market of online music services to end-customers.

210. The volume of the upstream market for online rights depends on the size and development of the downstream market for online music services to end-customers. Since the revenue from licensing of online rights is generally a percentage of the revenues the online music providers make by selling online music services to the end-customers, the current size and the prospective growth of that market result in a corresponding development of the market for the licensing of online rights.
211. The online rights market is currently still very small which is due to the fact that the provision of online music services to end-customers is still in a very early stage of development. The total market volume of publishing online rights in the EEA is estimated by the parties at EUR [20-30]* million for 2005. According to the notifying party, online rights represented approximately 2% of the parties' total publishing revenues in 2005. A similar share appears to apply to the total downstream market: According to the report "Interactive content and convergence: Implication for the Information Society"⁶⁷, the total revenues made on the market for online music services to end-customers (EUR 196 million in 2005) also represent approximately 2% of the total music revenues.
212. It is, however, undisputed that the market for online music services to end-customers will grow significantly in the next years and will be of critical importance for the overall future music market. The "Commission staff working document – study on a community initiative on the cross-border collective management of copyright"⁶⁸ indicates a considerable estimated growth of online music revenues until 2008. The total online music revenues in Western Europe in 2004 are indicated as EUR 27.2 million. The estimation for 2008 is EUR 559 million. In the US the market volume was already EUR 207 million in 2004 and the estimated revenue for 2008 is EUR 1 270 million.
213. Also according to International Federation of the Phonographic Industry ("IFPI"), online music is still in an early phase of development but grows at high rates. Considering only recording revenues, IFPI states that revenues by record companies in the online music business have doubled worldwide in 2006 to US-\$ 2 billion. They are now around 10% of the total recorded music sales (after 5.5% in 2005) and are expected to grow to at least 25% by 2010. In Europe, the number of single tracks downloaded has according to IFPI increased by 80% between 2005 and 2006.⁶⁹
214. In March 2007, Vivendi reported for Universal digital sales in 2006 "strong growth in all markets and sectors". Universal's digital revenues were up [50-100]*% versus 2005 and

⁶⁷ See Interactive content and convergence: Implication for the Information Society – A study for the European Commission, Final Report October 2006, pages 31 and 36. The same study forecasts a growth of total online and mobile music revenues to €1.8 bn by 2010, i.e. a multiplication by more than the factor 9.
http://ec.europa.eu/information_society/europe/i2010/docs/studies/interactive_content_ec2006_final_report.pdf

⁶⁸ See Commission staff working document - study on a community initiative on the cross-border collective management of copyright, 7 July 2005, page 6, referring to Rightscom, DRM and Services in Europe and the US, 2005.

⁶⁹ See International Federation of the Phonographic Industry; IFPI:07 – Digital music report: http://www.ifpi.org/content/section_resources/digital-music-report.html

represented [0-10]*% of its total revenues.⁷⁰ In its "2007 Outlook" Vivendi states that regarding Universal's revenues (even excluding BMG Publishing) a "strong release schedule and digital sales growth are expected".⁷¹

215. The above mentioned report "Interactive content and convergence: Implication for the Information Society"⁷² similarly forecasts that online music revenue which currently represents 2% of the total music revenues will in 2010 represent a share of 20.4%. This assumes that the online music market will be multiplied by 9 between 2005 and 2010. Applying this growth rate to the publishing market for online rights, it is estimated that this market will reach a value of EUR 230 million in Europe. This is in line with the forecast of the International Music Publishers Association (IMPA) which gathers the 5 current majors. Considering that the US and Europe have similar sized overall music markets, IMPA expects that the European digital market (which is currently 7 times smaller) should be similar to the US digital market.⁷³

(3) Steps of the assessment

216. The analysis focuses on unilateral effects of the merger on the market for online rights and in particular on the mechanical rights portion of those online rights for Anglo-American repertoire. It follows three main questions:
- **Independence in pricing:** After the restructuring of the administration of the online rights by the described withdrawal initiatives, will the publishers be able to price independently from the collecting societies and the regulation applicable to them?
 - **Increase in market power:** Will the merger increase Universal's market power in the market after restructuring vis-à-vis the online right users as compared to the restructured situation before the merger?
 - **Profitability of a price increase:** Is it likely that Universal will be able to profitably increase prices or will the reactions of other market participants offset the positive revenue effect and therefore render a price increase unprofitable and unlikely?

2.3.2 Independence in pricing

217. As a result of the withdrawal initiatives in the online rights market, the publishers are gaining control over the licensing tariffs. Despite the remaining future involvement of collecting societies in the current withdrawal initiatives the publishers are likely to exert direct influence on the pricing of their withdrawn repertoire.

⁷⁰ Vivendi's Annual Financial Report and Audited Consolidated Financial Statements for the Year Ended December 31, 2006, dated 12.03.2007, p.36.

⁷¹ Vivendi presentation "2006 Results and 2007 Outlook" by Jean Bernard Lévy and Jacques Espinasse on 07.03.2007.

⁷² See Interactive content and convergence: Implication for the Information Society – A study for the European Commission, Final Report October 2006, pages 33 and 39.
http://ec.europa.eu/information_society/europe/i2010/docs/studies/interactive_content_ec2006_final_report.pdf

⁷³ See Annex 5 provided by the parties, dated 22 January 2007, page 307.

(1) *The changing role of collecting societies*

a. The traditional role

218. So far, the collecting societies have been responsible for the licensing of mechanical, performance and online rights and the corresponding definition of the exact terms of licensing. In the traditional system, for most uses they issue blanket licences which cover the complete repertoire administered. Collecting societies are mostly considered as being dominant in their respective territories due to the reciprocal agreements which essentially prevent any competition between the collecting societies and restrict their activities to the own country. On this basis, special rules apply to them in most Member States. These rules consist (i) of the general principles of non-discrimination and equal treatment which the collecting societies derived from the requirements of competition law and (ii) of specific regulation in some countries.
219. Specific regulation: The parties have provided an overview of the different national conditions prevailing in this respect and have shown that there are different mechanisms in the affected territories which influence the setting of royalty rates, which has generally been confirmed by the market investigation. The mechanisms range from specific bodies with jurisdiction to approve or set rates to arbitration bodies. The nature, jurisdictional scope, and respective powers of these mechanisms vary among the affected territories. According to the parties, there is a level of uncertainty regarding the exact scope of application of these mechanisms especially in relation to new and emerging licensing platforms for pan-territorial licences, in particular for the online exploitation of music.⁷⁴
220. The parties indicate mechanisms with specific jurisdiction over royalty rates in Austria, the Czech Republic, Germany, Hungary, Greece and the United Kingdom⁷⁵. These Member States have in common that the rules provide for arbitration mechanisms rather than for any direct tariff regulation as it is the case for regulated industries, such as telecoms. Only in Hungary is an approval of the tariffs by the Ministry of Culture required. Moreover, the arbitration procedures in the other countries only become effective when users dispute tariffs charged by the collecting societies before the courts or specific arbitration bodies.⁷⁶

⁷⁴ See response by the parties' to the questionnaire to the parties, dated 7 February 2007.

⁷⁵ In Spain, there is only a mechanism which is entirely voluntary and in the Netherlands, there is a body which can only make non-binding recommendations.

⁷⁶ The parties provided the following information on the individual countries:

- *Austria*: The Verwertungsgesellschaftengesetz 2006 (the VGG) determines the conditions under which the collecting societies AKM and austro mechna operate. The usual way for setting a tariff is for the Austrian collecting societies to conclude "collective agreements" with representative organisations of users. A specific arbitration mechanism exists where negotiations for a collective agreement are unsuccessful. Where this arbitration fails, either party is entitled to apply to the "Copyright Senate" ("Urheberrechtssenat") which will decide on the appropriate tariff.
- *Czech Republic*: Collecting societies in the Czech Republic must be authorized by the Ministry of Culture which supervises the activities of those societies. The Czech collecting society OSA is obliged to set adequate tariffs which apply equally to all users. Users may ask the Ministry of Culture to review the rates.

221. Non-discrimination principle: Apart from these specific regulation, the general non-discrimination principle is applied by the collecting societies as stipulated in their statutes and membership agreements. According to this principle they may not treat users differently for comparable forms of music applications. As a result, tariffs only differ per category of use but not per user. The collecting societies also apply the policy of charging one price for the whole repertoire. Therefore, no differentiated pricing for the publishers' or authors' repertoires applies in the traditional collecting societies system.
222. In the traditional collecting societies system, the publishers do consequently not have any direct influence on these tariffs. Since the licences and tariffs cover the complete repertoire no publisher-specific tariffs exist. In this system as described above, the publishers are able to influence these terms only via their representation on the boards of the collecting societies which does not, however, in most collecting societies entail any decisive control for the publishers. Consequently, the individual publishers do not have control over prices of their individual repertoires as the control is with collecting societies.

b. The change brought about by the withdrawal trend

223. The restructuring of the market provides for a new role for the collecting societies and a new relationship between publisher and collecting society in the field of the withdrawn rights. This new role is determined by the newly introduced competition between collecting societies for right-holders. Due to the withdrawal from the traditional collecting societies system, collecting societies will (for the withdrawn rights) adopt a role as agents and service providers for the publishers and will no longer act in the traditional sphere of the usual membership agreement and collecting societies' statutes.
224. After the withdrawal of rights, the collecting societies will compete with one another for the administration of online rights. Universal provided presentations made by several collecting societies which presented their offers for the administration of online rights to the publishers.⁷⁷ Moreover, an own internal presentation indicates that Universal met with [...] in this matter.⁷⁸ It is clear that these collecting societies have to make an offer to the publishers which complies with their wishes. The Dutch collecting society BUMA-Stemra summarizes the new competitive situation: "Rights holders will evaluate

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- *Germany*: In Germany, users can appeal against tariffs set by GEMA to the Arbitral Tribunal at the Patent Office which may alter this tariff.
 - *Greece*: In Greece, users who consider tariffs set by AEPI as too high may request a court of first instance to set an adequate tariff. In addition, the Ministry of Culture has the power to act on complaints regarding tariffs.
 - *Hungary*: Royalty rates set by the Hungarian collecting society Artisjus are subject to Ministerial approval. Users may turn to an arbitration board, which can propose a new tariff. If the parties to the dispute do not agree to this proposal the tariffs of the previous year remain applicable.
 - *United Kingdom*: In the United Kingdom, the Copyright Tribunal is responsible for the determination of disputes arising between licensing bodies and users. The Copyright Tribunal may set the terms that are "reasonable". It has the authority to confirm or vary the pricing scheme.

⁷⁷ See Annex 5 provided by the parties, dated 22 January 2007, section 1.

⁷⁸ See Annex 5 provided by the parties, dated 22 January 2007, page 466.

the services delivered by their society and compare these to services provided by other European societies. The most attractive society to a rights holder will be the one that best represents the online music rights of the rights holders, based on efficiency and service."⁷⁹ On the basis of such competition between the collecting societies, the publishers select one or a few collecting societies for the administration of their rights. The respective publishers base their cooperation with respect to the withdrawn rights on new, individual agreements with the selected collecting society which define the specific terms of the administration of the withdrawn rights beyond the usual membership agreements.

225. In the restructured market, it is therefore very likely that the publishers will have decisive influence on the tariffs for their withdrawn rights. The publishers can no longer be considered as one of many members in a collecting society with only limited influence on the conditions of licensing. Due to the process of 'tendering' their rights, the publishers gain a position which shifts control over the conditions of licensing from the collecting societies to the publishers who have the possibility to terminate their cooperation with the selected collecting societies and to switch to another one if they are not satisfied with the conditions and services offered. This view is also reflected by IMPA (International Music Publishers Association) which refers in a presentation to Option 3 of the Commission Working Paper and states that "Option 3 changes relationship between societies and rights holders – Option 3 gives rights holders the ability to negotiate terms on which societies can license our rights and to protect rates"⁸⁰.
226. This was further confirmed by the responses to the market investigation. When asked whether the publisher or the selected collecting society will decide on the tariffs of the withdrawn rights in the future, several collecting societies indicated that the conditions would depend on the agreements between the selected collecting society and the individual publisher.⁸¹ The Belgian collecting society SABAM indicates, for example, that "Due to the shifted balance of power and the fact that instead of a collective of right-owners one single publisher will be represented, the collecting society will operate more as an agency for the publisher than as a true collecting society. In such a case, the concerned publisher will determine the conditions against which this repertoire will be licensed."⁸² In the same way, the German collecting society GEMA confirms that the tariff conditions will be agreed between the selected collecting society and the publisher.⁸³ Equally SACEM, the French collecting society, states that if selected by a major publisher, SACEM would have to apply the specific tariff required by the respective publisher.⁸⁴ Both GEMA and SACEM have already been in negotiations with one or

⁷⁹ See Annex 5 provided by the parties, dated 22 January 2007, page 16.

⁸⁰ See Annex 5 provided by the parties, dated 22 January 2007, page 317.

⁸¹ See collecting societies' responses to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 7d.

⁸² See SABAM's response to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 7d.

⁸³ See GEMA's response to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 7d: "In diesem Fall ist davon auszugehen, dass die Tarifbedingungen bereits in der Vereinbarung zwischen dem jeweiligen Verleger und der Verwertungsgesellschaft festgelegt werden."

⁸⁴ See SACEM's response to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 3e (applicability of the non-discrimination rule for withdrawn rights): "La SACEM aurait à appliquer le tarif

several major publishers on the administration of withdrawn rights. It can be assumed that their replies reflect their experience resulting from those negotiations. Their statements are in line with MCPS-PRS' explanation that the right-holder will select an agent on the terms offered to him which he feels best represents his interests and is free to switch to another agent (collecting society) if his interests are not properly represented by the one initially selected.⁸⁵

227. While many other collecting societies indicate that the tariffs would depend on the agreement between the publisher and the selected collecting society, a few of them stated that they would also be the ones deciding on the tariffs in the restructured market and with respect to withdrawn rights transferred to them according to the rules currently determined by the membership agreements and statutes (OSA, AEPI, Artisjus)⁸⁶. As far as the Commission is aware, none of those respondents are currently among those which are in detailed discussions with the major publishers or even selected for the EEA-wide administration of the mechanical part of their online rights.
228. Market participants other than the collecting societies share a similar view of the future pricing power over withdrawn rights as shown by the statement of one online music provider: "The withdrawal by publishers of their repertoire from the system of blanket licences has the effect of removing the pricing power from collecting societies and therefore from national copyright authorities and tribunals. In other words, insofar as access to the global repertoire is essential for users such as broadcasters and providers of music streaming services (one cannot for example have a call-in program where one only plays songs owned by certain publishers), the publishers are acquiring full and unfettered pricing power in relation to users."⁸⁷
229. It can be concluded that the collecting societies will no longer have the same pricing power as in the traditional collecting societies system as regards the withdrawn rights. On the basis of competition between the collecting societies, this power over the pricing will shift to the publishers.

(2) Applicability of regulatory provisions after withdrawal

230. The publishers' independence in pricing will also not be prevented by regulatory provisions existing for collecting societies. All current initiatives include the participation of one or a few collecting societies. The market investigation has shown that the current provisions will most probably not apply equally to the new initiatives. This conclusion is also implicitly confirmed by the response of EMI, a music publisher which has conferred inter alia its Anglo-American repertoire to CELAS, a joint venture of GEMA and MCPS-PRS. In its assertion that music publishers would not be able to price their copyrights

spécifique exigé par l'éditeur si ce dernier lui confiait la gestion de ses droits dans le cadre d'un mandat particulier distinct des apports de droits normalement effectués à la SACEM par ses membres, mandat donnant à l'éditeur en cause la possibilité de spécifier des conditions particulières d'exploitation de son catalogue différentes de celles définies par la SACEM pour ses propres membres."

⁸⁵ See MCPS-PRS' response to the Questionnaire to Collecting Societies 3, dated 5 February 2007, question 7d.

⁸⁶ See questionnaire to collecting societies 3, dated 5 February 2007, question 7d.

⁸⁷ See fax registered as document 2759 on 1 February 2007, page 3 (name of respondent confidential).

independently, EMI does not at all refer to any regulation preventing the publishers from doing so.⁸⁸

231. As described above, in the traditional system collecting societies are normally considered as dominant and consequently apply the principle of non-discrimination. In addition, in a few countries there is specific regulation – mostly arbitration procedures in case of complaints. In the new initiatives pan-European licences are intended to be granted by a national collecting society selected by the respective publisher. The market investigation has shown that it is highly unlikely that the selected collecting societies will with respect to the administration of the withdrawn rights be bound to the non-discrimination principle and to any country-specific regulation to the same extent as in the traditional system.

a. Non-discrimination

232. In the new initiatives, the collecting societies are selected by the publishers as service providers. As described already earlier, they do not act anymore as the traditional collecting societies but as agents for the publishers. By concluding new agreements different from the usual membership agreements, those membership agreements and consequently the statutes of the collecting societies concerning the membership will no longer fully apply with respect to the withdrawn rights.

233. While the collecting societies traditionally have had the control over the rights administered, they will in the future rather take the role of service providers to the publishers with respect to the withdrawn rights. In essence, the publishers will buy administration services from the collecting societies while keeping the ultimate control over the rights. The market power held by the collecting societies will therefore in this respect shift to the publishers. It is unlikely that this will still require the application of non-discrimination principles by the collecting societies with respect to the withdrawn rights.

234. This is also reflected in the agreements drafted for the new initiatives which reflect the expectation that a collecting society acting only as a service provider to a publisher will not be bound to the non-discrimination principle as the publisher would also not be bound when licensing directly: [...] allows for example in its draft agreement with [...], the application of different tariffs for right users [...]⁸⁹.

b. Specific regulation

235. Similar considerations have to be made with respect to specific regulation prevailing for collecting societies in the traditional system as described in general terms in paragraph above. While the licences can cover several countries, the specific regulation which is based on national laws does not apply fully to such multi-territorial licensing. With respect to the specific regulations, the questions may be raised whether (i) the regulation in the country in which the collecting society is located will also apply to users abroad and (ii) whether collecting societies granting licences in other countries for uses in these other countries would be bound by regulation there.

⁸⁸ Response of EMI to the Commission's questionnaire of 15.03.2007, p. (i).

⁸⁹ See [...].

236. (i) Applicability of regulation to users abroad: For most of the described regulation, the parties are of the view that it would also apply to users which are not located in the respective countries. The parties moreover indicate that such cases have never been tested, since to date the collecting societies have not granted EEA-wide licences.⁹⁰
237. The market investigation has not fully confirmed the notifying party's analysis. The collecting societies were asked whether any existing regulation relating to tariffs would equally apply to users in other countries acquiring a European-wide licence. The large majority of the collecting societies did not fully support the suggestion that the provisions applicable to users in the own country would equally apply to users acquiring a licence for the use of rights in other countries. The answers mostly either clearly rejected this possibility, stated that no tariff regulation existed in general or indicated that the legal situation was not clear.⁹¹
238. Of the countries identified as having some form of tariff regulation, it appears that particularly far-reaching provisions exist in the United Kingdom. The collecting society MCPS-PRS considers that the Copyright Tribunal's jurisdiction may be limited to licences concerning the exploitation of rights in the United Kingdom.⁹² This would mean that users who are located outside of the United Kingdom might be covered by the regulation in the United Kingdom, but only with respect to their activity in the United Kingdom. Since those users would have to be considered as British users rather than as foreign users, the statement of MCPS-PRS does in essence not confirm that users acquiring an EEA-wide licence for the use of music outside of the United Kingdom would be covered by the existing regulation.
239. Also the majority of collecting societies in those countries which were identified by the parties as having some form of tariff regulation, did not support the applicability of this regulation to users in other countries. According to GEMA for example, this question will depend on whether the applicability of the German law will be agreed upon in the contract between the publisher and the respective collecting society and whether it would be admissible to agree on such applicability according to the principles of international law. The Austrian collecting society in charge for mechanical rights Austro Mechana clearly rejected such applicability, while its counterpart for performance rights, AKM, indicated that there is no clear provision concerning the applicability of regulation to EEA-wide licences. A confirmation of the international applicability of the national tariff regulations

⁹⁰ The parties also did not indicate any cases which might have already touched upon this issue in the framework of the Santiago agreement which allowed for EEA-wide licensing and expired at the end of 2004. It seems, however, that the EEA-wide licensing on the basis of the Santiago agreement differs significantly from the EEA-wide licences envisaged after withdrawal and that any potential examples in this respect might not be applicable for the new initiatives. The Santiago agreement was concluded between a number of collecting societies granting each other the right to issue multi-territorial licences. The Santiago agreement was therefore no withdrawal from the traditional collecting societies system – it can rather be regarded as an addition to the traditional model in which the control over licenses and pricing remained fully in the collecting societies' hands.

⁹¹ See the collecting societies' reply to Questionnaire to collecting societies 3, dated 5 February 2007, question 6 c (applicability of regulation to European-wide licensing).

⁹² See MCPS-PRS' reply to Questionnaire to collecting societies 3, dated 5 February 2007, question 6 e.

was also not received from OSA (Czech Republic), AEPI (Greece) and Artisjus (Hungary).⁹³

240. (ii) Applicability of regulation to collecting societies abroad: It is moreover, unlikely that the specific regulations existing in some Member States would equally apply to the collecting societies being selected for the EEA-wide administration of rights.
241. Some respondents to the market investigation indicate that any specific regulation on tariffs would only apply to a foreign collecting society if this collecting society could – in case it granted licences in another country – still be defined as a collecting society under the national laws in the country of the right-user. In most countries, several conditions have to be fulfilled in order to qualify as a collecting society (for example, administration of rights for more than one right-holder, non-profit making organisation). Moreover, special accreditation often has to be granted by the authorities in charge. In some countries, it is very likely that no other organization could work as a formally acknowledged "collecting society". In Austria, for example, only one collecting society can obtain an operating licence for the administration of a specific category of rights⁹⁴. Further, the Hungarian collecting society Artisjus confirmed that a foreign collecting society could only act as agent in Hungary, since only Artisjus qualifies as collecting society.⁹⁵ In Italy, SIAE is appointed by law to act as a collecting society. While this does not prevent any publisher from licensing the own rights directly and independently or via a selected agent, it shows that the role of a traditional collecting society representing many different right-holders and its specific regulation is reserved for very specific organizations.
242. Apart from this, a number of respondents indicated that also a foreign collecting society granting licences in the own country would have to generally respect the law of this country. This affected mostly countries in which no specific tariff regulation exists.
243. The parties' analysis does not lead to a different result. For most countries, the parties find that the national rules would theoretically apply to a foreign collecting society if it qualified as a collecting society under these national rules. The parties indicate that this qualification may in some countries only be achieved if the organization is located in the respective country or may be excluded completely since this status is reserved for the established collecting society (e.g., Germany, Hungary, Italy). The parties state that regulation would probably apply also to foreign collecting societies only in the United Kingdom and the Czech Republic. MCPS-PRS considers that a licensing body would not necessarily have to be located in the United Kingdom to fall under the regulation in the UK indicating at the same time that there is no decided case on this issue.⁹⁶
244. It can be concluded, that the legal provisions are clearly aimed at the current traditional collecting societies system and do not take into consideration any EEA-wide licensing

⁹³ See the collecting societies' replies to Questionnaire to collecting societies 3, dated 5 February 2007, question 6 c.

⁹⁴ See parties' reply to the Questionnaire to the parties, dated 1 February, paragraph 3.2.6.

⁹⁵ See Artisjus' reply to the Questionnaire to collecting societies 3, dated 5 February 2007, question 6e.

⁹⁶ See MCPS-PRS' reply to the Questionnaire to collecting societies 3, dated 5 February 2007, question 6e.

activity. The results of the market investigation show that the future structure of the online licensing market is accordingly not considered in the various national laws. It is therefore unlikely that the national regulation (where it exists for the national collecting societies) will "neatly" apply to the EEA-wide licensing activities of the collecting societies being selected and acting as service providers for the publishers. This is even more unlikely if new entities are established by the collecting societies (and the publishers) for the EEA-wide administration of rights. The fact that the publishers are aiming at an EEA-wide tariff for the withdrawn rights as described above shows that a deviation from the standard rates for the withdrawn repertoire is considered as possible. This is also confirmed by the market investigation. When asked whether it can be expected that the new initiatives may apply tariffs for the withdrawn rights in the future which are different from those which are not withdrawn, the majority of collecting societies answered yes.⁹⁷

(3) Tariff provisions in Universal's current initiatives

245. In the restructured market and on the basis of the new role of the collecting societies, the publishers will via individual agreements be able to control the pricing over the own withdrawn rights and either define the tariff conditions directly or design approval procedures in the agreements with the selected collecting society. [...]*
246. The notifying party has been in contact with [...] regarding the EEA-wide administration of Universal's withdrawn rights. [...] ⁹⁸ [...] ⁹⁹.
247. While [...]*, the current initiatives mainly stipulate that for the time being, the current rates will continue to apply ("country of destination tariff"). This does not contradict the pricing power by the publishers. The use of the country of destination tariffs reflects the current transition period of this market which needs some time to develop. It is clearly a voluntary decision by these publishers who choose to stay with the old rates for a certain time. This decision does not reflect the absence of pricing independence, but rather confirms it. It would not be necessary to state in the new agreements the application of these tariffs if the selected collecting society would still be the one setting the tariffs in accordance with the traditional system of membership and reciprocal agreements.
248. It can be expected that the collection of local tariffs will be in the near future exchanged by a new EEA-wide tariff. The parties indicate for example [...]* that it is envisaged to establish an EEA-wide tariff.¹⁰⁰ MCPS indicates on its website, that the country of destination principle applies for withdrawn rights making clear at the same time that this is intended to be used only "initially"¹⁰¹. MCPS moreover indicates [...]* that:

⁹⁷ See the collecting societies' replies to Questionnaire to collecting societies 3, dated 5 February 2007, question 7f: Of 13 replies to this question, 8 collecting societies indicated yes, 3 indicated no and the answers of 2 collecting societies was not clear.

⁹⁸ See [...]*, Annex 5 provided by the parties, dated 22 January 2007, page 237.

⁹⁹ See [...]*

¹⁰⁰ See [...]*, Annex 5 provided by the parties, dated 22 January 2007, page 301 and the [...]*, Annex 5 provided by the parties, dated 22 January 2007, page 205.

¹⁰¹ See under <http://www.mcps-prs-alliance.co.uk/>- Licensing the future - Question and Answers.

"Obviously, there are significant practical difficulties in applying the ToD [Territory of Destination] principle in the online sphere [...] it inevitably leads to a very complex royalty structure in any pan territorial licence. One solution is obviously harmonized rates. [...] it could therefore be abandoned [...] MCPS-PRS and Rights Holders would then have an opportunity to control the tariffs on a Europe-wide basis. As indicated elsewhere in this response, the route to achieving purely repertoire-based licensing may not be immediate but until that point, however, ToD is a principle that should be retained."¹⁰²

249. It is therefore realistic to assume that an EEA-tariff for each specific repertoire ("repertoire-based") is intended which deviates from the country of destination tariffs, which shows the publishers' pricing independence compared with their situation in the traditional collecting societies' system. It can be questioned why [...]*. This is also confirmed by responses from the market. When asked whether in the current withdrawal initiatives the country of destination tariff will apply, SABAM for example indicates that the "risk" of tariffs in function of the repertoire exists.¹⁰³ SACEM also notes that withdrawals have as an aim the increased influence of the publishers on the tariffs.¹⁰⁴ Taking into account the difficulties which MCPS sees with respect to the country of destination tariff, it can be expected that the aim of an EEA-wide tariff will be pursued in the near future. The current focus on the old rates before the merger does not at all exclude a new pricing policy by Universal after the merger, which will allow for larger pricing power vis-à-vis the users and will therefore also create stronger incentives to apply an own rate.

(4) Conclusion

250. It can be concluded, that in most countries no explicit application of the national rules for international licences is considered. Many legal uncertainties as to the international applicability of national rules remain in most countries. It is therefore very likely that with the withdrawal of rights from the traditional system of collecting societies, the publishers will gain pricing independence with regard to their repertoire or may obtain it. Due to the limited applicability of specific national rules, it is also unlikely that existing regulation (where it exists) will be able to limit the enhanced pricing power of the parties on EEA-wide level in the foreseeable future environment.

2.3.3 Increase in market power

251. In the foreseeable licensing environment as described above, the proposed concentration is likely to significantly increase Universal's market power vis-à-vis the providers of online and mobile music services. This market power of the merged entity results from the heavy dependence of most¹⁰⁵ of these music providers on access to Universal's and BMG's music publishing rights and on Universal's recording rights. As a consequence of

¹⁰² See[...]*, Annex 5 provided by the parties, dated 22 January 2007, page 58.

¹⁰³ See SABAM's response to the Questionnaire to collecting societies 3, dated 5 February 2007, question 7a.

¹⁰⁴ See SACEM's response to the Questionnaire to collecting societies 3, dated 5 February 2007, question 7a.

¹⁰⁵ The Commission acknowledges the existence of some niche players such as E-Music specialising in repertoire of independents. However, the market investigation has shown that vast majority of the online and mobile music providers rely on the repertoire of the majors.

the proposed concentration, Universal will (co-)control publishing rights as regards a large number of the best-selling titles. This high control share of music publishing rights is further entrenched by Universal's strong position regarding recording (neighbouring) rights. In view of the specific features of the online and mobile music providers' demand it appears likely that Universal will be able to use its strong positions in both recording and publishing to exert pressure on online and mobile music providers and to impose higher rates.

(1) Features of demand of online and mobile music providers

a. Need to secure both publishing and recording rights

252. Any provider of online or mobile music needs licences for both the recording and the publishing rights for all titles it proposes on its platform.¹⁰⁶ Whilst publishing rights relate to the copyright of the author(s) in the "abstract" lyrics and melody of a work, the recording rights cover the rights of the performing artist in a specific recording of that song. The same work (melody and lyrics) may thus be recorded several times by different singers, for instance as "cover versions". If a provider offers music without having secured all necessary rights for a song it runs the risk of litigation and damage claims on the part of the right owners. In the absence of such licenses for the relevant recording rights and for the relevant publishing rights of a title, an online or mobile music service provider cannot offer that title and the title will thus normally not be available on that platform.
253. So far, online and mobile music providers have regularly acquired licences for the music publishing rights from the collecting societies and licences for music recording rights directly from the record companies. In the new environment as described above, music publishing rights of a given publisher will be only available from one single organisation (e.g. CELAS for EMI) or a limited number of organisations or collecting societies which administer the online rights of that publisher. As explained above, these organisations or selected collecting societies are rather acting as agent or service provider on behalf of their "principal" publisher which will determine the licensing terms and conditions. The licensing of music publishing rights is thus developing from a collective licensing towards an individual licensing and will thus converge towards a licensing model similar to the licensing of music recording rights.
254. The market investigation indicates that in some cases major record companies with large record repertoires and high market shares have succeeded in imposing higher licensing rates for recording rights than smaller major record companies. The online and mobile music providers which reported such rate differences referred to the higher bargaining power of those majors with higher market shares as their catalogues are of greater importance for an online and mobile music provider. In addition, several online or mobile music providers stated that record companies have refused or delayed wholesale licences

¹⁰⁶ This is also recognised by Universal: see paragraph 105 of the form CO. Ringtones as pure melodies (without performance) should normally not require a recording rights licence. However, according to the market investigation, even ringtones seem to require recording rights licences. In any event, even if ringtones were not to require recording rights licences, the following analysis would not be altered: ringtones are only one of several mobile music applications and not the most important one. In addition, they are losing relative importance as compared to mastertones and mobile audio and video downloads and streaming which have higher growth rates and all definitely require recording rights licences.

in the past. Some providers indicated that record companies have delayed the licensing of their repertoire in order to achieve higher rates. It is noteworthy that such behaviour has only been possible with respect to recording rights as publishing rights have so far been licensed by collecting societies.

255. In the restructured environment Universal as an integrated music company will directly and indirectly license both the recording and publishing rights and will thus be able to use its strong position in music recording to put additional pressure on online and mobile music providers in order to accept higher rates for music publishing rights. In view of this close link between the recording and publishing rights, both for the customers (the providers need licences for both rights) and the music companies (possibility of joint management within the same music company), the following analysis will also take into account Universal's control of recorded music rights.
256. The complementary character of music publishing and recording is also reflected in the way Vivendi presents the benefits of the BMG Music Publishing acquisition to financial analysts: Vivendi states that the announced acquisition of BMG Music Publishing will increase Vivendi's profit in the first year as it improves "UMG's ability to capitalize on a music market that is improving supported by technological innovations and digital sales".¹⁰⁷ The acquisition of BMG Music Publishing is presented as a unique opportunity as "BMG Music Publishing enhances the strategic position and value of UMG as the world's leading recorded music company AND music publishing company" (emphasis by Vivendi).

b. Licensing of the entire repertoire and not of individual titles

257. The offer of online and mobile platforms is permanently changing and they thus need to be able to put new songs quickly on their platforms. It would be extremely inefficient, time-consuming and very costly to open negotiations for each title. Therefore, online and mobile music providers regularly conclude general licence agreements with the right owners or their agents. These licence agreements are often concluded for one year and usually cover the entire repertoire owned or administered by the respective right owner or his or her agent. They can therefore be considered as 'blanket' licences for the full repertoire of the respective right owner.
258. To date, general or blanket licences have been the licensing model for both recording rights and publishing rights for online and mobile applications. For the recording rights, each record company has granted licences for its full repertoire whereas for publishing rights the collecting societies have granted blanket licences comprising all the repertoires which they administered.
259. As explained above, the rights of the performing artists (recording or neighbouring rights) are normally assigned to the record companies. Generally, the record companies have, in addition to the performing artists' rights, neighbouring rights of their own in the recordings. In any event, due to the assignment of the performing artists' rights, all

¹⁰⁷ Jacques Espinasse on Morgan Stanley Conference, Barcelona, 17.11.2006, p.7 and 8: http://www.vivendi.com/ir/download/pdf/MS_TMT_171106.pdf

recording rights are in the hands of the record companies each of which is therefore able to grant blanket licences for its full repertoire of recording rights.¹⁰⁸

260. Publishing rights were, prior to the recently initiated re-organisation of publishing rights for digital applications, licensed by the collecting societies to the online and mobile music providers. As explained above, the collecting societies regularly granted, for "their" territory, a blanket licence which comprised the "world repertoire" of virtually all publishers to which they had access on the basis of bilateral agreements with other collecting societies around the world.
261. In the likely future scenario, as described above, following the already initiated process of re-organisation of publishing rights, online and mobile music providers will no longer be able to get a blanket licence for publishing rights for the "world repertoire" from any collecting society. Similar to the situation regarding recording rights, they will instead have to turn to each individual publisher and its "partner" collecting society which is in charge of licensing the publishing rights of that publisher and of collecting royalties on its account. The individual publisher and its respective partner collecting society will tend to grant general licences covering the complete repertoire, initially limited to the Anglo-American repertoire, of that publisher.
262. Such a publishing rights licence agreement (or framework agreement) determines the licensing terms and conditions, including the applicable tariff or tariff formula.¹⁰⁹ As the terms and conditions are thus negotiated ex ante and for the bundle of titles which form the entire repertoire of the publisher, the size and the characteristics of the repertoire are of major importance for the bargaining position of the publisher vis-à-vis the online and mobile music provider.
263. These licences will cover all full or split publishing rights held by that publisher.¹¹⁰ For the online and mobile music provider a licence is necessary, irrespective whether the relevant publisher holds the full publishing right or only a part of it together with other co-publishers. In case of co-publishing, the provider needs licences from all co-publishers. Solely published works and co-published works thus do not differ with respect to the requirement of a licence. They are also similar in so far as the same licence rate (or royalty rate) applies to all works whether they are solely published or co-published. The only difference occurs regarding the actual payments, as a co-publisher only receives the percentage of the full rate which corresponds to the percentage of his co-publishing right.

¹⁰⁸ Although in some countries "recorded music collecting societies" exist, it appears from the market investigation that online and mobile music providers regularly have direct agreements with the record companies. There is thus no compulsory licensing of recording (neighbouring) rights through these "recorded music collecting societies" as it was the case so far for publishing rights (mechanical and performance rights) through the "publishing collecting societies".

¹⁰⁹ Whilst the blanket licence agreement sets the (abstract) tariffs or tariff formula, the actual payments or accounts receivables are calculated on the basis of the actual sales or usages which are reported by the provider to the publisher.

¹¹⁰ According to the parties, both Universal and BMG hold full publishing rights for [70-80]*% of their respective titles, i.e. approximately [20-30]*% of Universal's and BMG's titles are co-published. For some of these currently co-published titles (namely those currently co-published by Universal and BMG only without any other publisher) Universal acquires full control as a consequence of the merger.

264. With respect to publishing rights which have not been administered by collecting societies, e.g. adaptation rights for ringtones in Germany and Austria, the past experience has shown that music publishers tend to maximise royalty rates. This is illustrated by the fact that in Germany the rate paid to GEMA for the mechanical and performance rights amounts to 10.45% whereas the adaptation right which is in addition claimed by the publishers amounts to 18%. Similar examples have been mentioned with respect to synchronisation rights which are directly licensed by publishers and which are needed for some online applications.

c. Size of the repertoire

265. The market investigation has shown that many online service providers, in particular music downloading services, consider a large repertoire as necessary in order to be able to operate on the market and to be accepted by the final customers. T-online – the internet subsidiary of Deutsche Telekom which provides also music downloading services in addition to fixed online services - indicates for example on its website that it gives access to more than one million songs. Other online download providers have indicated a similar number of titles available.

266. In order to achieve an offer which is accepted by the final customer, an online or mobile music provider ideally needs (blanket) licences from all recording companies and all publishers. The online service providers already have to separately purchase licences for recording rights from each of the different recording companies. After withdrawal from the existing collective rights management, the online service providers will also have to buy several licences for the individual publishers' repertoires and will combine them in order to create their own offer to the market. While the repertoires of the different publishers are therefore in this respect complementary, publishers face (in the restructured market after withdrawal) competitive pressure to the extent that the customers may do without single repertoires and can vary their different combinations of repertoires by including the catalogues of different publishers and exclude one or a few repertoires.¹¹¹

267. Some online music providers have indicated that they would ideally need to cover the world repertoire. However, according to some other providers, it may be possible to run an online or mobile music platform without the titles of some smaller record companies or some publishers, and temporarily, possibly without the repertoire of one major. While it is highly likely that each major's repertoire is already a highly important component of every online service provider's offer it is possible that the online service providers could at present do without one of the majors' repertoires.

268. The parties have provided examples according to which some online music providers offer their platform without one or more of the majors' repertoires, e.g. Apple i-tunes

¹¹¹ This can be illustrated with a hypothetical example: If an online music provider needs to have at least 50% of the total world repertoire and 20 equally large publishers offer their individual repertoires (which are similarly attractive), then this online provider can use many different combinations of complementary repertoires in order to reach the amount of titles needed. Despite the complementary nature of the product, the publishers compete against each other in order to be among the selected ones. If in this scenario one publisher gains a market share of 60%, his repertoire will be a "must-have" since no online music provider can do without this publisher's repertoire. Only the other publishers will compete in order to be chosen in addition. The largest publisher can be sure to be selected in any case.

Australia launched its platform without SonyBMG recording rights. One online music provider also reported in the market investigation that he was able to do without one major's repertoire for one full year before finally also receiving the necessary recording rights from this music company. Moreover, a few niche players may focus for example only on independent music. E-music is known for being a specialized provider of music from independent record companies (its repertoire is not limited to independent publishers). It can, however, not be assumed that this could be a business model for the main market. It has to be concluded that the online service providers need a large repertoire and that they would not be able to provide an acceptable offer to end-customers if they lack more than one of the large majors' repertoires.

d. Importance of chart hits

269. The parties also argued that the online music business was based on the so-called "long-tail" approach. According to this theory, online music platforms have a significant cost advantage for back catalogue in comparison with physical CDs as the digital availability does not generate any storage costs or occupy any shelf space. It is therefore argued that online music platforms generate important revenues through sales of back catalogue. However, the market investigation has demonstrated that, although online music providers consider a large available repertoire, including back catalogue, to be important for their attractiveness in their customers' perception, they generate by far the largest share of their revenues through chart hits (on average approximately 60-80%).¹¹² For mobile music providers, chart hits are even more important. For these reasons, and in respect of both online and mobile music applications, the following analysis of the market power of the different music companies will focus in particular on their presence in the chart titles.
270. However, the larger the relevant¹¹³ repertoire which is lacking in the offer of an online or mobile music provider, the less attractive and the less viable its platform.¹¹⁴ If one music company disposes of a sufficiently large repertoire of publishing and/or recording rights for the relevant titles, this repertoire is to be considered as *incontournable* and therefore represents a *must-have repertoire* since the necessary size and coverage of an online platform will not be achieved without the repertoire of this music company. The following analysis demonstrates that the merger clearly reduces the online providers' possibilities to circumvent Universal/BMG and that the combined repertoire of Universal and of BMG Music Publishing even constitutes such a must have repertoire which cannot be replaced by the repertoire of other music companies.

¹¹² Cf. responses to question 14 of questionnaire of 22.02.2007.

¹¹³ Relevant repertoire means in this context the repertoire which is important for the online or mobile music provider to meet the demand of its customers.

¹¹⁴ A large online music provider explained: "*The larger the repertoire an online music platform can offer its customers, the more viable the service becomes. Consumers want to access a service that has the widest possible offerings and thus acts as a "one-stop-shop", and want to access their favourite music regardless of the label that a particular artist may belong to. If a consumer cannot find his or her favourite music from a music service, it is unlikely that the consumer will return to that service*"; Response of [...] to question 17b) of the Commission's questionnaire of 22.12.2006.

(2) *Measuring the publishers' market power in repertoires*

a. Market shares (revenue based, volume based)

Market share estimates (revenue based)

271. The market shares for online rights (covering the complete repertoire including Anglo-American and Continental European repertoire) on the basis of revenues according to estimates by the parties are set out in the following table. The data provided by the collecting societies deviates to some extent from these estimations and regularly provides for combined market shares for the parties between 20% and 40%.¹¹⁵

Parties' estimates¹¹⁶ – Publishing market shares (online rights)

Online	Universal	BMG	merged	EMI	Warner	Sony/ATV	Others
	%	%	%	%	%	%	%
Austria	[10-20]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Belgium	[0-10]*	[0-10]*	[0-10]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Czech Rep.	[0-10]*	[0-10]*	[10-20]*	[30-40]*	[20-30]*	[10-20]*	[10-20]*
Finland	[0-10]*	[0-10]*	[10-20]*	[0-10]*	[40-50]*	[0-10]*	[30-40]*
France	[10-20]*	[10-20]*	[20-30]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Germany	[0-10]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
Greece	[10-20]*	[0-10]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[10-20]*
Hungary	[20-30]*	[20-30]*	[40-50]*	[20-30]*	[10-20]*	[0-10]*	[0-10]*
Italy	[10-20]*	[10-20]*	[30-40]*	[10-20]*	[10-20]*	[0-10]*	[30-40]*
Netherlands	[10-20]*	[0-10]*	[10-20]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*
Poland	[10-20]*	[10-20]*	[30-40]*	[20-30]*	[10-20]*	[10-20]*	[20-30]*
Spain	[10-20]*	[30-40]*	[40-50]*	[10-20]*	[10-20]*	[0-10]*	[0-10]*
Sweden	[10-20]*	[0-10]*	[10-20]*	[10-20]*	[10-20]*	[0-10]*	[50-60]*
United Kingdom	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[30-40]*
Norway	[10-20]*	[0-10]*	[10-20]*	[10-20]*	[10-20]*	[0-10]*	[40-50]*
EEA	[10-20]*	[10-20]*	[20-30]*	[20-30]*	[10-20]*	[0-10]*	[20-30]*

Source: Notification - Parties

¹¹⁵ The collecting societies were asked to provide the distributions to publishers in 2005 and the total amounts distributed to publishers. The amounts distributed to authors directly as well as commission fees retained by the collecting societies are not included in the figures.

¹¹⁶ With respect to Austria, the parties stated that BMG does not capture separately revenues arising from licensing for digital exploitation in Austria. Such revenues may be included in the total mechanical and performance revenues reported. According to the parties estimates, BMG's 2005 market shares in Austria amounted to, respectively, [10-20]*% for mechanical rights and [0-10]*% for performance rights.

Collecting societies' data¹¹⁷ – Publishing market shares (online rights)

Online	Universal	BMG	merged	EMI	Warner	Sony/ATV	Others
	%	%	%	%	%	%	%
Austria	[...]*	[...]*	[30-40]	[...]	[...]	[...]	[...]
Belgium	[...]*	[...]*	[25-35]	[...]	[...]	[...]	[...]
Czech Rep.	[...]*	[...]*	[25-35]	[...]	[...]	<i>no data</i>	
Finland*	[...]*	[...]*	[25-35]	[...]	[...]	[...]	[...]
France	<i>no data</i>						
Germany	[...]*	[...]*	[20-30]	[...]	[...]	[...]	[...]
Greece	[...]*	[...]*	[30-40]	[...]	[...]	[...]	[...]
Hungary	[...]*	[...]*	[30-40]	[...]	[...]	[...]	[...]
Italy	[...]*	[...]*	[20-30]	[...]	[...]	[...]	[...]
Netherlands	[...]*	[...]*	[25-35]	[...]	[...]	[...]	[...]
Poland	<i>no data</i>						
Spain	[...]*	[...]*	[15-25]	[...]	[...]	[...]	[...]
Sweden*	[...]*	[...]*	[20-30]	[...]	[...]	[...]	[...]
United Kingdom	[...]*	[...]*	[15-25]	[...]	[...]	[...]	[...]
Norway *	[...]*	[...]*	[20-30]	[...]	[...]	[...]	[...]

Source: Collecting Societies - * as part of the Nordic area

272. The information provided by the collecting societies differs from the estimations from the parties in Hungary and Spain where the parties' estimated market shares were much higher than those of the collecting societies' estimates. In Germany, Italy and the United Kingdom the parties' estimates are close to the market shares calculated by the collecting societies. Conversely, the parties' estimates for the other countries (Austria, Belgium, Czech Republic, Finland, Greece, the Netherlands, Sweden and Norway) are underestimated.

Market share estimates (chart based)

273. The Commission also carried out an analysis of the annual top 100 single charts for 2006¹¹⁸ - as provided by the parties - in every affected country. From this analysis market shares were derived which are based on the number of chart hits which may be used as an approximation of volume based market shares. Due to the importance of chart hits for online customers, the analysis of this part of the total repertoire indicates the effects of the merger. 77% of the online and mobile respondents indicated that chart hits are very important, representing 50-90% of their revenues.
274. The following calculations are based on the number of individual titles represented by a major within the charts. The chart data includes the ranking of the best selling titles, however it does not systematically include the number of titles sold. Since the presence of

¹¹⁷ No online data was provided by the French and the Polish collecting societies, and the Czech data is incomplete. For the Nordic countries (Sweden, Norway, Finland), the figures provided by NCB were taken. NCB administers the mechanical rights (including those for online use) for all Nordic and Baltic countries – no split according to the different countries was provided.

¹¹⁸ In countries where no top 100 annual charts are set up, the most appropriate alternative charts were taken into account (Austria: www.austriatop40.at ; Belgium: www.ultratop.be; Czech Republic: www.ifpicr.cz; Finland: www.yle.fi; France: www.disqueenfrance.com; Germany: www.media-control.de; Greece: www.ifpi.gr; Hungary: www.mahasz.hu; Italy: www.fimi.it; the Netherlands: www.magacharts.nl; Poland: www.rmfm.pl; Spain: www.promusicae.es; Sweden: www.hitlistan.se; United Kingdom: www.theofficialcharts.com; Norway: www.ifpi.no)

titles in the charts and the shares of chart-hits represented by the different publishers are analyzed, the assessment values a number 1 hit equally to a number 100.¹¹⁹

275. The charts are of particular importance for online music providers, as they notably create traffic and attract customers on their platforms. An analysis focused on the charts therefore adequately represents the specific demand of these customers. Apart from this, the chart analysis may also be a rough proxy for the overall market position of the parties in the publishing industry. This can be shown on the basis of market shares derived from chart data and which gives a similar picture as the revenue-based market shares provided by the collecting societies. The following methodology was applied: When a title is controlled by two publishers, the market share associated to this title is distributed between the publishers according to their share of the title (i.e. share of 33% is counted as 0.33; share of 100% is counted as 1). By considering any title according to the specific share held by each publisher a similar perspective is chosen as in the revenue based market share calculations by the parties and the collecting societies since revenues also arise for each publisher only according to the individual share of the right.

276. The results from this analysis on the basis of official charts are summarized in the following table:

Publishing market shares – top 100 official charts- 2006

	Universal	BMG	comb.	EMI	Warner	Sony/ATV	Others
Austria	17%	9%	25%	26%	11%	4%	34%
Belgium	14%	6%	20%	11%	12%	3%	54%
Czech R.	11%	9%	20%	13%	10%	6%	52%
Finland	5%	7%	12%	12%	7%	4%	65%
France	5%	13%	18%	11%	9%	4%	60%
Germany	15%	10%	24%	21%	14%	2%	38%
Greece	8%	6%	13%	7%	10%	3%	67%
Hungary	9%	8%	17%	19%	9%	3%	53%
Italy	13%	8%	21%	18%	15%	1%	45%
Netherlands	17%	10%	27%	14%	10%	5%	44%
Poland	14%	6%	19%	10%	6%	6%	58%
Spain	5%	8%	14%	9%	13%	1%	64%
Sweden	9%	15%	24%	16%	12%	3%	45%
United Kingdom	11%	10%	21%	26%	13%	10%	30%
Norway	13%	6%	19%	17%	14%	6%	44%
Affected markets	11%	10%	21%	19%	12%	5%	43%

¹¹⁹ Therefore, for instance in the United Kingdom charts, the title n°1 "Crazy" from "Gnarls Barkley" accounts for 820,050 sales and the title n°100 "MYMYMY" from "Armand Van Helden" accounts for 75,267 sales in 2006. Despite this large difference, both titles will be considered as accounting for 1% of the top 100 titles. This methodology might appear misleading at first sight; however, as the majors are evenly represented in the top 100 chart among top 10, top 20 or top 50, the results are very similar to those obtained when weighting each title by its sales. Weighted calculations were conducted for several of the countries where sales are available with chart ranking (France, Germany, United Kingdom). The final results are generally similar to those obtained without weighting each title by its sales.

277. For the largest markets (United Kingdom, Germany, Italy, Spain, Sweden, and the Netherlands) the market shares of Universal + BMG calculated on this basis are close to those provided by the collecting societies for 2005. The results for the smaller countries (Austria, Belgium, Czech Republic, Finland, Greece, Hungary and Norway) deviate more significantly and market shares provided by the collecting societies are higher than those calculated from the official charts. Nevertheless, although deviations in specific countries cannot be excluded, the chart perspective may be used as a rough proxy for the parties' overall position in the market.¹²⁰
278. The position from EMI in the chart is slightly stronger than its position in terms of total digital revenue as calculated by the collecting societies. This might reflect the success of EMI in developing new successful authors. Warner Chappell and Sony/ATV are similarly strong in the charts and with regard to digital revenue distributed by collecting societies. The position of the independents is also similar in the charts and when considering total digital revenues distributed by collecting societies. It can therefore be assumed that the chart analysis is also relevant for the analysis of the complete catalogue (notably back catalogue), considering that the relative market position of the different publishers is globally reflected in the market shares as calculated for the official charts only.

Inadequacy of market shares to measure market power

279. The market investigation has shown that market shares on the basis of revenues alone might not fully reflect the market positions of the different publishers since they do not adequately take into account their power on the basis of **co-publishing** and **recording rights**.
280. In many cases, several authors under contract with different publishers write a song together which leads to split copyrights (co-publishing). Each author owns a share of the song and each publisher administers the shares of the author under contract. The parties have submitted that approximately [20-30]*% of their catalogue is composed of co-published works. This proportion is even higher for some independents and major publishers. In order to offer the song, an online music provider needs to have a licence for all shares of publishing rights held by the different authors or their publishers in a specific title so that each publisher can veto the use of the right. For instance the title "Crazy" from "Gnarls Barkley", which ranks n°1 in the United Kingdom 2006 charts, is co-published by BMG, Warner and one independent.
281. To date, the collecting societies have organized the combination of the co-published rights by granting blanket licences for the complete world repertoire which then automatically covered all split rights. In the near future music online providers will have to secure those rights directly from the different publishers or their representatives.

¹²⁰ A similar result can be derived from a chart analysis conducted by the parties on the basis of official charts for 2005. The combined market share of the parties resulting from the chart analysis and based on the methodology indicated above would be 24% for all affected countries together. The EEA-wide market share as estimated by the parties on the basis of revenues is 26% for 2005. The overall market position as it is reflected in the conventional revenue based market shares therefore seems to be adequately reflected by the chart analysis on the basis of weighted co-publishing shares.

282. Some market participants further indicated in their responses that the parties' market power is based on both recording and publishing rights. Recording rights have always been managed by the recording branches of the majors individually. After the withdrawal from the traditional collecting societies system, all vertically integrated music companies will in the future be able to negotiate the access to the combined package of recording rights and publishing rights including fully and partly owned rights.
283. In order to offer a title, an online music provider must acquire licences for all co-publishing rights and recording rights controlling this title. If one part of all these rights is not covered, the online provider cannot offer this title to its customers. As a consequence, also shares of publishing rights and recording rights alone may confer market power which consequently has to be estimated by fully taking into account titles co-published or recorded by the parties, in addition to titles 100% published. The following chart analysis reflects these considerations under the concept of "control shares".

b. Control shares (chart based)

General principle of the analysis

284. In order to assess the market power derived from co-publishing and control of recording rights, the annual top 100 single charts for 2006 were analysed. The conventional market share analysis was subsequently extended in order to take into account the specificities of the market: An online music provider which fails to reach a licensing agreement with a particular publisher does not only lose access to the titles for which the publisher has the full publishing rights but also to those for which only parts of them are owned. The access to the specific publisher's partly owned songs is lost not only partly but completely since it is not possible to use a split right independently.

Split rights counted as full control

285. In order to reflect this specific market situation, a further analysis was conducted by counting each split right as a full work. The resulting shares (hereinafter "control shares") therefore do not represent market shares – they add up to more than 100% due to the overlap between the co-publishers. For instance, in the United Kingdom chart, the n°1 hit "Crazy" by "Gnarls Barkley" is co-published between BMG (30%), Warner (35%) and an independent publishing company (35%). BMG, as well as Warner and the independent publisher, are considered to control this title. This does not mean that BMG alone could license this work. It means that any online service who wants to use this song needs a licence from all three co-publishers and loses the complete song if he fails to achieve a licence from any one of the three co-publishers.

Methodology

286. Moreover, the following methodological position was taken:
- There are some titles which are already currently co-published by Universal and BMG. Therefore, for all BMG songs in which Universal already owns a co-publishing right, the BMG publishing right was not counted. For instance in the United Kingdom, the title "Smack that" from "Akin ft. Eminem" is co-published by Universal and BMG. To calculate the number of titles controlled by the merged entity Universal/BMG, this title was counted only once. The control share of Universal/BMG is therefore lower than the arithmetic addition of Universal and BMG control shares.

- Only publishing rights in Anglo-American titles were counted, since a withdrawal from the existing collective rights management system in the near future is more certain for this part of the repertoire than for the rest of the repertoire. For instance, in Germany, Universal Music Publishing owns publishing rights of 23 of the top 100 online titles. Among these titles, 2 belong to Continental European repertoire. Thus it was considered that in the short term Universal Music Publishing will only be able to influence the commercialization of 21 top 100 online titles in Germany.
- According to the data presented by the parties, many chart titles can belong to both Continental European and Anglo-American repertoires. This is possible when a title is co-published with one share controlled by a Continental European publisher and the other by a publisher in the United Kingdom. Controlling a share of a work due to its full or split publishing rights in Anglo-American titles is sufficient to block licensing. Therefore, when the co-published share of a publisher lies in the Anglo/American repertoire, it has been considered in this Decision that this publisher can influence the commercialisation of the relevant title. The control share was always only allocated to the co-publisher owning the Anglo-American part of the right¹²¹.
- Annual charts are available in most countries. However in several ones¹²², only weekly charts are available. For these countries, the charts of 13 different weeks, evenly distributed over the year, have been aggregated.
- The analysis was conducted in detail for the year 2006 and was cross-checked against the year 2005. The results of the year 2005 were broadly comparable with the year 2006.

287. Nevertheless, the chart analysis of one or two years can only be a kind of "snapshot" to reflect the position of a music company in the recent past and proxy for its market position. As the control shares regularly alter from year to year and depend on the success and the combination of different authors and performing artists, these control shares can only constitute indications for the market power of a music company.

288. The analysis was conducted for official charts which exist in all affected countries. In some countries also specific online charts exist. Where such online charts existed, an analysis showed that the parties' control shares were slightly higher according to online charts as compared to the official charts (with the exception of Norway).

¹²¹ "Hung up" from "Madonna" ranked n° 50 in the French charts in 2006. This title is co-published by Universal and Warner. The share of publishing controlled by Universal is part of the European continental repertoire, whereas the share controlled by Warner is part of the Anglo/American repertoire. Following the methodology described above, it is considered that this title is controlled by Warner, but it is not controlled by Universal.

"Talk" from "Coldplay", ranked n° 24 in the Dutch charts 2006. This title is co-published by BMG, Warner, Sony/ATV and independent(s). The share of publishing controlled by BMG is part of the Anglo/American repertoire, whereas the shares controlled by all the other publishers are part of the European continental repertoire. Following the methodology described above, it is considered that this title is controlled by BMG, but it is not controlled by the other publishers.

¹²² Official charts 2006: Czech Republic, Spain, Finland, Greece, Norway, Poland.

289. In the following, the official charts are used since they constitute the most representative data and therefore the most reliable basis for an analysis. Online charts are still nascent and cover in most countries exclusively or mainly online downloads. Still in 2005, the online charts only covered a very limited number of titles. While in 2006 a larger coverage was reached, it remains uncertain whether these charts are sufficiently representative. It is worth noting that for the time being, the online downloading of music is mainly done by a relatively small group of persons which could exhibit a specific taste of music since they for example might represent a similar age. The retail online music market is, however, strongly developing and is expected to grow significantly in the near future. It is likely that the participation of a larger public in this market will lead to the online charts becoming closer to the official charts which cover a much larger customer base.
290. In addition, the online rights market does not only consist of online music services offering titles for downloading. There are also other online music applications such as audio and video streaming which have not been covered by online charts. Moreover, mobile music applications which account for approximately [...] *% of Universal's digital (combined online and mobile) music revenues are not covered by online charts. Therefore, online charts do not appear to better reflect the market conditions for the overall online market as defined above, i.e. including all online and mobile applications. In addition, it appears that mobile music applications, e.g. mastertones, are strongly driven by traditional chart hits. Customers to a large extent wish to have the current chart hits as mastertones on their mobile phones. For mastertone providers and other mobile music providers, as for online music providers other than download services, therefore the official charts reflect their demand more closely than the online charts.
291. In order to avoid the described uncertainties of the digital charts, in the following the official charts will be used for the analysis.

Control shares (chart based) for publishing rights in Anglo-American titles

292. The analysis of publishing rights based on this methodology shows that of all chart hits (including Continental European and Anglo-American titles), Universal and BMG will control on average 27 titles out of 100 due to their full or split publishing rights in Anglo-American titles (i.e. without taking into account their control of Continental European repertoire), whereas they respectively controlled 15% and 13% pre-merger¹²³:

¹²³ The same analysis conducted on the base of the 2005 official charts leads to close results. Universal controls (either as sole or co-publisher) pre-merger 21 titles out of 100, BMG controls 15 titles out of 100, and Universal/BMG would control 32 titles out of 100 at the EEA level. It can be noted that the overlap between Universal and BMG is greater in 2005, with 4 of the BMG titles co-published by Universal and BMG, whereas only one of the BMG title is co-published with Universal in 2006.

Control shares – only publishing rights

Percentage of titles controlled (100% published and co-published) by publishers due to their full or split publishing rights in Anglo-American titles – 2006

	Universal	BMG	comb.	EMI	Warner	Sony/ATV	Others
Austria	18%	8%	25%	30%	12%	7%	27%
Belgium	17%	12%	27%	20%	13%	6%	42%
Czech R.	13%	17%	29%	21%	13%	6%	29%
Finland	5%	6%	11%	13%	7%	4%	18%
France	4%	10%	14%	13%	9%	6%	16%
Germany	18%	11%	28%	29%	13%	8%	29%
Greece	12%	7%	18%	9%	9%	5%	21%
Hungary	19%	13%	29%	20%	12%	8%	24%
Italy	16%	12%	26%	24%	22%	2%	30%
Netherlands	19%	15%	33%	19%	11%	9%	27%
Poland	14%	8%	22%	16%	9%	11%	31%
Spain	5%	9%	13%	6%	14%	0%	31%
Sweden	9%	9%	17%	17%	10%	5%	25%
United Kingdom	20%	19%	38%	44%	22%	16%	48%
Norway	20%	9%	28%	23%	16%	9%	21%
Affected markets¹²⁴	15%	13%	27%	28%	16%	9%	33%

Source: official charts 2006 – Commission analysis

293. In Finland, Universal/BMG will control only 11% of the titles, whereas in the United Kingdom, it will control as high as 38% of the titles on the basis of their publishing rights. EMI will control on average 28% of chart titles across the affected markets, which is comparable to the merged entity. Conversely, Warner Chappell and Sony/ATV will be far behind with respectively 16% and 9%.
294. For the sake of clarity, when it is assumed that Universal/BMG controls 14% of the titles in France, this means that out of 100 chart titles in this country Universal/BMG has a publishing share (co-published or total publishing control) in 14 titles which all belong to the Anglo/American repertoire. Nevertheless, within the 100 chart titles, Continental-European repertoire is still present. For instance in France "Le diner" from "Benabar" ranks 19th and is co-published by Universal. It is however not counted in the 14 titles controlled by Universal/BMG as it belongs to the Continental-European repertoire.

Control shares (chart based) for publishing and recording rights in Anglo-American titles

295. Some market participants further indicated in their responses that the parties' market power is based on both recording and publishing rights. Generally a title is recorded by a single record company. Record joint ventures are rare as opposed to the situation prevailing in the publishing area where co-publishing is frequent. Therefore with regard to recording rights, a market share of 10% will correspond to the controlling of 10 titles out of 100.

¹²⁴ The figures show an average weighted on the basis of record sales. See precedent notes.

296. The recording rights analysis includes titles from both Continental European and Anglo-American repertoires as there is no need for such distinction in the recorded music industry. Indeed a record company directly controls the commercialization of all its titles, whatever the repertoire they belong to. For the merged entity's control share, only Universal's recorded titles were counted since BMG's recording business (SonyBMG) is not part of the merger. With respect to publishing, both Universal's and BMG's Anglo-American titles were counted in order to derive the control share of the merged entity.

Recording market shares

297. Based on the top 100 official charts, the recording market shares are the following:

Record industry market shares, based on top 100 official charts 2006

	Universal	BMG	comb.	EMI	Warner	SonyBMG	Others
Austria	42%		42%	11%	14%	26%	7%
Belgium	29%		29%	29%	9%	14%	19%
Czech R.	42%		42%	19%	17%	18%	5%
Finland	22%		22%	13%	15%	15%	34%
France	29%		29%	10%	18%	34%	9%
Germany	40%		40%	6%	13%	33%	8%
Greece	30%		30%	28%	8%	19%	15%
Hungary	30%		30%	16%	8%	21%	25%
Italy	18%		18%	24%	18%	22%	18%
Netherlands	27%		27%	14%	11%	16%	32%
Poland	43%		43%	14%	9%	25%	8%
Spain	8%		8%	25%	11%	27%	29%
Sweden	22%		22%	6%	18%	27%	27%
United Kingdom	43%		43%	6%	14%	24%	13%
Norway	34%		34%	8%	15%	31%	13%
Affected markets ¹²⁵	34%		34%	10%	14%	27%	14%

Source: official charts 2006 – Commission analysis

Chart-analysis: Publishing and recording rights

298. After the re-structuring of the online rights market all vertically integrated music companies will in the future be able to negotiate the access to the combined package of recording rights and publishing rights including fully and partly owned publishing rights for online applications. The reason for this is that both categories of rights are held and controlled by the same undertaking and the customers are also the same. An online music provider will therefore have to negotiate with a music company whose market power will derive from the titles it controls either by recording rights or by publishing rights.
299. The titles with one or several of the following characteristics are considered to be directly controlled by the music companies, since they can, or in the near future will be able to, influence the commercialization conditions of these titles:

¹²⁵ The figures show an average weighted on the basis of record sales. See precedent notes.

- a. Recording rights are controlled by the record sister company (i.e. Universal Music Group), including Continental European and Anglo-American repertoires.
 - b. Publishing rights are 100% controlled by the publishing sister company (i.e. Universal Music Publishing or BMG Music Publishing) for Anglo-American repertoire only.
 - c. Publishing rights are partly controlled by the publishing sister company (i.e. Universal Music Publishing or BMG Music Publishing) for Anglo-American repertoire only.
300. The titles with the following characteristics are considered not to be directly controlled by the music companies, considering that they are unlikely able to influence the commercialization conditions of these titles in the future:
- a. Anglo-American repertoire: Recording rights are not controlled by the record sister company (i.e. Universal Music Group), and the sister publishing company does not have publishing rights (100% control or co-published).
 - b. Continental-European repertoire: Recording rights are not controlled by the record sister company (i.e. Universal Music Group), whatever the share of publishing rights controlled by the publishing sister company (i.e. Universal Music Publishing). For instance, "Le diner" in France is recorded by Sony BMG and partly published by Universal, however as this title belongs to the continental repertoire, it is not counted as controlled by Universal. It is nevertheless still part of the top 100 in France.
301. The following table indicates how many titles out of the top 100 official charts the major companies control:

Control shares – publishing and recording rights

Percentage of titles controlled by majors due to either control over recording rights or control over publishing rights (100% controlled or co-published) in Anglo-American titles – 2006

	Universal	BMG increment	comb.	EMI	Warner	Sony BMG ⁽¹⁾	Others
Austria	50%	6%	56%	41%	22%	26%	33%
Belgium	36%	7%	43%	47%	18%	14%	57%
Czech R.	43%	10%	52%	38%	21%	18%	33%
Finland	26%	4%	30%	25%	19%	15%	47%
France	31%	9%	40%	23%	24%	34%	25%
Germany	47%	7%	54%	35%	22%	33%	36%
Greece	38%	6%	44%	35%	16%	19%	35%
Hungary	41%	7%	48%	35%	14%	21%	48%
Italy	28%	10%	38%	42%	28%	22%	46%
Netherlands	36%	10%	46%	32%	18%	16%	55%
Poland	47%	4%	51%	29%	15%	25%	37%
Spain	11%	8%	19%	27%	22%	27%	54%
Sweden	27%	6%	33%	23%	23%	27%	47%
United Kingdom	51%	10%	61%	49%	30%	24%	52%
Norway	40%	6%	46%	30%	24%	31%	34%
Affected markets¹²⁶	40-41%	8-9%	49-50%	37%	24-25%	27-28%	42-43%

Source: official charts 2006 – Commission analysis – ⁽¹⁾ Sony BMG data does not include overlap with Sony/ATV

302. On average, before the merger Universal can negotiate access to 40-41% of the official chart hits. Together with BMG's catalogue this share will increase to up to 49-50%¹²⁷. Universal/BMG will control as high as 61% of chart titles in the United Kingdom, whereas this figure is 19% in Spain¹²⁸.
303. Pre-merger, Universal is already ahead of the other majors, controlling 4% more titles than EMI notably. Post merger, the advantage over the other majors is significantly increased. Universal/BMG will control almost twice as many titles as Sony BMG (not including Sony/ATV)¹²⁹ and Warner and 1.3 times as many titles as EMI. The merger would allow Universal to become the only major controlling half of the catalogue.
304. The parties submitted that a part of the titles distributed by Universal Music Group (record) are distributed within distribution or licensing deals on behalf of the record

¹²⁶ The figures show an average weighted on the basis of record sales. See precedent notes.

¹²⁷ The same analysis was conducted based on the official charts 2005. According to this set of data, Universal can before the merger negotiate access to 45% of the official chart hits. Together with BMG's catalogue this share will increase to up to 52%.

¹²⁸ When analysing the official charts 2005, it appears that Universal/BMG would control as high as 60% of chart titles in the United Kingdom and as low as 30% in Sweden. It would control 38% of Spanish charts.

¹²⁹ SonyBMG is a Joint Venture grouping the recording activities of Sony and Bertelsmann companies. Sony/ATV is a Joint Venture between Sony and the artists Michael Jackson and active in the music publishing sector.

company which originally recorded the title. However, these deals account for a limited share of the titles recorded by Universal. In addition, the majority of these deals are licensing deals where the licensee (Universal Music Group) has a certain degree of commercial freedom to promote, distribute and market a title. Therefore the Commission considers that these titles should be considered as the other Universal titles in terms of control.

c. Analysis of affected markets

305. A number of the affected countries in the EEA are significantly impacted by the merger. In assessing the control shares set out above, it has to be taken into consideration that these shares are not equivalent to traditional market shares. Genuinely, control shares are higher than market shares and add up to more than 100% due to the consideration of co-publishing and recording. Any company with a high control share will be difficult to circumvent for the demand side. This is all the more the case where a company reaches 50% since only half or less of the repertoire remains available as substitute. In a cautious approach, the Commission therefore considers that the merger would have a significant impact in those markets where the merged entity would reach or exceed a control share of 50%.
306. Universal/BMG will control 50% or more of the titles in the top 100 charts in 5 countries and on EEA-level.

Austria

307. Universal controls 50 titles out of 100. Together with BMG, they will control 56 titles out of 100. This 6% increment is among the smallest if compared to the average increment calculated for the affected markets.
308. EMI is relatively strong in Austria, controlling 41 titles out of 100 in the official charts. Warner, SonyBMG and Sony/ATV are significantly smaller, controlling respectively 22%, 26% and 7% of the official chart hits. All these music companies are already smaller than Universal and would be far behind Universal/BMG.
309. On the basis of this entrenched market position it is likely that Universal/BMG will be able to increase prices for its repertoire after the merger. Any circumvention of Universal/BMG by an online user will become even more difficult after the merger since only 44% of the top titles remain free of any Universal/BMG interest.
310. As described above, the specific regulation which exists in Austria on the basis of the law on collecting societies¹³⁰ is not likely to prevent such a price increase. The arbitration mechanism only exists on the basis of the national activity of the collecting societies AKM and Austro Mechana but does not define an extended scope for multi-territorial licensing and licensing in Austria by foreign collecting societies. In Austria only one collecting society may obtain an operating licence per category of right. Foreign collecting societies could therefore not have the status of a collecting society but only that of an agent not bound to the specific collecting society's rules.

¹³⁰ Verwertungsgesellschaftengesetz

311. The merger therefore significantly impacts the Austrian market for online rights.

Belgium

312. Universal controls 36 titles out of 100. Together with BMG, they will control 43 titles out of 100.

313. EMI is already strong in Belgium, controlling 47 titles out of 100 in the official charts remaining larger than Universal, even after the merger. Warner, SonyBMG and Sony/ATV are significantly smaller, controlling respectively 18%, 14% and 6% of the chart hits. They are already smaller than Universal and would be far behind Universal/BMG.

314. In Belgium, the merger would increase Universal/BMG's control share to 43%. Universal's repertoire would therefore still be substitutable for a user by combining most of the other publishers' repertoires since 57% of all chart hits would still be free of any Universal interest. It is therefore unlikely that the merger creates competition concerns with respect to the Belgian market. The merger therefore does not lead to a significant impediment of competition in the Belgian market for online rights.

Czech Republic

315. According to official charts Universal controls 43 titles out of 100. Together with BMG, they will control 52 titles out of 100. This 9% increment is equal to the average increment calculated for the affected markets.

316. EMI controls 38 titles out of 100 in the official charts. Pre-merger EMI was comparable to Universal, whereas after the merger it will become significantly smaller than Universal/BMG. Warner, SonyBMG and Sony/ATV are significantly smaller, controlling respectively 21%, 18% and 6% of the official chart hits. All these music companies are already smaller than Universal and would be far behind Universal/BMG.

317. After the merger, Universal/BMG will have a controlling stake in more than half of the chart hits in the Czech Republic. No online service provider will be able any longer to substitute Universal/BMG by combining all other repertoires. While the tariffs of the Czech collecting society OSA may be reviewed upon appeal by the Ministry of Culture, there appear to be no legal provisions which would provide for explicit rules for EEA-wide licences which may in addition be granted by a foreign collecting society. It is unlikely that a price increase by Universal in the Czech Republic could be effectively prevented by the existing national regulation. If at all, this would be conceivable if Universal/BMG chose OSA as service provider which, on the basis of the current information, is not intended.

318. In the Czech Republic, the merger would increase Universal/BMG's control share above the 50% threshold which means that it is not possible anymore to replace Universal/BMG's repertoire even by the combination of all other repertoires since the repertoire without any Universal interests is smaller than the one in which Universal/BMG has a controlling stake in one form or the other. It is therefore likely that Universal/BMG will be able to increase prices after the merger in the Czech Republic. The merger therefore significantly impacts the market for online rights in the Czech Republic.

Finland

319. According to official charts Universal controls 26 titles out of 100. Together with BMG, they will control 30 titles out of 100. This 4% increment is the smallest in all affected countries if compared with the average increment calculated for the affected markets where official charts are available. Finland is the least affected market.
320. All the major music companies are relatively weak in Finland. EMI controls 25 titles out of 100 in the official charts and is comparable to Universal. Warner, SonyBMG and Sony/ATV are smaller. They control respectively 19%, 15% and 4% of the official chart hits.
321. On the basis of the comparably low control shares it seems that online music providers would, even after the merger, still be able to do without Universal/BMG in case Universal/BMG required excessive prices since more than 70% of the totality of chart hits are without any Universal/BMG interest and therefore available as alternative. It is likely that sufficient leeway would remain for the online music providers and competitive pressure on Universal/BMG would consequently not decrease due to the merger. In Finland, it can therefore not be concluded that the merger would create competition concerns on a purely national basis. The merger therefore does not lead to a significant impediment of effective competition on the market for online rights in Finland.

France

322. Universal controls 31 titles out of 100. Together with BMG, they will control 40 titles out of 100. This 9% increment is slightly more than the average increment calculated for the affected markets. EMI is relatively weak in France, controlling 23 titles out of 100 in the charts. Pre-merger EMI was already smaller than Universal – after the merger, it becomes significantly smaller than Universal/BMG. Universal/BMG will control almost twice as many titles as EMI in the charts (x 1.7). Warner, SonyBMG and Sony/ATV are significantly smaller, controlling respectively 24%, 34% and 6% of the official chart hits. They are already smaller than Universal and would be far behind Universal/BMG.
323. Universal will after the merger control 40% of the chart hits. Universal's repertoire would therefore still be substitutable for a user by combining most of the other publishers' repertoires since 60% of all chart hits would still be free of any Universal interest. It is therefore unlikely that the merger creates competition concerns with respect to the French market. The merger therefore does not lead to a significant impediment of effective competition on the market for online rights in France.

Germany

324. According to official charts Universal controls 47 titles out of 100. Together with BMG, they will control 54 titles out of 100.
325. EMI controls 35 titles out of 100 in the official charts. Pre-merger EMI was already smaller than Universal, it becomes significantly smaller than Universal/BMG. Universal/BMG will control 1.5 times as many titles as EMI in the official charts. Warner, SonyBMG and Sony/ATV are smaller, controlling respectively 22%, 33% and 8% of the chart hits. They are already smaller than Universal and would be far behind Universal/BMG.

326. In Germany, Universal/BMG will therefore significantly increase its control share and thereby its market power due to the merger. A specific arbitration mechanism exists in Germany where users can appeal against tariffs set by GEMA to the Arbitral Tribunal at the Patent Office. However, according to the parties' information a body applying for a status of a collecting society must be located in Germany. It is therefore - as in the other countries – probable that any foreign collecting society would rather act as agent of the respective publisher and would not fall under the national rules for collecting societies. The German collecting society GEMA indicates that it would likely depend on the agreement between the publisher and the selected collecting society whether the regulation applies or not. This clearly shows that any such regulation does not apply per se.¹³¹ Against this background it is likely that Universal/BMG will after the merger have the possibility to increase prices.
327. In Germany, the merger would increase Universal/BMG's control share above the 50% threshold which means that it is not possible anymore to replace Universal/BMG's repertoire even by the combination of all other repertoires since the repertoire without any Universal interests is smaller than the one in which Universal/BMG has a controlling stake in one form or the other. It is therefore likely that Universal/BMG will be able to increase prices after the merger in Germany. The merger therefore significantly impacts the online rights market in Germany.

Greece

328. According to official charts Universal controls 38 titles out of 100. Together with BMG, they will control 44 titles out of 100. This 6% increment is among the smallest in all affected countries if compared with the average increment calculated for the affected markets where official charts are available.
329. EMI is comparable to Universal/BMG. It controls 35 titles out of 100 in the official charts. Warner, SonyBMG and Sony/ATV are significantly smaller and control respectively 16%, 19% and 5% of the official chart hits.
330. In Greece, Universal will control 44% of the chart hits in Greece after the merger. Universal's repertoire would therefore still be substitutable for a user by combining most of the other publishers' repertoires since 56% of all chart hits would still be free of any Universal interest. It is therefore unlikely that the merger creates competition concerns with respect to the Greek market. The merger therefore does not lead to a significant impediment of effective competition on the market for online rights in Greece.

Hungary

331. According to official charts Universal controls 41 titles out of 100. Together with BMG, they will control 48 titles out of 100. This 7% increment is below average if compared to the average increment (9%) calculated for the affected markets where official charts are available.
332. EMI controls 35 titles out of 100 in the official charts. Pre-merger, it was smaller to Universal, it will become significantly smaller than Universal/BMG. Warner, SonyBMG

¹³¹ See GEMA's reply to Questionnaire to collecting societies 3, dated 5 February 2007, question 6.

and Sony/ATV are significantly smaller and control respectively 14%, 21% and 8% of the official chart hits.

333. In Hungary, Universal will therefore control 48% of the chart hits after the merger. Universal's repertoire would therefore still be substitutable for a user by combining most of the other publishers' repertoires since 52% of all chart hits would still be free of any Universal interest. It is therefore unlikely that the merger raises competition concerns with respect to the Hungarian market. The merger does not therefore lead to a significant impediment of effective competition on the market for online rights in Hungary.

Italy

334. Universal controls 28 titles out of 100. Together with BMG, they will control 38 titles out of 100. EMI will continue leading before Universal - however, with a smaller distance to Universal. Warner controls 28%, SonyBMG 22% and Sony/ATV 2% of the chart hits.
335. An online music provider wanting to circumvent Universal/BMG's catalogue will still have more than 60% of the total repertoire by which it could replace Universal/BMG. It is therefore unlikely that the merger will lead to competition concerns in Italy. The merger will not lead to a significant impediment of effective competition on the market for online rights in Italy.

The Netherlands

336. According to official charts, Universal controls 36 titles out of 100. Together with BMG, they will control 46 titles out of 100.
337. EMI controls 32 titles out of 100 in the official charts. After the merger, it becomes significantly smaller than Universal/BMG. Warner, SonyBMG and Sony/ATV are significantly smaller, controlling respectively 18%, 16% and 9% of the chart hits. They are already smaller than Universal and would be far behind Universal/BMG.
338. In the Netherlands, Universal will therefore control 46% of the chart hits after the merger. Universal's repertoire would therefore still be substitutable for a user by combining most of the other publishers' repertoires since 54% of all chart hits would still be free of any Universal interest. It is therefore unlikely that the merger raises competition concerns with respect to the Dutch market. The merger therefore does not lead to a significant impediment of effective competition on the online rights market in the Netherlands.

Poland

339. According to official charts Universal controls 47 titles out of 100. Together with BMG, they will control 51 titles out of 100. This 4% increment is among the lowest in all affected countries if compared to the average increment calculated for the affected markets where official charts are available.
340. EMI is relatively weak in Poland, controlling 29 titles out of 100 in the official charts. Pre-merger, it was already significantly smaller than Universal. Warner, SonyBMG and Sony/ATV are significantly smaller and control respectively 15%, 25% and 11% of the official chart hits.

341. Universal/BMG will after the merger control half of the chart hits in Poland and will thereby become a must-have publisher. The merger would increase Universal/BMG's control share above the 50% threshold which means that it is not possible anymore to replace Universal/BMG's repertoire even by the combination of all other repertoires since the repertoire without any Universal interests is smaller than the one in which Universal/BMG has a controlling stake in one form or the other. It is therefore likely that Universal/BMG will be able to increase prices after the merger in Poland. The merger therefore significantly impacts the online rights market in Poland.

Spain

342. According to official charts, Universal controls 11 titles out of 100. Together with BMG, they will control 8 titles out of 100. EMI leads in Spain with 27% together with SonyBMG which reaches an equal value.
343. Due to the unusually weak position of the parties in Spain, it is not likely that Universal will be able to increase prices after the merger. The merger therefore does not lead to a significant impediment of effective competition on the online rights market in Spain.

Sweden

344. Universal controls 27 titles out of 100. Together with BMG, they will control 33 titles out of 100.
345. EMI, Warner and Sony BMG are comparable and control respectively 23, 23 and 27 titles out of 100 in the official charts. Pre-merger they were all comparable to Universal, they become smaller than Universal/BMG. However the gap (in terms of number of titles controlled) between Universal/BMG and these three major companies is less pronounced than in the other affected markets. Sony/ATV is significantly smaller, controlling 8% of the chart hits.
346. With a control share of 33% for Universal in Sweden, the online music providers would still have almost 70% of the market as alternative. It therefore cannot be concluded that the merger will lead to competition concerns in this market. The merger therefore does not lead to a significant impediment of effective competition on the online rights market in Sweden.

United Kingdom

347. Universal controls 51 titles out of 100. Together with BMG, they will control 61 titles out of 100. This 10% increment is slightly inferior to the average increment calculated for the affected markets. The United Kingdom is the country where Universal/BMG controls the most titles due to the low penetration of the continental repertoire.
348. EMI is particularly strong in the United Kingdom and controls 49 titles out of 100 in the official charts. Pre-merger EMI was smaller than Universal, it becomes significantly smaller than Universal/BMG, however still controlling almost half of the chart titles. Warner, SonyBMG and Sony/ATV are significantly smaller, controlling respectively 30%, 24% and 16% of the official chart hits. They are already smaller than Universal and would be far behind Universal/BMG.

349. In the United Kingdom, Universal and BMG will together reach a very strong market position in terms of control shares. Any online provider wishing to switch in case of a price increase will have only less than 40% of the remaining repertoire of chart hits available. It is evident that this is not sufficient as an effective alternative and that Universal/BMG's repertoire will become a must-have product without which it will not be feasible for an online music provider to offer an acceptable platform to end-customers. It is also not likely that regulation in the United Kingdom would be applicable to an extent which could prevent any price increase resulting from the merger. As in all other affected countries the regulation is based on national licensing by the national collecting society. It is unlikely that the rules could equally cover EEA-wide licences and activities from other collecting societies in the United Kingdom.
350. It is therefore likely that Universal/BMG will be able to increase prices after the merger in the United Kingdom. The merger consequently significantly impacts the online rights market in the United Kingdom.

Norway

351. Universal controls 40 titles out of 100. Together with BMG, they will control 46 titles out of 100. This 6% increment is among the smaller ones in all affected countries.
352. EMI and Warner are comparable and control respectively 30 and 24 titles out of 100 in the charts. Sony BMG reaches a control share of 31%. After the merger EMI and Warner will be significantly smaller than Universal/BMG. SonyBMG will control 31%. Sony/ATV is significantly smaller, controlling 9% of the chart hits.
353. In Norway, Universal will therefore control 46% of the chart hits after the merger. Universal's repertoire would therefore still be substitutable for a user by combining most of the other publishers' repertoires since 54% of all chart hits would still be free of any Universal interest. It is therefore unlikely that the merger raises competition concerns with respect to the Norwegian market. The merger does not lead to a significant impediment of effective competition on the online rights market in Norway.

EEA

354. The figures analysed for the EEA are based on an average of the figures for the affected markets. It therefore does not cover some EEA countries, such as Denmark, Slovenia or Portugal. However the analysis includes all the largest EEA markets and the calculated control shares are sufficient good proxy for the EEA averages¹³².
355. According to weighted average of the national charts, Universal controls between 40 and 41% of the top 100 titles. Together with BMG, they will control between 49 and 50% of the charts. EMI is the second most important music company in terms of control of titles in the charts, where it controls 37 titles out of 100. Pre-merger, Universal is already

¹³² A proxy to capture the potential deviation between the EEA averages calculated in this document and those that would be obtained with the data from all EEA countries is the following: According to the IFPI (2006 – Global recording industry in numbers), among the 42 largest record markets in the world 14 correspond to the EEA affected markets, and 3 correspond to EEA non-affected markets (Denmark, Ireland, Portugal). The record market value in the 3 non-affected market accounts for 4% of the record market value of the 14 affected markets.

ahead of the other majors, controlling more titles than EMI notably. The merger would allow Universal to become the only major controlling up to half of the chart hits on an EEA-wide basis.

356. It is likely that after withdrawal the market for online rights will develop towards an EEA-wide market since the licences will cover the whole territory of the EEA and online music providers will look for collecting societies offering the specific publishers' repertoires equally EEA-wide. Universal will reach a considerable market position in Europe and gather approximately half of the total relevant repertoire. Any online music provider trying to cover the whole or at least the largest part of Europe will not be able to do without Universal.
357. Universal has a considerable strength and coverage of repertoire in the largest markets in Europe, such as the United Kingdom and Germany. The margins are at the moment not considered to be large in the downstream online market. Online music services therefore need to achieve a large number of customers and downloads in order to break-even. Any online music provider offering popular music (mainstream) on a European level will have to reach the customers of these revenue-strong countries and will therefore not be able to circumvent Universal.
358. Universal's activities also cover many EEA-countries. Universal has a strong position all over Europe (with a slightly lower tendency in the Nordic countries and a significantly weaker position in Spain). In addition, wide geographic coverage which could be alternatively sought by an online music provider to reach a minimum scale will necessarily involve countries in which Universal has a strong market position or even has a must-have repertoire. After the merger, the possibilities for online music providers to do without Universal and choose a combination of repertoires offered by the other publishers instead will therefore further decrease, also at EEA-wide level. The complete combined remaining repertoire which is free of Universal interest on EEA-wide level only reaches a share of 50%.
359. The merger consequently significantly impacts the online rights market on an EEA-level.

d. Conclusion

360. After the merger, the possibilities for an online music provider to substitute Universal's repertoire by one or a few others clearly decrease. This would be the case in Austria, the Czech Republic, Germany, Poland, and the United Kingdom as well as on EEA-wide level. In fact, an online music provider would have to replace on average 49-50% of the official chart hits, and up to 61% in the United Kingdom. Only the remaining 50% of all titles (39% in the United Kingdom) would be free of any Universal interest. Customer's possibilities to provide a viable online music platform without the repertoire from Universal are surely limited in some countries already before the merger. After the merger this possibility is further decreased.
361. An online/mobile music provider wishing to develop a service with a large catalogue will not be in a position to do so without an agreement with Universal. Ideally this online music provider will preferably sign an agreement with all music companies or their agents. However, a viable service can be proposed even if a reasonable portion of the world catalogue is not included. Several examples were provided by the parties where online music providers could work without one of the record majors to some extent.

Therefore, it is likely that an online or mobile platform could be temporarily operated without the part of the catalogue controlled by Warner, Sony BMG, Sony/ATV or independents. The situation of EMI is intermediate as it controls a substantial share of the charts, however significantly lower than Universal/BMG.

362. Considering that Universal/BMG agreement is necessary to operate an online platform covering a large part of the world catalogue, and that it is not necessary to reach an agreement with all the other music companies, it can be expected that Universal/BMG will be in a position to extract sustainable higher licence rates than its competitors.

2.3.4 Profitability of a price increase

363. As demonstrated above Universal will, after the proposed merger, most likely be able to impose a price increase on online and mobile music providers as the combined Universal and BMG Music Publishing repertoire represents must-have content which these providers cannot replace by the repertoire of other music companies. However, it may be argued that Universal would be deterred from raising the rates for its repertoire if a price increase entailed such a decrease of demand which would make any price increase unprofitable.
364. An increase of royalty rates may become unprofitable if (a) the price increase is likely to be passed on by providers to their customers and, as a consequence, (b) the end consumers were to reduce their demand (volume) of Universal music to such an extent that Universal would lose more than it would gain by the higher rate. By contrast, if online and mobile music providers are not able to pass on increased royalty rates, such rate increase would be profitable for Universal unless the service providers dropped Universal content. The latter reaction is, however, most unlikely as it would seriously threaten the viability of the online or mobile music platform.

Analysis for the different online and mobile music business models

365. The consequences of an increase of Universal's licence rates to online and mobile music providers depends to a large extent on the business model of the individual provider. There are three main business models: advertising-financed, subscription and pay-per-download/streaming.
366. Advertisement-financed platforms are free of charge for the user. Therefore any increase of the royalty rate by the online or mobile music provider will not be passed on to the end consumer but rather represent an increase in costs for the service provider which will ultimately be borne by this provider. It is highly unlikely that providers of advertisement-financed platforms will change their free-of-charge business model. It is also highly unlikely that they will reject Universal's price increase and do without Universal's repertoire because this would reduce their attractiveness and consequently the advertising revenues they could generate. It results from the market investigation that providers of advertisement-financed music offers depend to the same extent as other online music business models on an offer as complete as possible. Some of these providers stated that they would not be able to pass on higher royalty rates as advertising customers have a large choice of alternative online and offline advertisement carriers.

367. Subscription platforms are, theoretically, able to pass on an increase of Universal's licence rate to their end consumers. However, it is not certain that they will do so. Some of these providers pay different rates for the recording rights of the different record companies which does not prevent them from a uniform subscription price. Although many online music subscription providers have various subscription offers at different price levels, the Commission has not found any evidence for online music subscription services which put the record label with the highest royalty rates into a particular (more expensive) subscription offer. In case Universal's royalty increase is not passed on the price increase would be profitable for Universal. Again, it is highly unlikely that providers of music subscription platforms would renounce Universal's repertoire because such a step would jeopardise the attractiveness of their offer.
368. Even in case of a pass-on, i.e. an increase of the subscription rate, Universal would only bear a part of a potential loss in end consumer demand whilst it would gain the full benefits of the increased licensing rate. This is due to the fact that subscription platforms can only increase the subscription rate for access to their entire catalogue. They are not able to differentiate between the repertoires of the different music companies as users subscribe to the service in order to get access to all titles, irrespective of their provenance.
369. Therefore, if a general increase of the subscription fees led to a loss of customers who would no more be willing to pay the increased subscription fee for the music service, the provider would transfer less licence fees to all music companies as the licence fees are a function of the subscription fees. In case of a rate increase, Universal would thus retain the gain of a higher percentage share whereas it would only be partly hit by the reduced overall subscription revenues as the other music companies would bear, together, the largest part of this reduction. Universal would therefore be able to largely shift to its competitors the risk of a falling demand as a reaction of a rate increase. Therefore an increase of the licence rate vis-à-vis online or mobile music providers operating on a subscription basis would most likely be profitable.
370. Providers of online and mobile music platforms operating under a "pay-per-track" model, i.e. billing their users for each download, stream, ringtone etc., may pass on an increased royalty rate to their customers. There are currently two retail pricing models of "pay-per-track" platform operators: on the one hand those with a uniform price as practised e.g. by Apple's i-tunes: Apple has set a relatively low price level for its music sales as it focuses on the sale of music devices (i-pods) to which the downloading services are an additional "promotion". This pricing model has attracted many customers for two reasons: the price level and the simplicity of pricing; several competing providers, e.g. Virginmega or Mediamarkt have followed this pricing model. It is noteworthy that several of the providers with such a uniform price level pay different rates for the recording rights to the different record companies. On the other hand there are operators which apply a price differentiation among titles, e.g. T-Online's Musicload.
371. The first category of providers with a "uniform price" model has two options to react in case of an increase of royalty rates: either they keep their retail prices stable and bear themselves the additional costs in which case the rate increase would be profitable for Universal. In that scenario end consumers would probably also be harmed in their choice of music as some online or mobile music providers would, in view of low margins, drop out of the market. The second option would be to pass on the royalty increase and raise retail prices. However, in a uniform price model such a price increase would affect all titles across the board, irrespective of the recording or publishing company. Therefore,

Universal would share the risk of a decreased demand with all other music companies whereas it would gain the full benefits of the rate increase. As explained above, in such a scenario the price increase would most likely be profitable for Universal.

372. The second category of providers with a "differentiated prices" model has the possibility to pass on the royalty increase for Universal titles only in putting these titles into a higher price category. In that scenario, only Universal would be exposed to the reaction of end-consumers whereas the titles of other music companies would not be affected.
373. Such a "categorical" price increase for all Universal titles is not certain as end users do not purchase music of a certain label but music they like. Indeed, those online and mobile music providers applying differentiated price categories use also other criteria than their royalty costs when deciding into which price category to put a title. Although their costs on the wholesale levels are one of the elements taken into account in the determination of the retail price category, they also apply other criteria such as exclusivity, novelty, bonus editions and other features influencing the user's willingness to pay.
374. This is also evidenced by the current pricing strategy of online/mobile music providers with a differentiated pricing model: although they pay slightly different royalty rates to the four major record companies, they do not put the major with the highest royalty rates systematically into a higher price category. Therefore, it is possible that they will not behave differently with respect to the pass on of publishing royalties once those may vary among publishers.
375. In addition, the online provider would have to apply the price increase also to co-published titles, in proportion of the share of publishing rights controlled by Universal/BMG. This would, first, make the providers' pricing categories less comprehensible for the user and, second, for the titles for which it is co-publisher, Universal/BMG would share the risk of a decreased demand with all other involved music companies whereas it would gain the full benefits of the rate increase.
376. However, even where online music providers systematically increase the retail price for Universal titles in a differentiated price model, Universal does not have to fear a significant volume reduction through the reaction of end consumers. First, according to the responses of online and mobile music providers, end customers who want to buy a certain title are unlikely to switch to another title just because that one is cheaper. As music is a heterogeneous good and each user has individual preferences, each user only considers a limited number of titles as substitutable to each other. Second, as demonstrated above, many of these titles considered as potential substitutes to a given title are controlled by Universal and BMG which have (co-)control of the publishing rights for approximately 50% of all chart hits. Therefore, the number of potential alternatives for the end consumer is considerably reduced.
377. Third, the willingness to pay is also driven by other factors than price, such as being the first to have novelties¹³³ and thus being cutting-edge or subjective preferences of the individual consumer. It is true that a certain pricing constraint results, mainly for online download applications, from CDs and other physical music carriers and from illegitimate

¹³³ This is confirmed by the fact that some platforms apply higher prices to the download of new releases which they offer in exclusivity.

downloads. However, file-sharing and other non-commercial offers seem to play a rather limited role with respect to mastertones and other mobile music applications.

378. With respect to online downloads, some end consumers may indeed be expected not to buy a certain title in case of a price increase, and possibly acquire them via file-sharing. However, it is also to be expected that the number of those customers who would abstain from buying will be rather limited: first, those end consumers with a low willingness to pay are unlikely to be potential buyers even at the current price level. The volume reduction effect which is relevant for the assessment of the profitability of a royalty rate increase by Universal, will therefore be limited to those customers who are willing to buy at the current price level but would be deterred to do so in case of a small but significant increase of royalty rates. In view of the relatively small part of publishing royalties in the total price of an online or mobile application a price increase by 10% is unlikely to have a deterrent effect on the end consumer.¹³⁴ In the light of the above and taking into account the limited substitutability of songs in the end customers' view, it is thus very unlikely that an end consumer would quit buying in response to such a price increase.
379. Therefore, even in the scenario that online and mobile music providers were to pass on higher royalty rates for Universal music to Universal titles in a targeted way, the reaction of end consumers is unlikely to result in a significant reduction of the demand volume for Universal titles. An increase of royalty rates would thus be profitable for Universal vis-à-vis all kinds of online and mobile music providers.
380. Therefore, following the profitability analysis, it can be concluded that the merger raises serious doubts in the markets for online rights identified above, *i.e.* in Austria, Czech Republic, Germany, Poland and the United Kingdom as well as for the EEA.

2.3.5 Reactions of customers (online and mobile music providers)

381. The extent of the price increase by Universal/BMG will be affected by - on the one hand - the degree of complementarity of the rights in its combined repertoire and - on the other hand - by the change in the bargaining power of its competitors as well as in particular the reaction of the customers.
382. It may be argued that online and mobile music providers exert an effective constraint on Universal due to their countervailing buyer power. The parties submitted that in particular Apple would have considerable buyer power as its "i-tunes" platform is the most important online download service in many European countries. It is true that Universal has a strong interest of being present on i-tunes. On the other hand, however, Apple's business model is based on the sale of music at relatively low prices in order to attract consumers which will be obliged to buy an "i-pod", Apple's portable music device. It is noteworthy that music downloaded via i-tunes can, due to Apple's DRM, only be played on the i-pod but not on other portable devices. Consequently, Apple makes a much higher margin on the sales of i-pods than on the sale of music.
383. In order to attract as many people as possible to buy i-pods, Apple has an extremely high interest to be the most attractive and complete download platform. In view of the large

¹³⁴ Publishing royalties currently amount to 8-15% of the net retail sales price, varying among countries and applications.

Universal/BMG repertoire, Apple cannot really threaten to switch to other suppliers¹³⁵ but it is limited to the threat not to offer Universal titles on its platform. If Apple were not able to offer the content of the new entity, it would lose its current attractiveness and risk foregoing not only revenues from music sales but, more importantly, higher revenues from the sales of i-pod devices. Therefore, Apple's bargaining position vis-à-vis Universal, the by far largest catalogue after the merger, is rather limited. It is therefore concluded that even Apple would not exert effective constraints on Universal's pricing behaviour.

384. Even if it were assumed that Apple had effective countervailing buyer power, *quod non*, this would not exclude the finding of a significant impediment of effective competition. First, Apple only accounts for a limited part of Universal's online and mobile music sales. According to Universal's parent company Vivendi¹³⁶, mobile music accounted for 45% of its total global digital revenue. Among the remaining 55% of Universal's digital revenues from online sales, Apple seems to be the largest individual customer but followed by a large number of other important providers. Therefore Apple's share of the total demand is far below 40% of the overall demand.
385. In any event, even if Apple had, in spite of the above, countervailing buyer power, this could not sufficiently off-set the above-described negative effects of the proposed merger. Universal is able to price discriminate between its customers, i.e. the various online and mobile music provider, and Apple's possible, *quod non*, buyer power would thus not shield these other customers from a royalty rates increase. It is therefore concluded that Universal's increased pricing power is not constraint by countervailing buyer power.

VII. RESULTS

386. Against this background, it is very likely that Universal will post-merger, on the basis of non-coordinated effects, have the possibility and the incentive to increase prices for its repertoire of Anglo-American mechanical rights for online applications. The merger therefore raises serious doubts with respect to the online rights market both on an EEA-wide level and in the countries Austria, the Czech Republic, Germany, Poland, and the United Kingdom. By contrast, the Commission has not found any indications in the market investigation that, in a scenario following the withdrawal of online publishing rights from the existing system of collective rights management through collecting societies and the re-organisation of the administration of those rights, the merger could lead to coordinated effects in the market for online rights.

VIII. REMEDIES

387. The notifying party submitted a first set of remedies on 15 March 2007. In response to the results of the market test and the Commission's comments, these remedies have twice been substantially improved, namely on 26 March and on 30 March 2007. Subsequently,

¹³⁵ Cf. Section 65 of the Horizontal Merger Guidelines.

¹³⁶ Vivendi presentation "2006 Results and 2007 Outlook" by Jean Bernard Lévy and Jacques Espinasse on 07.03.2007.

the commitments text received some technical refinements and a final version was submitted on 23 April 2007.

1. Description of the commitments submitted by the notifying party

1.1 Description of the First Divestiture Package

388. On 15 March 2007, Universal proposed to divest a number of catalogues covering a package of Anglo-American repertoire ("the First Divestiture Package"). According to the parties, these catalogues are separate legal entities within BMG which, after their acquisition by BMG, have continued to sign authors directly. Universal submitted that the First Divestiture Package could be sold in parts or as a single package and was structured in such a way that the individual catalogues can be added to an existing music publishing business or be used to enter the market as a new music publishing company.

389. The First Divestiture Package comprised the following catalogues and contracts:

(a) BMG catalogues

- (i) Zomba Music Publishers Limited ("Zomba UK")
- (ii) Unisong Music Publishers B.V.
- (iii) 19 Music Limited
- (iv) First Avenue Music Limited
- (v) Deconstruction Songs Limited
- (vi) Minaret Music Limited
- (vii) 19 Songs Limited
- (viii) Strongsongs Limited
- (ix) Logo Songs Limited
- (x) Block and Gilbert Music Limited
- (xi) Red Star Songs Limited
- (xii) Point Music Limited
- (xiii) Mucho Loco Music Limited
- (xiv) BBC music publishing catalogue

(b) Universal catalogues

- (xv) Anxious Music Limited
- (xvi) Momentum Music Limited
- (xvii) Momentum Music 2 Limited

390. The four most important (and eventually maintained) catalogues of the First Remedies proposal are described in the following. Zomba UK's catalogue includes amongst others Bruce Springsteen, Billy Ocean, Iron Maiden and rights to music by Denniz Pop and Max Martin who were the writer/producer behind Britney Spears, The Backstreet Boys, NSYNC, Celine Dion and Westlife. Amongst the most successful hits are "Hit me baby one more time" and "Oops I did it again" by Britney Spears, Kelly Clarkson's "Behind these hazel eyes", "I want it that way" from the boy group The Backstreet boys, "Everything I do..." by Bryan Adams, Bon Jovi's "It's my life" and Celine Dion's "That's the way it is". The EEA-wide revenues of Zomba Music Publishers Limited constantly increased from EUR [5-10]* million in 2004 to EUR [5-10]* million in 2006.

391. 19 Music's catalogue includes titles of Culture Club (e.g. "Karma Chameleon"), Spice Girls (e.g. "Spiceworld and "Spice") Boyzone (e.g. "Said and Done" and "A Different Beat") and S CLUB 7 ("Don't stop moving") form part of this catalogue. 19 Music's EEA revenues amounted to EUR [0-500 000]* in 2006. 19 Songs is a joint venture in which BMG and the record and television producer Simon Fuller each hold 50% of the shares and which generated revenues of EUR [0-500 000]* in 2006. It consists of pop music linked to TV reality shows and other pop repertoire such as songs by Emma Burton. Its most popular title is the American Idol theme. The BBC catalogue contains copyrights in television themes which are broadcast in the United Kingdom and globally such as the "Teletubbies" and "Bob the Builder". It generated EEA wide revenues of EUR [0-5]* million in 2006.
392. In addition to rights in the songs of these catalogues, the First Divestiture Package also included ongoing contracts. The parties indicated that these ongoing contracts also encompass contracts with authors who are still under obligation to produce further songs for these catalogues in the future. Moreover, Zomba UK was described as a "full service publishing" company with its own creative team which would be part of the divestiture if requested by potential purchasers. Universal proposed to divest the full rights for the various catalogues but to set up a "licensing back" agreement with the acquirer under which Universal would receive the worldwide rights outside the EEA.
393. The revenues generated by the First Divestiture Package amounted to EUR [10-20]* million in the EEA with Zomba UK representing alone more than half of these revenues.¹³⁷ The parties submitted that the Divestiture Package would represent, both in the United Kingdom and in the other EEA countries, [20-30]*% of BMG's top 1 000 works and [25-35]*% of BMG's top 500 works.

1.2 Results of the market test for the First Divestiture Package

394. In the first market test approximately 100 questionnaires were sent to publishers, collecting societies and online and mobile music providers with a return of 44 responses. The market test indicated that a divestiture of catalogues is in principle an appropriate remedy to remove the competition concerns identified by the Commission. However, the market test showed that the First Divestiture Package was not sufficient to remove the competition concerns identified by the Commission.¹³⁸ A large number of respondents indicated that the suggested remedies would not reduce to an acceptable extent the increase of Universal's market power in the online rights market. Many market participants considered that the divestiture would

¹³⁷ 2005 figures as submitted by the notifying party.

¹³⁸ See responses to the Questionnaire Remedies, dated 15 March 2007, questions 14 and 15: Out of 41 substantive responses, 22 market participants answered directly to the question as to whether the remedies would remove the competition concerns. Most of the others declared not to have sufficient knowledge to make this assessment. Among the 22 respondents were

- 11 publishers; 3 of them considered the Divestiture Package as adequate to remove the Commission's concerns with 8 expressing a negative view or raising doubts.
- 6 online/mobile music providers 4 of them expressed an overall negative view, 2 considered the Divestiture Package as sufficient.
- Not many collecting societies considered themselves capable of making an assessment: 4 of the 5 respondents, however, indicated that the remedies would probably not remove the concerns – only 1 of those answering the relevant question found the Divestiture Package to be sufficient.

have to be more substantial than that proposed by the notifying party. In particular, some respondents emphasised that the First Divestiture Package lacked a strong U.S. catalogue.

395. With respect to the characteristics of an appropriate remedies package the market test provided valuable information. Many respondents considered it as essential that the catalogues are of good quality and represent a sufficient volume in number of titles and revenues. The catalogues further should be an adequate mixture of recent hits and successful back-catalogue in order to secure steady revenue stream and the continuity of the business. Moreover, the catalogues should cover Anglo-American titles and authors with a scope for the whole of the EEA and not only for one or two countries. The catalogues should also provide for a good combination of successfully established authors with the potential to supply further hits and of newly signed authors with the potential to break through and develop new business.
396. These conditions were not met by the First Divestiture Package. Many respondents indicated that the quality of most of the proposed smaller catalogues was insufficient, with only four exceptions: Zomba UK, 19 Songs, 19 Music and the BBC catalogue. All other catalogues were mostly considered as insignificant and of little value. They were described as having no chart hits and only rather old songs which were not "evergreens" and were thus unlikely to be released in cover versions in the future.
397. Moreover, the market test indicated that many of these smaller catalogues only had a limited geographical scope¹³⁹ and that their titles were largely unknown in other European countries. In addition, some catalogues of the First Divestiture Package represented niche products.¹⁴⁰ Such niche catalogues are of only minor relevance for online and mobile music providers and their divestiture would thus not address the competition concerns.
398. By contrast, according to a number of respondents, Zomba UK, the largest catalogue in the First Divestiture Package, represents an important part of BMG's Anglo-American music publishing activities and provides hits all across Europe. Many respondents also indicated that Zomba UK probably had a number of good authors under contract. It was also mentioned that the 19 Songs and/or 19 Music catalogues are attractive, have a larger than national scope and constitute a relatively good combination of hits, back catalogue and authors. As to the BBC catalogue, it was described as attractive but not very chart relevant.
399. In spite of certain positive elements in some catalogues the First Divestiture Package was thus considered by the majority of the respondents as insufficient in view of the overall increment of Universal's position through the acquisition of BMG.

1.3 Description of the Second Divestiture Package

400. On 26 March 2007, Universal modified its initial proposal in order to respond to the feed-back of the market test and the Commission's subsisting concerns. The Second Divestiture Package comprised the following catalogues:

¹³⁹ Unisong's catalogue is mainly known in the Benelux area whereas most of the other catalogues concentrate on the United Kingdom.

¹⁴⁰ For instance, Unisong was described as specialised in Gospel and Dutch songs, Logo Songs as focusing on electric folk and Red Star Songs as consisting mainly of heavy metal.

(a) BMG catalogues:

- (i) Zomba Music Publishers Limited ("Zomba UK")
- (ii) 19 Music Limited
- (iii) 19 Songs Limited
- (iv) BBC music publishing catalogue

(b) Universal catalogue:

- (v) Rondor Music (London) Limited ("Rondor UK")

401. The Second Divestiture Package thus added Rondor UK, whereas the previously proposed catalogues Unisong Music Publishers B.V., First Avenue Music Limited, Deconstruction Songs Limited, Minaret Music Limited, Strongsongs Limited, Logo Songs Limited, Block and Gilbert Music Limited, Red Star Songs Limited, Point Music Limited, Mucho Loco Music Limited, Anxious Music Limited, Momentum Music Limited and Momentum Music 2 Limited ("initially proposed smaller catalogues") were withdrawn.
402. Rondor UK's revenues in the EEA increased from EUR [5-10]* million in 2004 to EUR [5-10]* million in 2006. The catalogue includes the British band Kaiser Chiefs, winner of three Brit Awards in 2006. Their first album reached number 2 in the United Kingdom with 4 hit singles in the United Kingdom Top 20 charts after its release in 2005, including "I predict a riot" by Kaiser Chiefs which generated revenues of EUR [...] in 2006. The second album was released in March 2007 and has reached number 1 in the United Kingdom, the Netherlands and Greece, and ranking high in other national charts, too. One song of this album became number 1 in the United Kingdom and the European single charts ("Ruby").
403. The catalogue further includes artists such as Sophie Ellis Bextor and the Danish pop production team Jorgen/Larsson. Amongst its top authors is the songwriter and Dire Straits' lead singer Mark Knopfler whose former chart hits "Money for nothing", "Walk of Life", "Sultans of Swing" and "Private Investigation" are part of the catalogue. Other famous titles are "Lady in Red" by Chris de Burgh and "Wouldn't it be good" by Nick Kershaw. The divestiture of Rondor UK does not include the works of Supertramp, Squeeze and Yes. [...]*
404. As for the First Divestiture Package, Universal proposed to divest the full rights for the various catalogues but to set up a "licensing back" agreement with the acquirer under which Universal would receive the worldwide rights outside the EEA
405. The combined EEA-wide revenue of the Second Divestiture Package amounted to EUR [20-30]* million, increasing by EUR [0-10]* million in comparison with the First Remedies Package.

1.4 The results of the market test for the Second Divestiture Package

406. The second market test was sent to those 44 market participants who had answered to the first market test by that time. Approximately, half of the addressees responded within the available timeframe.
407. With respect to the qualitative criteria which were confirmed in the second market test, most of the respondents acknowledged that the additional catalogue, Rondor UK, significantly

improved the package. Most of those respondents who evaluated the quality of the catalogues confirmed that Rondor UK is of good quality, with a large number of important titles, especially in the back-catalogue. Some market participants signalled that Rondor UK contained a limited number of recent chart hits.

408. Overall, although some respondents considered the Second Divestiture Package as sufficient, a number of respondents stated that also the Second Divestiture Package was not sufficient in size to reduce the increase in Universal's market power to an acceptable extent.

1.5 Description of the Final Divestiture Package

409. On 30 March 2007, and after having been informed of the result of the second market test, the notifying party submitted a third remedies package. This Final Remedies Package includes the Second Remedies Package and adds an EEA-wide licence of the full catalogue of Zomba U.S. This licence encompasses all those copyrights held by Zomba U.S. in respect of exploitation in the EEA, including those currently in existence and those to be delivered, under existing agreements or following the exercise of any options provided for under existing agreements.

410. The Zomba U.S. catalogue generated revenues of EUR [0-10]* million in the EEA in 2006. The catalogue contains songwriters, composers and producers with ongoing obligations such as Justin Timberlake, Linkin Park, Shania Twain, Korn, Limp Bizkit and R. Kelly and some back catalogue. Amongst the most known songs are R. Kelly's "I believe I can fly" and "Outrageous", "Señorita" by Justin Timberlake and the U.S. group Linkin Park's "Numb".

2. Assessment of the Final Divestiture Package

411. The Commission carefully analysed the Final Divestiture Package (hereinafter "the Remedies Package" or "the Commitments"). In its analysis it took particular account of the results of the two market tests and of its own findings in the market investigations.

412. The Commission considered that a third market test was not necessary. The second market test confirmed the quantitative and qualitative criteria for suitable remedies as they had been described in the first market test. The Final Divestiture Package was built around the already market-tested Second Divestiture Package and addressed the shortcomings which had been pointed out in the two market tests. It added considerable revenues (almost 50% more than the Second Divestiture Package) and included an important U.S. catalogue with many chart hits and successful authors. On the basis of these improvements the Commission found that the modifications made by Universal removed the serious doubts and that it had to authorise the transaction in line with Article 10 (2) of the Merger Regulation.

413. The Commission came to this conclusion on the basis of the combined evaluation of a bundle of criteria which will be analysed in the following. These criteria are considered as the most appropriate to evaluate the future potential of the Remedies Package. The analysis therefore has not been backward looking on effects in the past but rather forward oriented in order to identify the structural growth potential of the Remedies Package.

414. The Commission considers that the Remedies Package is necessary and sufficient in terms of size, quality and composition of the catalogues, their relevance for online and mobile

music services, the number and quality of authors under contract and their potential for future success.

2.1 Characteristics of a viable remedies package

415. The market test clearly confirmed that the divestiture of entire music publishing catalogues constitutes a suitable remedy to remove the competition concerns identified by the Commission. The divestiture of catalogues has a structural effect on the market and permanently reduces the market power of Universal. By contrast, a commitment to remain in the existing collecting society system for a limited period of time, as suggested by some respondents in the market test, would counteract the general market development which is currently leading to a re-organisation of the administration of online rights, but would not permanently solve the issue of market power created by the transaction.
416. A viable remedies package should include the divestiture of the full copyright for all applications or categories, i.e. including mechanical, performance, synchronization and print rights. This is necessary to avoid a copyright split for different applications and to secure the economical efficiency of the divested catalogues. This further implies that the divestiture includes right categories (and turnover generated by the exploitation of these rights) which are not directly related to the competition concerns identified with respect to online applications.¹⁴¹
417. In order for the remedy to be swiftly and easily implemented it is important that the divestiture comprises entire catalogues which are held as separate legal entities. Whilst individual titles usually cannot be divested without the approval of the authors, catalogues in separate legal entities can be transferred pursuant to the rules applicable to the sale of companies, and thus regularly without the approval of the authors. As it is time consuming to obtain the approval of the authors concerned, the divestiture of individual titles (or the transfer of individual authors) is generally not a viable option for a merger procedure commitment which needs to be implemented quickly. All catalogues included in the Remedies Package are held in separate legal entities and their divestiture is not expected to encounter specific difficulties. The same applies to the licensing agreement for the EEA exploitation of the Zomba U.S. catalogue which will be discussed in detail below. The Remedies Package therefore fulfils the requirement of a quick and uncomplicated transferability.
418. The music publishing business is characterised by the great importance of intangible assets such as copyrights in works. Therefore, a divested catalogue can be successfully managed by an established publisher without the need to transfer any tangible assets.
419. Finally, as the competition concerns identified by the Commission only related to Anglo-American repertoire, the Remedies Package had to focus on Anglo-American catalogues.

¹⁴¹ According to Universal, music publishing revenues from online applications accounted for 2% of Universal's total music publishing revenues in 2005.

2.2 Size of the Remedies Package

420. The Remedies Package generated EEA-wide revenues of EUR [30-40]* million in 2006. The total revenues generated by all BMG's Anglo-American catalogues in 2006 amounted to EUR [80-100]* million.¹⁴² Therefore the revenues generated by the Remedies Package which consists exclusively of Anglo-American catalogues, correspond to approximately [30-35]*% of BMG's total revenues with Anglo-American titles. On the basis of a sample provided for the United Kingdom, the Remedies package would correspond to around [40-45]*% of BMG's total revenue for online exploitation.
421. The figures submitted by the parties show that two of the three main catalogues of the Remedies Package (Zomba UK and Rondor UK) generated considerably higher EEA-wide revenues in 2006 than in 2005 (6% higher for Zomba UK; and 23% higher for Rondor UK whereas the EEA revenues of Zomba U.S. decreased by 5%) which is considerably better than the average of the music publishing sector¹⁴³. It can be expected that these catalogues, including Zomba U.S. which had some very successful hits in early 2007, will continue to grow faster than the average.
422. The analysis of the relative size of the Remedies Package also has to take into account that, already pre-merger, Universal could impact on a considerable part of BMG's music publishing repertoire, whether as a co-publisher or as holder of the corresponding recording rights. In that respect, Universal submitted that [70-80]*% of the revenues generated by BMG's top 500 United Kingdom works stemmed from works which were either co-published or recorded by Universal. However, it appears that this figure overestimates the actual impact of Universal as they do not properly distinguish between "original" recordings and cover versions. The Commission therefore rather considers, on the basis of the parties' responses to various questionnaires that approximately 55-65% of BMG's publishing catalogue (both in terms of weighted revenues and number of works) is either co-published or recorded by Universal.

2.3 Universal does not retain control in most of the Remedies Package

423. The Remedies Package is composed of six catalogues which have grown over a number of years. As the different publishing catalogues have over time been co-published or recorded by various record companies, including Universal, there is no significant catalogue in which Universal would not hold any co-publishing or recording right. However, it seems that the control share of Universal in the titles of the Remedies Package is lower than in the overall BMG catalogue.¹⁴⁴

¹⁴² Parties' response to question 2 of questionnaire of 22.12.2006, as reiterated in subsequent submissions.

¹⁴³ Enders Analysis (Recorded Music and Music Publishing, page 29) forecasts an annual growth rate of 2.2% for the global music publishing industry between 2006 and 2012.

¹⁴⁴ It should be reminded that according to Universal, [70-80]*% of the revenues of BMG's catalogues were controlled by Universal either through co-publishing or through recording.

424. Of the sample of the 1 900 top works of the Remedies Package 58% are neither co-published by Universal nor have they ever been recorded by Universal.¹⁴⁵ However, in case of "multiple recording", i.e. the existence of several recordings of the same composition, Universal does not usually have the recording rights for all of them, and not for all charted recordings either. Therefore, the notifying party proposed to take account rather of those titles which have been recorded by Universal and also by other record companies. According to Universal, in 79% of the 1 900 works Universal does not have a co-publishing right nor does Universal have the only recording.
425. The Commission considers that the figure of 58% underestimates the pre-existing control of Universal because it does not take account of the actual number of songs which have been recorded by Universal. Similarly, the Commission considers that the figure of 79% overestimates the pre-existing control of Universal. Therefore the Commission considers it appropriate that approximately 65-70% (as a rough average of 58% and 79%) of the total works of the Remedies Package are not controlled by Universal.
426. More importantly, only 11% of the 1 900 top works are co-published by Universal. This means that 89% of these most successful works can be released as cover versions by other record companies without Universal being involved as co-publisher. In view of the success of these top titles it is quite likely that they will be used for cover versions by other record companies. The importance of cover versions in the music industry is illustrated by the fact that 15 of Universal's 2006 top 50 single record sales in the United Kingdom were cover versions.¹⁴⁶ In a prospective analysis, the titles which are not co-published are particularly relevant as they are those which allow for future hit recordings outside Universal's control.
427. In value terms, the titles which were neither co-published by Universal nor have ever been recorded by Universal account for [50-60]*% of the revenues generated by of the top 1 900 works the Remedies Package. Those titles in which Universal neither has a co-publishing right nor an exclusive recording (i.e. parallel recordings of other record companies exist) generated [80-90]*% of the revenues¹⁴⁷ of the top 1 900 works of the Remedies Package. In order to take due account of "multiple recordings" (see supra), it is also appropriate to consider that titles accounting for approximately [60-70]*% (as a rough average of [50-60]*% and [80-90]*%) of the total revenues of the Remedies Package are not controlled by Universal.
428. Most importantly for the future potential of the Remedies Package, 90% of the revenues were generated by titles in which Universal had no co-publishing rights. In case of successful cover versions released by other record companies, Universal would have no control at all over these titles.

¹⁴⁵ Response to question 2 of questionnaire of 03.04.2007. The Commission asked for the top 500 works of each of Zomba UK, Zomba U.S. and Rondor UK as well as the top 200 works of the BBC catalogue and the top 100 works of both 19 Songs and 19 Music.

¹⁴⁶ Seven of these 15 titles were pure cover versions and eight were samples, remixes and interpolations, i.e. other forms of using an existing title.

¹⁴⁷ The parties explained that it would be extremely difficult to calculate the allocation of the publishing revenues to the different recordings.

429. These figures demonstrate that Universal will have co-publishing rights in only a very minor part of the repertoire contained in the Remedies Package and control over only a limited part of it. Due to the composition of catalogues which have grown over time and whose works may have been recorded several times, it is impossible to find catalogues containing exclusively titles in which Universal (or any other major music company) does not have any control. However, Universal's control shares in the Remedies Package still seem to be considerably smaller than in the average of BMG's catalogues.
430. The fact that Universal will not have a co-publishing right in around 90% of the works included in the Remedies Package is relevant for the particularly important future recordings as it means that Universal will not be able to control future cover versions recorded on the basis of these rights. In this context it has to be kept in mind that the competition concerns mainly relate to music publishing rights and that the competitive assessment identified serious doubts as to a possible significant impediment of effective competition in the music publishing markets.
431. For these reasons, the Remedies Package generally addresses the competition concerns identified above, namely the control of Universal of works through co-publishing rights or/and recording rights.

2.4 Relevance of the Remedies Package for Online and Mobile Music Services

432. The Remedies Package has a significant impact on Universal's control share of those titles which are of particular importance for the success of online and mobile music platforms, namely good back catalogue and recent chart hits. Regarding successful back catalogue the qualitative analysis has shown that it is well represented in the Remedies Package and that Universal only maintains control of a minor part of it.
433. As to chart hits, 169 works of the remedies package made it into the United Kingdom weekly charts in the years 2003-2006 and they have appeared in these charts 1,540 times. This represents an average chart presence of more than 9 weeks per title. The 169 chart titles of the Remedies Package thereby account for 6.2% of all entries in the United Kingdom weekly charts over this period.¹⁴⁸ In 139 of these 169 titles Universal will not retain any co-publishing rights and they can thus be recorded as cover versions by other record companies in which case Universal does not have any control of the title.
434. Also in Member States other than the United Kingdom, the works of the Remedies Package had a high number of chart entries. For the Member States other than the United Kingdom the parties have analysed only the charts of the first week of each month for the period 2003-2006. They consider that this approach covers approximately 85% of all works charted. The parties also point out that in some Member States the weekly charts do not cover the top 100 (as in the United Kingdom) but a smaller number. On the basis of this analysis, the Remedies Package had 100 entries in the weekly charts in Germany and 66 entries in the weekly charts in Austria.
435. Also in respect of the 2006 chart hits which have been used as a proxy to evaluate the parties' position, the Remedies Package leads to a considerable reduction of the "net increment" of Universal's control of titles.

¹⁴⁸ According to the parties the total number of chart entries during this period amounted to 24,727.

436. As explained above, the chart analysis of one or two years can only be a kind of “snapshot” to reflect the position of a music company in the recent past. However, as the control shares regularly alter from year to year and depend on the success and the combination of different authors and performing artists, these control shares can only constitute indications for the market power of a music company.

437. For this reason, it is not necessary that the Remedies Package completely removes the “net increment” based on the chart analysis of past years. The past net increment would be completely removed in theory if only the limited number of BMG-titles which entered the charts in the last year and created this net increment in Universal's control were divested. The divestment of this limited number of past chart hits would, however, clearly not address the competition concern. The purpose of the Remedies Package is to avoid that Universal, through the proposed merger, gains a market position which enables it to exert market power vis-à-vis online and mobile music providers. In the prospective remedies assessment, the analysis of the impact on the control shares for past chart hits thus only constitutes one of several parameters together with the size, quality and composition of the catalogues and the potential of signed authors to generate future hits and thus revenues.

438. The following table shows the impact of the Remedies Package on the chart analysis in all Member States with affected markets for online rights:

Characteristics of divested catalogues – Impact on official charts 2006

	Sample Official Charts 2006	Chart titles controlled by BMG MP	Chart titles controlled by divested catalogues	BMG MP chart titles contributing to the increment	Titles in divested catalogues reducing the increment	Chart titles in divested catalogues which are not co-published by Universal
Austria	100	8,0%	2,0%	6,0%	1,0%	2,0%
Belgium	100	12,0%	4,0%	7,0%	1,0%	4,0%
Czech R.	200	16,5%	3,5%	9,5%	1,5%	3,5%
Finland	260	6,2%	1,5%	4,2%	1,2%	1,2%
France	100	10,0%	2,0%	9,0%	1,0%	2,0%
Germany	100	11,0%	4,0%	7,0%	2,0%	4,0%
Greece	667	7,2%	1,9%	5,7%	1,6%	1,8%
Hungary	100	13,0%	3,0%	7,0%	0,0%	3,0%
Italy	50	12,0%	2,0%	10,0%	2,0%	2,0%
Netherlands	100	15,0%	3,0%	10,0%	1,0%	3,0%
Poland	240	7,9%	4,2%	4,2%	1,7%	4,2%
Spain	260	9,2%	3,1%	8,1%	3,1%	3,1%
Sweden	100	9,0%	4,0%	6,0%	3,0%	4,0%
United Kingdom	100	19,0%	11,0%	10,0%	5,0%	11,0%
Norway	80	8,8%	3,8%	6,3%	2,5%	3,8%
Affected markets		13,3%	5,2%	8,6%	2,8%	5,2%

439. The table above shows that in all affected countries the catalogues of the Remedies Package are present in the charts of the annual best-selling titles. The catalogues of the Remedies Package further reduce the net increment in control shares brought about by BMG in all affected countries except Hungary. The above table also shows that almost none of the chart titles in the Remedies Package is co-published by Universal. This means that all those chart

titles in the Remedies Package which do not reduce the net increment in control shares were recorded by Universal in 2006. However, in the future they can be recorded by any record company and Universal would thus have no control of that title at all. As they charted in 2006 the compositions have proven their popularity and are therefore quite likely to be released in a cover version or as sample or extract in new songs (e.g. in rap or hip-hop).¹⁴⁹ They, therefore, have the potential to reduce Universal's control share in the future.

440. It is worth noting, that the remedies apply to the whole EEA and therefore have an effect also in the EEA-countries concerning which no serious doubts have been found.
441. In the United Kingdom, the Member State with the highest post-merger (pre-remedies) control share of Universal (61%), the highest number of chart titles controlled by BMG (19%) and one of the highest net increments (10%) and where Anglo-American music plays the most important role, the Remedies Package has the strongest effect. It contains 11% of the charted titles and halves the net increment (by 5%). In addition, the other 6% of charted titles are not co-published by Universal and would thus not be controlled at all by Universal in case of a future release by another record company.
442. In Germany where Universal's post-merger control share reaches 54% and BMG controls 11% of the chart hits and where the net increment amounts to 7%, the Remedies Package contains 4% of the chart hits and reduces the net increment by 2%. In addition, the other 2% of charted titles are not co-published by Universal and would thus not be controlled at all by Universal in case of a future release by another record company.
443. In Poland where Universal's post-merger control share reaches 51% and BMG controls 8% of the chart hits and where the net increment amounts to 4%, the Remedies Package contains 4% of the chart hits and halves the net increment (by 2%). In addition, the other 2% of charted titles are not co-published by Universal and would thus not be controlled at all by Universal in case of a future release by another record company.
444. In Austria where Universal's post-merger control share reaches 56% and BMG controls 8% of the chart hits and where the net increment amounts to 6%, the Remedies Package contains 2% of the chart hits and reduces the net increment by 1%. In addition, the other 1% of charted titles are not co-published by Universal and would thus not be controlled at all by Universal in case of a future release by another record company.
445. In the Czech Republic where Universal's post-merger control share reaches 52% and BMG controls 16.5% of the chart hits and where the net increment amounts to 9.5%, the Remedies Package contains 3.5% of the chart hits and reduces the net increment by 1.5%. In addition, the other 2% of charted titles are not co-published by Universal and would thus not be controlled at all by Universal in case of a future release by another record company.
446. On the level of all affected EEA countries where Universal's post-merger control share reaches 49-50% and BMG controls 13.3% of the chart hits and where the net increment amounts to 8.6%, the Remedies Package contains 5.2% of the chart hits and reduces the net increment by 2.8%. In addition, almost all of the other 2.4% of charted titles are not co-published by Universal and would thus not be controlled at all by Universal in case of a future release by another record company.

¹⁴⁹ According to the parties some songs in the divested catalogues have been recorded 20 or 30 times. See response to question 2 of questionnaire of 03.04.2007.

447. These examples illustrate that the Remedies Package has an important effect on Universal's control shares of chart hits. However, as explained above and as illustrated by the variations of chart relevant control shares both from year to year¹⁵⁰ and from country to country (for the same titles of the Remedies Package), the control shares in chart hits only constitute a proxy for the post-merger market position of Universal. It is therefore not necessary for the Remedies Package to remove most of the increment or compensates for all chart hits published by BMG. Instead, it is important that the Remedies Package contains a certain number of chart hits which have been successful in all affected Member States.
448. This also applies to Austria and the Czech Republic where the reduction of the increment brought about by the transaction is smaller than in other affected markets with serious doubts. In this respect it has to be recalled that the chart control analysis only represents a "snapshot" and is only one of several parameters taken into account by the Commission in its analysis of the Remedies Package.
449. On the basis of the analysis above it can therefore be concluded that the catalogues included in the Remedies Package have been present in the charts and are likely to continue to deliver hits which are of particular relevance for online and mobile music providers.

2.5 Quality and composition of the Remedies Package

450. The Remedies Package presents a good mixture of successful back catalogues and recent hits. It is composed of significant catalogues, both Anglo and American, with important works of renowned authors. It thus responds to two important requirements emphasised in the market tests.
451. Zomba UK is a strong catalogue with many chart number 1 hits and evergreens. It contains, for instance, the catalogues of Billy Ocean, Iron Maiden, Peter Sinfield (who wrote *inter alia* for Celine Dion, Cher, Cliff Richard, Barry Manilow and Diana Ross) and Mutt Lange (who wrote *inter alia* for Shania Twain, Bryan Adams, Huey Lewis and Michael Bolton). It also includes the Cheiron/Grantsville/Maratone catalogues with many titles written for Britney Spears, The Backstreet Boys, NSYNC, Bon Jovi, Celine Dion, Westlife and Kelly Clarkson. As these titles were successful hits at their time, they have very good chances of being reproduced as cover versions in the future. In addition, many of those past hits are regularly sampled in new rap and hip hop songs.
452. Zomba UK also has a number of recent chart hits and consequently a high potential for future hits. In 2006, Kelly Clarkson's "Since you've been gone" (written by Zomba UK authors Sandberg/Gottwald) was number 1 in the charts in Germany, Ireland, the Netherlands and the United Kingdom. Jamie T's debut album "Panic Prevention" (written by himself) entered the United Kingdom album charts at number 4 in January 2007. Zomba UK author Martin Brammer has written several songs, including the title track and "The Pieces don't fit" on James Morrison's recent debut album "Undiscovered" which charted in 2007. As analysed in detail below, Zomba UK also has signed a number of established and upcoming authors; it can therefore be reasonably expected that Zomba UK will continue to produce hits.

¹⁵⁰ See above in the Competitive Assessment: In 2006 BMG contributed to increase Universal control share in official charts by 9 percentage points on an EEA-wide level whereas in 2005 it only contributed to increase control shares of Universal by 6 percentage points.

453. Zomba U.S. is even better positioned as regards recent chart hits. It contains the works of Linkin Park (who had several chart hits in 2003 and 2004 and released their latest album in April 2007), R. Kelly (who had 13 number 1 hits), Justin Timberlake (who recently had several top chart hits such as "Sexyback", "My love" and "What goes around"), Korn (who charted in the United Kingdom and other Member States in 2005 and 2006 with "Coming Undone" and "Twisted Transistor", Ne-Yo (who had top chart hits in the United Kingdom and several other Member States in 2006 with "Sexy Love" (number 1 in the United Kingdom) and "So Sick" (number 5 in the United Kingdom) and who also wrote top chart hits for Mario ("Let me love you") and Rihanna ("Unfaithful") which both reached number 2 in several Member States.
454. Zomba U.S. also has a valuable back-catalogue, including Britney Spears (who co-wrote some of her hits), Shania Twain (who co-wrote four of her top ten hits), Macy Gray, Teddy Riley (who wrote for Blackstreet, Mary J. Blige and Michael Jackson). It is noteworthy that prior to its acquisition by BMG in 2002, Zomba was an important independent music publisher which had been very successful since the 1990s.
455. Rondor UK has a very strong back catalogue with more than 70 writers, including Mark Knopfler (Dire Straits), Wayne Hector (who co-wrote a number of Westlife chart hits, one of which has been already released in a successful cover version), William Orbit (who co-wrote six titles for Madonna), Nick Kershaw ("Wouldn't it be good"), Hammond and Hazelwood ("It never rains in Southern California" and "The air that I breathe" which has been released in numerous cover versions), Brenda Richie (who wrote for Lionel Richie hits such as "Hello", "All Night Long" and "Dancing on the Ceiling").
456. Rondor UK also has some recently very successful hit authors, in particular The Kaiser Chiefs (whose 2005 album "Employment" has brought four singles into the top 11 in the UK). Their latest album "Yours Truly, Angry Mob" was released in March 2007 and has already reached top album chart positions in several Member States (number 1 in Greece, the Netherlands and the United Kingdom). The first single release of this album, "Ruby" has hit the number 1 chart position in the United Kingdom and in the European singles charts. Another author with recent chart success is Sophie Ellis Bexter who had several chart hits in the years 2001-2004. Her latest album is due for release in May 2007 and the first single release of this album reached number 8 in the United Kingdom charts.
457. On the basis of the analysis above the Commission found that the catalogues included in the Remedies Package are of high quality and present a good mixture of recent hits and successful back catalogue. The latter can be expected to generate constant revenue flows (as it has done in the past) and to be the source for some successful cover versions in the future. The authors of recent hits seem particularly to meet the "current music taste" and usually write their own songs (in case of singer-songwriters such as The Kaiser Chiefs, Linkin Park, R. Kelly) or write for currently successful singers. It can therefore reasonably be expected that they will be able to maintain or repeat their success at least for the foreseeable future, i.e. the next album(s). In addition, some today's hits included in the Remedies Package have the potential to become "evergreens" and therefore to generate regular revenue streams and to be released again in cover versions.
458. The Remedies Package combines Anglo repertoire and U.S. American repertoire, as requested by several responses to the market tests. Zomba U.S. accounts for approximately one third of the EEA-wide revenues of the Remedies Package. The licensing of the repertoire of Zomba U.S. allows the acquirer to have direct access to U.S. hits which still

have a considerable impact on global hits. On the other hand, the European-wide success of The Kaiser Chiefs and other British groups (e.g Arctic Monkeys, Franz Ferdinand) shows that Anglo catalogue is very popular in Europe and therefore the larger part of the Remedies Package is composed of British catalogues.¹⁵¹

2.6 Potential of signed authors to produce future hits

459. The Remedies Package also contains an important percentage of BMG's top 200 authors, namely 58 (29%) which also account for [25-35]*% of the EEA revenues of BMG's top 200 authors. Rondor UK contributes four of Universal's global top 200 Anglo-American authors (and even 10 of the top 200 Anglo-American authors in terms of United Kingdom revenues) such as the Kaiser Chiefs, Chariscourt and Straitjacket Songs (Mark Knopfler).
460. Many of the most successful authors are still in their term, i.e. under contract. This means they have ongoing obligations to write or compose a certain number of works or, depending on the contracts, to publish via their publisher all works they create during the determined period of time. For instance Out of Pocket Productions (Mutt Lange) and Bruce Springsteen are still under contract with Zomba UK. The contracts with Daft Punk and The Delays are also still ongoing with another option (for extension) for Zomba UK. An option means that the publisher has the contractually agreed right to request an extension of the contract which implies that the author has to provide an additional number of works over a certain period of time. It is quite frequent that publisher and author stipulate several options, i.e. rights of extension, in the contract. In 19 Music, the contracts with the three most successful authors (Absoulte, Ray Hedges and Simon Ellis) are still running and 19 Music has another option for the contract with Simon Ellis. The contracts with the three top authors of 19 Songs are also still running, with an option for 19 Songs for one of them.
461. In Zomba U.S., the top [5-15]* authors ([...]*) are still under contract and Zomba U.S has [...]* options for [several]* of them. In Rondor UK, the contract with their top authors, The Kaiser Chiefs, is still ongoing and Rondor UK has at least [...]* to extend the contract. Contracts with Nik Kershaw and Deekay Music (both among Rondor UK's top 10 authors in 2006) and with Sophie Ellis Bextor (whose new album is to be released in [...]* 2007) are still ongoing with [...]*.
462. Moreover, the Remedies Package contains a high number of new authors with the potential to write future chart hits. [30-40]* of BMG's [60-70]* ([40-50]*%) newly signed authors in the United Kingdom since 01.01.2004 have been signed with Zomba UK and they have received advance payments of EUR [0-10]* million ([40-50]*% of all advances paid by BMG in the United Kingdom). Among these authors are Jamie T (advance payments of EUR [...]* and [...]*), Johnny Lipsey/Jony Rockstar (advance payments of EUR [...]* and [...]*), Ed Treacy/"Chopper Harris" (advance payments of EUR [...]* and [...]*), The Delays (advance payments of EUR [...]* and [...]*), M.I.A. (advance payments of EUR [...]* and [...]*), The Altekicks (advance payments of EUR [...]* and [...]*) and The Mystery Jets (advance payments of EUR [...]* and [...]*).
463. Also Zomba U.S. has signed [30-40]* new authors since 2003 and paid them more than US-\$ [0-10]* million from 2003 to 2006. This represents [10-20]*% of all authors signed in

¹⁵¹ It is noteworthy that there are also U.S. authors (e.g. writing for Britney Spears) have signed with Zomba UK.

the U.S. and [10-20]*% of the advances paid in the U.S. in that period. Among those authors are Ron Femster/Neff U (advance payments of US-\$ [...]*) and [...]*), Beau Dozier (advance payments of US-\$ [...]*) and [...]*), Cool & Dre (advance payments of US-\$ [...]*) and [...]*), The Bronx (advance payments of US-\$ [...]*) and [...]*), Brand New (advance payments of US-\$ [...]*) and [...]*), Ne-Yo (advance payments of US-\$ [...]*) and [...]*), T-Pain (advance payments of US-\$ [...]*) and [...]*)

464. These figures illustrate that considerable investments have been made in Zomba, and in particular in Zomba UK, and that the catalogues seem therefore well prepared for continuous success.

2.7 Geographical scope of the Remedies Package

465. The geographical scope of the Remedies Package is limited to the EEA. The catalogues Zomba UK, 19 Songs, 19 Music, BBC catalogue and Rondor UK will be assigned to the purchaser(s) who shall enter into an exclusive licensing agreement with Universal for the licensing back of the copyrights relating to the divested catalogues in respect of exploitation outside the EEA. The copyrights of Zomba U.S. in respect of exploitation in the EEA will be licensed to a purchaser.

466. The Commission considers the limitation of the geographical scope of the Remedies Package to be proportionate. The competition concerns identified by the Commission are confined to the markets for online music publishing rights in a number of EEA countries. In order to remove these competition concerns it is not necessary to prevent Universal from exploiting outside the EEA the music publishing rights contained in the Remedies Package. In the market test, some respondents stated that it would be preferable to have the catalogues divested for a worldwide exploitation. However, several answers to the market test also explained that the worldwide exploitation rights are not necessary for the viability of a catalogue. Many European publishers have conferred the overseas exploitation of their catalogues to foreign publishers either through sub-publishing agreements or in other ways.

467. With respect to the catalogues Zomba UK, 19 Songs, 19 Music, BBC catalogue and Rondor UK, the purchaser(s) will have ownership and control of the divested catalogues and the contractual relationship with the right owners (authors). The licensing back agreement which will transfer the exploitation rights for the areas outside the EEA to Universal will be negotiated at arm's length between the purchaser(s) and Universal and will be reflected in the purchase price of the divestment businesses. The mere receipt of licensing fees from Universal for the exploitation of the divested catalogues outside the EEA is not expected to negatively impact the exploitation of the divested catalogues by the purchaser(s) in the EEA and his/their competitive behaviour vis-à-vis Universal in the EEA. As it is in line with the standard business practice that publishers confer the exploitation of their catalogues in foreign territories to other publishers, the viability of the divested catalogues will not be affected.

468. Regarding Zomba U.S., the licensing agreement allows the purchaser (licensee) to exploit the full catalogue of Zomba U.S. in the EEA. The inclusion of Zomba U.S. strengthens the American repertoire in the Remedies Package and thus responds to the market test. The Commission considers that, under the specific circumstances of the present case, an assignment of this catalogue is not necessary. Zomba U.S. generates only [25-35]*% of its global revenues within the EEA whereas Zomba UK and Rondor UK achieve respectively

[60-70]*% and [70-80]*% of their global revenues within the EEA. In view of this geographical repartition of revenues it is acceptable that Zomba U.S. maintains the contractual relationship with the rights owners (authors) as it will be more familiar with the U.S. markets and negotiations with U.S. authors.

469. The terms of the licence agreement as set out in Schedule 3 of the Commitments will be negotiated at arm's length. Compositions existing at the date of the present decision shall be licensed on a royalty-free basis and be reflected in the purchase price. Thereby the purchaser/licensee will have to make an upfront payment but no more permanent royalty payments for the exploitation of existing works (without prejudice of the necessary payments to be made to authors). This structure should provide strong incentives to the purchaser/licensee to intensively exploit the licensed Zomba U.S. catalogue as he will not have to pass on any parts of the revenues to Universal. In addition, the licence agreement must not restrict the exploitation by the purchaser/licensee except for those restrictions contained in Zomba U.S.' agreements with its authors and licensors. In conclusion, the licence agreement for Zomba U.S. will thus enable the purchaser/licensee to compete effectively with Universal and other publishers in the EEA.

2.8 Conclusion on Remedies

470. In the light of the above the Commission concludes that the Final Remedies Package removes the serious doubts, both under an EEA-wide or national geographic market definition.

IX. CONDITIONS AND OBLIGATIONS

471. Under the first sentence of the second subparagraph of Article 8(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.

472. The achievement of the measure that gives rise to the structural change of the market is a condition, whereas the implementing steps which are necessary to achieve this result are generally obligations on the parties. Where a condition is not fulfilled, the Commission decision declaring the merger to be compatible with the common market no longer stands. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(5)(b) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2)(d) and 15(1)(c) of the Merger Regulation.

473. In view of the foregoing, this Decision is conditional upon full compliance with the undertaking that the concentration will not be implemented unless and until the parties have signed a binding sales and purchase agreement with one or several purchasers over the Divestment Business pursuant to paragraph 1 of the Commitments and further described in paragraph 4 including Schedules 1 to 7, attached as Annex to this Decision. Furthermore, this Decision is conditional upon full compliance with paragraph 3 of the Commitments. The other parts of the Commitments are obligations.

X. CONCLUSION

474. It is accordingly concluded that the Commitments as set out in the Annex modify the notified concentration to such an extent that the serious doubts of the Commission as to the compatibility of that concentration with the common market are removed. The concentration should, therefore, be declared compatible with the common market pursuant to Article 8(2) of the Merger Regulation and with the EEA Agreement pursuant to Article 57 thereof, subject to compliance with the commitments set out in the Annex which is an integral part of this decision.

HAS ADOPTED THIS DECISION:

Article 1

The notified operation whereby Universal Music Group Inc. acquires sole control within the meaning of Article 3(1)(b) of Regulation (EEC) No 139/2004 of the whole of the undertaking BMG Music Publishing is hereby declared compatible with the common market and the EEA Agreement.

Article 2

Article 1 is subject to compliance with the conditions set out in Section B, paragraphs 1, 3 and 4 (including Schedules 1-7) of the final version of the Commitments submitted by the parties on 23 April 2007 (attached as Annex to this Decision).

Article 3

Article 1 is subject to compliance with the obligations set out in the remaining provisions of Section B and in Sections C, D and E of the final version of the Commitments submitted by the parties on 23 April 2007 (attached as Annex to this Decision).

Article 4

This Decision is addressed to:

Universal Music Group, Inc.
1755 Broadway
United States of America - 10019 New
York, NY

Done at Brussels, 22/V/2007

For the Commission
Neelie KROES
Member of the Commission

**Case COMP/M.4404 Universal/BMG Music Publishing
COMMITMENTS TO THE EUROPEAN COMMISSION**

Pursuant to Articles 8(2) and 10(2) of Council Regulation No. 139/2004/EC as amended (the “**Merger Regulation**”), Universal Music Group, Inc (the “**Notifying Party**”) hereby provides the following Commitments (the “**Commitments**”) in order to enable the European Commission (the “**Commission**”) to declare the acquisition of BMG MP by the Notifying Party (the “**Notified Concentration**”) compatible with the common market and the EEA Agreement by its decision pursuant to Article 8(2) of the Merger Regulation (the “**Decision**”).

The Commitments shall take effect upon the date of adoption of the Decision.

This text shall be interpreted in the light of the Decision to the extent that the Commitments are attached as conditions and obligations, in the general framework of Community law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EEC) No 4064/89 and under Commission Regulation (EC) No 447/98.

Section A. Definitions

For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled by UMG and/or by the ultimate parent company of UMG (i.e. Vivendi S.A.), whereby the notion of control shall be interpreted pursuant to Article 3 Merger Regulation and in the light of the Commission Notice on the concept of concentration under Council Regulation (EEC) No 4064/89.

BMG MP: BMG Music Publishing is the music publishing division of Bertelsmann AG, a German stock corporation with its registered office in Guetersloh, Germany, registered in the commercial register of the local court Guetersloh, Germany, under HR B 3100

Closing: the transfer of the legal title of the Divestment Businesses to the Purchaser.

Divestment Businesses: the business or businesses as defined in Section B and Schedules 1 to 7 that the Notifying Party commits to divest.

Divestiture Trustee: one or more natural or legal person(s), independent from the Notifying Party, who is approved by the Commission and appointed by UMG and who has received from UMG the exclusive Trustee Mandate to sell the Divestment Businesses to one or several Purchasers at no minimum price.

Effective Date: the date of adoption of the Decision by the European Commission.

First Divestiture Period: the period of **[Business Secret]** months from the Effective Date.

Hold Separate Manager: the person appointed by UMG for the Divestment Businesses to manage the day-to-day business under the supervision of the Monitoring Trustee.

Monitoring Trustee: one or more natural or legal person(s), independent from the Notifying Party, who is approved by the Commission and appointed by UMG and who has the duty to monitor UMG's compliance with the conditions and obligations attached to the Decision.

Notifying Party: the company Universal Music Group, Inc, incorporated under the laws of Delaware, with its registered office at 1755 Broadway, New York, NY 10019, USA and registered with the State of Delaware Division of Corporations under number 2961379

Personnel: personnel listed in Schedule 2

Purchaser: each entity approved by the Commission as acquirer of the Divestment Businesses in accordance with the criteria set out in Section D.

Trustee(s): the Monitoring Trustee and the Divestiture Trustee.

Trustee Divestiture Period: the period of **[Business Secret]** months from the end of the First Divestiture Period.

UMG: incorporated under the laws of Delaware with its registered office at 1755 Broadway, New York, NY10019 and registered with the State of Delaware Division of Corporations under number 2961379.

Vivendi SA: a French Société Anonyme whose principal place of business is at 42 avenue de Friedland, 75380 Paris, France

Zomba US: the business defined in Schedule 3.

Section B. The Divestment Businesses

Commitment to divest

1. In order to restore effective competition, UMG commits to divest, or procure the divestiture of the Divestment Businesses by the end of the Trustee Divestiture Period as a going concern to a purchaser(s) and on terms of sale approved by the Commission in accordance with the procedure described in paragraph 15. To carry out the divestiture, the Notifying Party commits to find a purchaser(s) and to enter into a final binding sale and purchase agreement for the sale of the Divestment Businesses within the First Divestiture Period. If the Notifying Party has not entered into such an agreement at the end of the First Divestiture Period, the Notifying Party shall grant the Divestiture Trustee an exclusive mandate to sell the Divestment Businesses in accordance with the procedure described in paragraph 24 in the Trustee Divestiture Period.
2. The Notifying Party shall be deemed to have complied with this commitment if, by the end of the Trustee Divestiture Period, the Notifying Party has entered into the final binding sale and purchase agreements, if the Commission approves the Purchaser and the terms in accordance with the procedure described in paragraph 15 and if the closing of the sale of the Divestment Businesses takes place within a period not exceeding **[Business Secret]** months after the approval of the respective purchaser and the terms of sale by the Commission.
3. In order to maintain the structural effect of the Commitments, the Notifying Party and its Affiliated Undertakings shall, for a period of **[Business Secret]** years after the Effective Date, not acquire direct or indirect influence over the whole or part of the Divestment Businesses, nor solicit writers forming part of the Divestment Businesses in order for them to enter into music publishing agreements for exploitation of their rights within the EEA, unless the Commission has previously found that the structure of the market has changed to such an extent that the absence of influence over the Divestment Businesses is no longer necessary to render the proposed concentration compatible with the common market. For the avoidance of doubt, and subject to the terms of the licensing of the Compositions from Zomba US as described in Schedule 3 of these Commitments, this clause shall not apply to any writers or compositions which are the subject of the licence from Zomba US, described in Schedule 3 of these Commitments.

Structure and definition of the Divestment Businesses

4. The Divestment Businesses consist of a number of self standing corporate entities (subject to the collection of copyrights described at Schedule 6 of these Commitments) which contain the

music publishing rights of varying durations, including the rights to future compositions, for a balanced and diverse portfolio of Anglo-American music catalogues, ranging from some of today's most successful authors, back catalogue to evergreen tracks and a number of exciting up and coming authors. The present legal and functional structure of the Divestment Businesses as operated to date is described in Schedules 1 to 7. The Divestment Businesses, described in more detail in the Schedules, include:

- (a) all existing tangible and intangible assets (including all copyrights in musical works ("**Copyrights**") and other intellectual property rights), which contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Businesses. The Purchaser shall enter into an exclusive licensing agreement with UMG or one of its Affiliated Undertakings for the licensing back of the Copyrights relating to the Divestment Businesses in respect of exploitation outside the EEA, the key elements of which will be as follows:
 - (i) the Purchaser will have ownership and control of the Divestment Businesses and the contractual relationship with the rights owner;
 - (ii) the Copyrights will include those currently in existence and those to be delivered under existing agreements and any renewals of those agreements; and
 - (iii) the financial terms will be those negotiated at arms length with the Purchaser and will be reflected in the purchase price of the Divestment Businesses.
- (b) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Divestment Businesses; and
- (c) all contracts, leases, commitments and customer orders of the Divestment Businesses; all customer, credit and other records of the Divestment Businesses (items referred to under (a)-(c) hereinafter collectively referred to as "**Assets**");
- (d) all licences for the popular music Copyrights held by Zomba US in respect of exploitation in the EEA, the key elements of which will be as follows:

- (i) UMG or its Affiliated Undertakings shall have the contractual relationship with the rights owner;
- (ii) The Copyrights will include those currently in existence, and those to be delivered, under existing agreements, and those to be delivered following the exercise of any options provided for under existing agreements; and
- (iii) The financial and other terms will be as set out at Schedule 3 of these Commitments.

Section C. Related commitments

Preservation of Viability, Marketability and Competitiveness

5. From the Effective Date until Closing, the Notifying Party shall preserve the economic viability, marketability and competitiveness of the Divestment Businesses, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Businesses. In particular the Notifying Party undertakes:
- (a) not to carry out any act upon its own authority that might have a significant adverse impact on the value, management or competitiveness of the Divestment Businesses or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of the Divestment Businesses;
 - (b) to make available sufficient resources for the development of the Divestment Businesses, on the basis and continuation of the existing business plans;
 - (c) to make best efforts, including appropriate incentive schemes or other benefits (based on industry practice), to encourage the Personnel to remain with that part of the Divestment Businesses described in Schedule 2;
 - (d) to renew options arising in contracts forming part of the Divestment Businesses, where it would be commercially reasonable to do so; and
 - (e) not to transfer any Copyrights out of the Divestment Businesses.

Hold-separate obligations of the Notifying Party

6. The Notifying Party commits, from the Effective Date until Closing, to keep the Divestment Businesses separate from the businesses it is retaining and to ensure that the Personnel and the Hold Separate Manager have no involvement in any business retained and vice versa. The Notifying Party shall also ensure that the Personnel do not report to any individual outside the Divestment Businesses.
7. Until Closing, the Notifying Party shall assist the Monitoring Trustee in ensuring that the Divestment Businesses are managed as distinct and saleable entities separate from the businesses retained by the Notifying Party. The Notifying Party shall appoint a Hold Separate Manager who shall be responsible for the management of the Divestment Businesses, under the supervision of the Monitoring Trustee. The Hold Separate Manager shall manage the Divestment Businesses independently and in the best interest of the respective businesses with a view to ensuring their continued economic viability, marketability and competitiveness and their independence from the businesses retained by the Notifying Party.
8. To ensure that the Divestment Businesses are held and managed as separate entities the Monitoring Trustee shall exercise the Notifying Party's rights as shareholder in the Divestment Businesses (except for its rights for dividends that are due before Closing), with the aim of acting in the best interest of the businesses, determined on a stand-alone basis, as an independent financial investor, and with a view to fulfilling the Notifying Party's obligations under the Commitments. Furthermore, the Monitoring Trustee shall have the power to replace members of the supervisory board or non-executive directors of the board of directors, who have been appointed on behalf of the Notifying Party. Upon request of the Monitoring Trustee, the Notifying Party shall resign as member of the boards or shall cause such members of the boards to resign.

Ring-fencing

9. The Notifying Party shall implement all necessary measures to ensure that it does not after the Effective Date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to the Divestment Businesses, other than in respect of royalty processing, copyright registration and other administration and

accounting services carried out in the ordinary course of business, such services to be overseen by the Monitoring Trustee insofar as they relate to the Divestment Businesses, and other than is necessary for the implementation of the provisions of Schedule 3 in respect of the licensing of the Compositions as described therein. In particular, the participation of the Divestment Businesses in a central information technology network shall be severed to the extent possible, without compromising the viability of the Divestment Businesses. The Notifying Party may obtain information relating to the Divestment Businesses which is reasonably necessary for the divestiture of the Divestment Businesses or whose disclosure to the Notifying Party is required by law.

Non-solicitation clause

10. The Notifying Party undertakes, subject to customary limitations, not to solicit, and to procure that Affiliated Undertakings do not solicit, the Personnel for a period of **[Business Secret]** years after Closing, to the extent that the Personnel are transferred to the Purchaser after closing.

Due Diligence

11. In order to enable potential purchasers to carry out a reasonable due diligence of the Divestment Businesses, the Notifying Party shall, subject to customary confidentiality assurances and dependent on the stage of the divestiture process:
 - (a) provide to potential purchasers sufficient information as regards the Divestment Businesses;
 - (b) provide to potential purchasers sufficient information relating to the Personnel and allow them reasonable access to the Personnel.

Reporting

12. The Notifying Party shall submit written reports in English on potential purchasers of the Divestment Businesses and developments in the negotiations with such potential purchasers to the Commission and the Monitoring Trustee no later than 10 days after the end of every month following the Effective Date (or otherwise at the Commission's request).
13. The Notifying Party shall inform the Commission and the Monitoring Trustee on the preparation of the data room documentation and the due diligence procedure and shall submit a copy of an

information memorandum to the Commission and the Monitoring Trustee before sending the memorandum out to potential purchasers.

Section D. The Purchaser

14. In order to ensure the immediate restoration of effective competition, the purchaser(s), in order to be approved by the Commission, must:
- (a) be independent of and unconnected to the Notifying Party, subject to paragraph 4(a);
 - (b) have the financial resources, proven expertise and incentive to maintain and develop the Divestment Businesses as viable and active competitive forces in competition with the Notifying Party and other competitors;
 - (c) neither be likely to create, in the light of the information available to the Commission, *prima facie* competition concerns nor give rise to a risk that the implementation of the Commitments will be delayed, and must, in particular, reasonably be expected to obtain all necessary approvals from the relevant regulatory authorities for the acquisition of the Divestment Businesses (the before-mentioned criteria for the purchaser hereafter the "**Purchaser Requirements**").
15. The final binding sale and purchase agreement or agreements and all ancillary agreements shall be conditional on the Commission's approval. When the Notifying Party has reached an agreement with a purchaser, it shall submit a fully documented and reasoned proposal, including a copy of the final agreement(s), to the Commission and the Monitoring Trustee. The Notifying Party must be able to demonstrate to the Commission that each purchaser meets the Purchaser Requirements and that the Divestment Businesses are being sold in a manner consistent with the Commitments. For the approval, the Commission shall verify that the purchaser fulfils the Purchaser Requirements and that the Divestment Businesses are being sold in a manner consistent with the Commitments. The Commission may approve the sale of the Divestment Businesses without one or more Assets, if this does not affect the viability and competitiveness of the Divestment Businesses after the sale, taking account of the proposed purchaser.

Section E. Trustee

I. Appointment Procedure

16. The Notifying Party shall appoint a Monitoring Trustee to carry out the functions specified in the Commitments for a Monitoring Trustee. If the Notifying Party has not entered into a binding sales and purchase agreement(s) for each of the Divestment Businesses one month before the end of the First Divestiture Period or if the Commission has rejected a purchaser proposed by the Notifying Party at that time or thereafter, the Notifying Party shall appoint a Divestiture Trustee to carry out the functions specified in the Commitments for a Divestiture Trustee. The appointment of the Divestiture Trustee shall take effect upon the commencement of the Extended Divestment Period.
17. The Trustee shall be independent of the Notifying Party, possess the necessary qualifications to carry out its mandate, for example as an investment bank or consultant or auditor, and shall neither have nor become exposed to a conflict of interest. The Trustee shall be remunerated by the Notifying Party in a way that does not impede the independent and effective fulfilment of its mandate. In particular, where the remuneration package of a Divestiture Trustee includes a success premium linked to the final sale value of the Divestment Businesses, the fee shall also be linked to a divestiture within the Trustee Divestiture Period.

Proposal by the Notifying Party

18. No later than one week after the Effective Date, the Notifying Party shall submit a list of one or more persons whom the Notifying Party proposes to appoint as the Monitoring Trustee to the Commission for approval. No later than one month before the end of the First Divestiture Period, the Notifying Party shall submit a list of one or more persons whom the Notifying Party proposes to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the proposed Trustee fulfils the requirements set out in paragraph 17 and shall include:
 - (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;

- (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks; and
- (c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether different trustees are proposed for the two functions.

Approval or rejection by the Commission

19. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, the Notifying Party shall appoint or cause to be appointed, the individual or institution concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Notifying Party shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Notifying Party

20. If all the proposed Trustees are rejected, the Notifying Party shall submit the names of at least two more individuals or institutions within one week of being informed of the rejection, in accordance with the requirements and the procedure set out in paragraphs 16 and 19.

Trustee nominated by the Commission

21. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom the Notifying Party shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

22. The Trustee shall assume its specified duties in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or the Notifying Party, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee

23. The Monitoring Trustee shall:

- (i) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision.
- (ii) oversee the on-going management of the Divestment Businesses with a view to ensuring its continued economic viability, marketability and competitiveness and monitor compliance by the Notifying Party with the conditions and obligations attached to the Decision. To that end the Monitoring Trustee shall:
 - (a) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Businesses, and the keeping separate of the Divestment Businesses from the business retained by the Notifying Party, in accordance with paragraphs 5 and 6 of the Commitments;
 - (b) supervise the management of the Divestment Businesses as distinct and saleable entities, in accordance with paragraph 7 of the Commitments;
 - (c) (i) in consultation with the Notifying Party and subject to paragraph 9 of the Commitments, determine all necessary measures to ensure that the Notifying Party does not after the Effective Date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to the Divestment Businesses, and in particular strive for the severing of the Divestment Businesses' participation in a central information technology network to the extent possible, without compromising the viability of the Divestment Businesses, and (ii) decide whether such information may be disclosed to the Notifying Party as the disclosure is reasonably necessary to allow the Notifying Party to carry out the divestiture or as the disclosure is required by law;

- (d) as applicable, monitor the splitting of assets and the allocation of Personnel between the Divestment Businesses and the Notifying Party or Affiliated Undertakings;
- (iii) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision;
- (iv) propose to the Notifying Party such measures as the Monitoring Trustee considers necessary to ensure the Notifying Party's compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability or competitiveness of the Divestment Businesses, the holding separate of the Divestment Businesses and the non-disclosure of competitively sensitive information;
- (v) review and assess potential purchasers as well as the progress of the divestiture process and verify that, dependent on the stage of the divestiture process, (a) potential purchasers receive sufficient information relating to the Divestment Businesses and the Personnel in particular by reviewing, if available, the data room documentation, the information memorandum and the due diligence process, and (b) potential purchasers are granted reasonable access to the Personnel;
- (vi) provide to the Commission, sending the Notifying Party a non-confidential copy at the same time, a written report within 15 days after the end of every month. The report shall cover the operation and management of the Divestment Businesses so that the Commission can assess whether the business is held in a manner consistent with the Commitments and the progress of the divestiture process as well as potential purchasers. In addition to these reports, the Monitoring Trustee shall promptly report in writing to the Commission, sending the Notifying Party a non-confidential copy at the same time, if it concludes on reasonable grounds that the Notifying Party is failing to comply with these Commitments;
- (vii) within one week after receipt of the documented proposal referred to in paragraph 15, submit to the Commission a reasoned opinion as to the suitability and independence of the proposed purchaser and the viability of the Divestment Businesses after the Sale

and as to whether the Divestment Businesses are sold in a manner consistent with the conditions and obligations attached to the Decision, in particular, if relevant, whether the Sale of the Divestment Businesses without one or more Assets or not all of the Personnel affects the viability of the Divestment Businesses after the sale, taking account of the proposed purchaser.

Duties and obligations of the Divestiture Trustee

24. Within the Trustee Divestiture Period, the Divestiture Trustee shall sell at no minimum price the Divestment Businesses to a purchaser(s), provided that the Commission has approved both the purchaser and the final binding sale and purchase agreement(s) in accordance with the procedure laid down in paragraph 15. The Divestiture Trustee shall include in the sale and purchase agreement(s) such terms and conditions as it considers appropriate for an expedient sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the sale and purchase agreement(s) such customary representations and warranties and indemnities as are reasonably required to effect the sale. The Divestiture Trustee shall protect the legitimate financial interests of the Notifying Party, subject to the Notifying Party's unconditional obligation to divest at no minimum price in the Trustee Divestiture Period.
25. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the end of every month with a simultaneous copy to the Monitoring Trustee and a non-confidential copy to the Notifying Party.

III. *Duties and obligations of the Notifying Party*

26. The Notifying Party shall provide and shall cause its advisors to provide the Trustee with all such cooperation, assistance and information as the Trustee may reasonably require to perform its tasks. The Trustee shall have full and complete access to any of the Notifying Party's or the Divestment Businesses' books, records, documents, management or other personnel, facilities, sites and technical information necessary for fulfilling its duties under the Commitments and the Notifying Party and the Divestment Businesses shall provide the Trustee upon request with copies of any document. The Notifying Party and the Divestment Businesses shall make

available to the Trustee one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of its tasks.

27. The Notifying Party shall provide the Monitoring Trustee with all managerial and administrative support that it may reasonably request on behalf of the management of the Divestment Businesses. This shall include all administrative support functions relating to the Divestment Businesses which are currently carried out at headquarters level. The Notifying Party shall provide and shall cause its advisors to provide the Monitoring Trustee, on request, with the information submitted to potential purchasers, in particular give the Monitoring Trustee access to the data room documentation and all other information granted to potential purchasers in the due diligence procedure the Notifying Party shall inform the Monitoring Trustee on possible purchasers, submit a list of potential purchasers, and keep the Monitoring Trustee informed of all developments in the divestiture process.
28. The Notifying Party shall grant or procure Affiliated Undertakings to grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee to effect the sale, the Closing and all actions and declarations which the Divestiture Trustee considers necessary or appropriate to achieve the sale and the Closing, including the appointment of advisors to assist with the sale process. Upon request of the Divestiture Trustee, the Notifying Party shall cause the documents required for effecting the sale and the Closing to be duly executed.
29. The Notifying Party shall indemnify the Trustee and its employees and agents (each an "**Indemnified Party**") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to the Notifying Party for any liabilities arising out of the performance of the Trustee's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee, its employees, agents or advisors.
30. At the expense of the Notifying Party, the Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to the Notifying Party's approval (this approval not to be unreasonably withheld or delayed) if the Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate,

provided that any fees and other expenses incurred by the Trustee are reasonable. Should the Notifying Party refuse to approve the advisors proposed by the Trustee the Commission may approve the appointment of such advisors instead, after having heard the Notifying Party. Only the Trustee shall be entitled to issue instructions to the advisors. Paragraph 29 shall apply mutatis mutandis. In the Trustee Divestiture Period, the Divestiture Trustee may use advisors who served the Notifying Party during the Divestiture Period if the Divestiture Trustee considers this in the best interest of an expedient sale.

IV. Replacement discharge and reappointment of the Trustee

31. If the Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a conflict of interest:
 - (a) the Commission may, after hearing the Trustee, require the Notifying Party to replace the Trustee; or
 - (b) the Notifying Party, with the prior approval of the Commission, may replace the Trustee.
32. If the Trustee is removed according to paragraph 31, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in paragraphs 16-21.
33. Beside the removal according to paragraph 31, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section F. The Review Clause

34. The Commission may, where appropriate, in response to a request from the Notifying Party showing good cause and accompanied by a report from the Monitoring Trustee:

- (i) Grant an extension of the time periods foreseen in the Commitments, or
- (ii) Waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments.

Where the Notifying Party seeks an extension of a time period, it shall submit a request to the Commission no later than one month before the expiry of that period, showing good cause. Only in exceptional circumstances shall the Notifying Party be entitled to request an extension within the last month of any period.

.....

duly authorised for and on behalf of
the Notifying Party

23 April 2007

SCHEDULE 1

The Divestment Businesses as operated to date have the following legal and functional structure:

1 The Divestment Businesses are made up of the following companies:

- Zomba Music Publishers Limited
- Newco Limited (as described in Schedule 3)
- Rondor Music (London) Limited
- 19 Music Limited
- 19 Songs Limited
- BMG MP's BBC music publishing catalogue

2 In Schedules 2 to 7 which follow, revenues generated by each catalogue have been reported on the basis of revenues currently passed on to the legal entity in question, within the context of a broader group of local music publishing entities (either BMG MP or UMPG in the UK).

However, actual revenues generated by each of these catalogues are higher than those shown in Schedules 2 to 7 **[Business Secret]**.

SCHEDULE 2 – Zomba Music Publishers Limited

Summary

Zomba Music Publishers Limited (“ZMPL”) is a separate legal entity within BMG Music Publishing. ZMPL has been associated with some of the most successful Anglo American pop acts throughout the 1980s, 1990s, and 2000s, is a very significant and competitive music publishing catalogue, has a huge roster of current successful authors, with an independent, stand-alone creative infrastructure, which generated revenues of **€[5 - 10 million]** in the EEA and **€[10 - 20 million]** globally in 2006.

All staff are currently employed by BMG Music Publishing.

Asset Description

The ZMPL music catalogue consists of the following:

- Cheiron/ Grantsville/ Maratone – the various company names associated with Denniz Pop and Max Martin. Denniz and Max started one of the most successful writer/production teams in pop music history and shaped the modern pop sound of the 1990’s. After Denniz’s untimely death Max has continued to be one of the most in demand pop writers. Artists whose careers have been shaped by Denniz and Max include Britney Spears, The Backstreet Boys, NSYNC, Celine Dion, Westlife and Kelly Clarkson. Collectively they are responsible for 250 million album unit sales worldwide.
- Iron Maiden – one of the UK’s most successful rock bands selling in excess of 80 million records worldwide. Over 15 albums recorded and signed to Zomba Music from the start of their career.
- A Flock Of Seagulls – one of the first signings to Jive Records and one of the first UK bands from the MTV generation to break the US market. Their single ‘I

Ran' was one of the first videos to be championed by MTV and the album that the single was from went on to sell over 1 million units in the US.

- Billy Ocean – for many years Billy was the UK's best selling black artist. Still name checked and highly regarded by many current rap/hip hop stars.
- The Stone Roses – their debut eponymous album was recently voted by readers of the NME as the Greatest Album of All time. The catalogue of only one album for Silvertone Records / ZMPL continues to be one of the biggest earners.
- Mutt Lange – officially the most successful record producer of all time Mutt Lange has been the backbone of the company since its formation. Currently married to Shania Twain, Mutt has co-written her material. She has sold 100 million records worldwide. Other artists that Mutt has written hits for include Billy Ocean, Def Leppard, Bryan Adams, Michael Bolton, Huey Lewis, Billy Ray Cyrus, Heart, Britney Spears, Celine Dion, The Corrs and many more.
- Bruce Springsteen – ZMPL looks after the catalogue of Bruce Springsteen for the UK & Eire.
- Peter Sinfield – ZMPL acquired the catalogue of songwriter Peter Sinfield in 2005. Included are huge hits from Celine Dion 'Think Twice', Cher 'Heart Of Stone' and hits from Leo Sayer, Cliff Richard, Barry Manilow, Diana Ross, Five Star, Bucks Fizz & Gene Pitney. Peter has recently been back in the album charts with his song 'Have You Ever Been In Love' that was originally recorded by Leo Sayer and more recently by Westlife on their million selling 'Love' album.
- Current writers from the company include former BBMak frontman Christian Burns

- Vile Music – ZMPL has the largest catalogue of black/thrash metal in the world through one of its publishing divisions Vile Music. Vile Music signs songwriters introduced to it under a consultancy agreement with a record company run by Paul Halmshaw called Peaceville Records. We control the back catalogue of the trendsetting acts in this genre, such as Paradise Lost, Opeth & Cradle Of Filth and publish some of the hottest new acts in the world of metal including Anathema, Darkthrone, Madder Mortem, Novembre, My Dying Bride, Katatonia, Old & The Provence.
- Other selected highlights include writer Tim Friese Green's share of the Talk Talk song 'Its My Life' recently covered by No Doubt, Twisted Sister 'We're Not Gonna Take It', Jo Boxers 'Just Got Lucky' (featured in several big US movies in 2005/6), Steps '5678', Jona Lewie 'Stop The Cavalry', Gabrielle 'Dreams'.

Current active deals signed to ZMPL include:

- Daft Punk – French dance duo that have sold more than 7 million albums worldwide and have had their music used extensively in advertising including ads for iTunes & Motorola. Currently recording a new album for release later this year.
- Delays – Southampton based band that have released two albums on indie Rough Trade Records and have sold 250K units. The band is now working on a new album due for release 4Q07. They have also been successful in the synch world securing major ad campaigns for Bulldog Broadband, DeBeers Diamonds' & Sprite.

- Jamie T – one of our newer signings, Jamie T released his debut album ‘Panic Prevention’ in January 2007. The album entered at number 4 on the UK album chart and has so far sold 200K units. Jamie was also voted best solo artist at the 2007 NME awards.
- M.I.A – signed to XL Records in the UK and Interscope for America her debut album ‘Arular’ has now sold over 250,000 units worldwide. She has also co-written with Missy Elliot for her last album. M.I.A music has featured in a variety of ads including Honda cars. M.I.A is currently putting the finishing touches to her second album with producer Timbaland (Justin Timberlake/ Nelly Furtado) that is due for release 4Q07.
- Laura Izibor – Dublin based singer songwriter whose debut album is due for release 3Q07.
- The Mystery Jets – one of the most talked about acts on the UK indie scene in 2006. Their debut album ‘Making Dens’ has sold over 100,000 copies and they are currently putting the finishing touches to their second album due 3Q07.
- Nitin Sawhney – highly acclaimed artist and composer who has recently scored his first Hollywood movie ‘The Namesake’ for Fox Pictures. He has scored over 10 international films and provided music for numerous TV shows and ads including the BBC’s Natural World Symphony, and ads for Nike & The Financial Times. He has recently provided the score for the forthcoming Playstation 3 game ‘Heavenly Sword’. As an artist he has released 7 albums in his own right and has collaborated with Sir Paul McCartney.
- The Eagles Of Death Metal (“EODM”) – a side project from Queens Of The Stone Age front man Josh Homme and Jesse Hughes. ZMPL publishes Jesse.

EODM have sold over 200,000 albums sold so far and their music has been used in ads for VW, Budweiser, Wendy's, Microsoft Zune, Nissan and numerous TV shows and films.

- Kate Havnevik – London based Norwegian artist who has had huge success in the US with her music being used in numerous TV shows including The West Wing, The OC, and seven different songs being used in Grey's Anatomy. A total of [Business Secret] TV synchs so far. Kate's debut album 'Melankton' will be released on 27 March.
- Lethal Bizzle – the UK's leading grime MC. His debut album sold 60,000 units. His second album is due for release in May and features collaborations with new buzz acts Kate Nash and Mr Hudson and The Library.
- Alterkicks – a development project who are about to release their debut single. Their album has been produced by the acclaimed producer Stephen Street (The Smiths, Blur) and is set for release 3Q07.
- Chopper Harris – newly signed and currently working on his debut album due later this year.
- Other current signings that are in development are singer songwriter Vijay Kishore, 3 piece guitar band Freerunner and pop rock act Mamas Gun.
- Martin Brammer – Martin has written hits in the past for The Lighthouse Family, Tina Turner, Rachel Stevens & Nick Carter. He currently has several songs on the million selling debut album by James Morrison including the single 'The Pieces Don't Fit' and title track 'Undiscovered'. James Morrison has also recently won a Brit Award. Martin has also co-written five tracks with Beverly Knight for her new album that is due for release at the end of April. Martin has

five cuts on the forthcoming album by Jack MacManus and several cuts on debut act Jonas. He has two songs on debut artist Adam Argyle's album and numerous other songs cut with a whole range of acts including German Pop Idol.

- Jony Rockstar – writer producer known mainly for his work with The Sugababes. He has written several of their biggest hits. Currently working with ex Sugababe Mutya on her debut solo album, he is also writing with Cathy Dennis and Jennifer Lopez for her album. He has cuts on forthcoming albums from Siobahn Donaghy, Leon Jean Marie and Belle.
- Pete Kirtley – Ivor Novello winning pop songwriter who has just enjoyed a huge number 1 hit in Germany with the winners of German PopStars Monrose. The single has been one of the fastest selling ringtones in Germany selling 1.5 million ringtones. Pete had three songs on their number 1 album as well. Pete is currently working with new artist Sarah Jane Davis.

The ZMPL catalogue contains hit songs recorded by many leading contemporary artists:

- Britney Spears - “Hit me baby one more time” – chart #1 in countries including Belgium, Finland, France, Germany, Italy, the Netherlands, Norway and Spain;
- Britney Spears - “Oops I did it again” - #1 in Italy, the Netherlands, Norway and Sweden and top ten in Austria, Belgium, Finland, France and Germany.
- Bryan Adams - “Everything I do...” - #1 in Germany, the Netherlands, Belgium, Austria, Finland, Sweden, Denmark and Norway, amongst other countries.
- Backstreet Boys “I want it that way”, #1 in Portugal, Sweden, Ireland, the Netherlands, Norway, Greece, Austria, Belgium, Finland, Italy, Denmark and Latvia.

- Celine Dion – “That’s the way it is” #1 in Austria, Belgium, Denmark, Finland, France, Ireland, Italy, Latvia, the Netherlands, Norway, Poland, Spain and Sweden.
- Kelly Clarkson “Since You’ve been gone” #1 in the Netherlands, Ireland, Germany and UK.

This list is by no means exhaustive, but gives a flavour of the international success of the songs included in ZMPL’s catalogue.

The following table provides a summary of the financial information over the past three years:

SUMMARY	2004	2005	2006
EEA Revenue (€‘000)	[5,000 - 10,000]	[5,000 - 10,000]	[5,000 - 10,000]
Global Revenue (€‘000) ¹⁵²	[10,000 - 20-000]	[10,000 - 20-000]	[10,000 - 20-000]

¹⁵² See paragraph 4(a) of these Commitments.

1 Following paragraph 4 of these Commitments, the Divestment Businesses include, but are not limited to:

(a) the following main intangible assets:

The main assets are the music publishing rights of varying duration. The following table shows the top 100 copyrights in ZMPL for 2006.

	Title	Composers	Revenue (EUR)
1	SINCE U BEEN GONE	SANDBERG/GOTTWALD	[Business Secret]
2	BEHIND THESE HAZEL EYES	SANDBERG/CLARKSON/GOTTWALD	[Business Secret]
3	OOPS!...I DID IT AGAIN	SANDBERG/YACOUB	[Business Secret]
4	BABY ONE MORE TIME	SANDBERG	[Business Secret]
5	STRONGER	SANDBERG/YACOUB	[Business Secret]
6	I WANT IT THAT WAY	SANDBERG/CARLSSON	[Business Secret]
7	LONG TIME COMING	GILBERT/GILBERT	[Business Secret]
8	POUR SOME SUGAR ON ME	CLARK/COLLEN/LANGE/SAVAGE/ELLIOTT	[Business Secret]
9	OVERPROTECTED	SANDBERG/YACOUB	[Business Secret]
10	COTTON EYE JOE	EDENBERG/ERICSSON/OBERG	[Business Secret]
11	GET OUT OF MY DREAMS, GET INTO MY CAR	LANGE/OCEAN	[Business Secret]
12	U DRIVE ME CRAZY	KREUGER/MAGNUSSON/SANDBERG/ELOFSSON	[Business Secret]
13	THE BEST	CHAPMAN/KNIGHT	[Business Secret]
14	IT'S MY LIFE	FRIESE-GREENE/HOLLIS	[Business Secret]
15	YOU WIN MY LOVE	LANGE	[Business Secret]
16	JUST WANT YOU TO KNOW	SANDBERG/GOTTWALD	[Business Secret]
17	AS LONG AS YOU LOVE ME	SANDBERG	[Business Secret]
18	I'M NOT A GIRL, NOT YET A WOMAN	SANDBERG/YACOUB/ARMSTRONG	[Business Secret]
19	LUCKY	SANDBERG/YACOUB/KRONLUND	[Business Secret]
20	THE NUMBER OF THE BEAST	HARRIS	[Business Secret]
21	RUN TO THE HILLS	HARRIS	[Business Secret]
22	I RAN	MAUDSLEY/REYNOLDS/SCORE/SCORE	[Business Secret]
23	WE'RE NOT GONNA TAKE IT	SNIDER	[Business Secret]
24	I STILL	SANDBERG/YACOUB	[Business Secret]
25	TECHNOLOGIC	BANGALTER/DE HOMEM-CHRISTO	[Business Secret]
26	PLEASE FORGIVE ME	ADAMS/LANGE	[Business Secret]
27	BYE BYE BYE	SCHULZE/LUNDIN/CARLSSON	[Business Secret]
28	THAT'S THE WAY IT IS	SANDBERG/LUNDIN/CARLSSON	[Business Secret]
29	IT'S MY LIFE	BON JOVI/SAMBORA/SANDBERG	[Business Secret]
30	BORN TO MAKE YOU HAPPY	LUNDIN/CARLSSON	[Business Secret]
31	BREATHLESS	CORR/CORR/CORR/LANGE	[Business Secret]
32	ONE MORE TIME	BANGALTER/DE HOMEM-CHRISTO/MOORE	[Business Secret]
33	JUST GOT LUCKY	BALL/BOSTOCK	[Business Secret]
34	LOVE BITES	CLARK/COLLEN/ELLIOTT/SAVAGE/LANGE	[Business Secret]
35	LOVE WILL TEAR US APART	CURTIS/HOOK/MORRIS/SUMNER	[Business Secret]
36	THE ONE	SANDBERG/LITTRELL	[Business Secret]
37	HALLOWED BE THY NAME	HARRIS	[Business Secret]
38	TROOPER, THE	HARRIS	[Business Secret]
39	ROCK OF AGES	CLARK/ELLIOTT/LANGE	[Business Secret]
40	SIBERIA	SANDBERG/TALOMAA/YACOUB	[Business Secret]
41	DON'T LET ME BE THE LAST TO KNOW	LANGE/LANGE/SCOTT	[Business Secret]
42	WHEN THE GOING GETS TOUGH, THE TOUGH GET GOING	EASTMOND/OCEAN/LANGE/BRATHWAITE	[Business Secret]
43	FEAR OF THE DARK	HARRIS	[Business Secret]
44	PHOTOGRAPH	CLARK/ELLIOTT/SAVAGE/WILLIS/LANGE	[Business Secret]
45	WHEN YOU'RE LOOKING LIKE THAT	SANDBERG/CARLSSON/YACOUB	[Business Secret]
46	GALANG	ARULPRAGASAM/FRISCHMANN/MACKEY/ORTON	[Business Secret]
47	EVERYBODY (BACKSTREET'S BACK)	SANDBERG/VOLLE	[Business Secret]
48	KEEP THIS FIRE BURNING	CARLSSON/EKHE/LINDSTROM/SIGVARDT	[Business Secret]
49	ARMAGEDDON IT	CLARK/COLLEN/ELLIOTT/SAVAGE/LANGE	[Business Secret]
50	AROUND THE WORLD	BANGALTER/DE HOMEM-CHRISTO	[Business Secret]
51	SHAPE OF MY HEART	SANDBERG/YACOUB/MISKOVSKY	[Business Secret]
52	OBSESSION	DESBARRES/KNIGHT	[Business Secret]
53	ALL I WANNA DO IS MAKE LOVE TO YOU	LANGE	[Business Secret]
54	ANIMAL	CLARK/COLLEN/ELLIOTT/SAVAGE/LANGE	[Business Secret]
55	HYSTERIA	CLARK/COLLEN/ELLIOTT/SAVAGE/LANGE	[Business Secret]
56	TOUCH IT	SMITH/BANGALTER/DE HOMEM-CHRISTO/DEAN	[Business Secret]
57	TWO MINUTES TO MIDNIGHT	DICKINSON/SMITH	[Business Secret]
58	SOMETIMES	ELOFSSON	[Business Secret]
59	HAVE YOU EVER REALLY LOVED A WOMAN?	ADAMS/KAMEN/LANGE	[Business Secret]
60	FOOL'S GOLD	BROWN/SQUIRE	[Business Secret]
61	SHOW ME THE MEANING	CRICHLAW/SANDBERG	[Business Secret]
62	CARIBBEAN QUEEN (NO MORE LOVE ON THE RUN)	OCEAN/ALEXANDER	[Business Secret]
63	ROCKET	CLARK/COLLEN/ELLIOTT/SAVAGE/LANGE	[Business Secret]
64	FOOLIN'	CLARK/ELLIOTT/LANGE	[Business Secret]
65	(EVERYTHING I DO) I DO IT FOR YOU	ADAMS/KAMEN/LANGE	[Business Secret]
66	5,6,7,8	UPTON/CROSBY	[Business Secret]
67	LET'S GET ROCKED	COLLEN/ELLIOTT/SAVAGE/LANGE	[Business Secret]
68	BRINGIN' ON THE HEARTBREAK	CLARK/ELLIOTT/WILLIS	[Business Secret]
69	FLYING	ADAMS/LANGE	[Business Secret]
70	IT'S GONNA BE ME	SANDBERG/CARLSSON/YACOUB	[Business Secret]
71	STOP THE CAVALRY	LEWIE	[Business Secret]
72	IRON MAIDEN	HARRIS	[Business Secret]
73	THE CALL	SANDBERG/YACOUB	[Business Secret]
74	TOUCH ME (I WANT YOUR BODY)	ASTROP/HARRIS/SHREEVE	[Business Secret]
75	LARGER THAN LIFE	SANDBERG/LITTRELL/LUNDIN	[Business Secret]
76	LET'S MAKE A NIGHT TO REMEMBER	ADAMS/LANGE	[Business Secret]

77	MY LOVE	KREUGER/MAGNUSSON/ELOFSSON/NYLEN	[Business Secret]
78	ROBOT ROCK	WILLIAMS/BANGALTER/DE HOMEM-CHRISTO	[Business Secret]
79	TWO STEPS BEHIND	ELLIOTT	[Business Secret]
80	HAVE YOU EVER NEEDED SOMEONE SO BAD	COLLEN/LANGE/ELLIOTT	[Business Secret]
81	OBJECT OF MY DESIRE	ADEYEMO/ALEXANDER/PHILLIPS	[Business Secret]
82	PHANTOM OF THE OPERA	HARRIS	[Business Secret]
83	IF I LET YOU GO	KREUGER/MAGNUSSON/ELOFSSON	[Business Secret]
84	CLIMBING THE WALLS	SANDBERG/GOTTWALD	[Business Secret]
85	DREAMS	BOBB/LAWS	[Business Secret]
86	QUIT PLAYING GAMES (WITH MY HEART)	CRICHLOW/SANDBERG	[Business Secret]
87	WHEN LOVE & HATE COLLIDE	ELLIOTT/SAVAGE	[Business Secret]
88	I WANNA BE ADORED ('GARAGE FLOWER' ALBUM ONLY)	BROWN/SQUIRE	[Business Secret]
89	DROWNING	CARLSSON/YACOUB/THOMPSON	[Business Secret]
90	WATERFALL	BROWN/SQUIRE	[Business Secret]
91	STILL IN LOVE WITH YOU	LINDMAN/BOSTRIM	[Business Secret]
92	CAN'T STOP THIS THING WE STARTED	ADAMS/LANGE	[Business Secret]
93	ATMOSPHERE	CURTIS/HOOK/MORRIS/SUMNER	[Business Secret]
94	DO YOU BELIEVE IN LOVE	LANGE	[Business Secret]
95	MUSIC SOUNDS BETTER WITH YOU	BANGALTER/QUEME/COHEN/KING/MUSKER	[Business Secret]
96	HOME	YOUNG/SAWHNEY/POOLE	[Business Secret]
97	DANCING IN THE DARK	SPRINGSTEEN	[Business Secret]
98	TELEVISION RULES THE NATION	BANGALTER/DE HOMEM-CHRISTO	[Business Secret]
99	WRATHCHILD	HARRIS	[Business Secret]
100	I AM THE RESURRECTION	BROWN/SQUIRE	[Business Secret]

(b) the following main contracts, agreements, leases, commitments and understandings:

The following table shows the top 10 EEA revenue earning writers for ZMPL in 2006. These contracts are of varying terms and duration.

Top 10 Writers	Total EEA Revenues, 2006 (EUR)
Out of Pocket Productions (Mutt Lange)	[Business Secret]
Iron Maiden	[Business Secret]
Martin Sandberg	[Business Secret]
Daft Punk	[Business Secret]
Bruce Springsteen	[Business Secret]
Def Leppard	[Business Secret]
Fractured Music (Joy Division)	[Business Secret]
Stone Roses	[Business Secret]
Delays	[Business Secret]
Rami Yacoub	[Business Secret]
Mike Chapman Publishing Enterprise	[Business Secret]

(c) It is not anticipated that it would be necessary for arrangements to be put in place for the supply of any necessary services for a transitional period, but UMG or affiliated undertakings would be prepared to agree to supply any such services on arm's length terms, if required by the Commission at the request of the Purchaser, for a reasonable transitional period.

2 The following personnel are currently employed by BMG MP but are dedicated to the ZMPL business:

- (a) **[Business Secret]** (General Manager);
- (b) **[Business Secret]** (A&R Manager); and
- (c) **[Business Secret]** (A&R Manager)

The Notifying Party undertakes to take all reasonable steps and to offer all reasonable incentives to assist in procuring the transfer of these personnel to the Purchaser in the event that the Purchaser wishes to employ these personnel following Closing.

- 3 The Divestment Businesses shall not include the Zomba name. The Zomba name is owned by the SONY BMG record company which uses it in connection with its Zomba record label. The trade name is currently licensed to BMG MP under transitional arrangements, put in place at the time of the creation of the SONY BMG joint venture in 2004 (and which are due to expire in **[Business Secret]**).
- 4 The Divestment Businesses shall not include Strongsongs Limited, a wholly owned subsidiary of ZMPL.
- 5 The Divestment Businesses shall not include ZMPL's production music business.

SCHEDULE 3 – Zomba US

Summary

Zomba US is the popular music publishing business of Zomba Enterprises Inc. (“ZEI”), which is a single corporate entity operating with several divisions: Zomba Songs (BMI) and Zomba Melodies (SESAC), which themselves are divisions of ZEI (ASCAP) (“Zomba US”). On or before the Effective Date, Zomba US shall procure the grant to ZMPL, or a newly incorporated corporate entity formed for the purpose of the divestment (the “Newco”), of licences of all popular music copyrights currently in existence for the EEA and those due to be delivered under existing agreements with Zomba US (the “Compositions”). The Purchaser(s) may elect to purchase either ZMPL together with the Compositions, or the Newco containing the Compositions.

Zomba US produced revenues in 2005 in the EEA of **€5 - 10 million**. In 2006 these increased to **€5 - 10 million** in the EEA.

Asset Description

Zomba US operates as a boutique music publisher in the Pop, Rock, and Urban genres. Zomba US’s most notable songwriters include R. Kelly, Linkin Park, Britney Spears, and Justin Timberlake. Additionally, Brentwood-Benson Music Publishing, Bridge Building (BMI), New Spring (ASCAP), and Designer Music (SESAC) are all divisions of ZEI and operate in the Contemporary Christian business. Brentwood-Benson has co-publishing ventures with two of the top Indie labels in this genre, SRE and 7Spin as well as artist Aaron Shust. In addition to the successes of ZMPL signed authors, Zomba US had early success from the growing hip hop scene in which it had a particularly strong position. Ground breaking artists were signed including Whodini, A Tribe Called Quest, featuring the rap group Q-Tip, and a young R&B group called R. Kelly and The Public Announcement. R. Kelly has gone on to become one of the most prolific writer/producers in the last three decades.

The Zomba US catalogue includes acclaimed songwriters, composers and producers including Britney Spears, Justin Timberlake, Linkin Park and Backstreet Boys. Zomba US is also home to an old-school Rap catalogue of hits from KRS-ONE, DJ Jazzy Jeff and the Fresh Prince, Teddy Riley (who has co-written with Michael Jackson); rock and metal hits from Poison and Twisted Sister. Zomba US has recently signed new hit acts in all genres of music including Ne-Yo and T-Pain.

Zomba US has an impressive array of current authors with ongoing delivery commitments.

These authors will continue to contribute valuable songs to the Purchaser. Authors within term, with ongoing obligations include:

- Linkin Park - multi-platinum rock act whose hits include “Breaking The Habit”, which reached the UK charts in 2004, and also charted in Austria, Germany, Ireland, France and the Netherlands; “Crawling”; “One Step Closer”; “Somewhere I Belong”, which charted in 2003 in the UK, Austria, Germany, Belgium, France, Sweden, Norway, Finland and the Netherlands; “Numb” - which was released by Linkin Park as a single in 2003, and reached the charts in the UK, Germany, Belgium, Ireland, Sweden and France; and Numb/Encore, which was a “mash-up” of the original single “Numb” and another original song “Encore” by the rapper Jay-Z song – this was a Grammy award winning song, which charted in the UK, Austria, Belgium, Germany, Ireland, France, Sweden, Norway and the Netherlands. Their first album “Hybrid Theory” has sold 24 million copies since 2000 and their second album “Metora” topped the charts in both the US and the UK. Albums consistently sell four-five million units each. The band’s next album will be released on April 3.

- R. Kelly – one of the most successful R&B/Urban artists of all time. He has had 13 number 1's including "You remind me of something" and "I believe I can fly" (for which he won 3 Grammy Awards in 1998), and has sold over 50 million albums worldwide. He has written/produced number one hits for himself including "Bump N Grind" and "Ignition" which hit number 1 in the UK in 2003, and the top 10 "Down Low" and "I Wish". He has also written songs for other artists such as Michael Jackson's "You Are Not Alone" and B2K "Bump, Bump, Bump". Chart hits in the past three years include "Playa's Only" which hit the UK charts in 2005, as well as charts in Germany, Ireland and France; "So Sexy", which reached the charts in the UK in 2004, "Happy People/U Saved Me" which charted in the UK, Germany and Ireland in 2004; "Step In The Name Of Love/Thoia Thong" which reached number 14 in the UK charts in 2003; and "Snake" which peaked at number 10 in the UK charts, and also charted in Ireland.
- Justin Timberlake - former member of massively successful boy band NSYNC (which holds the record for the highest and the second highest first week album sales) Justin has had an equally successful solo career since 2002, has won 4 Grammy Awards and released 2 solo albums producing over 12 million sales worldwide. Justin has had chart hits such as "Sexyback," which reached number 1 in the UK, Germany, Ireland and Norway in 2006, as well as charting in Austria (number 5), Belgium (number 3), France (number 8), Sweden (number 4), Finland (number 3) and the Netherlands (number 5); "What Goes Around"; "My Love", which reached number 2 in the UK, and also charted in Austria, Germany, Belgium, Ireland, France, Sweden, Finland and the Netherlands; "Cry Me A

River”, which reached number 2 in the UK in 2003, and also charted in Austria, Germany, Belgium, Ireland, France, Sweden, and the Netherlands; and “Like I Like You” which charted in 2003 in the UK, Germany, Ireland, Sweden, Norway, the Netherlands and Spain. Justin’s current album *FutureSex/LoveSounds* has sold over five million copies worldwide since its release in late 2006. Justin is also a co-writer on a number of other artists’ works, including one of the biggest worldwide hits of 2003, “Where Is The Love”, recorded by the Black Eyed Peas (and in which Justin Timberlake is featured in recording the chorus), reached number 1 in the UK, Austria, Germany, Belgium, Ireland, Sweden, Norway and the Netherlands. He wrote/produced current top 30 U.S. singles for Young Jeezy (“Go Getta”) and Bow Wow (“I’m A Flirt”).

- Britney Spears - has sold over 76 million records worldwide, making her the eighth best-selling female artist in American history. She has won a Grammy award and had 7 of her singles reach number 1 in the World Charts. Britney is also the only female in music history to have her first 4 studio albums debut at number 1. Hits include “Baby One More Time”, “Oops!.. I Did It Again”, “I’m A Slave 4 U” and “Me Against The Music.” Recent chart successes in the UK include “My Prerogative” which peaked at number 3 in 2004 in the UK, and charted in Austria, Germany, Belgium, Ireland (number 1), France, Sweden, Norway (number 1), and Finland; and “Me Against the Music”, which peaked in the UK at number 2 in 2003, and which also charted in Austria, Germany, Belgium, Ireland (number 1), France, Sweden, Norway, and Finland.

- Shania Twain - pop/country superstar whose hits – most co-written by Mutt Lange whose catalogue is published by ZMPL – include the number one and top 10 hits “You’re Still The One,” “Man! I Feel Like A Woman,” “From This Moment On” and “That Don’t Impress Me Much”.
- Ne-Yo - R&B/pop artist whose top hits include “So Sick”, which reached number 5 in the UK charts in 2006, and also charted in Germany, Ireland, France and the Netherlands; and “Sexy Love”, which reached number 1 in the UK in 2006, and also charted in Austria, Germany, Belgium, Ireland, France, Norway and the Netherlands. Ne-YO is also a sought-after writer/producer for other artists including number one hits for Beyonce “Irreplaceable”, which reached number 4 in the UK charts, and also charted in Austria, Germany, Belgium, Ireland, France, Sweden and the Netherlands; Mario “Let Me Love You”, which reached number 2 in the UK in 2005, and number 1 in Germany and Sweden; Rihanna “Unfaithful”, which reached number 2 in the UK, Austria, Germany, Ireland and Norway ; as well as Whitney Houston and Enrique Iglesias. Ne-Yo’s first debut album “In my own words” reached number 1 on the Billboard 200 in 2006, in the same week as his second single from that album “So Sick” reached number 1 in the Billboard Hot 100.
- Korn - multiplatinum rock group whose hits include “Freak On A Leash” and “Falling Away From Me”. Korn have sold over 30 million records worldwide, have had two number 1 albums in the US and have won 2 Grammys. Recent hits in Europe include “Coming Undone”, which charted in the UK in 2006, Germany and Ireland; “Twisted Transistor”, which charted in 2005 in the UK, Austria, Germany and Ireland; and “Did My

Time”, which charted in 2003, in the UK, Austria, Germany, Ireland and Sweden.

- Limp Bizkit - rock/rap multiplatinum group fronted by Fred Durst, Limp Bizkit have sold over 30 million albums worldwide, two of which reached number 1 in the US. Hits include “Nookie,” “Rollin’” and “My Generation”, Recent singles chart successes also include “Eat You Alive”, which reached the UK chart in 2003, and also charted in Austria, Germany, Ireland and Sweden.
- Bowling For Soup - punky power pop group whose songs include “1985” and “Girl All The Bad Guys Want”, and UK chart hits “Almost” from 2005, and “Punk Rock 101” from 2003.
- Macy Gray - R&B/soul singer whose hits include “I Try.”, and “When I See You” (UK chart hit in 2003) and who is due to release a new album in 2007.
- Nas - rap pioneer whose most recent album *Hip Hop Is Dead* debuted at number one on the U.S chart. Hits include “I Can”, “If I Ruled The World” and “Hate Me Now”, while UK chart successes include “Bridging the Gap” (2004), “I Can”, and “Made You Look” (2003).
- 30 Seconds to Mars - platinum rock group fronted by Jared Leto. Their recent single “The Kill” spent over 50 weeks on the rock singles chart.
- Donald Lawrence - award-winning Gospel singer and writer/producer who has also crossed over into the pop world.

- Backstreet Boys - leading boy band pop group of the late 1990s whose hits include “Tearin’ Up My Heart,” “As Long As You Love Me,” “I Want It That Way” and “Incomplete.”
- Mike Shonoda is a member of bands Linkin Park and Fort Minor. Fort Minor won Ringtone of the Year for “Where’d You Go” at the MTV VMA’s in 2006 and their debut album has sold over 350,000 copies.
- Andrae Crouch - leading Gospel artist over the past three decades. Key titles include “He Is The Light,” “God Still Loves Me” and “Mercy.” Crouch has collaborated with important artists including Ce Ce Winans and Michael Omartian.
- Writer/producers include KNS (who has written for Kylie Minogue and songs in the movie *Happy Feet*), Ron ‘Neff-U’ Feemster (Ne-Yo, 50 Cent, The Game), Cool & Dre (50 Cent, The Game), Beau Dozier (Joss Stone, Avant, JoJo) and Steve Huff (Avant, Ron Isley, Joe).
- Development rock acts include Mutemath, Flyleaf, Saliva and The Crew.
 - Mudvayne Music – winners of the MTV2 Award for their single “Dig” in 2001 and their single “Happy?” was number 1 in the US Mainstream Rock Chart for one week in 2005. Mudvayne have been nominated for 3 Grammys.
 - Eamon Doyle - Eamon’s debut single “Fuck It (I don’t want you back)” reached number 1 in the UK, Australia, New Zealand, The Netherlands and Sweden, with his debut album “I Don’t Want You Back” making the Top 10 in the Billboard 200.

- Other authors still in term include Petey Pablo (who has recorded 3 albums and 9 singles, and featured on Ciara’s number 1 single “Goodies”), Lawrence Parker, Poison (have had 3 top 5 albums in the US), and Jolyon Skinner, and Andrew Gold (best known for his singles “Lonely Boy” (Top 10) and “Thank you for Being a Friend”).

The current authors listed above have generated an immense and impressive catalogue, as many have been signed to Zomba US for **[Business Secret]** or even over **[Business Secret]** years, and Zomba US holds music publishing rights for the life of copyright over the vast majority of these works.

Even on top of this catalogue from current writers, there is additionally a large back catalogue of important works by the following authors:

- Teddy Riley - a producer and artist of early hip-hop and “New Jack Swing” including Joe’s “Stutter” and Blackstreet’s “No Diggity,” which both reached number one on the pop and R&B charts. He has also written/produced songs for Mary J. Blige, Keith Sweat, Johnny Kemp, Michael Jackson and Al B. Sure. Works from 1992 to 2004 are covered in the Zomba US catalogue.
- Buddy Guy a blues legend whose 1960s classics include “Let Me Love You Baby,” “Ten Years Ago,” “Stone Crazy,” “My Time After A While,” “Leave My Girl Alone” and “No Lie.”
- Cowboy Junkies the rock band whose sound is rooted in country and blues. Hits include “Misguided Angel”.

- DJ Jazzy Jeff & The Fresh Prince, Will Smith’s rap duo with DJ Jazzy Jeff. Hits include top 5 “Summertime,” top 20 “Parents Just Don’t Understand” and “Girls Ain’t Nothing But Trouble”.
- Digital Underground the funky rap group whose hits include “The Humpty Dance”.
- Full Force with major hits for Lisa Lisa and Cult Jam including “Head To Toe,” “Lost In Emotion,” “All Cried Out” and “I Wonder If I Take You Home,” which was sampled on the 2005 Black Eyed Peas top five hit “Don’t Phunk With My Heart”.
- Forceful Music And Mokojumbi Music (Full Force). Full Force have written and produced songs for Britney Spears, James Brown, Cult Jam, Backstreet Boys and La Toya Jackson. They also produced Rihanna’s hit “Let Me” and the Black Eyes Peas hit “Don’t Phunk with my Heart”, which reached number 3 in the UK, and charted in Austria, Belgium, Germany, Ireland, France, Sweden and Norway (number 1).

The following table provides a summary of the financial information for the Zomba US catalogue over the past three years:

SUMMARY	2004	2005	2006
EEA Rev (€’000)	[5,000 - 10,000]	[5,000 - 10,000]	[5,000 - 10,000]

1 Following paragraph 4 of these Commitments, the Divestment Businesses include, but are not limited to:

(a) the following main intangible assets:

The main assets are the music publishing rights of varying duration. The following table shows the top 100 copyrights in the Zomba US catalogue for 2006.

	Title	Composers	Revenue (EUR)
1	STORCH/TIMBERLAKE/MOSLEY	CRY ME A RIVER	[Business Secret]
2	DOYLE/PASSY/ROBINSON	I DONT WANT YOU BACK	[Business Secret]
3	KELLY	HAPPY PEOPLE	[Business Secret]
4	STORCH/SMITH/HOUFF	LET ME LOVE YOU	[Business Secret]
5	KELLY	IGNITION	[Business Secret]
6	KELLY	BUMP 'N' GRIND	[Business Secret]
7	WEAVER JR./PROCTOR/LAYTON	COME IN HARD	[Business Secret]
8	HUGO/WILLIAMS/TIMBERLAKE	ROCK YOUR BODY	[Business Secret]
9	ZEKKARIYAS/ZEKKARIYAS	TEARDROPS	[Business Secret]
10	FARRELL/BOURDON/SHINODA/DELSON/BEN	NUMB	[Business Secret]
11	KELLY	I BELIEVE I CAN FLY	[Business Secret]
12	TAYLOR/MUHAMMAD/YANCEY/FAREED/FINDLAY/CA	IF EVERYBODY LOOKED THE SAME	[Business Secret]
13	STONE/DOZIER/DOZIER	SPOILED	[Business Secret]
14	TYSON/WARD	BLACK VELVET	[Business Secret]
15	MAY/TIMOTHY/WILLIAMS/JAMES	STRINGS OF LIFE (STRONGER ON MY OWN)	[Business Secret]
16	HUGO/WILLIAMS/TIMBERLAKE	LIKE I LOVE YOU	[Business Secret]
17	TIMBERLAKE/PINEDA/GOMEZ/FRATANTUNO/ADAMS	WHERE IS THE LOVE?	[Business Secret]
18	KELLY	TRAPPED IN THE CLOSET (CHAPTER 1 OF 5)	[Business Secret]
19	MAY/JAMES	STRINGS OF LIFE	[Business Secret]
20	KELLY	OUTRAGEOUS	[Business Secret]
21	BRATHWAITE/EASTMOND/LANGE/OCEAN	WHEN THE GOING GETS TOUGH, THE TOUGH GET GOING	[Business Secret]
22	KELLY	YOU ARE NOT ALONE	[Business Secret]
23	BOURDON/SHINODA/DELSON/BENNINGTON/HAHN	ENTH E ND	[Business Secret]
24	HANKERSON/KELLY	SHE'S GOT THAT VIBE	[Business Secret]
25	GRIFFIN/RILEY/BROWN	MY PREROGATIVE	[Business Secret]
26	ADEYEMO/ALEXANDER/PHILLIPS	OBJECT OF MY DESIRE	[Business Secret]
27	BOURDON/SHINODA/DELSON/HAHN/BENNINGTON	ONE STEP CLOSER	[Business Secret]
28	FEEMSTER/ARGSHEBEN	HERE I GO AGAIN	[Business Secret]
29	BORLAND/DEAN/DIMANT/DURST/OTTO/RIVERS	ROLLIN' (AIR RAID VEHICLE)	[Business Secret]
30	GOLD	NEVER LET HER SLIP AWAY	[Business Secret]
31	BAKER/JACKSON/FELDER/LYON/VALENZANO/TAY	HATE IT OR LOVE IT	[Business Secret]
32	GOLD	LONELY BOY	[Business Secret]
33	HUGO/WILLIAMS/TIMBERLAKE	SENorITA	[Business Secret]
34	FARRELL/BOURDON/SHINODA/DELSON/BENNINGT	BREAKING THE HABIT	[Business Secret]
35	BOURDON/SHINODA/DELSON/HAHN/BENNINGTON	POINTS OF AUTHORITY	[Business Secret]
36	DALL/MICHAELS/JOHANNESON/ROCKETT	EVERY ROSE HAS ITS THORN	[Business Secret]
37	DUDLEY/FLINT/HORN/HOWLETT/JECZALIK/DEAL/	FIRESTARTER	[Business Secret]
38	GEORGE/BEDEAU/CHARLES/CLARKE/GEORGE/GEOR	MOVE YA BODY	[Business Secret]
39	FROMM/LINZER/FranZEL	I DON'T WANNA SPEND ONE MORE CHRISTMAS WITHOUT YOU	[Business Secret]
40	DAVIS/SHAFFER/SILVERIA/ARVIZU/WELCH	DID MY TIME	[Business Secret]
41	BOURDON/SHINODA/DELSON/HAHN/BENNINGTON	PAPERCUT	[Business Secret]
42	FARRELL/BOURDON/SHINODA/DELSON/BENNINGT	LYING FROM YOU	[Business Secret]
43	KIERULE/SCHWARTZ	MY ONLY WISH (THIS YEAR)	[Business Secret]
44	GUPPY/RILEY/BROWN/REYES/BELLE	TWO CAN PLAY THAT GAME	[Business Secret]
45	OCEAN/ALEXANDER	EUROPEAN QUEEN	[Business Secret]
46	DAVIS/ARVIZU/WELCH/SHAFFER/SILVERIA	FALLING AWAY FROM ME	[Business Secret]
47	KELLY	TRAPPED IN THE CLOSET (PART 1)	[Business Secret]
48	FARRELL/BOURDON/SHINODA/DELSON/BENNINGT	FAINT	[Business Secret]
49	FARRELL/BOURDON/SHINODA/DELSON/BENNINGT	SOMEWHERE I BELONG	[Business Secret]
50	HUTCHINS/SMITH/CARDENAS SR.	SUMMERTIME	[Business Secret]
51	RENN/WRIGHT/SMITH	CHRISTMAS TIME	[Business Secret]
52	HUGO/WILLIAMS/TIMBERLAKE	GIRLFRIEND	[Business Secret]
53	KELLY	ONE MORE CHANCE	[Business Secret]
54	KELLY	YOUR BODY'S CALLIN'	[Business Secret]
55	BOLTON/GOLDMARK	SOUL PROVIDER	[Business Secret]
56	GEORGE/BEDEAU/CHARLES/CLARKE/GEORGE/GEOR	ALL I HAVE TO GIVE	[Business Secret]
57	FEEMSTER/UNKNOWN WRITER	COULDN'T SAY NO	[Business Secret]
58	DACHTLER	SHATTERED DREAMS	[Business Secret]
59	SMITH/FEEMSTER	SIGN ME UP	[Business Secret]
60	SMITH/JEFFERSON/BARRETT III	FREEK-A-LEEK	[Business Secret]
61	KELLY	NEXT TO YOU	[Business Secret]
62	WRITER UNKNOWN/FEEMSTER	HERE I GO	[Business Secret]
63	GOLD/GOULDMAN	BRIDGE TO YOUR HEART	[Business Secret]
64	HAMILTON/DIXON	STUTTER	[Business Secret]
65	BOURDON/SHINODA/DELSON/HAHN/BENNINGTON	CRAWLING	[Business Secret]
66	MCPHERSON/RUSSELL/HUGHES/MARTINEZ	MAKE IT UP WITH LOVE	[Business Secret]
67	MITCHELL/KELLY	SO SEXY	[Business Secret]
68	KELLY	IF I COULD TURN BACK THE HANDS OF TIME	[Business Secret]
69	GREGGS/RALPH/CHASEZ	SOME GIRLS (DANCE WITH WOMEN)	[Business Secret]
70	SERMON/SMITH	RIGHT NOW	[Business Secret]
71	KELLY	U SAVED ME	[Business Secret]
72	DAVIS/SHAFFER/SILVERIA/ARVIZU/WELCH	Y'ALL WANT A SINGLE	[Business Secret]
73	KELLY/MORGAN	SNAKE	[Business Secret]
74	HANNIBAL/RILEY/STEWART/VICK/WALTERS/WIT	NO DIGGITY	[Business Secret]
75	BENNINGTON/BOURDON/DELSON/FARRELL/HAHN/S	FROM THE INSIDE	[Business Secret]
76	KELLY/SMITH	BUMP, BUMP, BUMP	[Business Secret]
77	BOUCHET/DAVIS/BLACKMON	THINGS AIN'T THE SAME	[Business Secret]
78	KELLY/STORCH/TAYLOR	PLAYA'S ONLY	[Business Secret]
79	O'BRIEN/STEWART/NKHEREANYE/SPEARS/NASH/	ME AGAINST THE MUSIC	[Business Secret]
80	KELLY	THE TRUTH	[Business Secret]
81	DACHTLER	TURN BACK THE CLOCK	[Business Secret]
82	SMITH/TOWNES	FRESH PRINCE OF BEL AIR, THE	[Business Secret]
83	KELLY	MAKE YOU MY BABY	[Business Secret]
84	KELLY	STEP IN THE NAME OF LOVE	[Business Secret]
85	KELLY	I'M YOUR ANGEL	[Business Secret]
86	MYERS/BAKER/WILLIAMS	EVERY DAY I LOVE YOU	[Business Secret]
87	DAVIS/ARVIZU/WELCH/SHAFFER/SILVERIA	HERE TO STAY	[Business Secret]
88	WHITE	FROM THE BOTTOM OF MY BROKEN HEART	[Business Secret]
89	JONES/REMI/HAMMOND	I CAN	[Business Secret]

90	RILEY/JACKSON	IN THE CLOSET	[Business Secret]
91	KAYE/MONTENEGRO/SMITH/TOWNES	GIRLS AIN'T NOTHIN' BUT TROUBLE	[Business Secret]
92	KELLY	SEX IN THE KITCHEN	[Business Secret]
93	KELLY	THE WORLD'S GREATEST	[Business Secret]
94	DIAMOND/CARLSSON/DOROUGH	WHAT MAKES YOU DIFFERENT (MAKES YOU BEAUTIFUL)	[Business Secret]
95	WEAVER JR./SIMONS/ROWLANDS	BLOCK ROCKIN' BEATS	[Business Secret]
96	DEAL	CANNONBALL	[Business Secret]
97	WILLIAMS/BRITO	ALL OVER LOVE	[Business Secret]
98	MASCIS	FREAK SCENE	[Business Secret]
99	OCEAN/ALEXANDER	SUDDENLY	[Business Secret]
100	BURKS/FARRELL/BOURDON/SHINODA/DELSON/BE	JIGGA WHAT / FAINT	[Business Secret]

(b) the following main contracts, agreements, leases, commitments and understandings:

The following table shows the top 10 EEA revenue earning writers of Zomba US, together with EEA revenues in 2006.

Name	Total EEA Revenues in 2006 (EUR)
LINKIN PARK	[Business Secret]
KELLY, ROBERT (PUBLISHING)	[Business Secret]
JUSTIN TIMBERLAKE (TENNMANN TUNES)	[Business Secret]
SPEARS, BRITNEY DBA BRITNEY SPEARS MUSIC	[Business Secret]
LIMP BIZKIT DBA BIG BIZKIT MUSIC	[Business Secret]
DOYLE, EAMON DBA E CONTROVERSY	[Business Secret]
KORN	[Business Secret]
RILEY, TEDDY	[Business Secret]
FORCEFUL MUSIC AND MOKOJUMBI MUSIC	[Business Secret]
FEEMSTER, THERON PKA RON FEEMSTER	[Business Secret]

The Compositions shall be licensed on the following terms:

- (i) the territory of the Licence will be the EEA (the "Territory");
- (ii) the term of the Licence will be for the entire period of the rights Zomba US has for the Compositions in the Territory;
- (iii) the financial and other terms will be those negotiated at arm's length with the purchaser of ZMPL or Newco, as the case may be. However, Compositions existing at the Effective Date shall be licensed on a royalty-free basis (although the financial benefit to the purchaser of ZMPL (or, Newco, as the case may be) shall be reflected in the purchase price), subject to the purchaser being responsible to Zomba US for all royalty payments due to writers in respect of the Compositions. All Compositions due to be delivered in the future under existing agreements with Zomba US and those to be delivered following the exercise of any options provided for under those existing agreements shall be the subject of a separate royalty payment from the purchaser of ZMPL (or Newco, as the case may be) to Zomba US, to be agreed on arm's length commercial terms, which shall include royalty payments due to writers in respect of those compositions; and
- (iv) there will be no restrictions on exploitation of the Compositions by the Purchaser except for those contained in Zomba US' song-writer, administration and sub-publishing agreements with its writers and licensors.

- (c) It is not anticipated that it would be necessary for arrangements to be put in place for the supply of any necessary services for a transitional period, but UMG or affiliated undertakings would be prepared to agree to supply any such services on arm's length terms, if required by the Commission at the request of the Purchaser, for a reasonable transitional period.
- 3 The Divestment Businesses shall not include the Zomba name. The Zomba name is owned by the SONY BMG record company which uses it in connection with its Zomba record label. The trade name is currently licensed to BMG MP under transitional arrangements, put in place at the time of the creation of the SONY BMG joint venture in 2004 (and which are due to expire in **[Business Secret]**).
- 4 The Divestment Businesses shall not include ZEI's production music business.

SCHEDULE 4 – 19 Music Limited

Summary

19 Music Limited (“19 Music”) is a separate legal entity within BMG Music Publishing. In 2005, 19 Music’s total EEA revenues were **€(< 1 million]** and global revenues were **€(< 1 million]**.

The 19 Music catalogue is one of the most important UK-based pop catalogues in the last ten years. It comprises chart hits which continue to generate high revenues, such as songs from: Culture Club (including “Karma Chameleon”), Spice Girls (“Who do you think you are?”), B*Witched, S Club 7, Emma Bunton (Baby Spice) and Geri Halliwell (Ginger Spice). It also includes repertoire for reality television programmes, e.g. the Pop Idol repertoire.

The 19 Music and 19 Songs (see Schedule 5 below) catalogues include repertoire from the Spice Girls which charted as number 1 in many countries in Europe as well as from other authors which have featured in charts in both UK and continental European countries for a number of weeks, such as S Club 7, B*Witched, Boyzone and successful acts arising from reality TV shows around the EEA. Specific chart hits include:

- Spice Girls – Spiceworld - chart position # 1, sold over 10 million worldwide
- Stop (Absolute 50%) - chart position #2
- Too Much (Absolute 50%) – chart position #1
- Spice Girls – Spice - chart position # 1, sold 3 million worldwide
- Who Do You Think You Are (Absolute 50%) - chart position #1
- Boyzone – Said and Done - chart position UK #1, 900K worldwide
- Key To My Life (Ray Hedges 25%) - chart position #3
- Coming Home Now (Ray Hedges 25%) - chart position #4
- Boyzone – A Different Beat - chart position UK #1, 900K worldwide
- A Different Beat (Ray Hedges 20%) - chart position #1
- Isn't It A Wonder (Ray Hedges 33.33%) – chart position #2
- Will Young – From Now On – chart position UK # 1, sold 600K UK
- You And I (Johnsons 50%/ Peden 50%) – chart position #2
- S Club 7 – 7 - chart position UK # 1, sold 900K UK
- Never Had A Dream Come True (Simon Ellis 50%) – Chart Position # 1

- S Club 7 – S Club - chart position UK # 2, sold 600K UK
- Bring It All Back (Steelworks 53.32%) – chart position # 1
- Two In A Million (Simon Ellis 50%) – chart position # 2
- S Club 7 – Sunshine - chart position UK # 3, sold 600K UK
- You (Steelworks 50%) – chart position # 2
- Don't Stop Movin (Simon Ellis 50%)' – chart position # 1
- S Club 7 – Seeing Double - chart position UK # 17, sold 600K UK
- Love Ain't Gonna Wait For You (Simon Ellis 50%) – chart position # 2
- Alive (Simon Ellis 50%) – chart position # 5
- S Club Juniors – Together – chart position UK # 5, sold 600K UK
- Automatic High (Jewels & Stone 25%) - chart position #2
- B*Witched – B*Witched – chart position UK #3 / US #12, 600K UK
- C'est La Vie (Ray Hedges 27%) – chart position #1 / US #9
- Rollercoaster (Ray Hedges 28.33%) – chart position #1
- To You I Belong (Ray Hedges 33.33%) - chart position #1
- Blame It On The Weatherman (Ray Hedges 25%) – chart position #1
- B*Witched – Awake and Breathe – chart position #5, 300K UK
- Jesse Hold On (Ray Hedges 25%) – chart position# 4
- Billie Piper – Walk of Life - chart position # 14, sold 60K worldwide
- Day And Night (Steelworks 40%) - chart position #1

The following table provides a summary of the financial information over the past three years:

SUMMARY	2004	2005	2006
EEA Rev (€'000)	[< 1,000]	[< 1,000]	[< 1,000]
Global Revenue (€ '000) ¹⁵³	[< 1,000]	[< 1,000]	[< 1,000]

1 Following paragraph 4 of these Commitments, the Divestment Businesses include, but are not limited to:

(a) the following main intangible assets:

¹⁵³ See paragraph 4(a) of these Commitments.

The main assets are the music publishing rights of varying duration.
The following table shows the top 100 copyrights in 19 Music for 2006.

	Title	Composers	Revenue (EUR)
1	KARMA CHAMELEON	PICKETT/CULTURE CLUB	[Business Secret]
2	DON'T STOP MOVING	LEE/SPEARRITT/MCINTOSH/CATTERMOLE/O'MEAR	[Business Secret]
3	WHO DO YOU THINK YOU ARE	WILSON/WATKINS/SPICE	[Business Secret]
4	ONE STEP CLOSER	PERCY/LEVER/DENNIS	[Business Secret]
5	HANG UP	WILSON/WATKINS/ACKERMAN	[Business Secret]
6	AIN'T SUCH A BAD PLACE TO BE	MACKICHAN/POOLE	[Business Secret]
7	A PICTURE OF YOU	WILSON/WATKINS/KENNEDY/KEATING	[Business Secret]
8	STOP	WILSON/WATKINS/SPICE	[Business Secret]
9	NAKED	WILSON/WATKINS/SPICE	[Business Secret]
10	NEVER HAD A DREAM COME TRUE	ELLIS/DENNIS	[Business Secret]
11	SOMETHING KINDA FUNNY	WILSON/WATKINS/SPICE	[Business Secret]
12	LAST TIME LOVER	WILSON/WATKINS/SPICE	[Business Secret]
13	BREATHE	BALL/MINOUE/VAUK	[Business Secret]
14	STONED IN LOVE	BUTLER/HEDGES/PICKERING/BRACEGIRDLE	[Business Secret]
15	TOO MUCH	WILSON/WATKINS/SPICE	[Business Secret]
16	CHICCO LATINO	WILSON/WATKINS/HALLIWELL	[Business Secret]
17	BRING IT ALL BACK	PERCY/LEVER/KENNEDY/S CLUB 7	[Business Secret]
18	DON'T GIVE UP	HEDGES/BRACEGIRDLE/ADAMS	[Business Secret]
19	THE LADY IS A VAMP	WILSON/WATKINS/SPICE	[Business Secret]
20	LOOK AT ME	WILSON/WATKINS/HALLIWELL	[Business Secret]
21	DO IT	WILSON/WATKINS/SPICE	[Business Secret]
22	DENYING	WILSON/WATKINS/SPICE	[Business Secret]
23	EVERYBODY WANTS YOU	WILSON/WATKINS/ACKERMAN	[Business Secret]
24	LOVE AIN'T GONNA WAIT FOR YOU	ELLIS/SOLOMON	[Business Secret]
25	SALSOUL NUGGET (IF U WANNA)	SIDOLI/MORRISON/SIGLER/HARRIS/TYSON/FELD	[Business Secret]
26	LIFT ME UP	WILSON/WATKINS/HALLIWELL/ACKERMAN	[Business Secret]
27	SALT WATER	HEDGES/BRENNAN/BRACEGIRDLE/BRENNAN	[Business Secret]
28	PERFECT CHRISTMAS	ELLIS/DENNIS	[Business Secret]
29	DON'T MISTAKE ME	WILSON/WATKINS/ACKERMAN	[Business Secret]
30	BRING THE HOUSE DOWN	WILSON/WATKINS/ACKERMAN	[Business Secret]
31	ALIVE AGAIN	HEDGES/BRACEGIRDLE/ACKERMAN	[Business Secret]
32	IT'S ALRIGHT	PERCY/LEVER/KENNEDY/WOODCOCK	[Business Secret]
33	C'EST LA VIE	HEDGES/BRANNIGAN/ACKERMAN/B*WITCHED	[Business Secret]
34	GOOD THING	HEDGES/BUTLER/MARSH/FOSTER,SULLIVAN/SHA	[Business Secret]
35	DON'T GO BELIEVING	HEDGES/BUTLER/MARSH/FOSTER,SULLIVAN/SHA	[Business Secret]
36	CROSS MY HEART	WILSON/WATKINS/ACKERMAN	[Business Secret]
37	BACK FOR MORE	ELLIS/SHEYNE	[Business Secret]
38	IT'S A MIRACLE	PICKETT/CULTURE CLUB	[Business Secret]
39	BLAME IT ON THE WEATHERMAN	HEDGES/BRANNIGAN/ACKERMAN/CAINE	[Business Secret]
40	EAST SIDE STORY	HEDGES/BRACEGIRDLE/ADAMS/PETERS	[Business Secret]
41	ALIVE	ELLIS/SOLOMON	[Business Secret]
42	WHEN THE LIGHTS GO OUT	PERCY/LEVER/KENNEDY/MCLAUGHLIN/FIVE	[Business Secret]
43	BEDTIME STORY	HOOPER/DE VRIES/BJORK	[Business Secret]
44	NO ORDINARY MORNING	HEDGES/BRACEGIRDLE	[Business Secret]
45	YOU	LEVER/PERCY/KENNEDY/WOODCOCK	[Business Secret]
46	BEST OF MY LOVE	ELLIS/ROBBINS	[Business Secret]
47	BAG IT UP	WILSON/WATKINS/HALLIWELL	[Business Secret]
48	ALL THE WOMAN	WILSON/WATKINS/ACKERMAN	[Business Secret]
49	ISOBEL	HOOPER/DE VRIES/BJORK/SIGURDSSON	[Business Secret]
50	CHECKIN' IT OUT	BUTLER/HEDGES/OSBORNE/HARDMAN	[Business Secret]
51	2 IN A MILLION	ELLIS/DENNIS	[Business Secret]
52	PRETTY PIECE OF FLESH	DE VRIES/HOOPER/WARFIELD	[Business Secret]
53	WITHOUT YOU	WILSON/WATKINS/MAY	[Business Secret]
54	AUTUMN TACTICS	HEDGES/BRACEGIRDLE	[Business Secret]
55	IMPOSSIBLE	WILSON/WATKINS/ACKERMAN	[Business Secret]
56	MOVE AWAY	PICKETT/CULTURE CLUB	[Business Secret]
57	UNSPEAKABLE	ELLIS/LEWIS/DIOGUARDI	[Business Secret]
58	LAST ONE STANDING	LEVER/PERCY/KENNEDY/MERRILL/GIRLTHING	[Business Secret]
59	SPICE INVADERS	WILSON/WATKINS/SPICE	[Business Secret]
60	MISS YOU	DENNIS/KENNEDY/LINCOLN	[Business Secret]
61	FEEL THE FEAR	WILSON/WATKINS/HALLIWELL	[Business Secret]
62	STRONGER	ELLIS/MOLLOY/S CLUB 7	[Business Secret]
63	TOGETHER	HEDGES/BRANNIGAN/KEATING	[Business Secret]
64	TAKE ME HOME	WILSON/WATKINS/SPICE	[Business Secret]
65	LOVE IS GONNA GET YA	WOODCOCK/LEVER/PERCY/KENNEDY	[Business Secret]
66	SO GOOD	GRAHAM/HEDGES/BRANNIGAN/KEATING/GATELY/L	[Business Secret]
67	COMING HOME NOW	GRAHAM/HEDGES/BRANNIGAN/KEATING/GATELY/L	[Business Secret]
68	LIMBO	BALL/MINOUE/VAUK	[Business Secret]
69	BEEP BEEP	WINSTANLEY	[Business Secret]
70	WE'RE REALLY SAYING SOMETHING	HEDGES/BUTLER/TUCKER/LYNCH/WHITFIELD/STE	[Business Secret]
71	ONE OF THESE GIRLS	WILSON/WATKINS/SPICE	[Business Secret]
72	SABRINA (SHE'LL B*WITCH YA)	HEDGES/B*WITCHED/BRANNIGAN	[Business Secret]
73	DAY AND NIGHT	LEVER/PERCY/CAWLEY/KENNEDY/PIPER	[Business Secret]
74	SPEECHLESS	ELLIS/SOLOMON	[Business Secret]
75	ALL AROUND THE WORLD	PERCY/LEVER/OOSTERHUIS	[Business Secret]
76	ISN'T IT A WONDER	HEDGES/KEATING/BRANNIGAN	[Business Secret]
77	ROLLERCOASTER	HEDGES/BRANNIGAN/ACKERMAN/B*WITCHED	[Business Secret]
78	DON'T CALL ME BABY	WILSON/WATKINS/HALLIWELL	[Business Secret]
79	ALL IN LOVE IS FAIR	ELLIS/DENNIS	[Business Secret]
80	IT DON'T GET ANY BETTER	WILSON/WATKINS/HALLIWELL/ACKERMAN	[Business Secret]
81	TELL HER	HEDGES/BUTLER/HECTOR	[Business Secret]
82	POSSIBLY MAYBE	HOOPER/DE VRIES/GUDMUNSDOTTIR	[Business Secret]
83	TREAT ME LIKE A LADY	HEDGES/BUTLER/WHATMORE	[Business Secret]
84	JESSE HOLD ON	HEDGES/BRANNIGAN/B*WITCHED/HODGENS	[Business Secret]
85	A BETTER MAN	LIND/PICKETT/KENNEDY	[Business Secret]
86	KEY TO MY LIFE	HEDGES/BRANNIGAN/KEATING/GATELY/GRAHAM	[Business Secret]
87	GET THE MUSIC ON	HEDGES/BUTLER/PICKERING	[Business Secret]

88	THE STORY SO FAR	WILSON/WATKINS/ACKERMAN	[Business Secret]
89	BUMPER TO BUMPER	DENNIS/WILSON/WATKINS/SPICE	[Business Secret]
90	ARE YOU A GHOST?	HEDGES/BRANNIGAN/B*WITCHED	[Business Secret]
91	TAKE CONTROL	SIDOLI/MORRISON/DOUGLAS/FOWLER/RAMSAY	[Business Secret]
92	I COME ALIVE	WILSON/WATKINS/ACKERMAN	[Business Secret]
93	WE AIN'T GOIN' DOWN	BUTLER/HEDGES/ACKERMAN/BELLA	[Business Secret]
94	NO SIGN OF LIFE	ELLIS/LEE/BUNTON	[Business Secret]
95	WHEREVER YOU ARE	ELLIS/DENNIS	[Business Secret]
96	DANCE	ELLIS/SOLOMON	[Business Secret]
97	WHO THE HELL ARE YOU	HEDGES/BUTLER/BUNTON	[Business Secret]
98	THE DAY BEFORE THE RAIN	WILSON/WATKINS/ACKERMAN	[Business Secret]
99	WHEN THE EVENING COMES	ELLIS/LEE/CHEEKS	[Business Secret]
100	POWERPLAY	PICKETT/ROBERTSON	[Business Secret]

(b) the following main contracts, agreements, leases, commitments and understanding:

The following table shows the top EEA revenue earning writers of 19 Music in 2006.

Name	Total EEA Revenues in 2006, EUR
ABSOLUTE (Paul Wilson/Andy Watkins)	[Business Secret]
Ray Hedges	[Business Secret]
Simon Ellis	[Business Secret]
Phil Pickett	[Business Secret]
Tim Lever	[Business Secret]
Mike Percy	[Business Secret]
M & S PRODUCTIONS (SIDOLI/MORRISON)	[Business Secret]
Ingo Vauk	[Business Secret]
Marius De Vries	[Business Secret]

(c) It is not anticipated that it would be necessary for arrangements to be put in place for the supply of any necessary services for a transitional period on arm's length terms, but UMG or affiliated undertakings would be prepared to agree to supply any such services, if required by the Commission at the request of the Purchaser, for a reasonable transitional period.

SCHEDULE 5 – 19 Songs Limited

Summary

19 Songs Limited (“19 Songs”) is joint venture in which BMG Music Publishing holds 50% shares, the remaining 50% being held by Simon Fuller (a record and television producer). In 2005, 19 Songs’ total EEA revenues were €[< 1 million] and global revenues were €[< 1 million].

The 19 Songs catalogue consists of pop music linked to television reality shows. Indeed, the catalogue’s song generating the largest revenues of 19 Songs is the American Idol theme. It also includes other pop repertoire, for instance from: Emma Bunton, S Club 7 and Lisa Scott Lee (Steps).

The following table provides a summary of the financial information over the past three years:

SUMMARY	2004	2005	2006
EEA Rev (€’000)	[< 1,000]	[< 1,000]	[< 1,000]
Global Revenue (€’000)	[< 1,000]	[< 1,000]	[< 1,000]

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1 Following paragraph 4 of these Commitments, the Divestment Businesses include, but are not limited to:

(a) the following main intangible assets:

The main assets are the music publishing rights of varying duration.

The following table shows the top 100 copyrights in 19 Songs for 2006.

	Title	Composers	Revenue (EUR)
1	AMERICAN IDOL THEME	GINGELL/STONE/DENNIS	[Business Secret]
2	I SAID NEVER AGAIN (BUT HERE WE ARE)	GINGELL/STONE/DAVIS	[Business Secret]
3	IDOL (POP IDOL THEME)	GINGELL/STONE/DENNIS	[Business Secret]
4	HOME	LEWINSON/LEWINSON/HUCKNALL	[Business Secret]
5	YOU AND I	PEDEN/JOHNSON/JOHNSON	[Business Secret]
6	SLEEP	PEDEN/BUNTON/GORDINO/KEARNS	[Business Secret]
7	AUTOMATIC HIGH	GINGELL/STONE/MADHOO/RONALD	[Business Secret]
8	HOME LOAN BLUES	YASHIKI/JAIMES/KIRKHAM/SUZUKI/LEWINSON/H	[Business Secret]
9	COME AND FLY WITH ME	DAGGER/BURROWS	[Business Secret]
10	JUMPIN	PEDEN/RUSSELL/SILVAS	[Business Secret]
11	SUMMER ALL OVER AGAIN	LEWINSON/LEWINSON/MOMRELLE	[Business Secret]
12	NEW DIRECTION	DENNIS/WHITE/HANLEY	[Business Secret]
13	MISFIT	STUDT/ERIKSEN/POOLE	[Business Secret]
14	ALL CRIED OUT	PEDEN/ROBBINS/GATES/HUMAN LEAGUE	[Business Secret]
15	I’LL BE THERE	PEDEN/BUNTON/MUDDIMAN	[Business Secret]
16	POP IDOL (CUES)	GINGELL/STONE/DENNIS	[Business Secret]
17	FAKE	LEWINSON/HUCKNALL	[Business Secret]
18	JUST A LITTLE GIRL	STUDT/BONDY	[Business Secret]
19	WORLD STANDS STILL	LEWINSON/LEWINSON/LOVE	[Business Secret]

154 See paragraph 4(a) of these Commitments.

20	DOESN'T REALLY MATTER	STUDT/LEWINSON/LEWINSON	[Business Secret]
21	KICK ME	STUDT/BONDY	[Business Secret]
22	FINELINE	PEDEN/JOHNSON/JOHNSON	[Business Secret]
23	FAKE	LEWINSON/HUCKNELL/JAIMES	[Business Secret]
24	J'AI ENVIE DE SAVOIR	ARENA/BLACKWELL/BOCHENKO/GUARDIANI	[Business Secret]
25	EVERY LITTLE THING	GINGELL/STONE/DAVIS	[Business Secret]
26	SPEAK UP	JAMES/MARSTON	[Business Secret]
27	STRONGER	ELLIS/MOLLOY/S CLUB 7	[Business Secret]
28	RUNNING OUT	JAMES/MARSTON	[Business Secret]
29	LOVE YOU LIKE I DO	WHATMORE/KORPI/BLACKCELL/SILVAS	[Business Secret]
30	DANCE DANCE DANCE	GINGELL/STONE/DENNIS	[Business Secret]
31	FOOL NO MORE	CURNOW/WOODFORD/DENNIS/HANLEY	[Business Secret]
32	I CAN'T SLEEP AT NIGHT	GINGELL/STONE/DAVIS/MINOGUE	[Business Secret]
33	CAN'T LOSE WITH YOU	JOHNSON/MARSTON/REEVE	[Business Secret]
34	I GOTTA BE ME	MARSTON/DUNK/SERLIN	[Business Secret]
35	FREE ME	PEDEN/BUNTON/MUDDIMAN	[Business Secret]
36	SOONER OR LATER	PERCY/LEVER/KENNEDY/WOODCOCK/GIRLTHING	[Business Secret]
37	CRAZY SURF DUDE	PERCY	[Business Secret]
38	UNDER THE THUMB	STUDT/ERIKSEN/POOLE	[Business Secret]
39	GOING OUT OF MY MIND /HEY YOU	STUDT/LEWINSON/LEWINSON	[Business Secret]
40	EVERY LITTLE THING	GINGELL/STONE/DAVIS	[Business Secret]
41	SOMETHING SO BEAUTIFUL	LEWINSON/LEWINSON/BUNTON	[Business Secret]
42	MEMORY LANE	BROWN/WELLS/DUNK	[Business Secret]
43	TREAT ME LIKE A LADY	HEDGES/BUTLER/WHATMORE	[Business Secret]
44	HARLEM ONE STOP	DAGGER/BURROWS/RICHIE/ELLIS/ROWE	[Business Secret]
45	DISCOTEK	GINGELL/STONE/BARRETT	[Business Secret]
46	MY TIME	MARSTON/JAMES	[Business Secret]
47	NEW DIRECTION (MAGIC FLY MIX)	DENNIS/WHITE/HANLEY/MAROUANI	[Business Secret]
48	SINGING MY SONG	MARSTON/WALTMANN	[Business Secret]
49	DIG IT (INSTRUMENTAL)	DAGGER/BURROWS	[Business Secret]
50	(I'VE GOT NO) SELF CONTROL	GINGELL/STONE/DAVIS	[Business Secret]
51	GONNA BE FINE	STUDT/LEWINSON/LEWINSON	[Business Secret]
52	SENTIMENTAL	PEDEN/JOHNSON/JOHNSON/GATES/KEARNS	[Business Secret]
53	SINGLES NIGHT	GREGGS/O'DONOGHUE/SHEEHAN/BROWN/GAYLE	[Business Secret]
54	CLUB HOP	PEDEN/SHARPE/GATES/RUSSELL	[Business Secret]
55	PUT YOUR FAITH IN ME	STUDT/BONDY	[Business Secret]
56	DON'T YOU WANT MY NUMBER	DAGGER/BURROWS/SCOTT LEE	[Business Secret]
57	LET'S WORK	PEDEN/SILVAS/RUSSELL	[Business Secret]
58	SECONDS AWAY	STUDT/DENNIS	[Business Secret]
59	CREO EN MI	CARLSSON/LEWINSON/LEWINSON/NOVA/GARCIA	[Business Secret]
60	HEY (SO WHAT)	GINGELL/STONE/HANNAH	[Business Secret]
61	LONG FOR THE DAY	JAMES/MARSTON	[Business Secret]
62	SHOULD I	BROWN/RICH	[Business Secret]
63	IT AIN'T OBVIOUS	PEDEN/SILVERMAN/PARKER	[Business Secret]
64	THAT'S WHEN YOU KNOW	PEDEN/NEW/GORDINO	[Business Secret]
65	SUPERIOR MIND	STUDT/ERIKSEN	[Business Secret]
66	BEAUTIFUL LIE	STUDT/ERIKSEN/HANSSON	[Business Secret]

(b) the following main contracts, agreements, leases, commitments and understandings:

The following table shows the top 10 EEA revenue earning writers of 19 Songs in 2006.

Top 10 Writers	Total EEA revenue in 2006(EUR)
Barry Stone	[Business Secret]
Julian Gingell	[Business Secret]
Steve and Pete Lewinson	[Business Secret]
Mike Peden	[Business Secret]
Amy Studt	[Business Secret]
Edward and Henry Johnson	[Business Secret]
Lee Dagger	[Business Secret]
Marc Jackson Burrows	[Business Secret]
Matthew Marston	[Business Secret]
Gary White	[Business Secret]

(c) It is not anticipated that it would be necessary for arrangements to be put in place for the supply of any necessary services for a transitional period on arm's length terms, but UMG or affiliated

undertakings would be prepared to agree to supply any such services, if required by the Commission at the request of the Purchaser, for a reasonable transitional period.

SCHEDULE 6 – BMG MP’s BBC music publishing catalogue

Summary

The BBC music publishing catalogue consists of music publishing copyrights acquired from BBC Worldwide Limited in 2005. Assignment of these rights is subject to consent of BBC Worldwide Limited.

In addition, the BBC’s contracts with the writers of these works are likely to require author consent to assignment. Following the acquisition of the BBC catalogue by BMG MP, the BBC procured that writers entered into direct novations with BMG MP or the BBC continued to hold the catalogue as trustee for BMG MP acting under BMG MP’s direction, so that following the acquisition, the full benefit of all contractual rights vested in BMG MP. Similar arrangements could be put in place with the Purchaser. In 2005, total revenues originated by the BBC music publishing catalogue (virtually all in the EEA) were **€[1 - 5 million]**.

The BBC music publishing catalogue consists mainly of copyrights in television themes, broadcast in the UK and globally (which in some cases have obtained commercial success in the charts, e.g. Bob the Builder’s “Can we fix it?” and Teletubbies’ “Say eh-oh!”).

The following table provides a summary of the financial information over the past three years:

SUMMARY	2004	2005	2006
EEA Rev (€‘000)	[1,000 - 5,000]	[1,000 - 5,000]	[1,000 - 5,000]
Global Revenue (€‘000)	[1,000 - 5,000]	[1,000 - 5,000]	[1,000 - 5,000]

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1 Following paragraph 4 of these Commitments, the Divestment Businesses include, but are not limited to:

(a) the following main intangible assets:

The main assets are the music publishing rights of varying duration.

The following table shows the top 100 copyrights in the BBC catalogue for 2006.

	Title	Composers	Revenue (EUR)
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¹⁵⁵ See paragraph 4(a) of these Commitments.

1	TELETUBBIES	MCCRORIE-SHAND	[Business Secret]
2	CASH IN THE ATTIC	LOWE	[Business Secret]
3	WALKING WITH BEASTS	BARTLETT	[Business Secret]
4	BBC WORLD NEWS IDENTS 2002	LOWE	[Business Secret]
5	ANIMALS OF FARTHING WOOD	KUEHNE	[Business Secret]
6	BBC NEWS 2000	LOWE	[Business Secret]
7	CAR BOOTY	LEAVY	[Business Secret]
8	BBC BREAKFAST NEWS	LOWE	[Business Secret]
9	SHOEBOX ZOO - SERIES 1 AND 2	BALFE	[Business Secret]
10	BBC NEWS 24 CHANNEL MUSIC	LOWE	[Business Secret]
11	8TH WORLD WONDER	SHANKEL/PARKES/JACOBS	[Business Secret]
12	SPOOKS (SERIES 1)	MUSKETT	[Business Secret]
13	WALKING WITH DINOSAURS	BARTLETT	[Business Secret]
14	BBC TV NEWS REGIONAL - ENGLAND	LOWE	[Business Secret]
15	THE FIMBLES (BACKGROUND)	MULHALL/NEALE/NICHOLLS	[Business Secret]
16	TWEENIES (TELEVISION BROADCAST)	KITCHEN/PIKE	[Business Secret]
17	TOP OF THE POPS (ALL NEW)	GIBBER	[Business Secret]
18	WAKING THE DEAD SERIES 1	HART/CAMPBELL	[Business Secret]
19	BALAMORY	WILSON/MCLAUGHLIN	[Business Secret]
20	TELETUBBIES INCIDENTAL	MCCRORIE-SHAND	[Business Secret]
21	TELETUBBIES	HARTLEY	[Business Secret]
22	SPACE	UNWIN	[Business Secret]
23	STRICTLY COME DANCING	MCGRATH/PHILLIPS	[Business Secret]
24	READY STEADY COOK SERIES 1-6	BOLAM	[Business Secret]
25	HEY HEY ARE YOU READY TO PLAY	BRENTON/KITCHEN/LAUCHLAN/PIKE	[Business Secret]
26	TWEENIES THE BEE DANCE	BIGNOLD/JACKMAN	[Business Secret]
27	MONARCH OF THE GLEN	BRINT	[Business Secret]
28	WILD AFRICA	GUNNING	[Business Secret]
29	WILD WEATHER	MOLLISON	[Business Secret]
30	BB3B	JACQUEMIN/HOWMAN	[Business Secret]
31	THE HUMAN BODY	PARKER	[Business Secret]
32	LOST WORLD	LANE	[Business Secret]
33	BOO (SERIES 1)	HOWMAN/JACQUEMIN	[Business Secret]
34	D-DAY	PARKER	[Business Secret]
35	HAVE I GOT NEWS FOR YOU	WEBLEY	[Business Secret]
36	THE FLOWERPOT MEN	TAYLOR	[Business Secret]
37	WILLIAMS WISH WELLINGTONS - CLOSING TTILES	NICHOLLS/NEALE/MUHALL	[Business Secret]
38	JONATHAN CREEK - (INCIDENTALS)	LINDSAY	[Business Secret]
39	MYSTERIES OF THE LANDSCAPE	MOLLISON	[Business Secret]
40	TWEENIES OPENING TTILES (TV BROADCAST)	KITCHEN/PIKE/BRENTON/LAUCHLAN	[Business Secret]
41	ANIMALS OF FARTHING WOOD II	KUEHNE	[Business Secret]
42	BBC WORLD CHANNEL IDENT	GLASMAN	[Business Secret]
43	TANGO	LAWLOR	[Business Secret]
44	THE FIMBLES (THEME SONG)	JOYCE	[Business Secret]
45	POMPEII - THE LAST DAY	UNWIN	[Business Secret]
46	LIFE OF MAMMALS	SALISBURY	[Business Secret]
47	CBBC IDENTS	ARNON/RABJOHNS/LORD/DATTA	[Business Secret]
48	THE LIFE OF BIRDS	FAUX/BUTCHER	[Business Secret]
49	THE NATURAL HISTORY OF EUROPE	TAYLOR	[Business Secret]
50	DINNERLADIES (SERIES B) - SIGNATURE TUNE	FIRMAN/WOOD	[Business Secret]
51	THE LIFE OF MAMMALS OPENING MONTAGE	SALISBURY	[Business Secret]
52	TELETUBBIES THEME TUNE (OPENING TTILES)	MCCRORIE-SHAND	[Business Secret]
53	ROLY'S SONG	MULHALL/NEALE/NICHOLLS/WATTS/WHITELEY	[Business Secret]
54	TWEENIES: READY TO PLAY	KITCHEN/PIKE	[Business Secret]
55	AUF WIEDERSEHEN PET - SERIES 3	LUNN	[Business Secret]
56	THE STORY OF TRACY BEAKER (MOVIE VERSION)	APPLEBY	[Business Secret]
57	CASH IN THE ATTIC SERIES 2	LOWE	[Business Secret]
58	BBC1 TELEVISION IDENTS 2002	LAWLOR	[Business Secret]
59	MISS HOOLIE NURSERY SONG	PATERSON	[Business Secret]
60	ACROBAT	LAWLOR	[Business Secret]
61	CAN WE FIX IT?	JOYCE	[Business Secret]
62	THE SEARCH FOR THE LOCH NESS MONSTER	PARNELL/WADDELL/DAVIDSON	[Business Secret]
63	WALKING WITH CAVEMEN	PARKER	[Business Secret]
64	JUDGE JOHN DEED - SERIES 1	WISEMAN	[Business Secret]
65	CLICK ON LINE	DUNDAS	[Business Secret]
66	WAKING THE DEAD SERIES 3	HART/CAMPBELL	[Business Secret]
67	MAN AND BOY	LANE	[Business Secret]
68	GENERIC CLOCK STING	KITCHEN/PIKE	[Business Secret]
69	WAKING THE DEAD SERIES 2	HART/CAMPBELL	[Business Secret]
70	OPENING TTILES STINGS (TELETUBBIES)	MCCRORIE-SHAND	[Business Secret]
71	TO BUY OR NOT TO BUY	RAPHAEL/MORIS	[Business Secret]
72	THE FIMBLES: FINDING SONG - FLORRIE	JOYCE/PAGE	[Business Secret]
73	DOCTORS	HEMMINGS/BADGER	[Business Secret]
74	ANDES TO AMAZON	HOOPER	[Business Secret]
75	FLOG IT (INCIDENTALS/ STINGS)	SLATER	[Business Secret]
76	DEATH TRAP	CARTWRIGHT	[Business Secret]
77	TELETUBBIES : EVERYWHERE	MCCRORIE-SHAND	[Business Secret]
78	MONSTERS WE MET	LOCKE/NORFOLK	[Business Secret]
79	YOHO AHOY	TACKLEY	[Business Secret]
80	BOLLYWOOD	LAWLOR	[Business Secret]
81	TWEENIES : PARTY GAMES, LAUGHS & GIGGLES	BIGNOLD	[Business Secret]
82	COLOSSEUM	ESHKERI	[Business Secret]
83	TELETUBBIES SAY EH-OH	MCCRORIE-SHAND	[Business Secret]
84	JOSIE JUMPS HERO SONG	MUOTUNE	[Business Secret]
85	CLOSING TTILES STINGS (TELETUBBIES)	MCCRORIE-SHAND	[Business Secret]
86	THE COLOUR SONG	MCLAUGHLIN	[Business Secret]
87	THE PLANETS	MEACOCK	[Business Secret]
88	FULL CIRCLE WITH MICHAEL PALIN	PARKER	[Business Secret]
89	TAP DOGS	LAWLOR	[Business Secret]
90	SKATEBOARDING	LAWLOR	[Business Secret]
91	NUTS	WILSON	[Business Secret]
92	HIP HOP	DEWAR/HALE/LAWLOR	[Business Secret]
93	S.A.S.: ARE YOU TOUGH ENOUGH?	HENSON	[Business Secret]
94	OH,WE'RE GOING ON A PICNIC,YES WE ARE	MULHALL/NEALE/NICHOLLS/PAGE	[Business Secret]

95	IN SEARCH OF SHAKESPEARE	DAVIDSON	[Business Secret]
96	MURPHY'S LAW	BUTT	[Business Secret]
97	CAPOEIRA	LAWLOR	[Business Secret]
98	TELETUBBIES - UH-OH	MCCRORIE-SHAND	[Business Secret]
99	GENERIC CLOSING TITLE MUSIC- TWEENIES	KITCHEN/PIKE	[Business Secret]
100	ANIMAL GAMES	PARKER	[Business Secret]

- (b) the following main contracts, agreements, leases, commitments and understandings;

The following table shows the top 10 EEA revenue earning writers of BBC in 2006.

Name	Total EEA Revenues in 2006 (EUR)
BBC - LOWE, DAVID	[Business Secret]
RAGDOLL LIMITED (Andrew McCrorie-Shand/Paul Hartley) (Teletubbies)	[Business Secret]
TELL TALE PRODUCTIONS (Liz Kitchen/Graham Pike/Will Brenton/Iain Lauchlan) (Tweenies)	[Business Secret]
NOVEL FINDERS LTD (Paul Joyce/Lucinda Whitley/Terry Neale/Rick Nulhall/Ian David Nicholls) (Fimbles)	[Business Secret]
BBC - BARTLETT, BENJAMIN	[Business Secret]
BBC - LAWLOR, PETER	[Business Secret]
BBC - MCCRORIE-SHAND, ANDREW	[Business Secret]
BBC - LEAVY, KEVIN	[Business Secret]
BBC - BALFE, LORNE	[Business Secret]
BBC - KITCHEN, LIZ	[Business Secret]

- (c) It is not anticipated that it would be necessary for arrangements to be put in place for the supply of any necessary services for a transitional period on arm's length terms, but UMG or affiliated undertakings would be prepared to agree to supply any such services, if required by the Commission at the request of the Purchaser, for a reasonable transitional period.

SCHEDULE 7 – Rondor Music (London) Limited (“Rondor UK”)

Summary

Rondor UK is a pure pop catalogue which produced revenues in 2005 in the EEA of **€5 - 10 million]** and **€5 - 10 million]** globally. In 2006 these have increased dramatically to **€5 - 10 million]** in the EEA and **€10 - 15 million]** globally.

Of particular note is the depth of this catalogue, which includes over **[Business Secret]** writers which generated more than **€5,000** globally in 2006. Current writers include:

- The Kaiser Chiefs arrived on the UK music scene in 2005 following the release of their debut album ‘Employment’. This album went to number 2 in the UK, has sold 2.5 million copies worldwide to date and was the fourth biggest UK album of 2005, with four hit singles “(Everyday I Love You Less And Less”, which reached number 10 in the UK, “I Predict A Riot/Sink That Ship”, which reached number 9 in the UK, “Modern Way”, which reached number 11 in the UK, and “Oh My God” which reached number 6 in the UK). The band has gone on to win three Brit Awards in 2006, Britain’s most prestigious music awards (Best British Rock Act, Best British Live Act, Best British Group), and a prestigious Ivor Novello award (the top UK song-writing award) in 2006, as well as an NME Award for Best Album in 2006. The follow up album ‘Yours Truly, Angry Mob’ was released in March 2007 and has already reached number 1 in the UK, number 1 in Greece, number 1 in the Netherlands, number 2 in Ireland, number 4 in Austria and number 6 in Germany. It achieved platinum status in the UK (300,000 sales) within two weeks of release, and 540,000 total shipments globally by 24 March 2007. Sales of this album are anticipated to at least match sales of the first album. The single ‘Ruby’ reached number 1 in the UK charts in February 2007, and was number 1 in the European

singles charts. Gross income earned to date, over a period of just over one and half years, is in excess of €[Business Secret]. [Business Secret].

- Sophie Ellis Bextor was originally in a band called 'theaudience' but found fame singing and co-writing the worldwide hit 'Groovejet (If This Ain't Love)' by Spiller which was a number 1 single around the world including the UK where it sold 600,000 copies. Following this Sophie has pursued a successful solo career with album sales to date of 1.5 million copies and her debut album 'Read My Lips' entering the UK charts at number 2 in 2002. She has had 7 top 20 singles with 'Take Me Home' and 'Murder On The Dancefloor' reaching no 2 in 2001. The latter also topped the European Airplay Charts. In 2003 the single 'Mixed Up World' reached number 7 in the UK charts, and in 2004 'I Won't Change You' reached number 9 in the UK. Sophie's third album 'Trip the Light Fantastic' is due for release in May 2007, and the first single from this album 'Catch You' has already reached number 8 in the UK charts.
- Jorgen / Larsson - Danish pop production team whose credits include the boy band Blue who had several hits throughout Europe, including 'Breathe Easy' which reached number 4 in the UK and Ireland, and number 7 in Austria and Germany in April/May 2004.
- Other writers with ongoing delivery commitments include Aston Harvey and Jan Kask.

Key works in the catalogue include copyrights by top authors such as the following:

- Mark Knopfler - the songwriter and lead singer of Dire Straits, their biggest album 'Brothers in Arms' has sold in excess of 25 million copies, spent nine weeks at number 1 in the US and is the UK's fourth biggest selling album of all time. The

catalogue includes the Sting co-written song 'Money For Nothing' and other chart hits such as 'Walk Of Life', and 'Private Investigations'. Dire Straits have won numerous accolades and awards including two Grammys and three Brit Awards. To date, Mark Knopfler has sold over 60 million albums including approximately 10 million albums as a solo artist. Gross income earned to date is in excess of ~~€~~**[Business Secret]**.

- Wayne Hector - co-written work includes Westlife songs such as 'Flying Without Wings' which was a UK number 1 in 1999 and the UK Song of the Year. 'Flying Without Wings' was also covered in 2003 by American Idol contestant Ruben Studdard; this cover version entered at number 2 in the Billboard Hot 100 chart and had sold 751,000 copies by December 2006. Wayne also wrote the Westlife hits 'Swear it Again' (number 1 in the UK and Ireland in 1999), 'What Makes a Man' (number 2 in the UK in 2000) and 'Queen of My Heart' (number 1 in the UK and number 14 In Ireland in 2001). Wayne co-wrote songs for Westlife which appeared on their chart topping greatest hits album, released in 2002. Wayne has also written for a number of the American Idol contestants, and has also co-written a number 1 country hit in the US in 2006 with 'What Hurts The Most', recorded by the Rascal Flatts.
- Steve Robson - Steve has written for numerous artists including S-Club 7 and had a number 1 country hit in the US in 2006 with 'What Hurts The Most', recorded by the Rascal Flatts, which featured on the number 2 selling album in the US in 2006, also by the Rascal Flatts.
- Leo Sayer catalogue, which includes the song 'Thunder in My Heart' which originally reached #22 in the UK charts in September 1977 but was remixed by MECK as 'Thunder in My Heart Again' and reached #1 in the UK charts in

February 2006 and number 7 in the Dutch charts. The catalogue contains chart toppers from across the globe from the 1970's and 1980's, including 'You Make Me Feel Like Dancing'.

- Imogen Heap – this singer-songwriter has had significant recent chart success, with her recent single 'Hide and Seek', which reached the charts in 2006, 'Goodnight and Go' which reached the UK charts in 2006, and 'Headlock' which also reached the UK charts in 2006. So far she has released two solo albums 'Megaphone' and 'Speak for Yourself', as well as writing songs for her band Frou Frou. Imogen Heap was nominated for a Grammy for Best New Artist and for Best Song Written For A Motion Picture "Narnia" in December 2006.
- William Orbit – this writer producer, who is also an artist in his own right, co-wrote six works recorded by Madonna on her 1998 album 'Ray of Light', which sold 15 million copies worldwide, including the hit singles 'Ray Of Light' and 'Drowned World/Substitute For Love'. William also co-wrote 'Pure Shores' with Shaznay Lewis which achieved number 1 in the UK charts in 2000, as well as being the top selling single of that year with sales of 683,000. Orbit won a prestigious Ivor Novello award (the top UK song-writing award) for this song in 2001.
- Nick Kershaw – this singer-songwriter achieved success in the mid-1980's with the chart hits 'The Riddle', 'I Won't Let The Sun Go Down On Me', and 'Wouldn't It Be Good', and wrote 'The One and Only' which was a number one single in the UK for Chesney Hawkes in 1991.
- Hammond and Hazelwood – this 1970's songwriting team wrote the evergreen hits such as 'It Never Rains in Southern California' recorded by Albert Hammond which was a number 5 chart hit in the US in 1972 and 'The Air That I Breathe', recorded

by the Hollies, which was a number 2 hit in the UK in 1974, which was released on 136 different products including well known covers by Julio Iglesias, Olivia Newton John, Simply Red, and kd lang in 1997.

- Brenda Richie – this catalogue includes songs recorded by Lionel Richie (winner of 3 Grammy awards) such as ‘Hello’ reached number 1 in the UK, ‘All Night Long’ number 1 in the US, ‘Dancing On The Ceiling’ number 6 in the UK, and ‘Stuck On You’ was from the number 1 album in 1983 in the UK ‘Cant Slow Down’.
- Joan Armatrading – Joan achieved success in the 1970’s with the hits ‘Love And Affection’, which appeared on the album ‘Joan Armatrading’ released in 1976, along with other songs such as ‘The Weakness In Me’, ‘Show Some Emotion’ and ‘Me Myself and I’.
- Other key copyrights include Chris de Burgh’s ‘Lady In Red’ number 1 in 25 countries, worldwide sales of 8 million – which has been released on 201 different products, and Andy Fairweather Low’s ‘Wide Eyed And Legless’ - a number 6 hit in the UK.

The following table provides a summary of the financial information over the past three years:

SUMMARY	2004	2005	2006
EEA Rev (€‘000)	[5,000 - 10,000]	[5,000 - 10,000]	[5,000 - 10,000]
Global Revenue (€‘000)	[5,000 - 10,000]	[5,000 - 10,000]	[5,000 - 10,000] ¹⁵⁶

1 Following paragraph 4 of these Commitments, the Divestment Businesses include, but are not limited to:

(a) the following main intangible assets:

¹⁵⁶ These revenues exclude the three bands Supertramp, Squeeze and Yes, which has the effect of reducing global revenues in 2006 by €[Business Secret].

The main assets are the music publishing rights of varying duration.

The following table shows the top 100 copyrights in the Rondor UK catalogue for 2006.

	Title	Composers	Revenue (EUR)
1	I PREDICT A RIOT	Baines, Hodgson, Rix, White &	[Business Secret]
2	MODERN WAY	Baines, Hodgson, Rix, White &	[Business Secret]
3	EVERYDAY I LOVE YOU LESS AND LESS	Baines, Hodgson, Rix, White &	[Business Secret]
4	OH MY GOD	Baines, Hodgson, Rix, White &	[Business Secret]
5	YOU CAN HAVE IT ALL	Baines, Hodgson, Rix, White &	[Business Secret]
6	CAROLINE, YES	Baines, Hodgson, Rix, White &	[Business Secret]
7	WHAT DID I EVER GIVE YOU?	Baines, Hodgson, Rix, White &	[Business Secret]
8	THUNDER IN MY HEART	Sayer & Snow	[Business Secret]
9	BORN TO BE A DANCER	Baines, Hodgson, Rix, White &	[Business Secret]
10	SATURDAY NIGHT	Baines, Hodgson, Rix, White &	[Business Secret]
11	NA NA NA NA NAA	Baines, Hodgson, Rix, White &	[Business Secret]
12	TEAM MATE (BICYCLE FOR TWO)	Baines, Hodgson, Rix, White &	[Business Secret]
13	TIME HONOURED TRADITION	Baines, Hodgson, Rix, White &	[Business Secret]
14	SULTANS OF SWING	Knopfler	[Business Secret]
15	WALK OF LIFE	Knopfler	[Business Secret]
16	HEADLOCK	Heap	[Business Secret]
17	MONEY FOR NOTHING	Knopfler & Sumner	[Business Secret]
18	ROMEO AND JULIET	Knopfler	[Business Secret]
19	BROTHERS IN ARMS	Knopfler	[Business Secret]
20	ONE AND ONLY, THE	Kershaw	[Business Secret]
21	STOP	Brody, Brown & Sutton	[Business Secret]
22	AIR THAT I BREATHE, THE	Hammond & Hazlewood	[Business Secret]
23	SINK THAT SHIP	Baines, Hodgson, Rix, White &	[Business Secret]
24	LADY IN RED, THE	De Burgh	[Business Secret]
25	PRIVATE INVESTIGATIONS	Knopfler	[Business Secret]
26	WOULDN'T IT BE GOOD	Kershaw	[Business Secret]
27	ALL NIGHT LONG	Richie Jr.	[Business Secret]
28	WEAKNESS IN ME, THE	Armatrading	[Business Secret]
29	GOING HOME	Knopfler	[Business Secret]
30	LIGHT MY FIRE	Densmore, Krieger, Manzarek &	[Business Secret]
31	LOVE OVER GOLD	Knopfler	[Business Secret]
32	ON EVERY STREET	Knopfler	[Business Secret]
33	FLYING WITHOUT WINGS	Hector & McCutcheon	[Business Secret]
34	LOVE AND AFFECTION	Armatrading	[Business Secret]
35	DON'T STOP MOVIN'	Barrett, Cattermole, Ellis, Le	[Business Secret]
36	YOU'RE THE VOICE	Quinta, Reid, Ryder & Thomson	[Business Secret]
37	WHAT IT IS	Knopfler	[Business Secret]
38	YOUR LATEST TRICK	Knopfler	[Business Secret]
39	PRIVATE DANCER	Knopfler	[Business Secret]
40	PURE SHORES	Lewis & Orbit	[Business Secret]
41	SO FAR AWAY	Knopfler	[Business Secret]
42	HELLO	Richie Jr.	[Business Secret]
43	TUNNEL OF LOVE	Knopfler	[Business Secret]
44	DANCING ON THE CEILING	Frenchik, Richie Jr. & Rios	[Business Secret]
45	LAST THING ON MY MIND	Keating & Robson	[Business Secret]
46	CALLING ELVIS	Knopfler	[Business Secret]
47	HEART IN NEW YORK	Gallagher & Lyle	[Business Secret]
48	I WANNA STAY WITH YOU	Gallagher & Lyle	[Business Secret]
49	STUCK ON YOU	Richie Jr.	[Business Secret]
50	BITTER SWEET AND SOUR	Madden	[Business Secret]
51	TELEGRAPH ROAD	Knopfler	[Business Secret]
52	PENNY LOVER	Harvey-Richie & Richie Jr.	[Business Secret]
53	OOMPA LOOMPA	Bricusse & Newley	[Business Secret]
54	DONKEYTOWN	Knopfler	[Business Secret]
55	WHY WORRY?	Knopfler	[Business Secret]
56	SWEAR IT AGAIN	Hector & McCutcheon	[Business Secret]
57	GROOVEJET (IF THIS AIN'T LOVE)	Davis, Ellis-Bextor, Montana J	[Business Secret]
58	WHAT MAKES A MAN	Hector & McCutcheon	[Business Secret]
59	DROWNED WORLD/SUBSTITUTE FOR LOVE	Ciccone, Collins, Kerr, McKuen	[Business Secret]
60	END, THE	Densmore, Krieger, Manzarek &	[Business Secret]
61	I WON'T LET THE SUN GO DOWN	Kershaw	[Business Secret]
62	CANDY MAN, THE	Bricusse & Newley	[Business Secret]
63	MURDER ON THE DANCEFLOOR	Alexander & Ellis-Bextor	[Business Secret]
64	SAY YOU, SAY ME	Richie Jr.	[Business Secret]
65	BEAUTIFUL STRANGER	Ciccone & Orbit	[Business Secret]
66	BREATHE EASY	Jensen, Larsson & Ryan	[Business Secret]
67	MY DESTINY	Richie Jr.	[Business Secret]
68	LONG ROAD, THE	Knopfler	[Business Secret]
69	RIDDLE, THE	Kershaw	[Business Secret]
70	I DUG UP A DIAMOND	Knopfler	[Business Secret]
71	SAILING TO PHILADELPHIA	Knopfler	[Business Secret]
72	WHAT HURTS THE MOST	Robson & Steele	[Business Secret]
73	CREEP	Greenwood, Greenwood, Hammond,	[Business Secret]
74	IT NEVER RAINS IN SOUTHERN CALIFORNIA	Hammond & Hazlewood	[Business Secret]
75	HEART ON MY SLEEVE	Gallagher & Lyle	[Business Secret]
76	HIDE AND SEEK	Heap	[Business Secret]
77	RED STAGGERWING	Knopfler	[Business Secret]
78	RIDERS ON THE STORM	Densmore, Krieger, Manzarek &	[Business Secret]
79	HEAVY FUEL	Knopfler	[Business Secret]
80	NEVER LET ME DOWN	Allen, Boyd & Ellis-Bextor	[Business Secret]
81	TWISTIN' BY THE POOL	Knopfler	[Business Secret]
82	FEEL GOOD TIME	Ferguson, Hansen & Orbit	[Business Secret]
83	FREE ELECTRIC BAND, THE	Hammond & Hazlewood	[Business Secret]
84	FIVE TO ONE	Densmore, Krieger, Manzarek &	[Business Secret]
85	LADY WRITER	Knopfler	[Business Secret]
86	HIT THE ROAD JACK	Mayfield	[Business Secret]
87	I CAN'T TAKE IT IN (SOUNDTRACK VERSION)	Heap	[Business Secret]
88	DO YOU KNOW	Gayle & Solomon	[Business Secret]
89	YOU MAKE ME FEEL LIKE DANCING	Poncia & Sayer	[Business Secret]
90	DARLING PRETTY	Knopfler	[Business Secret]
91	SISTA SISTA	Gammons, Knight & Wolinski	[Business Secret]
92	WILD THEME	Knopfler	[Business Secret]
93	LADY	Richie Jr.	[Business Secret]

94	ROADHOUSE BLUES	Densmore, Krieger, Manzarek &	[Business Secret]
95	L.A. WOMAN	Densmore, Krieger, Manzarek &	[Business Secret]
96	RIDE ACROSS THE RIVER	Knopfler	[Business Secret]
97	YOU'RE THE VOICE	Qunta, Reid, Ryder & Thompson	[Business Secret]
98	RUNNING WITH THE NIGHT	Richie Jr. & Weil	[Business Secret]
99	PUSH UP	Brehony, Cantor, Harvey, Safin	[Business Secret]
100	BUBBLIN'	Costa, Jensen, Jorgensen & Ten	[Business Secret]

- (b) the following main contracts, agreements, leases, commitments and understandings;

The following table shows the top 10 EEA revenue earning writers of Rondor UK in 2006.

Name	Total EEA Revenues in 2006 (EUR)
KAISER CHIEFS	[Business Secret]
CHARISCOURT LTD. (Mark Knopfler)	[Business Secret]
STRAITJACKET SONGS LTD. (Mark Knopfler)	[Business Secret]
KERSHAW, NIK	[Business Secret]
DEEKAY MUSIC APS (Danish writing team for Blue)	[Business Secret]
RAZE WAYBLUE LTD (Sam Brown)	[Business Secret]
SILVERBIRD SONGS LTD. (Leo Sayer)	[Business Secret]
ROBSON, STEVE	[Business Secret]
GUERILLA STUDIOS LTD. (William Orbit)	[Business Secret]
RAMJ BRENDA RICHIE PUBL (Lionel Ritchie)	[Business Secret]

- (c) It is not anticipated that it would be necessary for arrangements to be put in place for the supply of any necessary services for a transitional period on arm's length terms, but UMG or affiliated undertakings would be prepared to agree to supply any such services, if required by the Commission at the request of the Purchaser, for a reasonable transitional period.

2 The Divestment Businesses shall not include:

- (a) The Rondor name.
- (b) The works of the three bands: Supertramp, Squeeze and Yes.



EUROPEAN COMMISSION

Competition DG

Policy and Strategic Support

OPINION

of the ADVISORY COMMITTEE on CONCENTRATIONS

given at its 150th meeting on 10 May 2007

concerning a draft decision relating to

Case COMP/M.4404– Universal Music Group/BMG Music Publishing

1. The Advisory Committee agrees with the Commission that the notified operation constitutes a concentration within the meaning of Article 3(1)(b) of the EC Merger Regulation and that it has a Community dimension pursuant to Article 1(3) of that Regulation.
2. The Advisory Committee agrees with the Commission that the relevant product markets can be characterised as follows:
 - a) Markets for the exploitation of music publishing rights
The relevant product markets need to be defined along the following categories of rights since the customer needs, the prices as well as the overall economic conditions differ significantly:
 - Mechanical rights;
 - Performance rights;
 - Synchronisation rights;
 - Print rights;
 - Online rights.
 - b) Market for music publishing services to authors.
3. The Advisory Committee agrees with the Commission that the geographic scope of the relevant product markets is:
 - a) Markets for the exploitation of music publishing rights
 - mechanical and performance rights: national;
 - print and synchronisation rights: largely national;
 - online rights: currently national, but it is possible that it will develop to an EEA-wide scope. However, there is no need to strictly define the geographic scope of the market for online rights as the competitive assessment will remain unchanged under a national or EEA wide dimension.

b) Market for music publishing services to authors

- The geographic scope of the market appears to be national. The exact geographic scope may, however, be left open since the conclusions of the analysis will be the same under any geographic dimension.
4. The Advisory Committee agrees with the Commission that the proposed concentration will not significantly impede effective competition on the market for music publishing services for authors.
 5. The Advisory Committee agrees with the Commission that the proposed concentration will not significantly impede effective competition on the market for the exploitation of synchronisation rights, on the market for the exploitation of print rights, on the market for the exploitation of mechanical rights and on the market for the exploitation of performance rights.
 6. The Advisory Committee agrees with the Commission's view that it is very likely that Universal will post-merger, on the basis of non-coordinated effects, have the possibility and the incentive to increase prices for its repertoire of Anglo-American mechanical rights for online applications. The Advisory Committee agrees that the merger therefore raises serious doubts with respect to the market for online rights (which are composed of mechanical and performance rights for online applications) both on an EEA-wide level and in the countries Austria, the Czech Republic, Germany, Poland and the UK.
 7. The Advisory Committee agrees with the Commission that the Final Remedies Package submitted on 23 April 2007 which comprises the following catalogues and contracts:
 - a) BMG MP catalogues
 - Zomba Music Publishers Limited
 - 19 Music Limited
 - 19 Songs Limited
 - BBC music publishing catalogue
 - Zomba U.S. (EEA-wide licence)
 - b) Universal catalogues
 - Rondor Music (London) Limited

is sufficient to remove the competition concerns on the market for publishing rights for online applications, both under an EEA-wide or national geographic market definition.

8. The Advisory Committee agrees with the Commission that, the proposed concentration as modified by the Commitments does not significantly impede effective competition in the common market or a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, and that pursuant to Articles 8 (2) and 10 (2) of the Merger Regulation and Article 57 of the EEA Agreement the proposed concentration is therefore to be declared compatible with the Common Market and with the EEA Agreement, subject to full compliance with the commitments offered by the notifying party.

9. The Advisory Committee asks the Commission to take into account all the other points raised during the discussion.

<u>BELGIË/BELGIOUE</u>	<u>BULGARIA</u>	<u>ČESKÁ REPUBLIKA</u>	<u>DANMARK</u>	<u>DEUTSCHLAND</u>
---	D. DIMITROVA	---	L. BREDAHL	K. HOOGHOFF
<u>ÉIRE/IRELAND</u>	<u>EESTI</u>	<u>ELLADA</u>	<u>ESPAÑA</u>	<u>FRANCE</u>
I. BAH	---	---	A. NUCHE BASCÓN	O. GUILLEMOT
<u>ITALIA</u>	<u>KYPROS/KIBRIS</u>	<u>LATVIJA</u>	<u>LIETUVA</u>	<u>LUXEMBOURG</u>
L. MICANGELI	---	---	---	---
<u>MAGYARORSZÁG</u>	<u>MALTA</u>	<u>NEDERLAND</u>	<u>ÖSTERREICH</u>	<u>POLSKA</u>
S. LENK	---	R. van HUTTEN	---	---
<u>PORTUGAL</u>	<u>ROMÂNIA</u>	<u>SLOVENIJA</u>	<u>SLOVENSKO</u>	<u>SUOMI-FINLAND</u>
R. MAXIMIANO	---	D. TOMŠE	E. BOCHNICKOVA	H. KAIPONEN
<u>SVERIGE</u>	<u>UNITED KINGDOM</u>			
P. HÖGSET	I. KOKKORIS			



EUROPEAN COMMISSION

The Hearing Officer

FINAL REPORT OF THE HEARING OFFICER
IN CASE COMP/M.4404 – Universal/BMG

**(pursuant to Articles 15 & 16 of Commission Decision (2001/462/EC, ECSC)
of 23 May 2001 on the terms of reference of Hearing Officers
in certain competition proceedings – OJ L162, 19.06.2001, p.21)**

On 3 November 2006, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004 by which the undertaking Universal Music Group Inc. (“Universal”) acquires within the meaning of Article 3(1)(b) of the Council Regulation sole control of the whole of the undertaking BMG Music Publishing (“BMG”) which currently forms part of the Bertelsmann group, by way of purchase of shares and assets.

Upon examination of the evidence submitted by the parties to the proposed concentration and after conducting a market investigation, the Commission concluded that the concentration raised serious doubts as to its compatibility with the common market and decided to initiate proceedings under Article 6 (1) (c) of the Merger Regulation on 8 December 2006.

Access to key documents was provided to the notifying party on 21 December 2006 and again on 26 January 2007, in accordance with the best practices on the conduct of EC merger control proceedings.

On 15 March 2007 the parties offered commitments that modified the original concentration plan. These commitments were modified on 26 March and again on 30 March, and final commitments were submitted on 23 April 2007. On the basis of these undertakings the relevant Commission service considered that the serious doubts had been removed. Accordingly no Statement of objections was sent to the parties.

No queries were raised before me by the parties or other companies as to the market test.

The case does not call for any particular comments as regards the right to be heard.

Brussels, 11 May 2007

(signed)

Serge DURANDE

EN

This text is made available for information purposes only.
A summary of this decision is published in all Community languages in the Official Journal of the European Union.

***Case No COMP/M.5440-
LUFTHANSA/
AUSTRIAN AIRLINES***

Only the English text is authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 8 (2)
Date: 28/08/2009

Commission Decision
of 28.8.2009
declaring a concentration to be compatible with the common market
and the EEA Agreement

(Case No COMP/M.5440 – Lufthansa/ Austrian Airlines)

(Only the English text is authentic)

(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to the bilateral Agreement between the European Community and the Swiss Confederation on Air Transport,¹

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings,² and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 1 July 2009 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations,³

Having regard to the final report of the Hearing Officer in this case,⁴

1 OJ L 114, 30.4.2002, p. 73.

2 OJ L 24, 29.1.2004, p. 1.

3 OJ 2010/C 16 p.8

4 OJ 2010/C 16 p.10

WHEREAS:

I. THE PARTIES AND THE TRANSACTION

- (1) On 8 May 2009, the Commission received a notification of a proposed concentration pursuant to Article 4 of Regulation (EC) No 139/2004 (hereinafter "the Merger Regulation"), by which the undertaking Deutsche Lufthansa AG (hereinafter "LH") acquires sole control, within the meaning of Article 3(1)(b) of that Regulation, of the undertaking Austrian Airlines (hereinafter "OS") by way of purchase of shares.
- (2) LH is the largest German airline. It provides scheduled passenger and cargo transport and related services (maintenance, repair and overhaul services ("MRO"), in-flight catering and IT services). In 2008, LH carried 45 million passengers to more than 200 destinations in 85 countries with its 272 aircraft. It has hubs at Frankfurt International Airport and Munich airport and a base at Düsseldorf airport. LH also controls Swiss International Air Lines Ltd. ("LX")⁵ based at Zurich airport, Air Dolomiti, Eurowings, and Eurowings' subsidiary, the low-cost carrier Germanwings ("4U"), and it recently acquired British Midland ("BMI") and Brussels Airlines ("SN").⁶ In addition, LH holds 19% of the shares of Jet Blue, a low-cost airline active in the United States of America. Both LH and LX are members of the Star Alliance.
- (3) OS is the Republic of Austria's largest airline with its principal hub in Vienna. It provides scheduled passenger and cargo transport and related services, and serves 121 destinations in 63 countries (including code-sharing). Its subsidiaries include Lauda Air and Tyrolean Airways. In addition, it holds a stake of 22.5% of the shares of Ukraine International Airlines, a Ukrainian network carrier. OS is a member of the Star Alliance.
- (4) LH intends to acquire sole control over OS. On 5 December 2008, in the context of the privatisation process of OS, LH agreed to indirectly acquire a 41.56% shareholding in OS from the publicly owned Österreichische Industrieholding Aktiengesellschaft ("ÖIAG"). In addition, on 27 February 2009, LH launched a public offer for all remaining free-floating shares in OS, for which it received more than the required amount of declarations of acceptance. Together with the shares it acquired from ÖIAG, LH will be able to acquire an at least 85% shareholding in OS.

5 See Commission Decision of 4 July 2005 in Case No. COMP/M.3770 - Lufthansa/Swiss, OJ C 240, 20.8.2005, p. 3.

6 The Commission authorized the proposed acquisition of SN by LH subject to conditions on 22 June 2009, see Case No. COMP/M.5335 – Lufthansa/SN Airholdings (Brussels Airlines), not yet published. The Commission approved the proposed acquisition of BMI by LH without conditions on 14 May 2009, see Commission Decision of 14 May 2009 in Case No. COMP/M.5403 - Lufthansa/BMI, OJ C 158, 11.7.2009, p. 1.

- (5) OS is currently encountering financial difficulties.⁷ In July 2008, OS's management considered that the stand-alone option was no longer maintainable, and its supervisory board concluded that it would be difficult to continue operating OS as a stand-alone business. Consequently, OS' supervisory board asked that Austria privatise the company and the Austrian Government issued a privatization mandate ("Privatisierungsauftrag") pursuant to which ÖIAG was authorised to dispose of all of its shares in Austrian Airlines. On 19 January 2009, the Commission approved rescue aid in the form of a 100% guarantee on a loan amounting to EUR 200 million for OS.⁸ In parallel to its assessment of the transaction under the Merger Regulation, the Commission assessed the terms and conditions of the intended acquisition of Austria's shareholding in OS by LH and a EUR 500 million capital increase in OS under Articles 87 and 88 of the Treaty.
- (6) Collectively, LH and OS are referred to as "the parties" in this Decision.

II. CONCENTRATION

- (7) As a result of the proposed transaction, LH would acquire sole control over OS. This transaction thus constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. COMMUNITY DIMENSION

- (8) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 billion (LH: EUR 27 870 million; OS: EUR 2 530 million).⁹ LH and OS both have a Community-wide turnover in excess of EUR 250 million each (LH: EUR [...]*; OS: EUR [...]*), but neither achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State. The methodology used by the notifying party to calculate the parties' turnover is the "point of sale" methodology, although in any event the thresholds would also be met under the "point of origin" method or "50/50 split" method.¹⁰ The proposed transaction therefore has a Community dimension within the meaning of Article 1(2) of the Merger Regulation.

IV. PROCEDURE

- (9) After examination of the notification, the Commission concluded on 1 July 2009 that the transaction fell within the scope of the Merger Regulation and that it raised serious doubts as to its compatibility with the common market and the EEA Agreement, despite the

* Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

7 In 2008, OS generated losses of EUR 430 million. According to OS' half-year 2009 financial report, the net result for the period January to June 2009 amounted to a loss of EUR 166.6 million.

8 Commission Decision of 19 January 2009 on State aid NN 72/2008, Austrian Airlines – Rescue aid.

9 Turnover calculated in accordance with Article 5(1) of the Merger Regulation.

10 These three methodologies are explained in Commission Decision of 27 June 2007 in Case No. COMP/M.4439 Ryanair/Aer Lingus, OJ C 47, 20.2.2008, p. 9-20, paragraph 13 et seq.

commitments submitted in phase 1. The Commission therefore initiated proceedings in accordance with Article 6(1)(c) of the Merger Regulation.

- (10) LH submitted commitments on 10 July 2009 pursuant to Article 8(2) of the Merger Regulation. On 17 July 2009 and 27 July 2009, LH submitted revised versions of the commitments. Following the submission of the revised version of the commitments on 27 July 2009, the Commission launched a market test in order to gather competitors', customers' and other market participants' views on these commitments. In light of the results of the market test, LH presented a final version of commitments on 31 July 2009 ("the Commitments"). According to Article 10(2) of the Merger Regulation, decisions pursuant to Article 8(2) of the Merger Regulation shall be taken as soon as it appears that any serious doubts referred to in Article 6(1)(c) of the Merger Regulation have been removed, particularly as a result of modifications made by the undertakings concerned. Accordingly, if parties offer commitments before the Commission has completed its in-depth investigation and issued a Statement of Objections, those commitments must be sufficient to rule out the existence of serious doubts.¹¹

V. RELEVANT PRODUCT AND GEOGRAPHIC MARKETS

A. Scheduled air transport of passengers

(1) *Point of origin/point of destination ("O&D") city pairs*

- (11) The Commission has in the past defined the relevant market for scheduled passenger air transport services on the basis of the "point of origin/point of destination" (hereinafter "O&D") city-pair approach.¹² This market definition reflects the demand-side perspective whereby customers consider all possible alternatives (including different modes of transport) of travelling from a city of origin to a city of destination. On this basis, every combination of a point of origin and a point of destination is considered to be a separate market.
- (12) More particularly, with regard to network carriers, the Commission has nevertheless taken into consideration supply-side elements such as network competition between airlines based on the hub and spoke structure of traditional carriers. Although from a supply-side perspective a network carrier could in theory fly from any point of origin to any point of destination, in practice network carriers build their network and decide to fly almost exclusively on routes connecting to their hubs. Similar considerations apply for airlines that focus on point-to-point services. From a demand-side perspective, the Commission has

11 Cf. the Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004, OJ C 267, 22.10.2008, p. 1, point 18.

12 See Case No. COMP/M.5335 – Lufthansa/SN Airholding (Brussels Airlines), paragraph 12 et seq.; Commission Decision of 9 January 2009 in Case No. COMP/M.5364 – Iberia/Vueling/Clickair, OJ C 72, 26.3.2009, p. 23, paragraph 30; Commission Decision of 11 February 2004 in Case No. COMP/M.3280 – Air France/KLM, OJ C 60, 9.3.2004, p. 5, paragraph 9 et seq.; Case No. COMP/M.3770 – Lufthansa/Swiss, paragraph 12 et seq. The O&D approach was also confirmed by the European courts. See for instance CFI, Case T-177/04 easyJet v Commission, of 4 July 2006 ECR (2006), II-1913, at paragraph 56; or Case T-358/94 AirFrance v Commission, ECR (1996), II 2109.

previously considered that while networks have some importance for corporate customers whose demand is driven both by network effects and O&D considerations, individual customers are mainly concerned with finding the cheapest and most convenient connection between two cities.¹³

- (13) The market investigation has generally confirmed the O&D approach. However, some respondents, particularly traditional network carriers, indicated that the O&D approach fails to take into account the hub and spoke function of major airports and the ensuing network effects. It should also be noted that several carriers pointed out that both the point of origin and the point of destination should include all airports that are substitutable from the perspective of passengers. In the past, the Commission has considered that, in instances where multiple airports serve a single point of origin or destination, such airports may be included in the same relevant market, provided that they are indeed perceived as substitutable by travellers.¹⁴
- (14) Therefore, the effects of the proposed transaction will be assessed on the basis of various affected city-pair O&Ds while substitutable airports will be included in the respective points of origin and points of destination.

(2) *Flight substitutability from/to different airports*

- (15) Previous Commission Decisions have recognised that flights from or to airports which have overlapping catchment areas can be considered as substitutes.¹⁵ Such airport substitution has often been accepted where several airports are located in the same city;¹⁶ moreover, the Commission recently noted in the Ryanair/Aer Lingus Decision that secondary airports are likely to be *prima facie* in the same catchment area of a city if they are within 100 km or one hour of travel time of the city centre.¹⁷ However, the 100 km/one-hour criterion was viewed as only a first "proxy".¹⁸ Also, the 100 km/one-hour criterion was defined by the Commission in the specific case of routes served out of Dublin by two airlines with typical attributes of low-frills point-to-point carriers. This "rule" is thus not necessarily valid for other cases, such as routes served by two network carriers.¹⁹ Therefore, a more detailed analysis taking into consideration the characteristics of the case at hand rather than a specific proxy should be used to correctly capture the competitive constraint that flights from/to two different airports exert on each other.

13 See Case No. COMP/M.3280 – Air France/KLM.

14 See Case No. COMP/M.4439 – Ryanair/Aer Lingus.

15 Case No. COMP/M.3280 – Air France/KLM, paragraphs 24 et seq.

16 Case No. COMP/M.3280 – Air France/KLM, paragraphs 31 et seq.

17 See Case No. COMP/M.4439 – Ryanair/Aer Lingus, paragraph 99.

18 This criterion was determined on the basis of information received from 50 different airports that were asked about the "commercial arguments and material that they use for the purpose of marketing airport services towards carriers and attracting them on their tarmac", see Case No. COMP/M.4439 – Ryanair/Aer Lingus, paragraph 82.

19 The Commission for example did not use the 100km/one-hour proxy in a number of cases involving network carriers. See Case No. COMP/M.3280 – Air France/KLM, paragraphs 24-35; Case No. COMP/M.5335 – Lufthansa/SN Airholding, paragraph 54 et seq.; Case No. COMP/M.5403 – Lufthansa/BMI, paragraphs 45-47.

(16) In this case, the issue of whether flights from different airports are substitutable has been investigated in relation to the following airports in particular:

(i) Bratislava Airport ("BTS airport") – Vienna International Airport Schwechat ("VIE airport");

(ii) Frankfurt Hahn Airport ("HNN airport") – Frankfurt International Airport ("FRA airport");

(iii) Cologne-Bonn Airport ("CGN airport") – Düsseldorf International Airport ("DUS airport");

(iv) Brussels South Charleroi Airport ("CRL airport") – Brussels National Airport Zaventem ("BRU airport").

(17) For the O&D pairs at issue in this Decision, it is not always necessary to determine whether the flights from/to the different airports would be substitutable as it does not affect the competitive assessment. However, insofar as it is relevant for the assessment of this case, this issue will be discussed in greater detail in the competitive assessment in section VII.A.

(3) *Time sensitive v. non-time sensitive passengers*

(18) The Commission has previously considered that unrestricted tickets primarily purchased by so-called *time sensitive* passengers may be in a different market from restricted tickets primarily purchased by so-called *non-time sensitive* passengers.²⁰ On the one hand, time sensitive passengers tend to travel for business purposes, tend to book close to departure, require significant flexibility with their tickets (such as cost-free cancellation and modification of the time of departure), tend to pay higher prices for this flexibility and require a higher number of frequencies on a given O&D pair. On the other hand, non-time sensitive passengers travel predominantly for leisure purposes or to visit friends and relatives, book long in advance and do not require flexibility with their booking. Time sensitive passengers have therefore different preferences than non-time sensitive passengers, which is reflected in the different types of tickets targeted by airlines at these two different groups of passengers.

(19) The investigation of this case has confirmed that there exist broadly two categories of passengers with different needs and different price sensitivities, although some respondents have indicated that the distinction between time sensitive and non-time sensitive passengers is becoming less evident, as even time sensitive travellers have become increasingly price-focused and tend to prefer a restricted ticket over an unrestricted ticket if the price is lower. In fact, in light of the shift towards restricted tickets, most carriers, including low-cost carriers, offer rebooking services for restricted tickets (modifying either the date or the passenger's name) for a fee. Nevertheless, the distinction between non-time sensitive and time sensitive passengers, and hence restricted and unrestricted tickets, remains important. Time sensitive passengers still require a higher number of frequencies and specific departure and arrival times at the point of origin and destination. Finally, given the need for flexibility

²⁰ See Commission Decision of 11 August 1999 in Case No. COMP/JV.19 – KLM/Alitalia, OJ C 96, 05.04.2000, p. 5, paragraph 21; Case No. COMP/M.3280 – Air France/KLM, paragraph 19, Case No. COMP/M.3770 – Lufthansa/Swiss, paragraph 15.

and short overall travel time, time sensitive passengers appear to be less inclined to use secondary airports than non-time sensitive passengers.

- (20) Most respondents consider that time sensitive passengers need to maximise their time at destination and minimise their travel time. Hence, for the majority of respondents, this segment of passengers requires early morning and late afternoon flights (with an ideal morning departure at around 7.00 within a maximum time window between 6.30 and 8.30, and an afternoon departure time at around 18.00 or 19.00 in a maximum time window between 17.00 to 20.00). Time sensitive passengers also require a sufficient number of daily flight frequencies. At a minimum, two daily flights are required to allow for a same-day return, although a majority of respondents indicated that more than two daily flights are required for time sensitive passengers depending on the respective destination. This is also related to the type of carrier preferred by time sensitive passengers: the majority of respondents consider that time sensitive passengers prefer full service network carriers to low cost carriers. These views are shared by all of the responding groups: corporate customers, travel agents, and competing airlines.
- (21) The possibility of same-day return trips to short-haul destinations was considered important by all of the responding corporate customers (mostly in view of the time and costs saved), and the majority is even prepared to pay a slight premium in order to benefit from same-day return trips. This is also confirmed in the replies of responding travel agents.
- (22) With respect to the airport location, the majority of the responding travel agents and competitors indicate that primary airports located close to business centres and short travel distances to airports were more important for time sensitive than for non-time sensitive passengers. Corporate customers indicated that they have clear preference for minimising the travel time (and costs for the business trips) of their employees, regardless of whether they considered their employees as time sensitive or non-time sensitive.
- (23) The precise market definition can be left open for the purposes of this case.

(4) Substitutability of direct and indirect flights

- (24) The level of substitutability of indirect flights to direct flights largely depends on the duration of the flight. As a general rule, the longer the flight, the higher the likelihood that indirect flights exert a competitive constraint on direct flights.
- (25) With respect to short-haul routes, the Commission has considered in previous Decisions that indirect flights generally do not provide a competitive constraint to direct flights, absent exceptional circumstances (for instance where the direct flight does not provide the option of a convenient one-day return trip, an issue of particular importance for business travellers).²¹ The market investigation largely confirmed that for short-haul flights, indirect flights do not generally constitute a competitive alternative to direct flights, as customers indeed prefer direct flights.

21 See Commission Decision of 12 January 2001 in Case No. COMP/M.2041 – United/US Airways, and Commission Decision of 5 March 2002 in Case No. COMP/M.2672 – SAS/Spainair, OJ C 93, 18.4.2002, p. 7.

- (26) In previous Decisions, the Commission has assessed mid-haul routes,²² which are routes of more than three hours where direct flights normally do not provide the option of one-day return trips so that indirect flights are able to compete with direct flights. Due to the longer flight duration on such mid-haul routes, indirect flights seem to be more credible alternatives and some respondents indicated that indirect flights, in certain circumstances, constitute a competitive alternative. This is in line with the Commission's previous practice.²³
- (27) With respect to long-haul flights (flights over six hours covering a distance of over 5 000 km), the Commission has previously found that indirect flights constitute a competitive alternative to non-stop services under certain conditions, in particular when (a) they are marketed as connecting flights on the O&D pair in the computer reservation systems, (b) they operate on a daily basis and (c) they only result in a limited increase in travelling time (maximum 150 minutes).²⁴ The market investigation largely confirmed that indirect flights constitute a competitive alternative to direct flights when it comes to flights above six hours, and several respondents find them substitutable.

B. Air transport of cargo

- (28) With respect to air cargo transport markets, the Commission found, in previous Decisions, that the O&D approach to market definition with regard to air cargo transport is inappropriate, given that cargo is generally less time sensitive than passengers, and that cargo is usually transported by transmodal means of transport "behind" and "beyond" the origin and destination points. Accordingly, the relevant geographic market should be defined more broadly.
- (29) In line with previous Commission Decisions and the notifying party's submission, the market investigation in this case confirmed that for intra-European cargo transport, the relevant market could be defined as European-wide and would include alternative modes of transport, notably road and train transport, and to a lesser extent sea freight.²⁵
- (30) As regards intercontinental routes, the corresponding catchment areas broadly correspond to continents, at least for those continents where adequate transport infrastructure allows onward connections²⁶ (for instance by train, truck, inland waterways, etc.) such as Europe and North America. In line with previous Commission Decisions and the notifying party's submission, the market investigation in this case confirmed that the transport infrastructure across Asia is insufficient to consider the whole of Asia as a catchment area. Similarly, the transport infrastructure across the Middle East is insufficient to consider the whole of the Middle East as a catchment area. Hence, these catchment areas shall be considered on a country by country basis. Therefore, air cargo transport from Europe towards Asia and

22 Case No. COMP/M.3770 – Lufthansa/Swiss, paragraph 17, Case No. COMP/M.4439 Ryanair/Aer Lingus, paragraph 288 et seq.

23 See Case No. COMP/M.5335 – Lufthansa/SN Airholding, paragraph 45.

24 See, for example, Cases No. COMP/M.2041 – United/US Airways and No. COMP/M.2672 – SAS/Spanair.

25 See Case No. COMP/JV.19 – KLM/Alitalia and Commission Decision of 10 May 1999 in Case No. IV/M.1506 – Singapore Airlines/Rolls-Royce, OJ C 176, 22.6.1999, p. 11.

26 See Case No. COMP/M.3280 – Air France/KLM and Case No. COMP/M.3770 – Lufthansa/Swiss.

Middle East should be assessed on continent (Europe) to country basis (the respective countries in Asia and Middle East).

- (31) In addition, the market investigation confirmed that, as air cargo transport markets are inherently unidirectional due to differences in demand at each end of the route, they must be assessed on a unidirectional basis.²⁷
- (32) In previous cases, the Commission left open the question whether the market for air cargo transport should be further sub-divided according to the nature of the cargo. The Commission, however indicated that some types of goods, such as dangerous goods, may require special handling so that they can be transported only on full-freighter aircraft.²⁸ The parties argue that this market should not be further divided by category or nature of transported products. In this regard, the market investigation confirmed that a further segmentation of the market would not be necessary. In any event, for the purposes of this Decision, such further segmentation is irrelevant as the proposed transaction would not significantly impede effective competition under any alternative market definition.

C. Supply of airline seats to tour operators

- (33) The Commission has in previous Decisions noted that the wholesale supply of airline seats to tour operators is distinct from the market for supply of scheduled air transport to end customers and that such markets for wholesale supply of airline seats to tour operators are national in scope.²⁹
- (34) The notifying party largely accepts the previously applied product market definitions, but submits that a market for the provision of airline seats to tour operators would geographically comprise both Austria and Germany, noting that all major charter operators in Austria are also active in Germany, and that the competitive conditions in both Member States are converging due to the lack of language barriers, similar customer preferences and minimal price differences between Austria and Germany.
- (35) In this case, the market investigation did not contradict the Commission's previous findings on the existence of a separate market of wholesale supply of airline seats to tour operators. Concerning the geographic scope of that market, the investigation did not fully clarify whether it is national in scope or comprises both Germany and Austria. While respondents pointed to different market conditions in Austria and Germany, some respondents also underlined the proximity of the Austrian and German markets, particularly for customers living in the western parts of Austria, for which the German market seems to be a viable alternative.

27 See Commission Decision of 6 August 2008 in Case No. COMP/M.5181 – Delta Air Lines/Northwest Airlines, OJ C 281, 5.11.2008, p. 3.

28 See Case No. COMP/M.3280 – Air France/KLM.

29 See, for example, Commission Decision of 17 December 2008 in Case No. COMP/M.5141 – KLM/Martinair, OJ C 51, 4.3.2009, p. 4-8, paragraph 121 or Case No. COMP/M.4439 – RyanAir/Aer Lingus, paragraph 299.

(36) For the purposes of this case and in line with previous cases, the relevant product market is the market for wholesale supply of airline seats to tour operators, whereby it can be left open whether it is necessary to distinguish between long-haul and short-haul routes. The geographic market definition can also be left open. The proposed transaction would not significantly impede effective competition under any geographic market definition.

D. Maintenance, Repair and Overhaul ("MRO")

(37) The Commission has previously distinguished four separate markets within the MRO sector, namely line maintenance, heavy maintenance, engine maintenance and components maintenance.³⁰

(38) Although the geographic scope of the market for MRO services is usually considered as at least EEA-wide,³¹ the geographic dimension of the market for line maintenance services could be considered narrower (regional). Furthermore, in its most recent Decisions, the Commission has left the geographic market definition with regard to MRO services open.³²

(39) For the purposes of this Decision, it is not necessary to determine the geographic scope of the market for MRO services as the proposed transaction would not significantly impede effective competition under any possible product market definition.

E. In-flight catering

(40) In previous cases, the Commission found that the in-flight catering market comprises all in-flight catering services, including for short-haul and medium-haul flights, economy and business class and hot/cold meals and snacks as well as other ancillary services.³³ The Commission has more recently indicated that this market has evolved significantly in the past few years and new types of in-flight catering services have emerged.³⁴

(41) For the purposes of this Decision, it is not necessary to determine whether the in-flight catering market should be further segmented into traditional catering services and new type suppliers' services or comprises both, since the proposed transaction would not significantly impede effective competition under any possible product market definition.

30 See Case No. COMP/JV.19 – KLM/Alitalia, Case No. COMP/M.3280 – Air France/KLM and Commission Decision of 14 April 2004 in Case No. COMP/M.3374 – SR Technics/FLS Aerospace, OJ C 180, 13.7.2004, p. 9.

31 See Case No. COMP/JV.19 KLM/Alitalia.

32 See Case No. COMP/M.3280 - Air France/KLM, Case No. COMP/M.3374 – SR Technics/FLS Aerospace, Commission Decision of 16 February 2009 in Case No. COMP/M.5399 – Mubadala/Rolls Royce/JV, OJ C 58, 12.3.2009, p. 4, and Case No. COMP/M.5403 – Lufthansa/BMI.

33 See Commission Decision of 1 June 2001 in Case No. COMP/M.2190 – LGS/OFSI, OJ C 238, 24.8.2001, p. 4.

34 See Commission Decision of 19 July 2006 in Case No. COMP/M.4170 – Lufthansa Service Holding/Gate Gourmet Switzerland, OJ C 11, 17.1.2007, p. 2.

(42) The geographic market for in-flight catering is considered to be limited to the relevant airport or airport region (where several airports are located in close proximity to each other).³⁵

F. Groundhandling

(43) In previous Decisions, the Commission found that groundhandling services – ranging from passenger and baggage registration and handling to leading the aircraft on the ground as well as cleaning and refuelling the aircraft – could be divided into several distinct segments but the determination whether each segment constituted a separate relevant market was left open.³⁶ The Commission further indicated that the relevant geographic market for groundhandling services is normally restricted to the airport where the groundhandling services are provided.³⁷

(44) It is not necessary for the purposes of this Decision to determine an exact market definition, as the transaction would not significantly impede effective competition under any possible product and geographic market definition.

VI. CONCEPTUAL FRAMEWORK FOR THE ASSESSMENT OF THE PROPOSED TRANSACTION

A. Introduction

(45) Prior to the notification of the proposed transaction, the Commission received a notification of a transaction on 26 November 2008 according to which LH intended to acquire sole control of SN Airholding SA/NV, the holding company of SN.³⁸ Having initiated proceedings in that case pursuant to Article 6(1)(c) of the Merger Regulation on 26 January 2009, the Commission authorised the acquisition of SN by LH subject to conditions on 22 June 2009.

(46) Moreover, on 3 April 2009, the Commission also received notification of a transaction whereby LH intended to acquire sole control of BMI.³⁹ The Commission approved this transaction on 14 May 2009 without conditions.

(47) Closing of LH's transactions with SN and BMI occurred on 24 June 2009 and 1 July 2009, respectively, and they were subsequently implemented. Both SN and BMI are therefore treated as subsidiaries of LH.

35 See Case No. COMP/M.4170 – Lufthansa Service Holding/Gate Gourmet Switzerland.

36 See Commission Decision of 11 January 2001 in Case No. COMP/M.2254 — Aviapartner/Maersk/Novia, OJ C 027, 27.1.2001, p. 60, and Commission Decision in Case No. IV/M.1913 – Lufthansa/Menzies/LGS/JV, OJ C 127, 27.4.2001, p. 11.

37 See Case No. COMP/M.1913 – Lufthansa/Menzies/LGS/JV.

38 Case No. COMP/M.5335 – Lufthansa/SN Airholding.

39 Case No. COMP/M.5403 – Lufthansa/BMI.

- (48) Prior to assessing the impact of the transaction on the relevant markets, the conceptual framework for the assessment of the transaction must be determined. In this respect, that transaction raises two conceptual issues.
- (49) The first issue concerns the treatment of LH's and OS's alliance partners for the purposes of both the determination of affected markets and the competitive assessment of the transaction.
- (50) The second issue relates to the determination of the relevant counterfactual for the assessment of the effects of the transaction with respect to the routes where LH (including LX, 4U, SN and BMI) and OS co-operate with each other.

B. Treatment of alliance partners

- (51) Both LH and OS are members of the Star Alliance. The notifying party submits that it would be inappropriate to treat any of its alliance partners as if they were parties to the transaction. First, there would be no legal basis for such a treatment as the Merger Regulation does not provide for an assessment of "spill-over effects" between companies that remain independent. Second, alliance relationships in question would not change the merging parties' incentives to compete because both LH and OS are already part of the same alliance pre-merger and because the overlap routes between OS's and LH's alliance partners are not covered by the respective co-operation agreements. In addition, LH's agreements would not automatically extend to OS and vice versa.

(1) Determination of affected markets

- (52) With respect to the determination of affected markets, horizontally affected markets consist of relevant product markets where the parties to the proposed transaction are engaged in business activities and hence on which the transaction produces merger-specific effects.⁴⁰ Accordingly, product markets where one party and a third party's activities overlap are in principle outside of the scope of the investigation as the transaction is not likely to produce merger-specific effects on these markets. However, a transaction may also have a significant impact on other markets in which case the effects on competition on such market should also be assessed.
- (53) In the airline sector, this is in particular the case where a factual inquiry indicates, as a direct result of the merger or as its foreseeable consequence, that close links are to be established between one merging party and a close partner of the other merging party, as was the case between KLM and Alitalia in the Air France/KLM merger case for instance.⁴¹ In such cases, the incentives to compete would indeed be altered as a result of the merger.

40 See paragraph III (a) in Annex I to the Commission Regulation (EC) 802/2004 of 7 April 2004 implementing Council Regulation (EC) 139/2004 on the control of concentrations between undertakings, OJ L 133, 30.4.2004, p. 1.

41 Case No. COMP/M.3280 – Air France/KLM, paragraph 47.

- (54) In this case, according to the notifying party, LH's co-operation agreements with SAS, LOT, United Airlines and Air Canada will not be extended to OS as the agreements do not provide for such an automatic extension unless they are renegotiated. Similarly, the parties have confirmed that none of the existing agreements between OS and other Star Alliance partners⁴² will be automatically extended to LH. As a result, no merger specific spill-over effects are expected to arise in this respect.
- (55) LH's and OS' alliance partners should not be taken into account for the determination of affected markets.

(2) *Competitive assessment*

- (56) With respect to the competitive analysis on the affected markets, the relationship between the airlines and for the subsequent impact on their incentive to compete post-merger ought to be assessed on a route-by-route basis. If it is found that a merging party and a third party have a lower incentive to compete as a consequence of the transaction, this fact must be taken into account in the assessment.

C. Relevant counterfactual for the routes on which the parties co-operate

- (57) LH and OS already co-operate in different ways pre-merger in varying degrees. In particular, the following forms of co-operation between the parties can be identified: (i) a cost and revenue sharing joint venture between LH and OS on all routes between Germany and Austria; (ii) a world-wide bilateral co-operation agreement between LH and OS; (iii) a code-share agreement between LX and OS on Switzerland-Austria routes; and (iv) a code-share agreement between BMI and OS on the Vienna-London route.
- (58) The notifying party submits that such pre-merger co-operation should constitute the relevant counterfactual for the assessment of the transaction. The notifying party further argues that, as a result of the existing co-operation agreements, the parties cannot be considered competitors, particularly as far as Austria-Germany routes are concerned, and therefore the transaction cannot result in any decrease in competition between LH and OS. The notifying party further submits that the Commission had previously found in its Lufthansa/Eurowings and Lufthansa/Swiss Decisions⁴³ that LH and OS did not compete on a global level. In those Decisions, the overlaps between LH, OS and 4U and between LH, OS and LX, respectively, had already been analysed and addressed, and therefore the present transaction could not be found to significantly impede effective competition on these routes.
- (59) Pursuant to paragraph 9 of the Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings ("the Horizontal Merger Guidelines") "[i]n assessing the competitive effects of a merger, the Commission

42 None of these agreements goes beyond a bilateral alliance and/or code-share agreement. In particular, none of them even comes close to a profit sharing joint venture such as that existing between LH and OS with respect to the Germany-Austria routes.

43 See Case No. COMP/M.3770 – Lufthansa/Swiss and Commission Decision of 22 December 2005 in Case No. COMP/M.3940 – Lufthansa/Eurowings, OJ C 18, 25.1.2006, p. 22.

compares the competitive conditions that would result from the notified merger with the conditions that would have prevailed without the merger. In most cases the competitive conditions existing at the time of the merger constitute the relevant comparison for evaluating the effects of a merger. However, in some circumstances, the Commission may take into account future changes to the market that can reasonably be predicted."⁴⁴

(60) In this case it appears, on the basis of the evidence collected in the investigation and in light of the Austrian Government's fundamental decision to find a private investor for OS that absent the acquisition by LH, OS would most likely have been acquired by Air France-KLM in which case the co-operation between OS and LH would have been terminated.

(61) On that basis and on the basis of the evidence available to the Commission, the relevant counterfactual scenarios for the assessment of the effects of the notified concentration on competition are:

(1) the pre-merger state of co-operation between the parties; or

(2) the most likely foreseeable future development in the event that the proposed acquisition of OS by LH does not take place, namely where OS is acquired by another airline, more specifically by Air France-KLM. In this scenario, OS would terminate its pre-merger co-operation with LH as well as its Star Alliance membership and would join Sky Team (the alliance to which Air France-KLM belongs).

(62) Both the counterfactual scenario of pre-merger co-operation and the counterfactual scenario of acquisition of OS by Air France-KLM are explained in paragraphs (63) - (105) in more detail.

(1) Counterfactual scenario of pre-merger co-operation

(63) As mentioned in paragraph (57), the following forms of co-operation between the parties can be distinguished: (a) a cost and revenue sharing joint venture between LH and OS on all routes between Germany and Austria; (b) a world-wide bilateral co-operation agreement between LH and OS and (c) a code-share agreement between BMI and OS on the Vienna-London route. In addition, the Commission has previously analysed and assessed (d) the overlaps between LH, OS and 4U in its Lufthansa/Eurowings Decision; and (e) the overlaps between LH, OS and LX in its Lufthansa/Swiss Decision, and where LX and OS currently co-operate under a code-share agreement on Swiss-Austrian routes.

⁴⁴ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31, 05.02.2004, p. 5-18.

a. Cost and revenue sharing joint venture between the parties on all routes between Germany and Austria

(i) Description of the pre-merger situation

- (64) The cost and revenue sharing joint venture provides that the parties pool revenues and costs for all routes between Germany and Austria, and coordinate on fares and other matters, including marketing and branding. Under the joint venture agreement, the parties established a joint route system (specifying which services are operated by which party), joint fare structures and flight schedules. Fares sold in Germany are set by LH, while fares sold in Austria are set by OS. The parties also entered into code-share agreements on all routes between Germany and Austria. On some routes, they both operate their own aircraft and code-share on the other party's flights.⁴⁵ On others, one of the parties operates its own aircrafts, whereas the other party is merely a marketing carrier with no operations of its own.⁴⁶
- (65) The parties initially notified the joint venture agreement to the Commission under Article 81(3) of the Treaty in 1999.⁴⁷ The Commission found that the agreement restricted actual and potential competition between LH and OS within the meaning of Article 81(1) of the Treaty on all routes between Austria and Germany,⁴⁸ but that it also contributed, under certain conditions, to economic progress within the meaning of Article 81(3) of the Treaty. In 2002, the Commission therefore exempted the joint venture agreement pursuant to Article 81(3) of the Treaty until December 2005, subject to commitments aimed at ensuring that consumers would share in the benefits of the expected cost savings, that the restrictions of competition did not go beyond what was necessary and that competitors would be present on the market. The remedies essentially consisted of a commitment to make slots available to a new entrant for any Austria-Germany route chosen by it up to a maximum of 40% of the slots that LH and OS operated on the route in question.⁴⁹
- (66) After the expiry of the exemption decision in 2005, the parties continued to co-operate under the joint venture agreement. Under the new procedural rules for the application of Article 81

45 This currently occurs on six routes: Vienna-Berlin, Vienna-Düsseldorf, Vienna-Frankfurt, Vienna-Hamburg, Vienna-Munich and Vienna-Stuttgart.

46 OS currently acts as an operating carrier on ten routes: Graz-Düsseldorf; Innsbruck-Frankfurt, Linz-Düsseldorf, Salzburg-Düsseldorf, Salzburg-Frankfurt, Vienna-Cologne, Vienna-Dresden, Vienna-Hannover, Vienna-Leipzig and Graz-Stuttgart. LH is an operating carrier on six routes: Graz to Frankfurt and Munich; Innsbruck-Hamburg, Klagenfurt-Munich, Linz to Frankfurt and Munich. OS ceased its operations on the route Vienna-Nuremberg in March 2009.

47 See Case No. IV/37.730 – Austrian Airlines Österreichische Luftverkehrs AG/Deutsche LUFTHANSA AG, Exemption with condition/obligation decision, Web publication of non-confidential version, OJ L 242, 10.09.2002, p. 25-43; Final version of Art. 19(3) notice, OJ C 356, 14.12.2001, p. 5-8; and Final version of Art. 19(3) notice, OJ C 193, 11.07.2000, p. 7-8.

48 In 1999, there were 33 routes between Austria and Germany. Only one route, namely the route Vienna-Friedrichshafen, was not operated by either LH or OS, but by Rheintalflug. Rheintalflug was taken over by OS in 2001.

49 Moreover, they included fare control remedies as well as capacity freezes in relation to those Austria-Germany routes on which new entrants would start operating.

of the Treaty, notably Regulation 1/2003,⁵⁰ it was not possible for the parties to apply for a new exemption. However, the parties carried out a self-assessment of their co-operation under the joint venture agreement with a view to complying with Article 81 of the Treaty.⁵¹

(ii) Impact of the transaction on the pre-merger situation

- (67) As previously stated, the notifying party submits that, as a result of their co-operation, LH and OS cannot be considered as competitors on any Austria-Germany routes, and that the proposed transaction can therefore not result in any lessening of competition between them.
- (68) However, even where a pre-merger situation that effectively limits or eliminates competition between the parties constitutes the relevant counterfactual, this does not automatically mean that the proposed transaction cannot lead to a significant impediment to effective competition. Indeed, where extensive pre-merger co-operation has been replaced by a permanent structural link, the Commission has analysed the specific effects of the creation of that permanent structural link on a route by route basis (in particular on hub-to-hub routes) in order to assess the extent to which competition may be affected post-merger.⁵²
- (69) Whether or not the creation of a permanent structural link in this case would lead to a significant impediment of effective competition in the form of elimination of actual or potential competition will therefore be assessed in the competitive assessment of the individual routes at issue in section VII.

b. World-wide bilateral agreement between LH and OS

(i) Description of the pre-merger situation

- (70) The world-wide bilateral agreement between LH and OS provides for joint network planning, a joint pricing policy and joint budgeting. However, each party is responsible for its own route and network development, bilateral co-operation with other carriers and sales and marketing activities. LH submits that LH and OS do not discuss prices on a regular basis and that the degree of co-operation varies from destination to destination. Nevertheless, LH claims that the scope of LH and OS' world-wide co-operation is already so extensive that they cannot be perceived as competitors for the purpose of establishing the proper counterfactual.
- (71) In 2002, the world-wide bilateral agreement between LH and OS was exempted by the Commission under Article 81(3) of the Treaty until December 2005, but without commitments on the part of LH or OS. In its exemption Decision, the Commission found that, except as regards traffic between Austria and Germany, the networks of LH and OS largely complemented one another. While OS focused on medium-haul routes in Europe, especially in Central and Eastern Europe, LH focused much more on long-haul services. The

50 Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, O.J. L 1, 04.01.2003, p.1.

51 The parties have provided the Commission with a copy of the self-assessment which seems to date from 2006.

52 See also Case No. COMP/M.5181 – Delta Air Lines /Northwest Airlines, paragraphs 32 and 33.

Commission found that the combination of these complementary networks resulted in important synergistic effects and attractive connections for consumers and that the establishment of a more comprehensive European network would produce cost savings for LH and OS through an increase in traffic throughout the network, improved network connection, better planning of frequencies, a higher load factor and improved organisation of sales systems and ground handling services.

(ii) Impact of the transaction on the pre-merger situation

- (72) As will be demonstrated in the competitive assessment in section VII, the issue whether the scope of LH's and OS' world-wide co-operation is already so extensive that they cannot be perceived as competitors for the purpose of establishing the proper counterfactual can be left open, since the proposed concentration would not significantly impede effective competition on any routes outside Germany and Austria that fall into this worldwide co-operation, irrespective of the precise counterfactual scenario.

c. Code-sharing between BMI and OS on the Vienna-London route

(i) Description of the pre-merger situation

- (73) OS has standard free-flow code-share agreements with BMI with regard to the Vienna-London route.
- (74) The notifying party submits that under such a code-share agreement, the marketing carrier does not have its own reserved inventory on the aircraft in question, but has real-time electronic access to the operating carrier's seat inventory. This means that prior to confirming a booking on the flight in question, the marketing carrier must ascertain whether a seat in the appropriate category is still available. The operating carrier retains inventory control in order to ensure that the marketing carrier does not fill the flight with low-yield traffic (that is, cheap restricted economy tickets for O&D passengers) when such bookings would squeeze out higher-yield passengers the operating carrier could otherwise attract (namely O&D or connecting business class passengers). This is achieved by a process of "mapping" the carriers' respective fare classes and providing the marketing carrier access to seats in the relevant corresponding fare category on a "first come, first serve" basis. Thus, the marketing carrier is offered equal treatment in terms of accessing seats on a flight, without however undermining the operating carrier's yield management system.
- (75) LH argues that due to OS' control over inventory available to BMI, competition between the parties on this route is limited and, as a result, the proposed concentration would not significantly impede effective competition on this route.

(ii) Impact of the transaction on the pre-merger co-operation

- (76) As will be shown in the competitive assessment in section VII, the question whether or not OS and BMI can be perceived as competitors under the current code-share agreement can be

left open, since the proposed concentration would not significantly impede effective competition on this route, irrespective of the precise counterfactual scenario.

d. Overlap routes between OS and Eurowings, where the Commission found in the Lufthansa/Eurowings merger Decision that LH and OS do not compete

(i) Description of the pre-merger situation

(77) Eurowings was not yet a subsidiary of LH at the time of the exemption Decision and was therefore not covered by the exemption. Moreover, Eurowings does not form part of any of the existing co-operation agreements between OS and LH nor does Eurowings (or its subsidiary 4U) have its own co-operation agreement with OS. The Commission found in its Lufthansa/Eurowings Decision that LH and OS did not compete on a global level. As a consequence, the Commission assessed the effects of a combination of Eurowings and LH, whereby it did not consider OS as a competitor to LH, and authorised the acquisition of Eurowings by LH subject only to slot release commitments with respect to the Vienna-Cologne and Vienna-Stuttgart routes, amongst others, where it considered that the transaction would eliminate Eurowings as LH's only competitor.

(78) As regards overlaps between OS and Eurowings, the notifying party argues that these overlaps have already been analysed and addressed in the aforementioned merger Decision and that, therefore, these overlaps cannot be considered as affected markets or, in any event, the transaction cannot be found to significantly impede effective competition on these routes.

(ii) Impact of the transaction on the pre-merger situation

(79) It should be noted that OS was not a formal party to the concentration between LH and Eurowings which were the subject of the previous Decisions nor did the previous Decision relate to the creation of a permanent structural link between OS on the one hand and LH or Eurowings on the other hand. Rather, the overlaps between Eurowings and OS were included in the competitive assessment of this previous Decision because of the extensive contractual co-operation that already existed between LH and OS at the time. Therefore, insofar as the transaction effectively eliminates actual or potential competition between Eurowings and OS, there is no reason why these overlaps could not be subject to review in this case.

(80) In this respect, it is important to note that Eurowings' activities do not in any way form part of the joint venture between LH and OS with respect to the Austria-Germany routes. The extent to which the present transaction eliminates actual competition between OS and 4U will therefore be examined in the competitive assessment in section VII.

e. *Overlap routes between OS and LX where the Commission found in the Lufthansa/Swiss merger Decision that LH and OS do not compete and where LX and OS currently cooperate under a code-share agreement on Swiss-Austrian routes*

(i) *Description of the pre-merger situation*

(81) Similarly, LX did not belong to LH at the time of the 2002 exemption decision and this cooperation was therefore not covered by the exemption of the world-wide bilateral agreement between LH and OS. However, the overlap between LX and OS has also already been subject of the Lufthansa/Swiss Decision where the Commission found that LH and OS could not be considered as competitors on a global level.⁵³ As a consequence, the Commission assessed the effects of a combination of LX and LH, whereby OS was not considered as a competitor to LH, and authorised the acquisition of LX by LH subject only to slot release commitments on several routes such as the Zurich-Vienna route.

(82) With regard to these overlaps, the notifying party argues that they have already been analysed and addressed in the merger Decision mentioned in the preceding paragraph and that, therefore, these overlaps cannot be considered as affected markets or, in any event, the transaction cannot be found to significantly impede effective competition on these routes. Furthermore, with respect to the code-share agreement between LX and OS in general, LH argues that due to OS' control over inventory available to LX on the Vienna-Zurich, Vienna-Geneva and Vienna-Basle routes and LX's control over inventory available to OS on the Vienna-Zurich route, competition between the parties is limited and, as a result, the transaction would not raise competition concerns with respect to these three routes.

(ii) *Impact of the transaction compared to the pre-merger situation*

(83) It should be noted that after the Commission's Lufthansa/Swiss Decision, LX and OS concluded a standard free-flow code-share agreement relating to all Austria-Switzerland routes. This represents a significant change on those routes, which was not assessed in that Commission Decision. In particular, this code-share agreement has allowed LX to gain a marketing presence on several of these markets, which would make it easier for LX to enter those routes.⁵⁴

(84) As will be shown in the competitive assessment in section VII, the establishment of the precise counterfactual can ultimately be left open since the proposed concentration would not significantly impede effective competition on any route between Austria and Switzerland.

(2) *Acquisition of OS by another airline, more specifically by Air France-KLM as relevant counterfactual for the assessment of the proposed transaction*

⁵³ See Case No. COMP/M.3770 – Lufthansa/Swiss.

⁵⁴ The assessment of the Vienna-Basel and Vienna-Geneva routes in the Lufthansa/Swiss Decision was based on the fact that LX did not provide direct services on the Vienna-Geneva route and that it had withdrawn from the Vienna-Basel route before the Decision (see paragraphs 90 et seq. of that Decision).

- (85) As indicated in paragraph (61), it appears likely that, absent the acquisition by LH, OS would have been acquired by another airline, namely Air France-KLM. Therefore, the most likely foreseeable alternative counterfactual to the pre-merger situation for the assessment of the transaction, would be a foreseeable situation whereby OS is acquired by another airline, more specifically by Air France-KLM. As a consequence of such a transaction, OS would terminate its existing agreements with LH as well as its Star Alliance membership to join another alliance, namely the SkyTeam Alliance, to which Air France-KLM belongs. As explained in more detail in section VII, OS would then operate several routes in competition with LH, instead of operating them in co-operation with LH, as it currently does (hereinafter the "Air France-KLM counterfactual").
- (86) In light of the fundamental political decision to privatise OS, the bidding process for the privatisation of OS would most likely have been prolonged and negotiations with other interested parties would have continued in case LH would not have made an offer during the initially foreseen deadline for the privatisation process. The evidence available to the Commission⁵⁵ suggests that the most likely alternative to an acquisition of OS by LH would have been the acquisition of OS by another airline, more specifically by Air France-KLM. As a consequence of this foreseeable scenario, OS would terminate its existing agreements with LH as well as its Star Alliance membership to join the SkyTeam Alliance, to which Air France-KLM belongs.
- (87) Based on the information available to the Commission, it appears that OS would not be financially viable in the long term without drastic recapitalisation, asset sales and restructuring, but that such drastic restructuring and downsizing would likely entail serious risks and significant negative consequences. Therefore, the privatisation of OS was considered the preferred option.⁵⁶ As a result, on 12 August 2008, the Austrian Government issued a privatization mandate ("Privatisierungsauftrag") pursuant to which ÖIAG was authorised to dispose of all of its shares in Austrian Airlines.
- (88) ÖIAG published notices in Austrian and international newspapers on 13 August 2008 inviting potential investors to express their interest on an acquisition of ÖIAG's stake in OS until 24 August 2008. On 28 August 2008 potential investors were notified that an acquisition concept including information on the bidder, a strategic concept on the future of OS, a proposal for the transaction structure, information on the proposed financing and certain additional information should be submitted by 12 September 2008. Only three acquisition concepts were received (namely Air France-KLM, LH and Siberian Airways). On 16 September 2008 the three remaining bidders were invited to submit their final offers excluding the purchase price by 21 October 2008 and their final offer including the purchase price by 24 October 2008.
- (89) On 21 October 2008, LH was the only bidder to submit an offer including contract and strategic concept, excluding price. On 24 October 2008 LH submitted a binding offer stating a negative purchase price for OS. While Siberian Airways submitted an explicitly non-

55 See in particular the documents quoted in footnotes 56 and 63.

56 See [various OS internal documents]*.

binding offer on 24 October 2008⁵⁷, it does not appear to be or have been a serious candidate for the purchase of OS, in particular since, for the time being, it is (apart from a few direct international connections) focused on flights to Russian destinations and destinations in the Commonwealth of Independent States with a large domestic route network in Russia and its main bases and hubs in Russia. Air France-KLM did not make any offer, binding or non-binding. According to Air France-KLM, the two main reasons why it decided to not submit an offer by 21 October 2008 were that (i) it had come to the conclusion that there was no viable financial offer meeting the conditions imposed by ÖIAG in the privatisation process, and that (ii) Air France-KLM was not provided with all the necessary information that would have enabled it to undertake an in-depth and definitive evaluation of OS' financial situation.⁵⁸

- (90) Following LH's offer, the Austrian authorities prolonged ÖIAG's privatisation order until 31 December 2008 and authorized ÖIAG to grant supporting measures to OS of up to EUR 500 million.⁵⁹
- (91) Despite the fact that Air France-KLM did not formally submit any offer in the context of the privatisation of OS, the Commission's investigation has shown that Air France-KLM would be the most likely alternative buyer. In this respect, it should be noted that, when Air France-KLM became aware of the supporting measures referred to in the preceding paragraph, it once again expressed its interest in continuing the negotiations for a possible purchase of OS by informing ÖIAG that it was prepared to consider submitting a final offer to OS (*"We are writing to you today to confirm that Air France-KLM remains keen to invest in Austrian and to express our willingness to continue to participate to the current privatisation process as the conditions seem to have become materially different from the ones envisaged both in terms of acceptable equity price, amount of debt burden and acceptable date for a fully binding offer"*).⁶⁰
- (92) Internal LH documents seemingly based on OS' business plan, also indicate that LH seriously considered a scenario whereby OS would be acquired by Air France-KLM.⁶¹ It can be assumed that such an alternative scenario would be less profitable for Air France-KLM than for LH since OS would lose revenues from the joint venture with LH and would need to pay alliance exit fees. Nevertheless, OS' current financial situation appears to be such that it would probably be very difficult, if not impossible, for OS to remain independent in the long term and to continue operating on a stand-alone basis without external support.
- (93) Indeed, LH assumes on the basis of OS' financial statements dated October 2008 that, without any external support, OS would be insolvent in the first half 2009.⁶² If OS were to

57 See the article entitled "Zwei Angebote zu AUA: Lufthansa prozesskonform, S7 in Prüfung" at www.kleinezeitung.at/nachrichten/wirtschaft/aua/1605399/index.do.

58 See reply to request for information to Air France-KLM of 18 June 2008, point 1.

59 Letter of the Bundesministerium für Finanzen of 29 October 2008 containing the respective request to the Austrian government.

60 See reply to request for information to Air France-KLM of 18 June 2008, point 2.

61 LH's document entitled [...]*

62 LH's document entitled [...]*.

remain independent it is likely that Austria, as the largest and sole controlling shareholder would have to recapitalise and restructure the company.

- (94) OS also assessed different options and an acquisition by Air France-KLM appeared to be the most credible foreseeable alternative to an acquisition by LH⁶³ and, in particular, the preferred option in comparison to a scenario whereby OS would remain independent, drastically restructure and downsize. More specifically, OS internal documents refer to the option of privatising and selling OS as "Plan A", whereas the option of OS remaining independent, restructuring and downsizing is referred to as "Plan B".⁶⁴ This can be further illustrated by the fact that OS estimates that a stand-alone OS operation would require additional funding of EUR 1.2 billion until 2011.⁶⁵ This amount significantly exceeds the amount of measures to be granted by ÖIAG in support of the privatization of OS by way of a sale to LH.
- (95) In addition, internal documents of the various parties involved in the privatisation process show a clear political will to privatise OS.
- (96) Finally, if LH would not have submitted an offer, the bidding process for the privatisation of OS would have been prolonged and negotiations with other interested parties would have continued. Air France-KLM was also the most likely alternative purchaser in the bidding process organised in autumn 2008 with a view to privatising OS.
- (97) In this respect, it should be recalled that Air France-KLM refrained from making a final binding offer by 21 October 2008 because of OS's financial situation. When it subsequently became clear that the Austrian authorities would underwrite a EUR 500 million capital increase in OS, however, Air France-KLM re-expressed its interest in acquiring OS under these changed circumstances, but ÖIAG stated that it was obliged to follow the established sales process and refused to re-enter into negotiations with Air France-KLM and, instead, proceeded with the sale of OS to LH.⁶⁶
- (98) On the basis of the evidence available to the Commission, it therefore seems that, if LH would not have submitted an offer, the bidding process for the privatisation of OS would have been prolonged and negotiations with other interested parties would have continued, and the acquisition of OS by Air France-KLM would likely have been the most likely outcome.

63 See [various OS internal documents]* From these documents it follows also clearly that an acquisition of OS by Air France-KLM would necessarily imply that OS would need to exit Star Alliance and join SkyTeam.

64 See in particular the documents quoted in footnotes 56 and 63.

65 OS internal document [...]*

66 See letters of Air France/KLM to Merrill Lynch of 21 October 2008 and 5 November 2008; see further some press articles reporting on the matter, such as the articles entitled "Air France-KLM buhlt um AUA und Alitalia: Wird fristgerecht ihr Angebot einreichen" of 9 September 2008 and "Air France-KLM will wieder ins AUA Rennen: Die ÖIAG lehnt einen erneuten Einstieg ab" at www.news.at, the articles entitled "Airline-Übernahme, Air France zieht bei AUA zurück" of 22 October 2008 and "Übernahmepoker um Austrian Airlines, Air France fühlt sich benachteiligt" of 21 November 2008 at www.handelsblatt.com/unternehmen, and the articles entitled "AUA: Air France/KLM hat die Nase vorn" of 7 October 2008 and "AUA-Verkauf: Air France will wieder mitbieten" of 7 November 2008 at www.diepresse.com.

- (99) Based on the evidence available to the Commission, the conclusion would have been no different today compared to when the bidding process took place. Indeed, while the economic environment since the end of the bidding process might have had a negative impact on the airline industry as a whole, including Air France-KLM and OS, it is considered that the main reasons that motivated Air France-KLM to acquire OS in the course of the bidding process are still valid today.⁶⁷ Furthermore, adverse economic circumstances in fact reinforce the conclusion reached in paragraph (94) that OS would not be financially viable in the long term without drastic recapitalisation, asset sales and restructuring, that such drastic restructuring and downsizing would likely entail serious risks and significant negative consequences and that the privatisation of OS would therefore also represent the preferred option in the medium- and long-term.
- (100) The fact that the Air France-KLM counterfactual is the most likely future development, if the proposed acquisition of OS by LH were to fail, can be further illustrated by the parties' internal documents which show that both parties seriously considered an alternative acquisition of OS by Air France-KLM. In response to several requests for information, LH did not submit any internal documents in which purchasers other than Air France-KLM are considered. In OS's documents, alternative purchasers are discussed, but LH and Air France-KLM are considered the two preferred options.
- (101) Therefore, the acquisition by Air France-KLM is the most likely foreseeable alternative counterfactual to the pre-merger situation for the assessment of the transaction.
- (102) Taking this counterfactual scenario as a basis for the competitive assessment, the transaction raises serious doubts as to its compatibility with the common market because it may significantly impede effective competition, insofar as the transaction eliminates actual or, at least potential competition between the parties on a number of routes, as set out in more detail in the competitive assessment in section VII, in the foreseeable situation whereby OS would be acquired by Air France-KLM and, as a result, OS would terminate its existing co-operation agreements with LH, exit Star Alliance and join SkyTeam. In particular, as a result of the foreseeable acquisition of OS by Air France-KLM and the subsequent termination of the co-operation agreements between LH and OS, OS and LH would have been actual or potential competitors on the relevant routes.
- (103) In this respect, LH internal documents indicate that LH examined the possible risks of OS terminating the existing co-operation agreements and joining SkyTeam and concluded that, in that foreseeable scenario, LH would need to add frequencies and new routes to its current network ⁶⁸ [...]*. In the relevant internal documents, LH noted in particular that it would need to add [...]* weekly frequencies to the Vienna-Munich and Vienna-Frankfurt routes. The extent to which actual or potential competition between LX and OS on these routes will be eliminated post-merger as compared to the alternative acquisition of OS by Air-France-KLM is therefore assessed in this Decision.

67 In particular, it follows from an analysis of the network of Air France/KLM and the location of its hubs Paris (CDG) and Amsterdam (AMS) that by purchasing OS Air France/KLM would considerably extend its market position towards destinations in Central and Eastern Europe ("CEE"). [...]*.

68 LH's document entitled [...]*.

(104) In contrast, as regards all routes where the transaction would not significantly impede effective competition, the establishment of the proper counterfactual can be left open.

(3) *Conclusion*

(105) The relevant affected markets for air transport of passengers will be assessed both under the counterfactual of the pre-merger situation and under the foreseeable situation whereby OS would be acquired by Air France-KLM, terminate its existing agreements with LH, exit Star Alliance and join SkyTeam where such an assessment is relevant to the question of whether the transaction leads to a significant impediment of effective competition. Ultimately, however, the question as to which of these two counterfactual scenarios constitutes the relevant counterfactual for the assessment of the transaction can be left open, as explained in more detail in the competitive assessment in section VII.

(106) In the assessment in this Decision, the Commission does not take a position on the compatibility of the existing co-operation agreements with Article 81 of the Treaty. The Commission cannot be required to accept pre-merger co-operation between the parties that is contrary to Article 81 of the Treaty as a counterfactual.⁶⁹ As the competition concerns identified in this case will be eliminated as a result of the Commitments offered by the parties, it is not necessary for the purposes of this Decision to further discuss the compatibility of the pre-merger co-operation between the parties with Article 81 of the Treaty.

VII. COMPETITIVE ASSESSMENT

A. Scheduled passenger air transport services

(107) The transaction gives rise to a number of horizontal overlaps that can be grouped in several categories:

- (i) 23 short-haul routes between Austria and Germany, which are served under the parties' cost and profit sharing joint venture;
- (ii) three short-haul routes between Austria and Switzerland;
- (iii) one short-haul route between Austria and Kingdom of Belgium;
- (iv) one short-haul route between Austria and the United Kingdom of Britain and Northern Ireland;

⁶⁹ In the context of merger control, if the illegality of a pre-merger agreement between the parties could not be taken into account, the parties could argue that there would only be a small reduction or even no reduction of competition as a result of the merger. A merger decision in such circumstances would effectively incorporate and perpetuate the pre-merger illegality forever, since mergers that are approved under the Merger Regulation are no longer challengeable under Article 81 of the Treaty, see paragraph 42 and footnote 30 of the Commission's decision in Case No. COMP/M.5403 – Lufthansa/BMI as well as paragraph 263 and footnote 265 of the Commission's decision in Case No. COMP/M.5335 – Lufthansa/SN Airholding.

(v) "direct-indirect overlaps" (namely routes where one party offers a direct connection while the other party offers an indirect connection); and

(vi) "indirect-indirect overlaps" (namely routes where both parties only offer indirect services).

(1) Routes between Austria and Germany

a. The Vienna-Stuttgart route

(108) Approximately [300 000 – 350 000]* passengers travel on the Vienna-Stuttgart route ("VIE-STR") annually, of which approximately [250 000 - 300 000]* passengers fly from point to point ("O&D" passengers), while the remaining are transfer passengers. According to surveys conducted by the parties, up to [50-60]*% of the passengers on the VIE-STR route travel for business purposes.

(109) VIE-STR is served by both OS (through Tyrolean) and LH (through Contact Air and City Line). In addition, 4U, which is controlled by LH, operates VIE-STR. LH operates three daily frequencies on weekdays on VIE-STR (22 weekly frequencies), on which OS code-shares. OS (through Tyrolean) operates three daily frequencies (18 weekly frequencies), on which LH code-shares. 4U operates two to three daily frequencies (16 weekly frequencies). Currently no other airline operates this route. Air Berlin discontinued its operations on VIE-STR in May 2008. The notifying party submits that, as regards inter-modal competition, train services do not represent a significant constraint on air travel on this route.

(110) As regards airport substitutability, the parties maintain that VIE airport and BTS airport should be considered as substitutable. BTS airport is situated 87 km from Vienna city centre, which corresponds to a driving time of more than 60 minutes by car and 75-95 minutes by bus. The parties' contention that BTS airport would be substitutable for VIE airport has not been confirmed by the market investigation in this case. However, given that no airline is currently serving Stuttgart airport ("STR airport") out of BTS airport, it is not necessary to determine whether BTS airport is substitutable with VIE airport for the purpose of serving STR airport.

(111) The table below illustrates the market structure of VIE-STR during the IATA Summer season 2008 and the Winter season 2008/2009.

Airline	SS 08 figures on VIE-STR		WS 08/09 figures on VIE-STR	
	Time Sensitive	All passengers	Time Sensitive	All passengers
LH	[10-20]*%	[10-20]*%	[10-20]*%	[10-20]*%
OS	[10-20]*%	[10-20]*%	[5-10]*%	[10-20]*%
4U	[60-70]*%	[60-70]*%	[70-80]*%	[70-80]*%
Combined	100%	100%	100%	100%

Source: MIDT data provided by the notifying party. Unless indicated otherwise, all market shares mentioned hereinafter are MIDT data (or estimates on the basis of MIDT data) provided by the notifying party.⁷⁰

- (112) VIE-STR was subject to commitments under the Commission's 2002 exemption Decision concerning the joint venture agreement as described in paragraphs (65) et seq. Furthermore, in its Lufthansa/Eurowings Decision, the Commission approved LH's acquisition of 4U subject to commitments on VIE-STR. The commitments included slot releases at VIE airport and STR airport within 30 minutes from the initial request by the new entrant and other ancillary remedies. These commitments are still in place.
- (113) The parties submit that due to their co-operation under the joint venture agreement, LH and OS do not currently compete on this route. They further submit that the overlaps between OS and 4U should not form part of the Commission's assessment as they have already been analysed in the Lufthansa/Eurowings case.
- (114) The Commission found in the Lufthansa/Eurowings case that LH and OS did not compete on VIE-STR because of their joint venture agreement. As a consequence, the Commission assessed the effects of a combination of Eurowings and LH, whereby it did not consider OS as a competitor to LH. The Commission thus considered that the transaction would eliminate 4U as LH's only competitor on VIE-STR.
- (115) It should be noted that despite its acquisition by LH, 4U is not a party to LH's joint venture agreement with OS. The market investigation in phase I and II indicated that OS and 4U compete on prices to some extent. This is due to the fact that while LH and OS operate under a joint venture that shares the resulting profits equally, LH is the sole recipient of any profits from 4U's operations. This therefore implies that OS incentives on the one hand and LH group incentives on the other hand are not currently aligned on this route and that difference in incentives will be eliminated by the transaction.
- (116) A clear majority of respondents to the Commission's market investigation consider that there in fact exists residual competition between OS and 4U. Particularly non-time sensitive passengers recognize that both carriers offer attractive prices and schedules, while time sensitive passengers responded that the carriers compete against each other to a more limited extent. Therefore, the transaction will eliminate OS as 4U's actual competitor. Given that after the transaction both 4U and OS will belong to LH, the transaction leads to a monopoly on VIE-STR.

⁷⁰ LH estimated market shares for some air carriers, whose bookings are not reflected in MIDT (like 4U, Niki, SkyEurope etc.) based on data published by the German Statistical Office and other publicly available information about schedules, frequencies and utilized aircraft, see paragraphs 336-347 of the Form CO. The parties did not consistently provide estimates for all airlines which are only partly covered by MIDT.

- (117) The transaction also raises competition concerns under the alternative counterfactual scenario, whereby OS is acquired by Air France-KLM. Given that both OS and 4U are presently competing on this route to some extent, it can be expected that this actual competition would be even more intensive if OS terminated its joint venture agreement with LH relating to VIE-STR as LH would then not be in a position to influence OS' pricing strategy relating to this route. This is further supported by internal OS documents which indicate that OS would keep operating on this route even in the case of a down-sizing in a stand alone scenario.⁷¹ In that scenario, OS would not only compete against 4U but also against LH.
- (118) In terms of barriers to entry, VIE airport is a level 3 coordinated airport with slot shortage during peak times. Peak times have been indicated as 08.30-11.00 and 16.00-20.45. In the IATA Winter season 2008/2009, runway capacity has also been exhausted in the mornings (as early as 07.35 until 11.50), with capacity being almost full as early as 06.00. In some cases, slot requests by new entrants could only be accommodated within 80 minutes of the initial slot request. The capacity situation at VIE airport is not expected to change within the next three years. LH and OS have been allocated up to 67% of peak time slots at VIE airport.
- (119) With regard to STR airport, which is a coordinated airport, runway capacity constraints also exist during peak times, which are between 08.00-11.00. These constraints are predicted to remain unchanged in the short to medium term.
- (120) It follows that entry barriers, in particular slot constraints at VIE airport and STR airport, render market entry difficult on the VIE-STR route. Additionally several respondents indicated that the transaction will have a negative impact on the entry plans of competitors on VIE-STR.
- (121) It is concluded from the above that regardless of the exact market definition, the transaction raises serious doubts as to its compatibility with the common market on VIE-STR.

b. Vienna-Cologne

- (122) On the Vienna-Cologne route ("VIE-CGN"), over [250 000 – 300 000]* passengers travel every year, of which some [250 000 – 300 000]* are O&D passengers. According to a study conducted by OS, the share of business passengers on this route is about [40-50]*% while [50-60]*% are leisure passengers.
- (123) VIE-CGN is served by OS (through Tyrolean). LH does not operate VIE-CGN itself but markets seats on OS-served flights under a code-share with OS. In addition, 4U (which is indirectly controlled by LH) operates on VIE-CGN. OS operates three daily frequencies on weekdays (18 weekly frequencies) and 4U operates three daily frequencies on weekdays (20 weekly frequencies). Apart from OS and 4U, no other carrier operates this route. TUIfly

⁷¹ OS' presentation [...]*.

started marketing its operations on the CGN-VIE route as of 31 August 2009 with two frequencies on weekdays and with one frequency each on Saturdays and Sundays. These flights are also available for booking in the upcoming IATA Winter season 2009/2010. However, TUIfly's City Carrier Business is in the process of being sold to Air Berlin and it is therefore uncertain whether or not VIE-CGN will be actually served if the transaction between TUIfly and Air Berlin is completed. The notifying party submits that train services do not represent a significant constraint on air travel on this route.

- (124) As regards airport substitutability, the parties submit that CGN airport and DUS airport should be considered as substitutable. It should be noted that the distance from DUS airport to the city centre of Cologne is approximately 61 km, which amounts to travel time of slightly more than 40 minutes by car or train. However, as explained in paragraph (15), the distance between airports can only serve as a first "proxy" to define a catchment area; a more detailed analysis is necessary on a case-by-case basis.
- (125) On the demand side, a considerable number of respondents to the Commission's market investigation indicated that CGN airport and DUS airport would not be substitutable for time sensitive passengers. In addition, the Commission also obtained pricing data on a number of common destinations that LH serves from DUS airport and CGN airport, and the resulting movement of fares for flights that originate out of DUS airport and CGN airport is in many instances not consistent with both of those two airports belonging to the same market.
- (126) On the supply side, LH operates on a number of routes out of both airports (including CGN-VIE and DUS-VIE) thereby meeting a specific demand on each of these airports. In addition, there are significant slot constraints at DUS airport unlike at CGN airport (a facilitated airport), which contradicts the idea that the competitive landscape is sufficiently homogenous between the two airports. For the purposes of this Decision, it is therefore concluded that DUS airport cannot be regarded as a substitute to CGN airport, at least for time sensitive passengers travelling on the CGN-VIE route.
- (127) The table below illustrates the market structure of VIE-CGN in the IATA Summer season 2008 and IATA Winter season 2008/2009.⁷²

Airline	SS 08 figures on VIE-CGN		WS 08/09 figures on VIE-CGN	
	Time Sensitive	All passengers	Time Sensitive	All passengers
LH	[5-10]*%	[0-5]*%	[5-10]*%	[0-5]*%
OS	[5-10]*%	[5-10]*%	[5-10]*%	[5-10]*%
4U	[80-90]*%	[80-90]*%	[80-90]*%	[80-90]*%
Others	[0-5]*%	[0-5]*%	0%	0%
Combined	100%	100%	100%	100%

⁷² LH estimated market shares for some air carriers, whose bookings are not reflected in MIDT (like 4U, Niki, SkyEurope etc.) based on data published by the German Statistical Office and other publicly available information about schedules, frequencies and utilized aircraft, see paragraph 336-347 of the Form CO. The parties did not consistently provide estimates for all airlines which are only partly covered by MIDT.

- (128) Similarly to VIE-STR, VIE-CGN was also subject to commitments in the Commission's 2002 exemption decision and commitments still apply according to the Commission's Lufthansa/Eurowings decision.
- (129) The parties submit that due to their co-operation under the joint venture agreement, LH and OS do not currently compete on this route. They further submit that the overlaps between OS and 4U should not be assessed due to the fact that they were analysed in the Lufthansa/Eurowings case.
- (130) The Commission found in the Lufthansa/Eurowings case that LH and OS did not compete on VIE-CGN due to their joint venture agreement. As a consequence, the Commission assessed the effects of a combination of Eurowings and LH, whereby it did not consider OS as a competitor to LH. The Commission considered that the transaction would eliminate 4U as LH's only competitor on VIE-CGN.
- (131) It should be noted that despite its acquisition by LH, 4U is not a party to LH's joint venture agreement with OS. The market investigation in phase I and II has indicated that OS and 4U compete to some extent on prices. This is due to the fact that while LH and OS are operating under a joint venture that shares the resulting profits equally, LH is the sole recipient of any profits from 4U's operations. This therefore implies that LH's and OS' incentives are currently not aligned on this route and this difference in incentives will be eliminated by the transaction.
- (132) A clear majority of respondents to the Commission's market investigation consider that there is in fact residual competition between OS and 4U. Particularly non-time sensitive passengers recognize that both carriers offer attractive prices and schedules, while time sensitive passengers responded that the carriers compete against each other to a more limited extent. Therefore, the transaction will eliminate OS as 4U's actual competitor. Given that after the transaction both 4U and OS will belong to LH, the transaction would lead to a monopoly on VIE-STR.
- (133) As regards TUIfly's plans to start operations on VIE-CGN, it is not yet clear what, if any, competitive constraint TUIfly will exercise on the parties given that TUIfly's City Carrier Business is in the process of being sold to Air Berlin and it is uncertain whether this route will be actually operated on once the transaction between TUIfly and Air Berlin is completed. In any event, the announced entry of TUIfly on a route that would become a monopoly route post merger, is not sufficient to dismiss serious doubts regarding this route.
- (134) The transaction also raises competition concerns under the alternative counterfactual scenario, whereby OS is acquired by Air France-KLM. Given that both OS and 4U are presently competing on this route some extent, it can be expected that this actual competition would be even more intensive if OS terminated its joint venture agreement with LH relating to VIE-CGN as LH would then not be in a position to influence OS' pricing strategy relating to this route. This is further supported by internal OS documents which indicate that OS would keep operating on this route even in the case of down-sizing in a

stand alone scenario.⁷³ In that scenario, OS would not only compete against 4U but also against LH.

- (135) Entry barriers exist on VIE-CGN as a result of significant slot constraints at VIE airport, as described in detail in paragraph (118). CGN airport is a schedules facilitated rather than coordinated and there are no material slot constraints in CGN.
- (136) It is concluded from the above that the transaction raises serious doubts as to its compatibility with the common market at least with regard to time sensitive passengers on VIE-CGN. It is not necessary to conclude whether or not the transaction raises serious doubts on a possible market for non-time sensitive passengers or the market comprising all passengers travelling on VIE-CGN given that the Commitments proposed by LH address competition concerns under any alternative market definition.

c. Vienna-Munich

- (137) On the Vienna-Munich route ("VIE-MUC") [350 000 – 400 000]* passengers travel annually, out of which some [200 000 – 250 000]* are O&D passengers, the rest being transfer passengers. The parties estimate that up to [60-70]*% of passengers on this route travel for business purposes.
- (138) VIE-MUC is served by both OS (through OS and Tyrolean) and LH (through LH and Cityline). Additionally, the parties market seats on each other's flights. OS (together with Tyrolean) operates four daily frequencies on weekdays (26 weekly frequencies), LH (together with Cityline) operates five daily frequencies on weekdays (33 weekly frequencies). The only other air carrier active on this route is Niki Luftfahrt GmbH ("Niki"), with three daily frequencies on weekdays (17 weekly frequencies), which began operating flights on the route in November 2007 and was granted slots through the normal slot allocation procedure. Air Berlin code-shares on Niki's services. Deutsche Bahn and ÖBB offer an average of 6 daily direct train connections (ICE/IC) between Vienna (Westbahnhof) and Munich (Hauptbahnhof) with a duration of 4.10-4.17 and a number of indirect one-stop connections.
- (139) The table below illustrates the market shares of air carriers active on VIE-MUC in the IATA Summer season 2008 and Winter season 2008/2009 estimated by the parties according to the MIDT data.⁷⁴

⁷³ OS' presentation [...]*.

⁷⁴ LH estimated market shares for some air carriers, whose bookings are not reflected in MIDT (like 4U, Niki, SkyEurope etc.) based on data published by the German Statistical Office and other publicly available information about schedules, frequencies and utilized aircraft, see paragraph 336-347 of the Form CO. The parties did not consistently provide estimates for all airlines which are only partly covered by MIDT.

Airline	SS 08 figures on VIE-MUC		WS 08/09 figures on VIE-MUC	
	Time Sensitive	All passengers	Time Sensitive	All passengers
LH	[50-60]*%	[30-40]*%	[40-50]*%	[30-40]*%
OS	[20-30]*%	[20-30]*%	[20-30]*%	[10-20]*%
Combined LH+OS	[70-80]*%	[50-60]*%	[70-80]*%	[50-60]*%
Niki	[20-30]*%	[40-50]*%	[20-30]*%	[30-40]*%
Air Berlin	[0-5]*%	[0-5]*%	[0-5]*%	[10-20]*%
Others	[0-5]*%	[0-5]*%	[0-5]*%	[0-5]*%
Combined all	100%	100%	100%	100%

(140) On the basis of the market investigation the Commission has endeavoured to reconstruct the market for all passengers for the IATA Summer season 2008 and Winter season 2008/2009. The market shares are based on figures of flown passengers provided by the parties and Niki.⁷⁵

Figures on VIE-MUC: all passengers		
Airline	SS 08	WS 08/09
LH	[30-40]%	[30-40]%
OS	[20-30]%	[20-30]%
Combined LH+OS	[60-70]%	[50-60]%
Niki ⁷⁶	[30-40]%	[40-50]%
Combined all	100%	100%

(141) With respect to inter-modal competition, the parties consider that train services on VIE-MUC should be seen as a viable competitive alternative to flights on this O&D city pair and should therefore be included in the market. The parties estimate that some [60 000 – 70 000]* O&D passengers travel yearly on VIE-MUC by train, out of which around [10 000 – 20 000]* passengers are time sensitive. According to the parties' estimates, if train services are included in the relevant market, train passengers would account for around [20-30]*% of all passengers on this route ([20-30]*% of time sensitive passengers) and the parties' combined market share would total [40-50]*% ([50-60]*% for time sensitive passengers). In such a scenario, the parties estimate Niki's market share would be [10-20]*% for time sensitive passengers and [30-40]*% for all passengers.

(142) The market investigation has, however, shown that given the short total travel time by plane on VIE-MUC, the train service does not a viable alternative for time sensitive passengers. The parties estimate the total travel time by plane to be 3.10 to 3.25. Even if the parties' assumptions were taken as a basis for comparison, the total travel time by plane is considerably less than the train journey alone of 4.10 to 4.17 (even using the city centre as a benchmark, that is, ignoring the journey to/from the train station, boarding the train etc.⁷⁷).

75 The comparability of the data collected in the market investigation from different companies may be affected by possibly different methods of data collection. In particular, the parties provided various sets of "flown passenger data".

76 Including Air Berlin's passengers.

77 Since for most travellers the train station is not their real point of origin or destination, a realistic total travel time by train should also include the average travel time between the train station and the real point of origin and destination. In a large city (like Vienna and Munich), this travel time is likely to amount to at least 20

Indeed, a clear majority of respondents did not consider train services to be a credible alternative for time sensitive passengers on this route. They consider the travel time to be too long and the cost saving in terms of ticket prices not sufficient to compensate for the longer travel time. As pointed out by respondents to the market investigation, train services on this route also do not cater for typical one day return business trips due to the train's late arrival in the morning and early departure in the evening. Where a time sensitive passenger needs to attend a morning meeting in one of the two cities, the earliest arrival time in Vienna (Westbahnhof) of a non-stop train is 11.40 and 10.31 in Munich (Hauptbahnhof). By that time, four planes operated by the parties have already landed at VIE airport and two planes operated by the parties have already landed at MUC airport.

- (143) As regards non-time sensitive passengers, the views of the respondents to the Commission's market investigation questionnaires on the substitutability between plane and train services on this route were rather varied.
- (144) In addition to the qualitative market investigation, the Commission also obtained pricing data from Deutsche Bahn on the MUC-VIE route to compare them with the fares of OS and LH. OS' and LH's average fully-flexible economy and unrestricted business fares are more than three times as expensive as Deutsche Bahn's average fully-flexible first-class fares. OS' and LH's average semi-flexible economy fares are more than twice as expensive as Deutsche Bahn's average fully-flexible second-class fares. Even OS' and LH's average non-flexible economy fares are more than [50-60]*% more expensive than Deutsche Bahn's average fully-flexible second-class fares. These considerable price differences suggest that train travel cannot be considered as a close competitor to air travel, particularly for time sensitive passengers.
- (145) As regards the relevant counterfactual, VIE-MUC is one of the routes where LH and OS operate under the joint venture agreement, according to which all revenues and costs incurred in connection with the operation of this route are shared between LH and OS. The market investigation revealed that the current competition between the parties on this route is at the most rather limited. In fact, the main consequence of the creation of a permanent structural link between the parties is the elimination of potential competition between them on the VIE-MUC route. However, the question whether the creation of a permanent structural link between LH and OS as such significantly impedes effective competition on the common market due to the elimination of potential competition between the parties can be left open since, in any event, the transaction raises serious doubts as to its compatibility with the common market under the Air France-KLM counterfactual scenario whereby OS is acquired by Air France/KLM and subsequently terminates its co-operation with LH, and the Commitments proposed by LH solve competition concerns under each alternative counterfactual scenario.

minutes. Equally, boarding/arrival times for train services should also be taken into account. Although there is no check-in for ICE services, travellers need around 10 minutes to go from the station entrance to the train and also around 10 minutes to disembark and reach the station exit; see Case No. COMP/M.5335 – Lufthansa/SN Airholding, paragraph 121.

- (146) First of all, VIE-MUC is a thick route with a large number of O&D and transfer passengers. Currently, LH and OS both operate a significant number of frequencies on VIE-MUC and MUC airport is a hub for LH, while VIE airport is a hub for OS. Given the specific features of this route and the fact that OS and LH are both presently active on this route, it is reasonable to assume that both carriers would maintain those operations if OS terminated its joint venture agreement with LH. This scenario is supported by internal OS documents that indicate that OS would keep operating on the VIE-MUC route even in the case of down-sizing in a stand alone scenario.⁷⁸ As this route is already served by more than one (network-) carrier pre-merger, it is reasonable to assume that demand on the route will stay sufficiently large for more than one (network-) carrier to sustainably operate on this route regardless of whether these carriers belong to the same alliance or not. Secondly, according to the Air France-KLM counterfactual scenario, for the two alliances to be able to compete effectively for traffic to/from their respective hubs, both LH and OS would probably have to maintain, if not increase, the frequencies of their flights. In fact, as noted at paragraph (103), LH's internal documents indicate that LH would need to add [...] weekly frequencies on VIE-MUC if OS is acquired by Air France-KLM and joins SkyTeam. On that basis, the proposed concentration would eliminate actual or at least potential competition between the parties.
- (147) The market investigation (including quantitative and qualitative evidence) shows that the remaining competition from Niki on VIE-MUC would not sufficiently constrain the merged entity to prevent anti-competitive effects at least for time sensitive passengers. Moreover, it is clear from paragraphs (142) to (144) above that train services cannot be considered a credible alternative to air transport for time sensitive passengers on this route, while the same train services seem to exert some competitive constraint on non-time sensitive passengers.
- (148) A majority of respondents do not consider the presence of Niki a sufficient competitive constraint on the parties. In particular, Niki is not perceived as a credible alternative to the LH/OS merged entity in terms of its flight times and the number of frequencies it offered for time sensitive passengers. Several respondents indicated that the parties have an important competitive advantage vis-à-vis Niki on VIE-MUC due to their higher number of flight frequencies. In addition, some respondents considered the morning departure time from VIE airport (6.15; arrival at MUC airport at 7.20) offered by Niki as too early and the evening departure from MUC airport (21.30; arrival at VIE airport at 22.35) as too late, and thus inconvenient for business travellers.⁷⁹ Moreover, several respondents concluded that a competitor (such as Niki) would need to offer at least four frequencies on VIE-MUC to be able to offer a sufficiently attractive schedule for time sensitive passengers.
- (149) The results of the market investigation, finding that Niki does not sufficiently constrain OS/LH at least as far as time sensitive passengers are concerned, are also supported by the data analysis that was based on the pricing data obtained from the parties which assessed the

78 OS' presentation [...]*.

79 This evidence is supported by the fact that, according to the Commission's market investigation, time sensitive passengers have a very clear preference for morning departures after 7.00 and return flights in the evening between 18.00 and 19.00 (not later than 21.00).

effect of Niki's November 2007 entry on the parties' prices. The analysis suggests that Niki's entry in November 2007 had no impact at least on LH's and OS' fares for time sensitive passengers. This evidence supports the finding that, at least in the case of time sensitive passengers, Niki does not constitute a strong constraint on the parties.

(150) The Commission further found that with respect to tickets purchased close to the flight date which appear to be purchased by time sensitive passengers, Niki's position is considerably weaker than LH's and OS' and than estimated by the parties in their notification. The Commission further found that LH and OS charge significantly higher fares than Niki to passengers booking close to the flight date. These large price differences are further evidence that Niki is not viewed as a close competitor by time sensitive passengers, as the parties can extract significantly higher rents than Niki thanks to more flight frequencies and more convenient schedules.

(151) With regard to barriers to entry, although Niki managed to obtain three frequencies on VIE-MUC in 2007, there currently remain considerable barriers to entry or expansion for competitors in particular for time sensitive passengers, who require a larger number of frequencies at convenient times. Significant slot constraints exist at VIE airport (paragraph (118)) as well as at MUC airport. In the most recent IATA season, capacity was exhausted at MUC airport between 06.00-10.00 and 15.00-22.00 of any given weekday. Indeed, time sensitive passengers have a very clear preference for morning departures after 7.00 and return flights in the evening between 18.00 and 19.00 (and not later than 21.00). Given that these are precisely the times when capacity at MUC airport is exhausted, competitors currently face significant barriers to entry or to expansion should they want to offer a credible service catered to time sensitive passengers. This situation will remain unchanged until at least 2011.⁸⁰

(152) In conclusion, therefore, the proposed transaction raises serious doubts as to its compatibility with the common market under the Air France-KLM counterfactual at least for time sensitive passengers on VIE-MUC. It is not necessary to determine whether or not the transaction raises serious doubts on a possible market for non-time sensitive passengers or the market comprising all passengers travelling point-to-point on VIE-MUC given that the Commitments proposed by LH address any competition concerns under an alternative market definition.

d. Vienna-Frankfurt

(153) On the Vienna-Frankfurt route ("VIE-FRA"), [400 000 – 450 000]* passengers travelled point-to-point in 2008. Over [600 000 – 650 000]* passengers travelled on this route when transfer passengers are included. The parties estimate that up to [50-60]*% of passengers travel for business purposes on VIE-FRA.

⁸⁰ It should be noted that MUC airport expects significant capacity extensions to be in place as of 2011. In particular, a third runway is currently in the second phase of an extensive approval process and is expected to be operational as of 2011. This third runway will increase co-ordination of up to 120 movements per hour compared to 90 movements per hour with the existing two-runway system and will be available to both terminals at MUC airport.

- (154) Both OS (through OS and Tyrolean) and LH operate on VIE-FRA. The parties market seats on each other's flights. Additionally, Adria Airways, a Star Alliance member based in Slovenia operates flights on this route, on which LH code shares.⁸¹ The other competitors are Niki and Air Berlin. Air Berlin merely code-shares on Niki's services. Currently, those carriers have the following number of flight frequencies: LH and OS – five daily frequencies each (35 weekly each), Adria Airways – three daily frequencies (16 weekly); Niki – two daily frequencies (11 weekly).
- (155) Frankfurt is served by two airports: FRA airport and HHN airport. OS, LH, Adria Airways and Niki fly from VIE airport to FRA airport. Ryanair (FR) currently operates three weekly frequencies between BTS airport and HHN airport. The parties consider that FR exerts at least some competitive pressure on them, particularly in relation to non-time sensitive passengers. Based on the results of the market investigation, the Commission considers that FR's services do not constrain the parties on VIE-FRA to any meaningful degree, regardless of whether there is a separate market for time sensitive passengers or not. First, given the considerable distance from Vienna to BTS airport and from Frankfurt to HHN airport, the total travel time is much longer than a trip involving VIE airport and FRA airport. BTS airport is situated 87 km from Vienna city centre, which corresponds to a driving time of more than 60 minutes by car and 75 to 95 minutes by bus. Bus connections are generally infrequent; notably there are only three 75 minute-bus connections on Vienna-BTS airport daily. HHN airport is situated 124 km from Frankfurt city centre, which corresponds to 85 minutes by car and 105 minutes by bus. Secondly, respondents to the market investigation in this case did not consider BTS airport a substitute for VIE airport, at least in relation to time sensitive passengers. Moreover, the majority of respondents did not consider HHN airport to be a substitute for FRA airport, even in relation to non-time sensitive passengers. Lastly, the parties have not provided any data in support of their contention that FR should be regarded as their competitor on VIE-FRA despite the Commission's repeated request for the parties' data and estimates as to the structure of the market comprising carriers active on VIE airport-FRA airport as well as BTS airport-HHN airport.
- (156) As regards inter-modal competition, the notifying party submits that train services do not represent a significant constraint on air travel on this route.
- (157) The table below provides the market shares of air carriers active on the VIE-FRA route in the IATA Summer season 2008 and Winter season 2008/2009 estimated by the parties according to the MIDT data.⁸²

81 The code-share agreement between LH and Adria Airways is a standard free-flow code-share agreement.

82 LH estimated market shares for some air carriers, whose bookings are not reflected in MIDT (like 4U, Niki, SkyEurope etc.) based on data published by the German Statistical Office and other publicly available information about schedules, frequencies and utilized aircraft, see paragraph 336-347 of the Form CO. The parties did not consistently provide estimates for all airlines which are only partly covered by MIDT.

Airline	SS 08 figures on VIE-FRA		WS 08/09 figures on VIE-FRA	
	Time Sensitive	All passengers	Time Sensitive	All passengers
LH	[50-60]*%	[30-40]*%	[50-60]*%	[40-50]*%
OS	[20-30]*%	[20-30]*%	[20-30]*%	[20-30]*%
Combined LH+OS	[70-80]*%	[60-70]*%	[70-80]*%	[60-70]*%
Adria Airways	[0-5]*%	[0-5]*%	[0-5]*%	[0-5]*%
Niki	[20-30]*%	[20-30]*%	[20-30]*%	[20-30]*%
Air Berlin	[0-5]*%	[5-10]*%	[0-5]*%	[5-10]*%
Others	[0-5]*%	[0-5]*%	[0-5]*%	[0-5]*
Combined all	100%	100%	100%	100%

(158) On the basis of the market investigation, the Commission has endeavoured to reconstruct the market for all passengers for the IATA Summer season 2008 and Winter season 2008/2009. The market shares are based on figures of flown passengers.⁸³

Figures on VIE-FRA: all passengers		
Airline	SS 08	WS 08/09
LH	[30-40]%	[40-50]%
OS	[20-30]%	[20-30]%
Combined LH+OS	[60-70]%	[60-70]%
Adria Airways	[0-5]%	[0-5]%
Niki ⁸⁴	[30-40]%	[20-30]%
Combined all	100%	100%

(i) Competitive assessment of creation of permanent structural link between the parties

(159) As regards the relevant counterfactual, VIE-FRA is one of the routes where LH and OS operate under the joint venture agreement, according to which all revenues and costs incurred in connection with the operation of this route are shared between LH and OS. The market investigation revealed that the current competition between the parties on this route is at most rather limited. In fact, a consequence of the creation of a permanent structural link between the parties would be the elimination of potential competition between them on the VIE-FRA route.

(160) However, it is to be recalled that the parties' joint venture was temporarily exempted by the Commission under Article 81(3) of the Treaty subject to commitments. When the Commission's 2002 exemption Decision expired in 2005, the parties continued their joint venture co-operation based on a self-assessment of the compliance with Article 81 of the Treaty of their co-operation.

(161) The self-assessment conducted by the parties of the compliance with Article 81 of the Treaty of their co-operation categorises the VIE-FRA route as a route with a "high" risk

⁸³ The comparability of the data collected in the market investigation from different companies may be affected by possibly different methods of data collection. In particular, the parties provided various sets of "flown passenger data".

⁸⁴ Including Air Berlin's passengers.

grade, that is, according to the parties' assessment, that "serious concerns" regarding its compatibility with Article 81 of the Treaty exist on this route. The self-assessment thus concludes that it is "very likely" that slots will need to be transferred to competitors and that the transfer of three to four slots following a request by another airline, possibly in combination with further measures, is therefore necessary in order to remove these competition concerns.⁸⁵

(162) On the basis of that self-assessment, LH transferred two slots at Frankfurt airport to its competitor Niki in 2006, so as to enable Niki to enter VIE-FRA with two daily frequencies. In July 2009, LH transferred a further slot to Niki, so as to enable Niki to operate a third frequency on VIE-FRA as of the IATA winter season 2009/2010.⁸⁶ The relevant slot lease agreements between LH and Niki are unlimited in time but will end, with the result that Niki will have to hand back the Frankfurt slots to LH, if the joint venture between LH and OS is terminated.⁸⁷ Moreover, following the completion of the proposed acquisition of OS by LH, namely, when OS and LH belong to the same group, Article 81 of the Treaty will cease to be applicable to the parties' pre-merger co-operation under the joint venture agreement and therefore the underlying reason for the slot transfer to Niki for VIE-FRA will no longer exist. As a consequence of the proposed transaction, the joint venture between the parties will likely cease to exist and, in any event, the decision whether or not to terminate the joint venture will be fully with LH. The transaction will thus not only convert the parties' contractual co-operation into a permanent structural link, eliminating potential competition between the parties on VIE-FRA, but it will also allow LH to terminate the slot lease agreements with Niki.

(163) As a result of the termination of the slot lease agreements, Niki would effectively have to exit the VIE-FRA route. Indeed, the market investigation revealed that FRA Airport is congested throughout the day and that access to requested slots is therefore virtually impossible. Niki would thus not only have to return its current slots to LH but would also have difficulty obtaining any own slots at all due to the congestion at FRA airport, and even less any morning and evening slots, under the normal slot allocation procedure. The transaction would thus eliminate the parties' most important competitor on VIE-FRA. In view of the elimination of actual competition from a third party, the extent to which the creation of a permanent structural link between the parties also leads to the elimination of potential competition between them on VIE-FRA can be left open.

(164) Therefore, the only remaining competitor on the VIE-FRA route would be Adria Airways, which would not sufficiently constrain the parties to counterbalance the elimination of Niki as an actual competitor.

(165) The parties submit that Adria Airways should be regarded as a competitor on this route as the code-share agreement between LH and Adria Airways does not provide for price

85 See "LH/AUA Self-Assessment", pp. 4, 13 and 14.

86 See "Annex Update Agreement" of 29 June 2009.

87 According to section 9 of the slot lease agreement between LH and Niki, the agreement will be terminated when Niki transfers all of LH's slots back to LH. According to section 10 of the slot lease agreement, Niki is obliged to return LH's slots if the joint venture between LH and OS is terminated.

coordination. However, the Commission considers that Adria Airways, a Star Alliance member, cannot be considered as exercising a strong constraint, if one at all, on the merged entity.

- (166) Despite its 16 weekly frequencies and the fact that it has been operating on this route for several years now (Adria Airways entered VIE-FRA in the IATA Winter season 2001/2002), Adria Airways has never gained a meaningful market share of this route and currently accounts for about [0-5]% of the market. This is because it uses small aircraft and its load factor is relatively low ([50-60]-[60-70] %). Furthermore, it is to a large extent dependent on LH for its customer base, illustrated by the high percentage of passengers it transports with a ticket issued by LH. It is thus clear that Adria Airways, at best, exercises a limited competitive constraint upon the parties, as is also illustrated by the statements of respondents to the Commission's market investigation. Several respondents pointed out that Adria Airways does not compete on prices with LH/OS but, rather, that its prices are adjusted to match those of LH. Some respondents consider that this is due to the code-share agreement with LH, others think that the underlying reason might be that Adria Airways participates in LH's Partner Plus contracts with corporate customers. As a consequence, several respondents perceive Adria Airways' service as an additional LH service rather than an independent service offered by a competitor. It is pointed out that some corporate customers/travel agents whose employees/customers fly on VIE-FRA are not even aware of the presence of Adria Airways on this route or the proportion of their bookings with Adria Airways is very low (below 5%). In addition, Adria Airways is considered by some respondents to offer an inferior level of on board service, low capacity and a relatively unattractive schedule.
- (167) Moreover, even if the presence of Adria Airways on this route is considered a constraint, it is not clear to what extent Adria Airways will be able to operate on VIE-FRA in the future. Since the IATA Winter season 2006, LH has been granting slots for Adria Airways' operations on a season-by-season basis. The initial Slot Exchange Agreement between LH and Adria Airways was terminated in July 2006 and, since then, LH and Adria Airways have entered into a Slot Exchange Renewal Agreement in advance of every season. Since there is no longer a long-term slot lease agreement with LH in place, LH can withdraw slots from Adria Airways after every season. Given that slot capacity at FRA airport is exhausted throughout the entire day, it is doubtful whether Adria Airways would be able to continue offering its VIE-FRA service if LH withdraws slots from Adria Airways.
- (168) Taking into account the fact that Adria Airways is largely dependent on LH to fill its planes due to its low load factor, its low market share, the results of the market investigation that dismiss Adria Airways as an important source of competition on the VIE-FRA route, and the uncertainty of how long Adria Airways will operate on the route, it is clear that this marginal player cannot sufficiently constrain LH/OS.
- (169) It must therefore be concluded that the creation of a permanent structural link between LH and OS as a result of the proposed concentration raises serious doubts as to its compatibility with the common market on VIE-FRA.

(ii) Competitive assessment of the proposed concentration under the Air France-KLM counterfactual

- (170) Moreover, the transaction raises serious doubts as to its compatibility with the common market under the Air France-KLM counterfactual scenario whereby OS is acquired by Air France-KLM. The acquisition of OS by Air France-KLM would likely lead to the termination of the joint venture agreement between LH and OS and in case of the termination of the joint venture agreement, the relevant slot lease agreements between LH and Niki will come to an end and consequently, Niki will have to return the Frankfurt slots to LH.⁸⁸ As a result of the termination of the slot lease agreements, Niki would effectively have to exit the route, given that FRA airport is congested throughout the day and that access to requested slots is therefore virtually impossible. Niki would thus not only have to return its current slots to LH, but would also have difficulty obtaining any own slots under the normal slot allocation procedure.
- (171) On the other hand, the evidence available to the Commission suggests that, under the Air France-KLM counterfactual, both LH and OS would likely operate the VIE-FRA route in competition with each other.
- (172) First of all, VIE-FRA is a thick route (in fact the thickest route affected by this transaction), with a large number of O&D and transfer passengers travelling in both directions and with a large proportion of business travellers. As this route is served by more than one (network-) carrier already pre-merger, it can generally be assumed that it is sufficiently large for more than one (network-) carrier to sustainably operate it.
- (173) Secondly, both LH and OS already operate a significant number of frequencies on VIE-FRA. Given the features of this route and the fact that OS and LH are presently both active on this route, it can be expected that both carriers would maintain their operations if OS terminated its joint venture agreement with LH. This is supported by internal OS documents which indicate that OS would continue operating on the VIE-FRA route even in the case of down-sizing in a stand alone scenario.⁸⁹ In the Air France-KLM counterfactual scenario, for the two alliances to be able to compete effectively against each other, both LH and OS would not only have to continue operating flights in competition on this route in order to attract traffic to/from their respective hubs but also they would probably even increase their frequencies. Indeed, as noted in paragraph (103), LH's internal documents indicate that LH would need to add [...] weekly frequencies on VIE-FRA, if OS is acquired by Air France-KLM and joins Sky Team.
- (174) On the basis of this counterfactual scenario, the proposed concentration would thus eliminate actual or at least potential competition between the parties.

⁸⁸ According to section 9 of the slot lease agreement between LH and Niki, the agreement will be terminated when Niki transfers all LH's slots back to LH. According to section 10 of the slot lease agreement, Niki is obliged to return LH's slots back to LH if the joint venture between LH and OS is terminated.

⁸⁹ OS' presentation "[...]".

- (175) Therefore, also under this counterfactual, the only remaining competitor on the route would be Adria Airways. However, for the reasons set out in more detail in paragraphs (165) to (168), Adria Airways is unlikely to sufficiently constrain the parties to prevent anti-competitive effects on passengers.
- (176) Moreover, even if Niki were to continue operating its services on the VIE-FRA route under the Air France-KLM counterfactual (*quod non*), the evidence available to the Commission shows that it would not place a sufficient constraint on LH/OS to compensate for the elimination of competition between LH and OS.
- (177) For good measure, the Commission also investigated the constraint that Niki currently places on LH/OS. The market investigation shows that several corporate customers consider that the parties have an unmatched competitive advantage towards Niki on VIE-FRA due to better frequency offering that is particularly valued by time sensitive passengers. In particular, Niki's morning departure from FRA airport (9.40) is considered to be too late and thus inconvenient for time sensitive passengers. This evidence is supported by the Commission's market investigation which revealed that time sensitive passengers have a very clear preference for morning departures after 7.00 and return flights in the evening between 18.00 and 19.00 (not later than 21.00). Moreover, several respondents considered that a competitor (such as Niki) would need to offer at least five frequencies on VIE-FRA in order to be able to offer a sufficiently attractive schedule for time sensitive passengers. In addition, the majority of respondents reported that the proportion of their bookings with Niki on VIE-FRA is around or below 10%, which is consistent with the findings that corporate customers do not view Niki as a credible alternative. Some travel agents also characterize competition from Niki as limited.
- (178) The results of the market investigation are supported by the Commission's pricing analysis that, using the passenger-level data requested from the parties, examined the effect of Niki's entry in October 2006 on the parties' prices on this route. Niki's entry had no effect on OS' and LH's prices for fully flexible business and economy tickets. Somewhat of an impact by Niki's entry was observed in relation to LH's non flexible economy tickets, however less of an impact was noticeable in relation to OS' non flexible tickets. This suggests that Niki does not constitute a strong constraint on the parties at least in relation to time sensitive passengers but probably for all passengers.
- (179) Furthermore, the slots currently held by Niki have several shortcomings: first, Niki's morning slot in Frankfurt is 30 minutes later than Niki's initial slot request. As a result, Niki has inconvenient arrival and departure slots at morning peak times in Frankfurt, as a result of which Niki's morning flight from FRA airport arrives at VIE airport at 10.55. Second, the slot lease agreement between Niki and LH does not provide for grandfathering rights on slots granted to Niki and Niki is required to try to obtain suitable slots at FRA airport from the slot coordinator every season prior to obtaining them from LH. Third, Niki needs to comply with a contractual obligation with LH to use its slots according to the 80%-"use-it or-lose-it rule", while other airlines currently do not need to comply with this rule since the relevant regulation has been suspended for the IATA Summer 2009 season.⁹⁰ Lastly, the slot

⁹⁰ See paragraph (384) below.

lease agreement with Niki foresees very high penalties if a slot is lost and no obligation for LH to safeguard LH's grandfathering rights with regard to slots leased to Niki exists. These shortcomings translate into less flexibility of Niki to respond to changes in passenger demand. Consequently, Niki has a significant competitive disadvantage vis-a-vis the parties.

(180) In addition, given that slot capacity at FRA airport is exhausted throughout the day, it is noted that Niki's entry on VIE-FRA was only possible because LH leased FRA slots to Niki. However, Niki would lose these slots if the parties terminate the joint venture following an acquisition by Air France-KLM as the slot lease agreement between LH and Niki contains a provision whereby LH may terminate that agreement if the joint venture between LH and OS is terminated.

(181) In the course of the Commission's in-depth investigation of the transaction, LH and Niki extended their slot lease agreement to include a third slot at FRA airport at 16.45 (arrival from VIE airport) and 17.25 (departure to VIE airport) as of the IATA Winter season 2009/2010, which will enable Niki to operate three frequencies on VIE-FRA as of the Winter season. The timing of these additional slots is nearly exactly that requested by Niki. The parties claim that this will further increase the already strong competitive pressure exercised by Niki on this route. However, this additional slot will not alter the fact that Niki's morning flight is inconvenient for the purposes at least of time sensitive passengers. Moreover, given the shortcomings of the slot lease agreement between LH and Niki, Niki's competitive pressure stemming from its three operations a day under the current conditions would in any case be limited.

(182) Finally, significant barriers to entry exist on this route, and thus the threat of potential entry cannot discipline OS/LH on this route either. Indeed, the VIE-FRA route is characterised by significant barriers to entry. A first barrier to entry is the congestion of the airports at both ends of the VIE-FRA route. Both VIE airport and FRA airport experience significant levels of congestion. As regards VIE airport, slot shortage exists from 07.35 until 11.50 and from 16.00 to 20.45, as explained in paragraph (118). FRA airport is congested throughout the day and competitors have unanimously indicated that access to requested slots at FRA airport is virtually impossible.

(183) It must therefore be concluded that the proposed concentration also under the Air France-KLM counterfactual, raises serious doubts as to its compatibility with the common market on VIE-FRA.

(iii) Conclusion on the competitive assessment of the transaction regarding VIE-FRA

(184) In conclusion, the proposed transaction raises serious doubts on the VIE-FRA route as to its compatibility with the common market both under the pre-merger situation and under the Air France-KLM counterfactual and regardless of the precise market definition.

e. The Vienna-Berlin, Vienna-Düsseldorf, Vienna-Hamburg, Vienna-Hannover and Vienna-Nuremberg routes

(185) On several routes between Austria and Germany, namely the Vienna-Berlin ([400 000 – 450 000]* O&D and [450 000 – 500 000]* total passengers), Vienna-Düsseldorf ([450 000 – 500 000]* O&D and [500 000 – 550 000]* total passengers), Vienna-Hamburg ([350 000 – 400 000]* O&D and [400 000 – 450 000]* total passengers), Vienna-Hannover ([200 000 – 250 000]* O&D and [200 000 – 250 000]* total passengers) and Vienna-Nuremberg ([100 000 – 150 000]* O&D and [100 000 – 150 000]* total passengers) routes, the parties face significant competition from Air Berlin in particular. Indeed, as is illustrated by the table below for the IATA seasons winter 2008/2009 and summer 2008, no competition concerns arise on these routes as a result of the limited market shares of the parties (below [20-30]*% in all possible markets) and the strong market position of Air Berlin.

	WS 08/09 figures				SS 08 figures			
	Time Sensitive		All passengers		Time Sensitive		All passengers	
	Parties	Competitors	Parties	Competitors	Parties	Competitors	Parties	Competitors
Vienna-Berlin	LH [10-20]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [5-10]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [10-20]*% OS [5-10]*% Total [20-30]*%	Air Berlin [70-80]*%	LH [10-20]*% OS [5-10]*% Total [20-30]*%	Air Berlin [70-80]*%
Vienna-Düsseldorf	LH [10-20]*% OS [5-10]*% Total [20-30]*%	Air Berlin [70-80]*%	LH [10-20]*% OS [10-20]*% Total [20-30]*%	Air Berlin [70-80]*%	LH [10-20]*% OS [5-10]*% Total [20-30]*%	Air Berlin [70-80]*%	LH [10-20]*% OS [10-20]*% Total [20-30]*%	Air Berlin [70-80]*%
Vienna-Hamburg	LH [10-20]*% OS [5-10]*% Total [20-30]*%	Air Berlin [70-80]*%	LH [10-20]*% OS [10-20]*% Total [20-30]*%	Air Berlin [70-80]*%	LH [10-20]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [10-20]*% OS [5-10]*% Total [20-30]*%	Air Berlin [70-80]*%
Vienna-Hannover	LH [5-10]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [5-10]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [5-10]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [0-5]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%
Vienna-Nuremberg	LH [0-5]*% OS [5-10]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [0-5]*% OS [0-5]*% Total [5-10]*%	Air Berlin [40-50]*% HG [40-50]*%	LH [5-10]*% OS [10-20]*% Total [10-20]*%	Air Berlin [80-90]*%	LH [0-5]*% OS [10-20]*% Total [10-20]*%	Air Berlin [80-90]*%

(186) The absence of competition concerns is confirmed by the market investigations both in phase I and phase II which did not reveal any specific substantiated concerns for these routes. Although a few responding travel agents and corporate customers voiced single concerns, with respect to potential price increases and reduction of frequencies for instance, the vast majority of the respondents does not see any impact on the competitive situation on these routes as a result of the transaction.

(187) In phase II, the position of Air Berlin and the closeness of services between LH/OS and Air Berlin on the Vienna-Berlin, Vienna-Düsseldorf, Vienna-Hamburg and Vienna-Hannover routes were further investigated. The vast majority of respondents (both travel agents and corporate customers as well as competitors) clearly indicate that they perceive Air Berlin as a credible alternative to an LH/OS merged entity in terms of the timing and the frequencies of its flights when compared to the timing and frequencies of the LH/OS flights.

This is valid both for time sensitive and non-time sensitive passengers. Concerning the levels of service both at airports and on board, and concerning the frequent flyer programmes ("FFP") offered by LH and OS on the one hand, and by Air Berlin and Niki on the other hand, the opinions of the respondents have been varied. One group of respondents considered the services offered by Air Berlin inferior to those offered by LH and OS, particularly due to perceived more limited advantages of Air Berlin's FFP. However, another group of respondents clearly perceives Air Berlin's services as on par or comparable to those provided by LH and OS. In sum, it is concluded that the respondents to the market investigation largely perceive Air Berlin as a valid alternative to LH and OS on these routes.

(188) The transaction does not, therefore, significantly impede effective competition on any of these routes, regardless of the relevant counterfactual.

f. The Munich-Linz route

(189) On the Munich-Linz route (it is estimated by the parties that [50 000 – 60 000]* O&D passengers travel on this route by plane or train), the parties are the only air carriers present (LH as operating carrier and OS as marketing carrier) but they face strong competition from the train services offered by Deutsche Bahn and ÖBB on this route. In addition to a number of indirect connections, Deutsche Bahn and ÖBB offer an average of nine to ten direct train connections between Linz (Hauptbahnhof) and Munich (Hauptbahnhof) a day, with travel times mostly less than or around 3 hours, that is to say travel times which are comparable to the total travel time by plane of approximately 3:00h from city centre to city centre. The market investigation confirmed that those train services represent a viable competitive alternative for both time sensitive passengers and non-time sensitive passengers on this O&D pair. They therefore belong to the same market. In view of the strong market position of the train services, which according to the parties' estimate amount to a market share above [90-100]*% both for time sensitive and non-time sensitive passengers and which has broadly been confirmed by the market investigation, no competition concerns arise in relation to this route, irrespective of whether or not OS can be considered as a potential entrant on this route.

(190) The transaction does not, therefore, significantly impede effective competition on this route, regardless of the relevant counterfactual.

g. Routes which are only operated by OS and where the transaction could eliminate LH as a potential competitor

(191) On the Vienna-Dresden, Vienna-Leipzig, Salzburg-Düsseldorf, Graz-Düsseldorf, Linz-Düsseldorf, Graz-Stuttgart, Innsbruck-Frankfurt and Salzburg-Frankfurt routes, only OS is active as an operating carrier while LH merely markets seats on OS's flights within the framework of the parties' profit and loss sharing joint venture. In view of the absence of actual competition between the parties pre-merger (as a result of their joint venture co-operation), the proposed transaction could significantly impede effective competition only if it resulted in the elimination of LH as a potential competitor.

(192) However, the market investigation revealed that LH would not enter any of these routes absent the co-operation with OS.

(193) At the outset, it should be noted that demand on all these routes is rather low (between [10 000 – 20 000]* and [40 000 – 50 000]* O&D passengers per year). The market investigation indicated that it is not usual for traditional network carriers to enter European short-haul routes of such a limited size in competition to another operating carrier.⁹¹ Accordingly, none of the routes currently operated by OS were operated in parallel by both LH and OS before they began to co-operate with each other in 2000. Also, LH's self-assessment referred to in paragraph (66) considers almost all relevant routes as too thin to attract entry by another player.⁹² Those findings strongly indicate that it would not be economically sustainable for both LH and OS to be present as operating carriers on these routes.⁹³

(194) In addition, as explained in more detail hereafter for each route, a review of internal LH documents on entry strategies and other route-specific elements confirm that LH would not enter any of these routes in competition to OS.

(i) Vienna-Dresden and Vienna-Leipzig

(195) The Vienna-Dresden ([10 000 – 20 000]* O&D and [10 000 – 20 000]* total passengers) and Vienna-Leipzig ([10 000 – 20 000]* O&D and [20 000 – 30 000]* total passengers) routes are thin routes. This is evidenced by the fact that OS bundles these routes together as a stop-over connection. LH has operated only one intra-European route in the form of such a stop-over since 2008⁹⁴ and is therefore unlikely to adopt the same strategy as OS to serve these routes. The low local traffic on these routes indicates that these routes will most likely not viably sustain an operation by both OS and LH.

(196) Furthermore, LH has no international flights departing from Dresden and Leipzig but rather connects both cities to its hubs in Munich and Frankfurt and to its base in Düsseldorf. The unlikelihood of LH's entry on these routes is further underlined by a internal LH document that analyses a possible acquisition of OS by another carrier and clearly states that LH would not enter the Vienna-Leipzig route. [...]*⁹⁵

(197) LH's subsidiary 4U, which already operates out of Dresden airport, previously assessed a business case issued by Dresden airport in April 2006 in which its entry onto the Vienna-Dresden route is discussed. 4U did not execute these plans in 2006 nor the following years, which confirms the parties' submission that 4U did not consider that the operation of this route would be commercially profitable.⁹⁶

91 See replies to question 11 of the phase II market investigation questionnaire to competitors.

92 See "LH/AUA Self-Assessment", pp. 4, 6-8. [...]*

93 The parties further argue that on several routes currently operated by OS, OS would leave the route absent the transaction for various reasons [...]*.

94 See reply to question 3 of request for information to LH of 4 June 2009.

95 LH's internal document [...]*.

96 See reply of LH to request for information of 30 July 2009 and follow-up correspondence of 5 August 2009.

(ii) Salzburg-Düsseldorf, Graz-Düsseldorf, Linz-Düsseldorf

(198) The Salzburg-Düsseldorf ([20 000 – 30 000]* O&D and [20 000 – 30 000]* total passengers), Graz-Düsseldorf ([30 000 – 40 000]* O&D and [30 000 – 40 000]* total passengers) and Linz-Düsseldorf ([30 000 – 40 000]* O&D and [30 000 – 40 000]* total passengers) routes are thin routes. The low local traffic on these routes thus indicates that it would not be economically sustainable for both LH and OS to be present as operating carriers on these routes. This is further underlined by the fact that OS operates the Linz-Düsseldorf route as one leg of the Salzburg-Linz-Düsseldorf and Graz-Linz-Düsseldorf routes in order to bundle demand for travel to Düsseldorf.

(199) In addition, it should be noted that it is very unusual for LH to operate routes out of Düsseldorf below [40 000 – 50 000]* O&D passengers on which a competitor is active.⁹⁷ Also an internal LH document comparing the importance of destinations out of Düsseldorf conveys a low ranking for Graz, Linz and Salzburg ([...]*)⁹⁸, and a further internal LH document explains that [LH would not enter]* if OS was acquired by another carrier.⁹⁹

(200) LH's subsidiary, 4U, which already has operations out of Salzburg airport, is unlikely to enter the Salzburg-Düsseldorf route since it does not currently operate any flights out of DUS airport and has never made a business case to enter this route.¹⁰⁰

(iii) Graz-Stuttgart

(201) The Graz-Stuttgart ([30 000 – 40 000]* O&D and [30 000 – 40 000]* total passengers) route is served by OS since April 2009, while it had previously been served by LH. [...]*¹⁰¹

(202) In addition to OS, the Graz-based local airline Robin Hood is also active on the route, having entered the route in November 2008 with small aircraft. In view of the relatively low traffic on this route and the presence of two operating carriers, it is unlikely that it would be economically sustainable for both LH and OS to be present as operating carriers on this route.¹⁰²

(203) LH's subsidiary, 4U, which already has operations out of STR airport, is unlikely to enter the route since it does currently not operate any flights from Graz airport [...]*.¹⁰³

97 See reply of LH to request for information of 10 June 2009.

98 LH's internal document [...]*.

99 LH's internal document [...]*.

100 See reply of LH to request for information of 30 July 2009.

101 [...]*

102 Similarly, in a scenario where the route would still be operated by OS it is unlikely that OS would enter this route absent its co-operation with LH in view of the presence of two operating carriers and the fact that the only international route out of Graz served by OS is part of the joint venture (Graz-Düsseldorf, except for some leisure routes in Greece served by Lauda Air).

103 See reply of LH to request for information of 30 July 2009.

(iv) Innsbruck-Frankfurt

(204) The Innsbruck-Frankfurt route ([20 000 – 30 000]* O&D and [60 000 – 70 000]* total passengers) is a relatively thin route. Accordingly, a internal LH document states that due to [...] LH would not enter this route if OS was acquired by another carrier.¹⁰⁴ It follows that this route is unlikely to sustain an operation by both LH and OS.

(205) LH's subsidiary, 4U, is unlikely to enter the route since it does not have any operations at either end of the route and [...]*.¹⁰⁵

(v) Salzburg-Frankfurt

(206) The Salzburg-Frankfurt route ([40 000 – 50 000]* O&D and [100 000 – 150 000]* total passengers) is the thickest of all routes between Austria and Germany operated by OS only. [...]*¹⁰⁶

(207) However, an internal LH document explains that LH would not enter this route in case of a possible acquisition of OS by another carrier [...]*.¹⁰⁷ This conclusion is confirmed by information received in the course of the market investigation according to which Salzburg is within the overall catchment area of MUC airport.¹⁰⁸

(208) LH's subsidiary, 4U, which already operates out of Salzburg airport, is unlikely to enter the route since it does not currently operate any flights from FRA airport and has never made a business case to enter this route.¹⁰⁹

(vi) Conclusion

(209) It can therefore be concluded that, due to the low demand on all routes mentioned in (i) – (v) above and on the basis of a review of relevant internal LH documents on entry strategies and other route-specific elements LH is unlikely to enter any of those routes. Hence the elimination of LH as a potential competitor does not significantly impede effective competition, regardless of the relevant counterfactual.¹¹⁰

104 LH's internal document [...]*.

105 See reply of LH to request for information of 30 July 2009.

106 [...]*

107 LH's internal document [...]*.

108 See reply of MUC airport to question 12 of the phase I market investigation questionnaire to airports.

109 See reply of LH to request for information of 30 July 2009.

110 This conclusion is not altered by the fact that most of these routes have been operated profitably by OS in recent years. Indeed, Graz-Düsseldorf, Düsseldorf-Linz, Dresden-Vienna, Frankfurt-Salzburg and Stuttgart-Graz were operated profitably in recent years while the Innsbruck-Frankfurt, Düsseldorf-Salzburg and Vienna-Leipzig routes have been loss-making in one or more recent years, see reply of the parties to question 9 of request for information of 27 April 2009.

h. Routes which are only operated by LH and where the transaction could eliminate OS as a potential competitor

- (210) Only LH is active as operating carrier on the Innsbruck-Hamburg, Klagenfurt-Munich, Graz-Frankfurt, Graz-Munich and Linz-Frankfurt routes, while OS merely markets seats on those flights in the framework of the parties' joint venture. In view of the absence of actual competition between the parties pre-merger, the proposed concentration could significantly impede effective competition on these routes only if it resulted in the elimination of OS as a potential competitor on these routes.
- (211) However, the market investigation revealed that OS would not enter any of these routes absent the co-operation with LH.
- (212) Indeed, demand on these routes is often relatively low and none of the routes currently served by LH (except the Graz-Frankfurt route) was served by both parties before they started their co-operation in 2000. [...] ¹¹¹ These findings strongly indicate that it would not be economically sustainable for both LH and OS to be present as operating carriers on these routes.
- (213) Furthermore, none of these routes are mentioned in an internal OS document that sets out the restructuring measures to be taken if OS were to remain independent, ¹¹² which is in line with the fact that OS has no hubs at either end of any of these routes. This further underlines the fact that OS would not enter any of these routes absent the co-operation with LH.
- (214) Furthermore, OS argues that in view of its financial situation it will henceforth focus on routes with high passenger rates, which further underlined that it would not enter any of the routes at issue. In line with that submission, OS appears to have decided to remove a number of 50-seater aircraft and partly replace them by larger aircraft from the existing OS fleet. ¹¹³
- (215) In addition to these general observations, a review of internal OS documents on entry strategies and other route-specific elements confirm that OS would not enter these routes in competition to LH.

(i) Klagenfurt-Munich and Innsbruck-Hamburg

- (216) The Klagenfurt-Munich ([0 – 10 000]* O&D and [10 000 – 20 000]* total passengers) and Innsbruck-Hamburg ([0 – 10 000]* O&D and [0 – 10 000]* total passengers, a seasonal route) routes are thin routes.

111 [...]*

112 OS document [...]*.

113 See reply of OS to request for information of 5 August 2009; see also <http://www.nur-flug-tours.de/news/airlinenews-8140.htm>. It should also be noted in this context that apart from the Graz-Frankfurt route, the Graz-Munich, Innsbruck-Hamburg, Klagenfurt-Munich and Linz-Frankfurt routes have been loss-making in one or more recent years, see reply of the parties to question 9 of request for information of 27 April 2009.

(217) Out of Klagenfurt airport, OS currently only serves Vienna (it ceased operations on the Klagenfurt-Frankfurt route in April 2008) which underlines that Klagenfurt airport is not of strategic importance to OS' international flights. As regards the Innsbruck-Hamburg route, it should be noted that Transavia entered in December 2008 with five weekly frequencies in winter seasons and that TUIfly announced a direct service in winter seasons starting in Winter 2009/2010. Consequently, several players will henceforth be active on the route and it is therefore unlikely that OS would enter this thin route as a further player. In view of these reasons, OS is unlikely to enter both routes absent its co-operation with LH.

(ii) Frankfurt-Graz and Graz-Munich

(218) In the case of the Frankfurt-Graz route ([50 000 – 60 000]* O&D and [100 000 – 150 000]* total passengers), local traffic may sustain the operation of two carriers while local traffic is more limited in case of the Graz-Munich ([10 000 – 30 000]* O&D and [80 000 – 90 000]* total passengers/year) route.¹¹⁴

(219) However, an analysis of the routes where OS entered in the recent past strongly indicates that OS is unlikely to enter the Frankfurt-Graz route or Munich-Graz route: indeed, OS' last entry from Graz was in 2003 (the Graz-Düsseldorf route in the framework of the joint venture with LH). In the more recent past, OS most often entered routes that connect Vienna with a destination in the East, [...]*¹¹⁵ Entering the Frankfurt-Graz route or the Munich-Graz route would thus not fit into OS' entry strategy. In addition, an analysis of OS' recent entries revealed that it is very unusual for OS to enter intra-European routes against existing competition.¹¹⁶

(iii) Frankfurt-Linz

(220) For similar reasons, OS is also unlikely to enter the Linz-Frankfurt ([40 000 – 50 000]* O&D and [100 000 – 150 000]* total passengers) route absent the co-operation with LH. While local traffic is rather limited and it is therefore unclear if the route might sustain the presence of two operating carriers, it is to be recalled that before the parties' co-operation began in 2000, only one of the parties was active on this route. OS' last entry involving Linz airport was in 2003 (Düsseldorf-Linz-Graz/Salzburg, that is to say a stop-over) and an analysis of the routes where OS entered in recent years showed that OS mostly entered routes that connect Vienna with a destination in the East, [...]*.

114 It should be noted that prior to the co-operation between the parties, the Frankfurt-Graz route was operated by the regional airline Tyrolean Airways, which OS acquired in 1998 shortly before LH and OS entered into their co-operation. The parties argue that it was natural to shift Tyrolean Airways' operations to LH upon their co-operation.

115 [OS internal documents]*

116 See reply of OS to question 7 of request for information of 4 June 2009 and to question 2 of request for information of 10 June 2009 according to which - apart from seasonal routes and the Vienna-Luxembourg route which was before operated by OS as a stop-over connection via Strasbourg - OS has entered only the Vienna-Basel route (35 000 O&D passengers and 45 000 total passengers in the year of entry) against existing competition.

(iv) Conclusion

(221) It can therefore be concluded that due to the relatively low demand on all these routes and on the basis of a review of the relevant internal OS documents on entry strategies and other route-specific elements, the transaction does not eliminate OS as a likely potential competitor on any of those routes and does therefore not significantly impede effective competition on these routes, regardless of the relevant counterfactual.

(222) As the proposed transaction does therefore not lead to the elimination of potential competition on either of the routes on which OS currently operates, nor on the routes which are currently only served by LH, no competition problems arise, regardless of the counterfactual situation.

(2) Routes between Austria and Switzerland

(223) Direct-direct "overlaps" between OS and LH's subsidiary LX exist on the following routes between Austria and Switzerland.

(i) Vienna-Basel: served by OS; LX markets seats under code share;

(ii) Vienna-Geneva: served by OS; LX markets seats under code share;

(iii) Vienna-Zurich: served by both LX and OS who also code share.

(224) With regard to the Vienna-Geneva ("VIE-GVA") and Vienna-Basel ("VIE-BSL") routes, LX does not operate on these routes, but rather markets seats under a code-share agreement with OS. The parties submit that on both routes the code-share arrangement eliminates competition between LX and OS and that there is no residual competition.

(225) According to the notifying party, the code-share agreement between LX and OS is a standard "free-sale" (also "free-flow") agreement. The notifying party submits that the marketing carrier does not have its own reserved inventory on the aircraft in question. Instead, under a free-sale code-share agreement, the marketing carrier has real-time electronic access to the operating carrier's seat inventory. This means that prior to confirming a booking on the flight in question the marketing carrier must ascertain whether a seat in the appropriate category is still available. The operating carrier retains inventory control in order to ensure that the marketing carrier does not fill the flight with low-yield traffic (such as cheap restricted economy tickets for O&D passengers) when such bookings would squeeze out higher-yield passengers that the operating carrier could otherwise attract (such as O&D or connecting business class passengers). This is achieved by a process of "mapping" the carriers' respective fare classes and providing the marketing carrier access to seats in the relevant corresponding fare category on a "first come, first serve" basis. Thus, the marketing carrier is offered equal treatment in terms of accessing seats on a flight, without however undermining the operating carrier's yield management system.

(226) In standard free-sale code share agreements, the marketing carrier remains free to set its fares, subject to the "mapping" process that aligns the marketing and operating carrier's

booking classes. The operating carrier typically retains the revenue for the sector in question and pays the marketing carrier a commission. For direct flights on the route in question, the relevant revenue is the marketing carrier's ticketed fare, for indirect flights (for instance the Geneva-Vienna-Tel Aviv route), part of the ticketed fare for the whole journey is pro-rated to the code shared sector (for instance the VIE-GVA route) based on general industry principles or a specific agreement among the carriers (so-called special prorate agreements, or SPAs). The marketing carrier sells the tickets for a flight of the operating carrier exclusively under its own code.

a. The Vienna-Basel route

(227) The total number of passengers on the VIE-BSL route in 2008 was approximately [40 000 – 50 000]*, out of which [30 000 – 40 000]* passengers were O&D passengers. On VIE-BSL, the parties do not face competition from another operating carrier. The joint venture agreement between LH and OS does not cover the operations of LX, and therefore does not cover the routes between Austria and Switzerland. The route is currently served by OS while LX markets the seats of OS flights under a free-sale code-share agreement. The market investigation has indicated that there is no or limited competition between OS and LX due to their code-share agreement.

(228) While internal LH documents show that LH would consider entering the route if OS was bought by Air France-KLM,¹¹⁷ and further review of documents for the Swiss Management Board on the "Basel update and outlook"¹¹⁸ suggested that Swiss was considering possibly adding another aircraft to its Basel base, it seems unlikely that LH's subsidiary LX would enter this route. The route is currently served with [30 000 – 40 000]* O&D passengers and [40 000 – 50 000]* total passengers. As Basel airport is not a hub for LX, it could not rely on any large feeder traffic element, and it is thus unlikely that the route is thick enough to support two carriers that would have to share the current number of O&D passengers (although it is likely that Swiss would generate some additional demand on the route on its own).¹¹⁹ This is further confirmed by LX's profitability analysis that the Commission requested during phase II [...]*¹²⁰. Moreover, the Basel update also notes that "under the aspect of the unsatisfying results in the first year as well as the uncertain outcome of 2008 results it is questionable if a capacity increase should already be considered." Given the currently negative economic conditions that also characterized 2008, it thus follows that it is unlikely that Swiss will base another aircraft at Basel airport in the near future.

(229) The conclusion that the VIE-BSL route is not thick enough to support two carriers is also supported by internal OS documents indicating that OS would exit this route in case of

117 LH's internal document [...]*.

118 Management Board, 4.4. 2008, Basel update and outlook.

119 Moreover, with two carriers competing on the route, prices would be bound to go down, which further decreases the attractiveness of entering the route.

120 [...]*.

down-sizing in a stand alone scenario, which was further confirmed by OS' submission that shows that the route has been loss-making [...]*121.

(230) It follows that the transaction is unlikely to eliminate LX as a potential competitor on this route which is currently served by OS. As the transaction does therefore not lead to the elimination of a likely potential competitor on the route, it would not significantly impede effective competition, regardless of the relevant counterfactual or the precise market definition.

b. Vienna-Geneva

(231) In 2008 approximately [100 000 – 150 000]* passengers travelled on the route VIE-GVA, out of which [60 000 – 70 000]* passengers were O&D passengers. The route is served by OS while LX markets seats under the code-share agreement the details of which have been set out above.

(232) The route is served by OS while LX is only a marketing carrier. Considering the commercial balance between the operating and the marketing carrier in such code-share agreements it seems that there is limited residual competition between the parties on VIE-GVA and that the marketing carrier has limited ability and incentive to compete aggressively with the operating carrier for O&D traffic. This has been confirmed by the market investigation which showed that LX and OS currently compete only to a very limited extent on this route.

(233) An internal LH document indicates that if OS was acquired by Air France/KLM, LH would consider entry on VIE-GVA with [...] weekly frequencies if this is justified by [...]*.¹²² The Commission thus investigated whether there would be sufficient corporate demand such that LX would likely enter this route in the future.

(234) In recent years, LX significantly downscaled its operations out of Geneva airport ("GVA airport") in favour of its hub at Zurich Airport ("ZRH airport"). Its strategy from 1995 was to favour ZRH airport" as a hub and to limit its activities out of GVA airport. From 2002 (LX's first full year of operation) to 2006 (LX's first profitable year, following its acquisition by LH and turnaround), LX further downscaled operations out of GVA airport. The overall number of LX's planes was reduced by 50%, the number of intra-European routes from GVA airport was reduced by 60%, and the number of GVA flights was cut by 64%. Today, LX has only four or five aircraft based at GVA airport (out of 100 LX' aircraft based in Switzerland, principally in Zurich) and maintains a minimal level of activity at GVA airport to maintain its image as the Swiss national flag carrier.

(235) Moreover, during the phase II investigation, LH submitted a profitability analysis of all of LX's eleven intra-European routes out of GVA airport, [...]*. It is particularly noteworthy that two of these nine routes [...] have a significant O&D element of more than 100 000 passengers, and yet they are highly unprofitable. It would thus seem likely that the entry on

121 OS' presentation [...]*

122 LH presentation entitled [...]*

VIE-GVA would not be profitable for LX, as the total traffic of [100 000 – 150 000]* passengers (including the [60 000 – 70 000]* O&D passengers) would be divided between LX and OS. Moreover, prices would be reduced as a result of two carriers competing on the route.

(236) On the basis of the above, it is concluded that LX would not be likely to enter the market in the absence of the merger. It follows that the transaction is unlikely to eliminate LH/LX as a likely potential competitor on this route which is currently served by OS. The transaction therefore would not significantly impede effective competition on the common market on VIE-GVA, regardless of the relevant counterfactual or the precise market definition.

c. The Vienna-Zurich route

(237) Annually about [500 000 – 550 000]* air passengers travel on the Vienna-Zurich route ("VIE-ZRH") out of which [300 000 – 350 000]* passengers are O&D passengers. Both OS and LX operate on this route. They also code-share their flights on this route.

(238) On VIE-ZRH, LX currently operates 28 weekly frequencies and OS operates 27 weekly frequencies. Niki is the only competitor and operates 18 weekly frequencies albeit with larger aircrafts. Niki operates three daily frequencies on weekdays, one daily frequency on Saturdays and one daily frequency on Sundays. Since its entry in 2004 Niki has increased its weekly frequencies from 12 to 18, and in the relatively short period since its entry, Niki has been able to increase its market share significantly.

(239) According to the parties' estimates the market structure on the VIE-ZRH route in the Summer season 2008 and the Winter season 2008/2009 was as follows:

Airline	SS 08 figures on VIE-ZRH		WS 08/09 figures on VIE-ZRH	
	Time Sensitive	All passengers	Time Sensitive	All passengers
LX	[10-20]*%	[20-30]*%	[10-20]*%	[20-30]*%
OS	[10-20]*%	[10-20]*%	[10-20]*%	[10-20]*%
Combined	[30-40]*%	[30-40]*%	[30-40]*%	[30-40]*%
Niki	[60-70]*%	[60-70]*%	[60-70]*%	[50-60]*%
Air Berlin	0%	0%	0%	[5-10]*%
Others	0%	0%	0%	[0-5]*%

Source: Estimates of the parties on the basis of MIDT data¹²³

(240) On the basis of the market investigation the Commission has endeavoured to reconstruct the market for all passengers for the IATA summer season 2008 and the winter season 2008/09. The market shares are based on figures of flown passengers.¹²⁴

123 LH estimated market shares for some air carriers, whose bookings are not reflected in MIDT (like 4U, Niki, SkyEurope etc.) based on data published by the German Statistical Office and other publicly available information about schedules, frequencies and utilized aircraft, see paragraphs 336-347 of the Form CO. The parties did not consistently provide estimates for all airlines which are only partly covered by MIDT.

Figures on VIE-ZRH: all passengers		
Airline	SS 08	WS 08/09
LX	[40-50]%	[30-40]%
OS	[20-30]%	[10-20]%
Combined	[60-70]%	[50-60]%
Niki (incl. Air Berlin)	[30-40]%	[40-50]%

- (241) The market investigation has indicated that LX and OS compete on this route to a limited extent.
- (242) As regards Niki's position on VIE-ZRH, a considerable number of corporate customers does see Niki as a credible alternative to LH/OS for time sensitive customers and consider Niki's frequencies, flight schedules and prices attractive. In addition, the clear majority of travel agents consider Niki a credible alternative for time sensitive passengers. Thus, to a certain extent, Niki seems a credible alternative for both time sensitive and non-time sensitive passengers.
- (243) The finding that Niki constrains the merging parties to quite some extent is further confirmed by the additional booking analysis performed in phase II.
- (244) It results from this analysis that Niki is the largest carrier for the non-time sensitive segment that generally seems to book fairly early prior to departure, while it seems to constrain the parties to a considerable extent with regard to time sensitive passengers booking close to the date of departure, which is consistent with the findings from the qualitative analysis.
- (245) The finding that Niki represents, to a considerable extent, a credible constraint for time sensitive passengers is confirmed by the comparison of the average prices of the tickets bought by passengers that book close to the date of departure on the three carriers. Niki's prices seem to be more or less comparable to Swiss' prices, and, in certain months, Niki's tickets appear to be on average more expensive. Moreover, when compared with OS, Niki's tickets are consistently, albeit only slightly, more expensive.
- (246) In addition to this quantitative and qualitative analyses which indicate that Niki exerts a considerable competitive constraint on the parties, it is to be recalled that the VIE-ZRH route has already been examined in the previous Lufthansa/Swiss merger Decision¹²⁵ where the Commission authorised the acquisition of LX by LH subject to slot release remedies on several routes. With regard to the VIE-ZRH route, LH committed to release slots necessary to support up to four daily frequencies operated by a new entrant. This remedy will continue to be in place for this route after the closing of the transaction.

124 The comparability of the data collected in the market investigation from different companies may be affected by possibly different methods of data collection. In particular, the parties provided various sets of "flown passenger data".

125 See Case No. COMP/M.3770 – Lufthansa/Swiss.

(247) This possibility to obtain slots under the remedies of the Lufthansa/Swiss Decision considerably lowers entry barriers which would otherwise exist due to the fact that both VIE airport and ZRH airport are congested. In particular, with regard to ZRH airport, runway constraints exist during peak hours and most peak hours are completely full. The peak arrival times are between 06.00 to 06.55, 08.00 to 08.55, 11.00 to 11.55, 16.00 to 16.55, 19.00 to 19.55 and 21.00 to 21.55 and peak departure times are between 07.00 to 07.55, 09.00 to 09.55, 12.00 to 12.55 and 17.00 to 17.55. It follows that the remedies of the Lufthansa/Swiss Decision which will continue to be in place will significantly facilitate entry.¹²⁶ Those remedies not only enable new entrants to enter the route, but also allow Niki to further increase its frequencies on the route which would strengthen its market position in particular in relation to time sensitive passengers.

(248) Accordingly, in view of the competitive constraint exercised by Niki, combined with reduced barriers to entry on VIE-ZRH stemming from the remedies under the Lufthansa/Swiss Decision which will continue to be in place after the completion of the proposed transaction, the transaction would not significantly impede effective competition regardless of the relevant counterfactual or the precise market definition.

(3) *The Vienna-Brussels route*

(249) With respect to the Vienna-Brussels route ("VIE-BRU"), someone which [250 000 – 300 000]* O&D and [350 000 – 400 000]* total passengers travelled in 2008, OS operates five daily frequencies on weekdays and three and four frequencies on Saturday and Sunday respectively. In the IATA Summer season 2009 SN operates 3 daily frequencies on weekdays and 1 and 2 on Saturday and Sunday respectively, a total of 18 weekly frequencies. In the IATA Winter season 2008/09 SN operated 21 weekly frequencies and will also operate those frequencies in the coming winter season. SkyEurope, a low-cost carrier, entered this route in March 2007 and operates one daily frequency, albeit with larger planes. On 22 June 2009, Sky Europe filed for bankruptcy. However, it is still operating and it recently appears to have received some additional funds.¹²⁷

(250) It should be noted that FR started operations between the secondary airports on BTS airport – CRL airport in April 2009 with three weekly frequencies.

(251) As regards the relevant counterfactual, SN and OS currently compete on VIE-BRU. OS and SN do not have any bilateral or alliance agreement with respect to this route.

(252) According to the parties' estimates the market structure is as follows:¹²⁸

126 It should be noted that Niki entered VIE-ZRH with slots acquired under the normal slot allocation procedure in 2004, namely before the remedies of the Lufthansa/Swiss decision were in effect.

127 See: http://www.ftd.de/unternehmen/handel_dienstleister/:Angeschlagene-Fluglinie-SkyEurope-findet-Investor/547636.html.

128 LH estimated market shares for some air carriers, whose bookings are not reflected in MIDT (like 4U, Niki, SkyEurope etc.) based on data published by the German Statistical Office and other publicly available information about schedules, frequencies and utilized aircraft, see paragraphs 336-347 of the Form CO. The parties did not consistently provide estimates for all airlines which are only partly covered by MIDT.

Airline	SS 08 figures on VIE-BRU		WS 08/09 figures on VIE-BRU	
	Time Sensitive	All passengers	Time Sensitive	All passengers
SN	[0-5]*%	[20-30]*%	[0-5]*%	[20-30]*%
OS	[50-60]*%	[30-40]*%	[60-70]*%	[40-50]*%
BMI	[0-5]*%	0%	[0-5]*%	[0-5]*%
Combined	[50-60]*%	[50-60]*%	[60-70]*%	[60-70]*%
SkyEurope	[40-50]*%	[40-50]*%	[30-40]*%	[30-40]*%

Source: Estimates of the parties on the basis of MIDT data.

(253) The combined market share of the parties for time sensitive passengers seems to have been underestimated as the parties have based their market share estimates on a split between business class and economy class tickets and SN does not offer any business class tickets, but only flexible economy tickets. SN's response also suggests that SN sells a considerable percentage of fully flexible economy class tickets. Taking into account the fact that many corporate customers consider fully flexible tickets as suited to their needs in view of their time constraints, these tickets should be also considered as belonging to the market of time sensitive passengers. Also, SkyEurope's market share for time sensitive figures as provided by the parties seems highly overestimated.

(254) The table below illustrates the parties' and competitors' market shares on VIE-BRU on the basis of the market investigation.¹²⁹

WS 08/09 figures on VIE-BRU	
Airline	All passengers ¹³⁰
SN	[30-40]%
OS	[40-50]%
BMI	[0-5]%
Combined	[70-80]%
NE (SkyEurope)	[20-30]%

Source: transported passengers figures provided by the parties and SkyEurope.

(255) The parties argue that significant slot constraints are absent at BRU airport and VIE airport and that there would therefore be no substantial barriers to entry. According to the parties, competition concerns are unlikely to arise with respect to this route given that the parties face competition from SkyEurope and Ryanair and, in addition, EasyJet has operations at both VIE airport and BRU airport and could easily enter this route if OS/SN were to increase prices.

(256) In the market investigation, the majority of travel agents responded that customers would not switch to a competing carrier even in the case of a significant price increase by OS/SN.

¹²⁹ The comparability of the data collected in the market investigation from different companies may be affected by possibly different methods of data collection. In particular, the parties provided various sets of "flown passenger data".

¹³⁰ The Commission was not able to reconstruct the market for time sensitive passengers since SkyEurope does not distinguish between time sensitive and non-time sensitive passengers, but offers only one fare class and the price of tickets is purely driven by demand. It provided only a very rough estimate which could not be used for the purpose of market reconstruction. Its estimate seemed too high given its low number of frequencies and the average split between time sensitive and non-time sensitive passengers.

They also predicted a price increase by OS/SN on this route. In addition, many corporate customers stated that the merger will have an impact on this route and voiced concerns that the merger will reduce competition which will lead to increased prices.

- (257) In light of the above, under the current conditions and at the current level of services SkyEurope does not exert sufficient competitive pressure on the parties. The in-depth investigation has clearly confirmed that SkyEurope is not seen as credible alternative to the merged entity even for non-time sensitive passengers. With seven weekly frequencies, namely one daily flight, SkyEurope's services are clearly not an alternative for time sensitive passengers because this frequency does not allow for one-day return trips. In addition, the future of SkyEurope is unclear since the company has recently filed for bankruptcy and might undergo a restructuring process.
- (258) A pricing analysis conducted by the Commission also confirmed that SkyEurope does not constitute a strong constraint for the parties in the market for time sensitive passengers. In relation to business class tickets, the entrance of SkyEurope did not have a noticeable impact on SN and OS's prices. In relation to fully flexible tickets only SN's prices seemed affected while OS' prices seemed unaffected. Regarding non-time sensitive passengers the data did not allow for a conclusive answer.
- (259) FR's activities on BTS airport – CRL airport do not constrain the parties to any meaningful degree. FR started operating on BTS airport – CRL airport in April 2009 with three weekly frequencies. The market investigation has confirmed that flights from VIE airport to BRU airport and BTS airport to CRL airport are not in the same market, as (i) BTS airport is situated 87 km from Vienna city centre, which corresponds to a driving time of more than 60 minutes by car and 75 to 95 minutes by bus, and (ii) CRL airport is located 46 km from the centre of Brussels and is reachable by car in 45 minutes, by bus in 45 minutes or by train in 50 minutes. In addition, the operations between two secondary airports represent a far less immediate constraint than operations between two primary airports. The in-depth market investigation has confirmed that FR operations on CRL-BTS would not act as a competitive constraint on the merged entity, but rather, will create its new demand.
- (260) As regards the Air France-KLM counterfactual, it can be reasonably expected that OS and SN will continue to compete on this route and the transaction therefore raises serious doubts as to its compatibility with the common market also under this alternative foreseeable scenario.
- (261) In terms of barriers to entry, as explained in paragraph (118), VIE airport is congested during peak times. Peak times for VIE airport are between 08.30 and 11.00 and between 16.00 and 20.45. In the IATA Winter season 2008/2009 runway capacity has also been exhausted in the mornings as early as 07:35 until 11:50, with capacity being close to full as early as 06.00. Moreover, there are runway capacity limitations from 21.00 until 06.55. Regarding BRU Airport, although SkyEurope was able to enter the route in March 2007, the market investigation has shown that this airport is currently capacity-constrained during peak times (08.00-10.00 and 18.00-20.00). The capacity constraints at both airports mean that market entry is difficult.

(262) It is concluded from the above that regardless of the exact market definition, the proposed transaction raises serious doubts as to its compatibility with the common market on VIE-BRU, under any possible counterfactual and any possible market definition.

(4) *The Vienna-London route*

(263) On the Vienna-London route ([300 000 – 350 000]* O&D and [500 000 – 550 000]* total passengers), an overlap between the parties arises since OS operates Vienna-Heathrow while BMI code-shares on OS on this route by way of a standard free-flow code-sharing agreement. Irrespective of whether or not the transaction leads to the elimination of actual or potential competition, the parties face significant competition coming from British Airways ("BA") in any event, which also operates flights to Vienna from London Heathrow. The current competitive situation on the route is illustrated as follows.

Airline	SS 08 figures on Vienna-London		WS 08/09 figures on Vienna-London	
	Time Sensitive	All passengers	Time Sensitive	All passengers
OS	[50-60]*%	[40-50]*%	[50-60]*%	[50-60]*%
BMI	[0-5]*%	[0-5]*%	[0-5]*%	[0-5]*%
Combined	[50-60]*%	[50-60]*%	[50-60]*%	[50-60]*%
BA	[40-50]*%	[40-50]*%	[40-50]*%	[40-50]*%

(264) In addition, EasyJet serves Vienna-London Luton, and Aer Lingus opened a new base at London Gatwick in April 2009 from which it started operating flights to Vienna.

(265) It can be left open whether the services offered by Easyjet and Aer Lingus belong to the same market as the parties' services on London Heathrow-Vienna, since in any event no competition concerns arise due to the limited increment brought about the transaction and the presence of BA as a strong competitor of the parties on Vienna-Heathrow. This has also been confirmed by most respondents to the market investigation.

(266) It follows that also in relation to the Vienna-London route, the transaction would not significantly impede effective competition, regardless of the relevant counterfactual or the precise market definition.

(5) *Direct-indirect and indirect-indirect overlaps*

(267) The proposed transaction gives rise to a large number of affected routes concerning direct-indirect overlaps between LH and OS both within Europe and from European airports to extra-European destinations. The routes include both short- and medium-haul routes, and long-haul routes. In addition, numerous affected routes, on which both LH and OS provide indirect services, were identified. Also these routes include routes for short-, medium- and long-haul distances both within Europe, and from European airports to extra-European destinations.

(268) The routes were analysed with respect to the market position of the parties and the market share increment brought about by the transaction. Furthermore, the presence and position of

competitors and the number of passengers on each route were assessed. Where necessary, the number and duration of frequencies offered by competitors and their suitability for time sensitive passengers, in particular, were assessed. On the basis of these criteria, no competition concerns were identified. In addition, the market investigation did not reveal any competition concerns with respect to the identified direct/indirect and indirect/indirect overlaps with the exception of LH's and OS' market position in Central and Eastern Europe ("CEE").

- (269) Some respondents to the market investigation in phase I voiced concerns with respect to the strong market position of LH and OS in CEE, concerning mainly the post-transactional control by LH of a very substantial part of a so-called Central European market, particularly as a result of their control of the most important hubs catering CEE and their well-developed networks concerning this area. The results of the more refined phase II market investigation showed, however, that the vast majority of corporate customers in particular do not see any negative impact in relation to a potentially strengthened position of the merged entity for flights serving the CEE and indicated existing alternative competitors.
- (270) OS served 48 destinations in CEE,¹³¹ and LH 40 destinations¹³² in 2008, with 26 destinations being served by both LH and OS.¹³³ There appear, however, to be other significant competitors that serve CEE. In particular, Europe's largest carrier Air France/KLM serves 15 destinations in CEE using its own network, while it serves an additional 11 destinations in co-operation with its SkyTeam partners Aeroflot (the national airline of Russia that has a significant network in CEE due to its current and historical links with CEE countries) and CSA (the Czech flagship carrier).¹³⁴ In addition, the third largest European airline, BA, serves 13 destinations in CEE using its own network, while Malev (the Hungarian flagship carrier), a BA partner in the oneworld alliance, serves 22 destinations in CEE. Hence, there are other important carriers that serve CEE and that can provide an alternative to LH and OS.
- (271) The finding that Eastern European carriers can also provide an alternative to LH/OS is further confirmed by the market investigation that revealed that the vast majority of travel agents compare the LH/OS's prices with those of alternative carriers, including Eastern European carriers (such as MALEV or Czech Airlines). Also, the majority of corporate customers indicate that they do not procure their flights from one airline, but, depending on the CEE destination, search for flight alternatives with other carriers, including Eastern European carriers. It thus appears that there are other carriers competing with LH/OS in CEE and can offer alternatives to customers who want to fly to CEE destinations.

131 Source: OS internal documents, OS Management presentation dated September 2008, p. 3. From the 48 destination, 5 destinations are operated by partner airlines.

132 Source: OS internal documents, OS Management presentation dated September 2008, p. 3. From the 40 destinations served by LH, 23 destinations were served from the LH hub Munich.

133 In 2008, LH, LX and OS served each the following 8 destinations in CEE: Sofia, Prague, Budapest, Warsaw, Bukarest, Belgrade, Moscow, St. Petersburg. Moreover, LH and OS served each further 18 destinations: Tirana, Yerevan, Baku, Sarajevo, Minsk, Tbilisi, Zagreb, Astana, Vilnius, Riga, Krakow, Sibiu, Timisoara, Nizhniy Novgorod, Rostov, Ekaterinburg, Donetsk, Kiev.

134 Source: OS internal documents, BCG presentation to the Supervisory Board dated 28 July 2009, p. 90.

- (272) Some competitors indicated in the market investigation that a lack of air traffic rights to non-EU countries in CEE poses barriers to competition with regard to services to CEE destinations. The Commission is aware of the situation regarding traffic rights, however, recalls that Member States have the obligation to review the allocation of rights under air service agreements, and are also encouraged to give a prominent role to the competition criterion in this review.
- (273) On the basis of Regulation (EC) No 847/2004,¹³⁵ and in particular Article 5 thereof, Austria has to ensure the distribution of traffic rights among eligible Community air carriers on the basis of a non-discriminatory procedure when it concludes an agreement, or amends an agreement or its Annexes, that provide for limitations on the use of traffic rights or the number of Community air carriers eligible to take advantage of traffic rights. On the basis of Article 6 of Regulation (EC) No 847/2004, Austria notified the Commission of the procedures that will be applied, which are about to be published in the Official Journal of the European Union for information purposes. In those procedures,¹³⁶ the promotion of competition between providers of air services is one of the elements in the allocation of traffic rights under paragraphs 15 (3), (4), (5) of the procedures.
- (274) In light of the above, it is concluded that the proposed concentration would not significantly impede effective competition with respect to those routes.

B. Air transport of cargo

- (275) LH is active in the air cargo market through its wholly-owned subsidiaries LH Cargo AG and Swiss WorldCargo. It currently operates 15 freighter aircrafts¹³⁷ and sells capacity on chartered freighters, in addition to the "belly space" of its passenger flights. OS's activities in the cargo sector are rather limited as they rely on "belly space" cargo capacity on passenger flights.
- (276) As regards intra-European routes, the parties have estimated their combined market share to be approximately [10-20]*% in volume of the total air cargo transport in Europe and well below that percentage if alternative means of transport are taken into account.
- (277) As mentioned in section V of this Decision, air cargo markets are unidirectional and, regarding routes from Europe to Asia and the Middle East, are assessed on a continent to country basis. On intercontinental routes, the figures provided by the parties and based on

135 Regulation (EC) No 847/2004 of the European Parliament and of the Council of 29 April 2004 on the negotiation and implementation of air service agreements between Member States and third countries, OJ L 157, 30.4.2004, p. 7.

136 96. Bundesgesetz über den zwischenstaatlichen Luftverkehr 2008 (BGzLV 2008), published on 2 July 2008 in the Bundesgesetzblatt für die Republik Österreich. Paragraph 16 (3) of the procedures foresees the reallocation of allocated scarce traffic rights by the Austrian Ministry for Transport, Innovation and Technology on the expiry of five years after a previous allocation of traffic rights.

137 In March 2009 Lufthansa Cargo decided to temporarily remove four freighters from its fleet.

the parties' best estimates¹³⁸ show that combined, the parties will exceed [10-20]*% of the market share on the following routes: Europe-North America, North America-Europe, Europe-Iran, Iran-Europe, Europe-India, Armenia-Europe, Europe-Kazakhstan.

(278) On the routes Europe-North America, North America-Europe, Europe-Kazakhstan, Europe-Iran, the increment after the merger is very small, as OS has a market share of less than [0-5]*% on all these trade-lanes. Moreover, on all these trade-lanes the parties' combined market share does not exceed [20-30]*% (on the basis of incomplete CASS data) or [10-20]*% (on the basis of the parties' best estimates).

(279) With regard to the other routes, the overlap is more significant but still small:

	Market shares based on parties' estimates	
	LH's market share (including LX and BMI)	OS's market share
Armenia – Europe route	[10-20]*%	[5-10]*%
Europe – India route	[20-30]*%	[0-5]*%
Iran – Europe route	[10-20]*%	[0-5]*%

Source: Form CO.

(280) Armenia-Europe is a thin route with outbound traffic of less than [500 – 1000]* tonnes a year. On such small trade lanes, the merged entity still will face competition from Aeroflot, Air Armenia, Armavia, Czech Airlines and Air Baltic.

(281) Iran to Europe is also a relatively thin route with traffic of [1 000 – 5 000]* tonnes a year. The parties' market shares are outweighed by those of Iran Air ([40-50]*%) and Air France-KLM ([20-30]*%). Other competitors such as Emirates and Turkish Airlines are present on this market.

(282) With regard to Europe-India, the merged entity still will face competition from important and effective competitors such as BA, whose market shares are comparable to those of the parties, and Singapore Airlines, Cathay Pacific and Jet Airways.

(283) The Commission has also analyzed these markets on the basis of CASS and/or WorldACD data only. On such a basis, the merged entity would have market shares exceeding [10-20]*% on five additional routes: India-Europe, Israel-Europe, Russia-Europe, Europe-Armenia and Syria-Europe.

(284) According to such data, the parties' market share would be over [40-50]*% on the trade lane from Israel to Europe and from Russia to Europe only. However, as noted, no reliable, public market data for the transport of cargo is available and CASS and/or WorldACD data do not reflect the entire air cargo markets. CASS does not include sales to agents that are not

138 It should be noted that as there are no public sources offering reliable market data for the transport of cargo towards Asian and Middle Eastern countries, the market shares referred to in this analysis are based on the parties' best estimates on the basis of incomplete CASS data.

registered with IATA, nor direct sales to end-customers. Further, CASS does not include cargo transported by integrators such as DHL, FedEx and UPS. WorldACD data reflect an even smaller proportion of the market as only twenty-four carriers provide their data to WorldACD.

- (285) As a matter of fact, on the trade lane from Israel to Europe, other important carriers like EL Al, CAL (an Israeli all cargo airline) and MNG (an all cargo airline) are also active and are not reflected in the data referred to in the preceding paragraph. Similarly on the trade lane from Russia to Europe, Aeroflot, whose activities are not reflected in the available data, also operates on that route, as well as other significant competitors such as Air France-KLM and Cargolux (an all cargo airline). In the same way, other effective competitors such as BA, Singapore Airlines, Cathay Pacific and Jet Airways (from India to Europe), Aeroflot, Air Armenia, Armavia, Czech Airlines and Air Baltic (from Europe to Armenia) and Cargolux and Turkish Airlines (from Syria to Europe) operate on the India-Europe, Europe-Armenia and Syria-Europe trade lanes. Again, many of those competitors' activities are not reflected in the available data.
- (286) The available data are therefore substantially incomplete: the data do not represent all the players on the markets and do not reflect the real markets sizes and therefore significantly overestimate the parties' market shares. For this reason and in light of the presence of strong competitors on all of the five trade-lanes, the Commission considers that these routes do not raise any competitive issue.
- (287) More generally, it follows from the above that on all the affected routes, other significant competitors are present (combined airlines, all cargo carriers and, to a lesser extent, integrators) that are in a position to substantially constrain the competitive position of the parties in all possible segments of the market. Barriers to entry are lower than in the scheduled passenger air transport services, given the existence of the flexibility of cargo carriers as regards schedules and the possibility to use alternative airports, as shown by the market investigation. The Commission has found that companies operating freighter aircrafts can easily enter new routes in response to demand. As a matter of fact new entrants have entered some of the above routes. Moreover, the market investigation indicated that there is available capacity on the market.
- (288) Finally, the market investigation revealed that contracts are normally concluded for a short duration (six months to a year) and with no exclusivity clause, which allows customers to switch easily between different suppliers.
- (289) In the light of the above, the proposed transaction would not significantly impede effective competition on any of these markets.

C. Supply of airline seats to tour operators

- (290) Both LH and OS sell airline seats to tour operators. In addition, LH exercises, together with Turkish Airlines, joint control over the airline SunExpress, which sells seats to tour

operators and is active in both Germany and Austria. LH and OS are selling more seats to tour operators on short- and medium-haul flights than on long-haul flights.

- (291) The notifying party estimates the size of the market of supply of airline seats to tour operators on short- and medium-haul flights in 2008 at [0-5]* million seats sold in Austria and [20-30]* million seats sold in Germany; a combined Austria-Germany market would thus amount to [20-30]* million seats in 2008.
- (292) On the basis of a combined Austrian-German market for short- and medium-haul flights, the combined market share of the parties would be [10-20]*% (LH [5-10]*%¹³⁹/SunExpress [0-5]*% and OS [0-5]*%). For the German market, OS has a market share of [0-5]*% and LH [5-10]*%/SunExpress [0-5]*%. The combined market share would be [5-10]*%. Neither a combined Austrian-German market nor a German market for short- and medium-haul flights would be technically affected as the combined market share of the parties is below [10-20]*%.
- (293) On an Austrian market for short- and medium-haul flights, OS has a market share of [30-40]*%, LH has a market share of [0-5]*% and Sun Express has a market share of [5-10]*%. The combined market share of the parties would be [40-50]*%. The notifying party estimated that the biggest competitor, FlyNiki, also has a market share of [40-50]*%.¹⁴⁰ Further competitors Tunis Air and Nouvel Air have market shares of around [5-10]*% each.
- (294) The market of the supply of airline seats to tour operators on long-haul flights was estimated by the notifying party at [300 000 – 350 000]* seats sold in Austria and [3 500 000 – 4 000 000]* seats sold in Germany. A combined market Austria-Germany would thus amount to [3 500 000 – 4 000 000]* seats in 2008.
- (295) The combined market shares of the parties on a German, Austrian and a combined Austrian-German market for long-haul flights are in all three cases between [5-10]*% and [5-10]*% and thus below [10-20]*%. On this basis, the markets are technically not affected.
- (296) In the market investigation, some competitors pointed to a strengthening of the position of the combined entity. While some customers indicated that they see a risk of reduction of OS services following the transaction as well as a possible worsening of competitive conditions offered to tour operators, the majority of customers did not see any major impact on their activities.
- (297) In view of the above, and in particular due to the strong market presence of FlyNiki in the Austrian market and the relatively small increment brought about by the transaction, the proposed transaction would not significantly impede effective competition on the market for the supply of airline seats to tour operators.

139 The market share of LH entails a [0-5]*% market share of 4U which is only active in the German market for wholesale supply of airline seats to tour operators.

140 The market investigation suggests that the parties overestimated their own market shares.

D. MRO services

- (298) LH is active in MRO through its wholly-owned subsidiary Lufthansa Technik ("LHT") and provides line maintenance, heavy maintenance, components maintenance and engine maintenance services. OS is active in the provision of line maintenance for its own fleet and for several third party customers through Austrian Technik. OS also provides limited heavy maintenance services at VIE airport and BTS airport and limited components maintenance services at VIE airport.
- (299) With regard to heavy maintenance, components maintenance and engine maintenance services, the overlap between the parties' activities is marginal, in light of the fact that OS' market shares both at a world-wide level and at a European level do not exceed [0-5]*%. Moreover, in a market characterized by the presence of many important providers of MRO services (such as Air France Industries, KLM Engineering, SAS Components, British Airways Engineering & Maintenance as well as independent providers such as SR Technik, Aveos, Delta Tech Ops and others), the combined entity's market shares will not exceed [10-20]*% in any of the relevant markets. In light of the limited market shares of the parties, the transaction does not raise any vertical issue.
- (300) With regard to line maintenance, OS is only active in Austria, where LH does not operate. Consequently, no horizontal overlap arises between the parties' activities. With respect to vertical issues, it should be noted that Austrian Technik provides limited line maintenance services to LH: at VIE airport the line maintenance services provided by Austrian Technik to LH represent only [5-10]*% of the line maintenance services provided to third customers. Similarly, the line maintenance services provided to OS represents a limited percentage of LHT line maintenance services in each of the airports where LHT is active: with regard to German airports, the line maintenance services provided by LH to OS represent [0-5]*% of all line maintenance services provided to third customers in Germany. Moreover, LHT only accounts for 10 to 20% of the line maintenance provided out of BRU airport and does not provide line maintenance to OS, while SN does not provide MRO services to third parties.¹⁴¹ Consequently, the transaction will only have limited effects on those markets. For these reasons, the Commission considers that the transaction will not lead to any foreclosure by the parties in these markets.
- (301) In light of the above the proposed transaction would not significantly impede effective competition on any of the above markets for MRO services.

E. In-flight catering

- (302) LH is active in the in-flight catering markets through LSG Lufthansa Service Holding AG ("LSG"), operating under the brand name LSG SkyChefs, which provides catering services

¹⁴¹ With the exception of one or two customers per year and limited to Avro aircrafts.

to LH as well as to third party customers. OS does not have any activities in these markets but purchases catering services from external suppliers.

- (303) As mentioned in the market definition (section V of this Decision), the Commission has recently found that new types of in-flight catering services have come to existence. However, as LH is only active in the traditional catering services, the following analysis only refers to that segment.
- (304) With regard to vertical relationships between the parties, LSG used to provide catering to OS at several European airports but since October 2008 the latter has opted for return catering for all its short- and medium-haul flights, loading catering for both outbound and inbound flights at Vienna. In any event, the transaction will only have limited effects on those markets. In 2008, LGS accounted for approximately [0-5]*% of OS' total catering costs; moreover, the percentage of in-flight catering provided to OS represented a small percentage of LSG overall in-flight catering sales at each of the airports where LSG used to provide catering to OS (such percentage was below [0-5]*% at the majority of these airports and did not exceed [5-10]*% at any of them). For these reasons, the Commission considers that the transaction will not lead to any foreclosure by LH in these markets.
- (305) In light of the above, the proposed transaction would not significantly impede effective competition on the market for in-flight catering.

F. Groundhandling

- (306) Through local groundhandling companies, LH is active at Dresden airport, Leipzig airport, Friedrichshafen airport, and MUC airport. OS provides groundhandling services mainly at VIE airport and to some limited extent at other airports in Austria and abroad.
- (307) The parties' groundhandling activities do not overlap at any airport. On the other hand, the parties provide groundhandling services to one another at some airports. Within the EU, OS provides services to LH at VIE airport and at Timisoara airport, while LH provides services to OS at MUC airport and Dresden airport.
- (308) In light of the significant presence of the parties on the downstream market of scheduled air passenger transport, the markets for ground-handling at VIE, MUC and Dresden airports are considered vertically affected markets. However, it should be noted that at each of these airports, the parties' market shares in the markets for groundhandling never exceed 15%.
- (309) At VIE airport, OS' market shares in the groundhandling segment do not exceed [0-5]*% while many other effective competitors are active at that airport, such as Fraport Ground Services Austria GmbH and Flughafen Wien AG which operates VIE Airport and is the main provider of ground-handling services.
- (310) Similarly, the dominant provider of groundhandling services at MUC airport is the operator of the airport, Flughafen München GmbH, with a market share of [80-90]*%, while other competitors such as Aviapartner GmbH, Aerogate München Gesellschaft für

Luftverkehrsabfertigungen mbH and AHS Aviation Handling Services GmbH are also active. Consequently LH's market share at MUC airport is only marginal.

- (311) At Dresden airport, the main provider of groundhandling services is PortGround GmbH, an indirect subsidiary of the operator of the airport, which provides ramp handling services. Passenger handling services are provided by AHS Aviation Handling Services GmbH and Lufthansa Airport Services Dresden GmbH. The latter's market shares do not exceed 15%.
- (312) In light of the above the proposed transaction would not significantly impede effective competition on the market for groundhandling.

G. Impact of State aid granted to OS on effective competition

- (313) The Commission approved EUR 200 million rescue aid for OS on 19 January 2009.¹⁴² This rescue aid consisted of a cash deposit of EUR 200 million provided by ÖIAG in order to secure a EUR 200 million term loan facility for OS [...]*.
- (314) Furthermore, ÖIAG and LH have agreed that ÖIAG will grant EUR 500 million for a capital increase in OS.
- (315) By Decision adopted by the Commission on the same day as this Decision, the Commission has found that the granting of EUR 500 million by ÖIAG constitutes restructuring aid in favour of OS.¹⁴³ As a further consequence of this Decision, the rescue aid will have to be brought to an end.¹⁴⁴
- (316) This Decision needs to take into account the consequences which the rescue aid and the restructuring aid in favour of OS may have on the maintenance of effective competition in the markets described in sections A to F above.¹⁴⁵
- (317) Such additional funds at OS' disposal could strengthen its commercial position. However, it is to be recalled that OS is at present in a dire financial situation. Indeed, on 19 December 2008 Austria notified the Commission of its decision to grant rescue aid to the OS Group. On 22 December 2008 the Commission learned that a first tranche of EUR 67 million of this rescue aid was granted to OS to allow it to continue operations, before the Commission could take a position on its compatibility with the common market.
- (318) OS' perilous financial situation is further illustrated by the fact that any stand-alone OS operation would require additional funding, extending significantly beyond the amount of the rescue aid and the restructuring aid.¹⁴⁶ Furthermore, the rescue aid of EUR 200 million

142 Commission Decision of 19 January 2009 on State aid NN 72/2008, Austrian Airlines – Rescue aid.

143 Commission decision of on State aid C 6/2009.

144 Commission Decision of 19 January 2009 on State aid NN 72/2008, Austrian Airlines – Rescue aid, paragraph 71.

145 CFI, Case T-156/98 RJB Mining, of 31 January 2001 ECR (2001), II-337, paragraph 114, CFI, Case T-374/00 Verband der freien Rohrwerke and Others v Commission, of 8 July 2003, ECR (2003), II-2275, paragraph 169, and CFI, Case T-114/02 BaByliss v Commission, of 3 April 2003, ECR (2003), II-1279, paragraphs 440-441.

146 According to OS internal document [...]*.

has to a very large extent already been exhausted by OS in order to repay aircraft financing.¹⁴⁷

- (319) The extent of OS' financial needs is in line with the findings in Commission Decision C6/2009 adopted on the same day as this Decision, according to which the overall cost of restructuring OS exceeds EUR 500 million very significantly.¹⁴⁸
- (320) Against this background, OS is unlikely to have used or to use the rescue aid and the restructuring aid in a way that would call into question any of the findings in sections A to F above, such as preventing the expansion of competitors. Both the rescue and the restructuring aid aim at rendering the acquisition of OS by LH economically sustainable, in particular at securing the liquidity for OS, reducing its liabilities and restoring its profitability in the long term. The use of these funds by OS will also be monitored by the Commission in the future.¹⁴⁹
- (321) The rescue and restructuring aid at issue therefore primarily serve the purpose of helping to ensure the survival of OS.¹⁵⁰ Due to this purpose and due to their low level compared to the overall financial need of OS, it follows that none of the conclusions mentioned in sections A to F above are altered by the rescue and restructuring aid.
- (322) That conclusion is further underlined by the strong financial position of LH. Indeed, LH achieved operating results above EUR 1 billion both in 2007 and 2008 and had a total liquidity of EUR 5.2 billion (out of which a strategic minimum liquidity of EUR 2 billion) on 31 March 2009.¹⁵¹ Compared to such financial strength, any impact of the rescue and restructuring aid on the overall strength of the merged entity is limited.
- (323) In addition to all these reasons, with regard more in particular to the VIE-BRU, VIE-STR, VIE-CGN, VIE-FRA and VIE-MUC routes, the conclusion remains unchanged that the proposed transaction raises serious doubts as to its compatibility with the common market because it may significantly impede effective competition on these routes.
- (324) As regards all other markets mentioned in sections A to F above, for the reasons set out in this section, the State aid will not lead to any significant impediment of effective competition. With regard more in particular to the Vienna-Berlin, Vienna-Düsseldorf, Vienna-Hamburg, Vienna-Hannover, Vienna-Nuremberg, Munich-Linz, Vienna-Zurich and Vienna-London routes as well as the cargo markets, the markets for supply of airline seats to tour operators, MRO services, in-flight catering and groundhandling, it is to be further underlined that strong competitors are present on these markets.

147 According to OS internal document [...]*.

148 See paragraph 307 of the Commission decision on State aid C 6/2009.

149 Pursuant to Article 2(5) of Commission Decision C6/2009, the Commission shall until 2015 be provided with annual reports on the implementation of the restructuring plan assessed in that Decision.

150 Accordingly, clause 2 of the Amendment and Waiver Agreement between the Parties states that the amount of EUR 500 million is granted "for the purpose of financial restructuring". See also paragraph 268 of the Commission decision on State aid C 6/2009.

151 See LH financial outlook of 25 June 2009, accessible at <http://investor-relations.lufthansa.com/fileadmin/downloads/en/charts-speeches/LH-Financial-Outlook-2009-06-25-e.pdf>.

(325) Furthermore, as regards the direct-direct routes which are only served by one of the parties, the market investigation has not revealed that the granting of the additional funds to OS would change the findings in relation specifically to these routes, that is to say that the transaction would lead to the elimination of potential competition. On the contrary, the main reasons why no competition concerns arise in relation to these routes (namely low demand on most of these routes, entry strategies of LH and OS as evidenced by internal documents, absence of parallel operations pre-co-operation on almost all of these routes) apply irrespectively of the State aids at issue. Furthermore, with regard more in particular to the entry strategy of OS, the market investigation did not reveal any indications that OS would change its entry strategy in view of the additional funds at issue, which is also evidenced by the fact that OS already exhausted almost all the rescue aid without changing its entry strategy. It is therefore unlikely that OS would use any such additional funds to enter these routes.

VIII. EFFICIENCIES

(326) While the notifying party argues that the proposed transaction will likely generate significant cost savings and other efficiency gains for the benefit of consumers, LH has not put forward any evidence in support of such efficiencies. In particular, LH merely notes that small carriers such as OS suffer from inherent competitive disadvantages in areas such as fleet optimization and that without the transaction, OS would likely have to discontinue or at least massively reduce its activities. At the same time, LH points to its successful integration of LX and argues that the transaction will have comparable benefits to OS and its customers as LX' turnaround had on LX and its customers. As set out in the Horizontal Merger Guidelines, the three following cumulative conditions apply: (i) the efficiencies will benefit consumers, (ii) the efficiencies are merger specific and (iii) the efficiencies are verifiable. LH's broad claims clearly do not provide the necessary evidence for the Commission to accept that these three conditions are satisfied. It is thus concluded that there is not sufficient evidence that the efficiencies are verifiable, merger-specific, and that they would benefit consumers. Consequently, the Commission rejects the claim that efficiencies generated by the merger counteract the negative effects on competition identified in Section VII.

IX. COMMITMENTS SUBMITTED BY LH

(327) In order to address the competition concerns identified by the Commission during its market investigation on the VIE-STR, VIE-CGN, VIE-MUC, VIE-FRA, and VIE-BRU routes, LH submitted commitments on 10 July 2009 pursuant to Article 8(2) of the Merger Regulation. On 17 July 2009 and 27 July 2009, LH submitted revised versions of the commitments. Further to the submission of the revised version of the commitments on 27 July 2009, the Commission launched a market test in order to gather the opinion of competitors and customers on these commitments. In light of the results of the market test, LH presented a final version of commitments on 31 July 2009 ("the Commitments"), which addressed weaknesses identified in its previous proposal.

(328) The Commitments submitted by LH aim at reducing the barriers to entry and at facilitating entry of (a) New Entrant(s) or expansion of competitors already present on any

of the above-mentioned routes. The Commitments comprise a number of measures and consist, in particular, in the release and transfer of a number of slots at the airports in Vienna, Stuttgart, Cologne/Bonn, Munich, Frankfurt and Brussels, as well as several ancillary measures.

A. Description of the Commitments

(1) Commitments concerning slots

a. Slot release on city pairs with competition concerns

(329) Under the Commitments, the parties commit to make slots¹⁵² available, according to a specific procedure, at the airports in Vienna, Stuttgart, Cologne/Bonn, Munich, Frankfurt and Brussels on the five routes on which the Commission identified competition concerns¹⁵³ (hereafter the "Identified City Pairs").

(330) The number of slots to be made available shall enable a New Air Service Provider¹⁵⁴ (hereafter also referred to as the "New Entrant") to operate the following numbers of frequencies on the Identified City Pairs:

(i) VIE-STR: up to three (3) frequencies per day;

(ii) VIE-CGN: up to three (3) frequencies per day, but not more than 18 frequencies per week;

(iii) VIE-FRA: up to five (5) frequencies per day;

(iv) VIE-MUC: up to four (4) frequencies per day;

(v) VIE-BRU: up to four (4) frequencies per day, but not more than 24 frequencies per week.

(331) The number of slots will be reduced by the number of slots already transferred to a New Entrant under the Commitments, unless these slots cease to be served by the New Entrant and revert subsequently to the parties.

(332) With regard to all Identified City Pairs except for VIE-FRA and VIE-MUC, where specific provisions apply, frequencies already served by an airline independent of or

152 That is to say, a permission given to an aircraft to use infrastructure at a given airport on a specific date and time for the purpose of landing and take-off.

153 These are routes between the following city pairs: VIE-STR, VIE-CGN, VIE-MUC, VIE-FRA and VIE-BRU.

154 Defined as "Any airline or airlines that are each members of the same alliance (other than the Parties including all airlines controlling it/them or controlled by it/them), that individually, or collectively by Codeshare, provide(s) a new or additional Competitive Air Service". 4U or any other carriers controlled by the parties at any time during the application of the Commitments are not considered as eligible to obtain slots under the Commitments.

unconnected to the parties on an Identified City Pair shall be counted against the number of slots to be made available by the parties to that airline under the Commitments.

- (333) With regard to the VIE-FRA route, the two daily frequencies currently operated by Niki (three frequencies to the extent that Niki obtains a third slot from LH as from the IATA Winter Season 2009/2010) will be deducted from the number of slots to be made available under the Commitments. If Niki were to exit one or more of these frequencies in advance of acquiring grandfathering rights, such frequencies will be made available to New Entrants under the Commitments.
- (334) Niki will be entitled to exchange the slots it received from LH in Frankfurt according to the existing slot lease agreement between LH and Niki against slots, which LH makes available under the Commitments. However, in order to take LH's wave structure at FRA airport into account, LH shall not be obliged to transfer to Niki more than one slot at FRA airport during each of the following time periods:¹⁵⁵

Arrival	Departure
05:35 - 08:00	06:30 - 08:15
08:05 - 10:20	08:20 - 11:35
10:25 - 14:00	11:40 - 15:05
14:05 - 15:30	15:10 - 16:15
15:35 - 17:50	16:20 - 19:45
17:55 - 21:50	19:50 - 22:25

- (335) Furthermore and regardless of whether Niki opts for obtaining new slots from the parties in exchange for its current slots at FRA airport,¹⁵⁶ LH undertakes to amend its existing slot lease agreement with Niki to reflect the provisions of the Commitments, in particular as regards the possibility for Niki to acquire grandfathering rights with regard to these slots, as described in more detail in paragraph (342) (whereby the period necessary to obtain grandfathering rights foreseen in the Commitments will begin with the start of the IATA Winter Season 2009/2010).
- (336) In addition, and only if no applicant that is not member of Star Alliance requests a remedy slot for the IATA Summer season 2010 (or the first season for which the procedures for implementation of the Commitments would be in place, whichever is the later) one frequency operated by Adria Airways will be deducted from the number of slots to be made available under the Commitments. Such a deduction would initially apply for a period of four consecutive IATA seasons and for every subsequent period of two years until a Non-Star Alliance applicant requests a remedy slot.

¹⁵⁵ If Niki already has two slots in one time period, LH shall be obliged to grant any request by Niki to exchange up to two slots in that time period, but shall be entitled to ensure that the relevant slots are at least 105 minutes apart.

¹⁵⁶ Niki may retain any or all of its existing slots for which it would not seek an exchange.

- (337) Moreover, LH undertakes to amend its existing agreements with Adria Airways with respect to one slot to reflect the provisions of the Commitments, provided however that Adria Airways shall not acquire grandfathering rights.
- (338) With respect to the VIE-MUC route, where Niki currently operates three daily frequencies for which it received slots via the normal slot allocation procedure, the Commitments provide that Niki will be entitled to exchange its current slots on this route against slots which LH makes available under the Commitments. Regardless of whether or not Niki decides to re-time its current slots under the Commitments, Niki's frequencies shall be deducted from the total number of slots to be made available by the parties on this route. If Niki were to exit from one or more of its frequencies,¹⁵⁷ such frequencies will be made available to New Entrants under the Commitments.
- (339) Finally, with respect to the routes VIE-STR and VIE-CGN, LH is already obliged to make slots available to New Entrants on the basis of a previous merger decision, namely the Commission's Decision in case COMP/M.3940 – Lufthansa/Eurowings.¹⁵⁸ To the extent that the parties have already made slots available to a New Entrant pursuant to the commitments in that case, such slots will be counted against the number of slots to be made available pursuant to the Commitments in this case. New Entrants will be able to choose slots for these two routes pursuant to which commitments they want to apply, namely those submitted in the previous case or those submitted in this case.

b. Conditions pertaining to the slot transfer

- (340) The slot transfer procedure foreseen by the Commitments will run in parallel with the normal slot allocation procedure. An airline wishing to obtain slots on one of the Identified City Pairs will request slots through the normal slot allocation procedure and apply for a slot transfer under the Commitments at the same time. If the applicant's slot request to the slot coordinator is not met as a result of the IATA Scheduling Conference, the Commitments provide that the parties must offer to transfer the requested slots to the applicant within one week following the applicant's commitment to operate them. Slots must be released free of charge and within 20 minutes of the time requested by the applicant if either of the parties has slots available in this timeframe. Otherwise, the parties must offer the slots closest in time to the applicant's request.
- (341) The slot lease agreement between the parties and the applicant must be signed and the transfer performed within three weeks after the Slot Handback Deadline, which is 15 January for the IATA Summer season and 15 August for the IATA Winter season. The slot lease agreement will have a duration equal to the Utilization Period of the relevant Identified City Pair,¹⁵⁹ but the New Entrant will have the right to terminate the agreement at the end of

157 As regards slot obtained by Niki under the present Commitments, this only applies if Niki has not yet obtained grandfathering rights at the time of its exit.

158 Case No. COMP/M.3940 – Lufthansa/Eurowings.

159 I.e. two consecutive IATA seasons for all Identified City Pairs except for the route VIE-FRA, and eight consecutive IATA seasons for VIE-FRA.

each IATA season without penalty. Finally, the Commitments provide that a New Entrant who decides to operate the greatest number of routes will be favoured.¹⁶⁰

c. Grandfathering rights

(342) The Commitments also provide for the New Entrants' possibility to acquire grandfathering rights in relation to slots obtained from the parties. The New Entrant will obtain grandfathering rights over these slots, that is to say, will be entitled to use the slots transferred from the parties at both ends of any Identified City Pair for a different intra-European city pair than the Identified City Pairs, once it has served the relevant Identified City Pair(s) during two full consecutive IATA seasons for all Identified City Pairs except for the VIE-FRA route; and eight consecutive IATA seasons for the VIE-FRA route (respectively, the "Utilization Period"). By contrast, if the New Entrant ceases to operate the slots transferred in the relevant Identified City Pair before the end of the Utilization Period, these slots will be handed back to LH and will be made available under the Commitments for another New Entrant.

d. Star Alliance members as New Entrants

(343) The above described provisions are only fully applicable to New Entrants which are not members of Star Alliance.

(344) In principle, Star Alliance members can also obtain slots in the framework of the Commitments but non-Star Alliance members will be given a higher priority if several potential entrants apply for slots on the same route under the Commitments. Priority will always be given to a non Star Alliance applicant, that is, even if the Star Alliance Member applies for a larger number of routes than a non-Star Alliance applicant.

(345) Furthermore, a Star Alliance entrant will not have the possibility to acquire grandfathering rights in relation to slots obtained from the parties. A Star Alliance entrant will not be able to enter into code-share agreements or revenue-sharing/profit-sharing joint ventures with the parties or other Star Alliance partners on the Identified City Pairs. When the Star Alliance member ceases operating any of the slots released under the Commitments, the parties have to offer these slots to New Entrants again.

(346) Lastly, if a Star Alliance member obtains slots under the Commitments, specific conditions can be imposed by the Commission, notably to guarantee the independence of the Star Alliance applicant from the parties.

¹⁶⁰ This applies only in case there are at least two applicants that are not member of Star Alliance.

(2) *Other commitments and other provisions*

a. *Special prorate and code-share agreements*

(347) The Commitments offer a New Entrant the possibility to enter into a special prorate and code-share agreement allowing the New Entrant to place its codes on flights with a true origin and destination in either Austria, Germany and/or Belgium, provided part of the journey involves an Identified City Pair. The conditions of such a special prorate agreement shall be such that the New Entrant has equal treatment with LH's Star Alliance partners on the same Identified City Pair.

b. *Other provisions*

(348) The slot release commitments are supplemented by other commitments such as the possibility for a New Entrant to conclude interlining and Frequent Flyer Programme access agreements with the parties as well as intermodal agreements with a railway or other surface transport company.

(349) The Commitments foresee the appointment of a Monitoring Trustee who will monitor the parties' compliance with the Commitments and will assist the Commission during the slot transfer procedure provided for by the Commitments.

(350) The Commitments also contain provisions on fast-track dispute resolution according to which the New Entrant can decide to settle any dispute with the parties in relation to the Commitments through arbitration. Both the New Entrant and the parties will then be bound by the arbitration decision. The burden of proof in any dispute requires the New Entrant to provide *prima facie* evidence of its case and the parties to provide evidence to the contrary.

(351) The Commitments, in particular the obligation of slot transfer, are indefinite in time but contain a review clause.

B. Analysis of the Commitments

(352) Concerning the suitability of commitments aiming at facilitating entry of a new competitor, the Commission notice on remedies acceptable under the Merger Regulation and under Commission Regulation (EC) No 802/2004¹⁶¹ ("the Commission notice on remedies") states that "[o]ften, a sufficient reduction of entry barriers is not achieved by individual measures, but by [...] a commitments package aimed at overall facilitating entry of competitors by a whole range of different measures."

(353) The Commitments submitted by the notifying party constitute a comprehensive package which takes into consideration past experience with commitments in merger cases in the

¹⁶¹ OJ C 267, 22.10.2008, p. 1.

aviation sector. The Commitments have generally received a positive evaluation from the competitors, customers and other market participants who replied to the market test.

(1) *Slots*

(354) The Commitments take account of the fact that slot congestion is the main entry barrier on the problematic routes in this case. In effect, with the exception of CGN airport, which is a "Schedules Facilitated" airport,¹⁶² all the airports concerned by the Identified City Pairs are congested (and in some cases heavily so). In the light of this, the Commitments are designed to remove this barrier and foster entry on the routes where competition concerns were identified.¹⁶³

a. *Number of slots*

(355) The slots made available by the parties will enable existing competitors or one or more New Entrants to sufficiently replace the competitive pressure between the parties that is eliminated by the proposed transaction.¹⁶⁴

(356) Concerning all Identified City Pairs the market test has largely confirmed that the number of slots offered in the Commitments is sufficient for another player(s) who will offer new or additional frequencies to effectively compete with the parties.

(357) Some respondents have voiced concerns with regard to the fact that the Commitments foresee a deduction of frequencies of existing players on the VIE-FRA and VIE-MUC routes from the number of slots to be made available under the Commitments for these routes and thus limit in particular entry on these routes.

(358) However, both the VIE-FRA and the VIE-MUC route present particular circumstances which justify such a deduction of frequencies of existing players in this case:

Vienna-Frankfurt

(359) As regards the VIE-FRA route, it should be noted that both Niki and Adria Airways have entered this route on the basis of slots that LH made available to these players with a view to

162 A "scheduled facilitated airport" is an airport with potential for congestion but which is amenable to resolution by voluntary co-operation between air carriers and where a schedules facilitator has been appointed to facilitate the operations of current and intended operators at that airport.

163 Although CGN airport is not coordinated, VIE airport is congested with slot shortage during peak times. The slot pairs offered on the VIE-CGN route will therefore also serve to facilitate entry on this route, notably at VIE airport.

164 In this regard, it should be noted at the outset that the level of frequencies presently operated by the parties does not result from an independent operation pre-merger, but is primarily based on a "divisions of tasks" in the framework of their joint venture co-operation. Indeed, the parties' joint venture co-operation has for operational reasons led at various instances to a change of operating carriers and/or level of frequencies operated by both parties (See for example Form CO p. 63, "LH/AUA Self-Assessment" p. 4 and reply of the parties to question 21 of request for information of 27 April 2009). It follows that the level of frequencies currently operated by the parties only has a limited relevance for the level of frequencies required under the Commitments in order to remove the serious doubts identified for the relevant routes.

complying with Community competition rules. As explained in paragraph (65), the Commission exemption decision of 2002 essentially consisted in a commitment of the parties to make slots available to (a) New Entrant(s) for any Austria-Germany route chosen by it/them up to a maximum of 40% of the slots that LH and OS operated on the route in question. LH appears to have made available slots to Adria Airways in 2001 by means of a lease agreement in view of the imminent exemption decision.¹⁶⁵ Similarly, as explained above in paragraph (162), Niki entered the route in 2006 on the basis of two slots at FRA airport which LH transferred to Niki by means of a lease agreement with a view to complying with Article 81 of the Treaty following the parties' self-assessment, and it recently received a further slot from LH in order to operate a third frequency on the route as of the winter season 2009/2010.

(360) As the slots currently used by Niki were thus effectively made available by LH, it appears justified to deduct Niki's frequencies from the number of slots to be made available under the Commitments, subject to the further provisions in the Commitments (such as the possibility of re-timing). For the same reason, and taking into account the fact that the competitive constraint emanating from Adria Airways upon the parties is limited, it appears justified to further deduct one frequency of Adria Airways, subject to the further provisions in the Commitments (temporary restriction of such a deduction etc.). However, such a deduction of an Adria Airways' slot only takes place unless an applicant that is not member of Star Alliance submits a slot request for the summer season 2010.¹⁶⁶ In addition, the deduction of an Adria Airways' slot is not permanent but New Entrants have the opportunity to apply for that slot every four IATA seasons or in case Adria Airways ceases its operations on the VIE-FRA route.

(361) This conclusion is reinforced by the fact that the Commitments on VIE-FRA are designed so as to allow either expansion of Niki, which could obtain up to two additional slots in addition to the three slots already transferred to it, or entry of a new player with two frequencies, subject to the circumstances outlined above.¹⁶⁷

(362) These considerations are confirmed by the positive overall assessment of the remedies for this route in the market test. Indeed, a majority of respondents take the overall view that the Commitments will enable Niki and/or a New Entrant to provide a competitive and viable air service on the VIE-FRA route. Furthermore, respondents widely agree that the Commitments overall sufficiently facilitate and increase the likelihood of entry/expansion, and thus solve the competition concerns on the VIE-FRA route.

Vienna-Munich

(363) As regards the VIE-MUC route, it is to be recalled that Niki already operates the route with three frequencies which it obtained under the normal slot allocation procedure. In order to assess the impact of a deduction of Niki's existing frequencies on the effectiveness of the

165 See reply to request for information to Adria Airways of 22 July 2009.

166 Or the first season whereby the procedures for implementation of the present Commitments would be in place.

167 In particular, in order to receive more than one additional slot, Niki and/or a new entrant need to apply for remedy slots for the IATA season summer 2010 or periods of two years afterwards.

Commitments, it is illustrative to distinguish the situations in which Niki may either wish (i) to expand its existing services; (ii) to exit the route; or (iii) to maintain the current level of frequencies.

(i) With regard to an expansion of Niki's existing services, it should be recalled that according to the findings of the market investigation mentioned in paragraphs (147) et seq., Niki does not represent a sufficient competitive constraint on the parties, due in particular to the timing of its flights and the number of its frequencies. The Commitments allow Niki both to obtain an additional slot as well as to re-time all of its existing frequencies and therefore sufficiently address the shortcomings of Niki's existing services on the route. Accordingly, almost all respondents to the market test consider that the Commitments enable Niki to provide a viable and competitive air service.

(ii) If Niki decided to leave the route, the Commitments would enable (a) New Entrant(s) to enter the route with up to four frequencies, thus allowing the New Entrant(s) to provide a viable and competitive air service.

(iii) If Niki decided to maintain its current level of frequencies, any New Entrant would only be able to obtain one slot under the Commitments. While the provision of competitive air services in particular for time sensitive passengers generally requires more than one daily frequency, it should be noted, as mentioned in footnote 80 above that MUC airport expects significant capacity extensions to be in place in the near future. In particular, a third runway is currently in the second phase of an extensive approval process and is expected to be operational as of 2011. This third runway will increase co-ordination of up to 120 movements per hour compared to 90 movements per hour with the existing two-runway system and will be available to both terminals at MUC airport. These planned capacity extensions increase the likelihood that New Entrants would in the near future (in particular once the economic climate for air transport services referred to below in paragraphs (384) and seq. has improved) be able to obtain slots under the normal slot allocation procedure.¹⁶⁸ At the same time, they can obtain one slot under the Commitments in relation to which they can have grandfathering rights after two seasons and which will therefore further incentivise them to enter the route.

(364) The Commission considers that these elements taken together justify a deduction of Niki's existing frequencies from the slots to be made available under the Commitments and will therefore allow Niki and a New Entrant to adequately reproduce the constraining effect that LH and OS would exercise upon each other in the absence of the transaction.

(365) Those conclusions are further in line with the overall assessment of the remedies for this route in the market test. In particular, respondents widely agree that the Commitments solve the competition concerns on the VIE-MUC route. Furthermore, a majority of respondents take the view that the Commitments overall sufficiently facilitate and increase the likelihood of entry/expansion, and thus enable Niki and/or a New Entrant to provide a competitive and viable air service on the route.

¹⁶⁸ In this context it should be noted that Niki was able to commence its services on the VIE-MUC route in 2007 on the basis of slots it has obtained in the normal slot allocation procedure.

b. Allocation of slots

- (366) The slots must be allocated within only 20 minutes from the initial request which allows tightly adjusted schedules in order to ensure short turnaround times. Furthermore, apart from LH's wave structure at FRA airport referred to in paragraph (334), the Commitments contain no limitations concerning the transfer of slots in peak times, which increases the attractiveness of the slots offered. Moreover, the Commitments contain more convenient and efficient procedures for the allocation of slots than the procedures foreseen by remedies in previous airline merger cases. The enhanced slot allocation mechanism in this case enables New Entrants to submit their slot allocation requests much earlier in the season, thus giving such New Entrants sufficient time to launch and market their new services.
- (367) Moreover, already for the duration of the slot lease agreement and, in any case, once the New Entrant has acquired grandfathering rights, it will not have to go through the slot allocation procedure provided for in the Commitments every season.¹⁶⁹ The market test has confirmed the efficiency of the slot allocation mechanism proposed. In fact, a large majority of the respondents considered that the procedure foreseen by the proposed remedies for the slot release would allow a New Entrant to obtain the required slots in a timely and satisfactory manner.

c. Possibility for Niki to exchange slots on the Vienna-Frankfurt and Vienna-Munich routes and amendment of existing slot lease agreement regarding the Vienna-Frankfurt route so as to include the provisions of the Commitments

- (368) The Commitments provide that Niki will be entitled to exchange its current slots on the VIE-FRA and VIE-MUC routes against slots which LH makes available under the Commitments and that the existing slot lease agreement between LH and Niki for the VIE-FRA route will be amended so as to reflect the provisions in the Commitments (in particular, concerning the possibility of Niki to acquire grandfathering rights). These provisions enable Niki to better adapt the timing of its slots to demand and to improve its current offer and market position on both routes. As a result, Niki's offer is likely to become more attractive and Niki will be able to exert increased competitive pressure on the parties.
- (369) While the possibility for Niki to exchange its current slots for the VIE-FRA route is restricted by Section 1.1.3(iii) of the Commitments in view of LH's wave structure at FRA airport, that is, that LH shall not be obliged to transfer to Niki more than one slot at FRA airport during each wave as defined in that Section, the revised version of the Commitments of 31 July 2009 introduced several improvements in that regard.
- (370) First of all, if Niki already has two slots in one time period, LH shall be obliged to grant any request by Niki to exchange up to two slots in that time period, but shall be entitled to ensure that the relevant slots are at least 105 minutes apart. This ensures that Niki will be able to maintain its two slots in the attractive afternoon/evening wave (from 16.20 to 19.45) and to re-time all its existing slots.

¹⁶⁹ This is of particular relevance for the VIE-FRA route where the Utilization Period necessary for grandfathering is eight IATA seasons.

(371) Furthermore, the revised Commitments of 31 July 2009 clarify that Niki will also be free to retime any or all of its slots.¹⁷⁰

(372) These improvements ensure the effectiveness of the re-timing provisions on the route VIE-FRA.

d. Grandfathering rights

(373) The attractiveness of the Commitments is also enhanced by the prospect of acquiring grandfathering rights after a Utilization Period of only two full consecutive IATA seasons for slots on all Identified City Pairs except the VIE-FRA route, and eight full consecutive IATA seasons for the VIE-FRA route. Granting of grandfathering rights represents an additional incentive for New Entrants to enter on the Identified City Pairs as slots are particularly valuable assets especially at FRA, VIE and MUC airports due to considerable slot constraints at these airports.

(374) As regards the VIE-FRA route, while some respondents have voiced concerns as regards the length of this period, the longer Utilisation Period is justified by the higher value of the slots at FRA airport, which in turn increases the risk that an entrant would enter on the VIE-FRA route merely to obtain these valuable slots and to use them subsequently on other routes.¹⁷¹ Indeed, the market investigation revealed that FRA airport is far more congested than any other airport subject to the Commitments (see paragraph (182)) and in order to ensure utilisation of the slots to be made available by LH at FRA airport on the very route VIE-FRA a longer utilisation period appears to be justified. Furthermore, in line with previous Commission decision practice,¹⁷² a Star Alliance entrant will not have the possibility to acquire grandfathering rights in relation to slots obtained from the parties.

(375) The majority of the respondents to the market test confirmed that they consider the Utilization Period proposed in the Commitments after which grandfathering rights will be granted to the New Entrant as adequate.

(2) Other commitments and other provisions

a. Special prorata and code-share agreement

(376) Many respondents to the market test considered the possibility offered to the New Entrant(s) to enter into a special prorata and code-share agreement with the parties as an additional incentive to enter on the Identified City Pairs, while several other respondents only see limited added value in such agreements.

170 In addition, the revised Commitments of 31 July 2009 provide, with regard to the interaction of the "20 minute-rule" (see paragraph (340)) and LH's wave structure, that, in case a slot is granted by LH in a different wave than in which Niki had requested it, such a slot will be deemed to be granted in the time period in which Niki had requested it. This ensures that the "20 minute-rule" will not have a negative impact on the ability of Niki to obtain slots in LH's wave structure.

171 See also Case No. COMP/M.5335 – Lufthansa/SN Airholding, paragraph 454.

172 See Case No. COMP/M.5335 – Lufthansa/SN Airholding, paragraph 440.

b. Other provisions

- (377) As regards other provisions in the Commitments, such as the possibility for a New Entrant to participate in Frequent Flyer Programs, interlining agreements or intermodal agreements, respondents to the market test considered these provisions generally as additional, although not critical, incentives for a New Entrant. As regards interlining agreements, the Commission's investigation indicated that the lack of such a solution was in fact one of the reasons for third party carriers to exit routes between Germany and Austria.
- (378) As a further improvement introduced in the Commitments of 31 July 2009, a Monitoring Trustee, approved by the Commission, will have to be appointed before the closing of the transaction, thereby ensuring a swift implementation of the Commitments.
- (379) The Commitments of 31 July 2009 further foresee that the Monitoring Trustee will ensure that the availability of slots is made public well in advance of each IATA season. This provision will ensure and increase the future effectiveness of the Commitments. This is of particular importance for the VIE-FRA route where the slots currently held by Adria Airways will become available in two years intervals.

C. Overall assessment of the Commitments

- (380) With respect to commitments aiming at facilitating entry of new competitors, the Commission notice on remedies states they can be sufficient to remove the competition concerns raised by a proposed concentration in that they entirely remove any obstacle to effective competition, if they "actually make the entry of new competitors timely and likely". If it cannot be concluded that the lowering of the entry barriers by the proposed commitments will likely lead to the entry of new competitors in the market, however, the remedies package will normally be rejected.¹⁷³

(1) Interest expressed by competitors in entering or expanding on the Identified City Pairs

- (381) In this case, several competitors responding to the market test expressed interest in entering some or all Identified City Pairs in the IATA Summer season 2010. In particular, M.A.P. Management + Planning GmbH, a charter airline, expressed interest in entering all routes at issue with one to two frequencies. Furthermore, Croatia Airlines and Robin Hood expressed interest, under certain reservations, to enter with two frequencies on the VIE-MUC route and, respectively, on the VIE-STR and VIE-BRU routes.
- (382) It should also be noted in this context that some of the parties' most important competitors already have bases at almost all the airports concerned. More specifically, Niki has a base at

¹⁷³ It should be noted, however, that paragraph 63, footnote (4), of the Commission notice on remedies state that, in air transport mergers, a mere reduction of barriers to entry by a commitment of the parties to offer slots on specific airports may not always be sufficient to ensure the entry of new competitors on those routes where competition problems arise and to render the remedy equivalent in its effects to a divestiture.

VIE airport while its partner Air Berlin has bases at the airports of FRA, MUC and STR.¹⁷⁴ Furthermore, TUIfly, which currently does not compete with the parties on any of the Identified City Pairs and is in the process of being acquired by Air Berlin, has bases at FRA, MUC, STR and CGN airport. Moreover, SkyEurope which is currently under insolvency protection but reportedly received new capitals also has a base at VIE airport. These airlines therefore appear as plausible candidates for taking up the slot remedies at least on some of the routes.

(383) The market test of the commitments submitted on 27 July 2009 and the market investigation thus revealed some interest and indications for a likely and timely entry or expansion of competitors on the Identified City Pairs.

(2) *Evaluation in the current economic context of the air transport industry and attractiveness of the remedies package as a whole*

(384) Furthermore, in assessing the likelihood of entry on any of the Identified City Pairs in this case, the Commission must take into account the fact that the air transport industry is facing a dire crisis at the time of the market test (i.e. in July 2009). These difficulties are recognised in the recent suspension of the "use it or lose it" rule of Article 10 of Council Regulation (EEC) No 95/93 on common rules for the allocation of slots at Community airports.¹⁷⁵

(385) This greater than usual uncertainty about the evolution of the market in the coming months is also reflected in the limited interest or reservations expressed by competitors to enter and/or expand on the Identified City Pairs. Indeed, in the present exceptional economic circumstances, any such expressions of interest are more cautious than they would have been under normal circumstances.

(386) That the crisis is likely to have seriously reduced any entry or expansion plans of many airlines on any routes, including the Identified City Pairs, is also illustrated by the statements of several corporate customers responding to the market tests in phase I and II which explicitly noted that the current general economic situation is likely to constitute a significant obstacle for air carriers to enter or expand services on any of the Identified City Pairs. For instance, one corporate customer stated that the "significantly decreased total travel demand could reduce the likelihood that competitors will start or expand operations" while another corporate customer emphasised that the "current economic climate could be an obstacle to enter (or expand) on the Identified City Pairs".¹⁷⁶

(387) Against this background, the expression of interest expressed by competitors in entering the Identified City Pairs or expanding services on them mentioned above in paragraph (381)

174 See reply to question 43 of the phase I market investigation questionnaire competitors and reply to question 14 of the phase II market investigation questionnaire competitors.

175 OJ L 14, 22.1.1993, p. 1. See Regulation (EC) No 545/2009 of the European Parliament and of the Council of 18 June 2009 amending Regulation (EEC) No 95/93 on common rules for the allocation of slots at Community airports, OJ L 167, 29.6.2009, p. 24. Section 1.3.4 of the present Commitments refer to Article 10 of Regulation (EEC) No 95/93 in the context of defining situations of "Misuse" and thus make clear that any suspension of the "use it or lose it" rule under EU law also applies for slots available under the Commitment.

176 Replies to question 12 of the phase II market test.

rather illustrate that the Commitments make entry/expansion as timely and likely as possible under the present economic circumstances. Furthermore, it is clear that these exceptional circumstances are temporary in character and first signs of recovery have already been reported for several Member States as well as non-EU countries such as the United States of America, whereas the Commitments remain in place for an indefinite time period.

(388) That the Commitments are likely to result in actual entry or expansion, in particular once the current crisis is over, is further illustrated by the following considerations.

a. Attractiveness of Identified City Pairs as such

(389) All of the Identified City Pairs included in the remedies package are highly attractive in that these routes connect some of the main business centres in Europe and therefore attract a significant proportion of high yield business traffic.¹⁷⁷ This is illustrated by the fact that the VIE-FRA ([600 000 – 650 000]* total passengers, and thereof [400 000 – 450 000]* O&D passengers) and VIE-MUC ([350 000 – 400 000]* total passengers, and thereof [200 000 – 250 000]* O&D passengers) routes are highly profitable and very commercially attractive routes for both parties.¹⁷⁸

b. Improvements in comparison with previous cases in the air transport sector

(390) Moreover, in comparison with previous practice in the air transport sector¹⁷⁹ the Commitments in this case introduce some major improvements designed to ensure their effectiveness and to increase their attractiveness to competitors wishing to enter the Identified City Pairs or to expand their existing services on them.

(391) As already explained in more detail in paragraph (342), improvements include, firstly, the possibility to acquire grandfathering rights for the slots transferred under the Commitments once these slots have been used for only two IATA seasons with respect to all of the Identified City Pairs, except VIE-FRA, for which such grandfathering rights will be acquired after eight IATA seasons. This possibility to acquire grandfathering rights after a relatively short period significantly improves the incentive of the parties' competitors to enter the Identified City Pairs.

(392) Secondly, the slots must be allocated within only 20 minutes from the initial request (instead of 30 minutes, as provided for in the above mentioned previous air transport cases).

177 According to passenger surveys conducted by the parties the percentages of business travellers on these routes are as follows: up to [50-60]*% for VIE-STR, [40-50]*% for VIE-CGN, [60-70]*% for VIE-MUC and [60-70]*% for VIE-FRA. Whilst for the VIE-BRU route, the parties did not provide figures of the basis of passengers surveys, it appears that also this route is characterised by a high percentage of business traffic.

178 See reply of the parties to question 9 of request for information of 27 April 2009.

179 See for instance Case No. COMP/M.3280 – Air France/KLM and Case No. COMP/M.3940 – Lufthansa/Eurowings.

(393) Thirdly, apart from the (wave structure) restriction for Niki to re-time its existing slots on the VIE-FRA route (see paragraph (334)) the Commitments do not contain any specific limitation regarding the number of slots to be released at peak hours.

(394) Finally, the Commitments contain more convenient and efficient procedures for the allocation of slots than the procedures foreseen by remedies in the above mentioned previous air transport case.

c. Attractiveness of the remedies package in view of congestion levels at relevant airports

(395) Some of the airports for which the parties offer to make slots available under the Commitments are highly congested. This is particularly true for FRA airport, for which the market investigation has confirmed that it is one of the most congested airports in Europe. Consequently, slots at FRA airport are highly valuable, rendering the Commitments particularly attractive for the FRA-VIE route.

(396) However, even more importantly, also VIE airport is congested at peak hours (namely between 8.30 and 11.00 and between 16.00 and 20.45) (see paragraph (118)) and, under the Commitments, slots at VIE airport will have to be made available by the parties for each of the Identified City Pairs. This leaves New Entrants at this airport a choice between several different destinations and thereby increases the likelihood of entry on the Identified City Pairs

(397) The remedies comprise slots on five routes from and to VIE airport with altogether up to 19 daily frequencies (and up to 126 weekly frequencies). This considerable number of slots facilitates the establishment of a base by a new entrant and/or the enlargement of the bases of the competitors already present at VIE airport.¹⁸⁰ It has to be borne in mind that in the allocation of slots preference shall be given to those applicants that intend to operate the greatest number of Identified City Pairs. Indeed, some respondents indicated that they do not rule out the possibility of establishing a base at VIE airport.

(398) In addition, the parties propose a particularly short Utilization Period of only two consecutive IATA seasons for the acquisition of grandfathering rights for the slots to be obtained by competitors under the Commitments for all Identified City Pairs except VIE-FRA.

(399) This particularly short Utilization Period gives strong additional incentives to the parties' competitors to enter or expand on the Identified City Pairs, at the latest once the current crisis is over.

¹⁸⁰ As regards establishment of a base at VIE airport, the market investigation indicates that, depending on the business model of an air carrier, the minimum investment required might be as low as EUR 350 000.

d. Confirmation of attractiveness and effectiveness of remedies packages by the market test

(400) Finally, the large majority of respondents to the market test confirmed that, overall, the Commitments would sufficiently facilitate entry or expansion on the Identified City Pairs and solve the competition concerns raised by the proposed concentration.

(3) Conclusion on the overall assessment of the Commitments

(401) Considering all these elements together and, especially taking into account the effect of the current but temporary crisis in the air transport industry and the particular attractiveness of some elements of the remedies package, such as the short Utilization Period for the acquisition of grandfathering rights, and on the basis of the information available to the Commission, it is concluded that the Commitments are likely to lead to entry by one or several airlines on the Identified City Pairs in a timely manner and that this entry will suffice to remove the serious doubts identified on these markets.

X. CONDITIONS AND OBLIGATIONS

(402) Pursuant to the second subparagraph of Article 8(2) of the Merger Regulation, the Commission may attach to its Decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.

(403) The fulfilment of the measures that give rise to the structural change of the market is a condition, whereas the implementing steps which are necessary to achieve this result are generally obligations on the parties. Where a condition is not fulfilled, the Commission's Decision declaring the concentration compatible with the common market no longer stands. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance Decision in accordance with Article 8(6) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Article 14(2) and Article 15(1) of the Merger Regulation.

(404) In accordance with the distinction between conditions and obligations, this Decision should be made conditional on full compliance by the notifying party with Sections 1.1.1, 1.1.3 (iii), 1.2.2, 1.2.5, 1.2.8, 1.3.2, 2, 4.1, 5.1, 6.1 and 7.1 of the Commitments submitted by the notifying party on 31 July 2009. All other Sections of the Commitments should be obligations within the meaning of Article 8(2) of the Merger Regulation. The full text of the Commitments is set out in the Annex to this Decision and constitutes an integral part thereof.

XI. CONCLUSION

- (405) It is accordingly concluded that the Commitments as set out in the Annex to this Decision modify the notified concentration to such an extent that the serious doubts of the Commission as to the compatibility of that concentration with the common market are removed. The concentration should, therefore, be declared compatible with the common market pursuant to Article 8(2) of the Merger Regulation and with the EEA Agreement pursuant to Article 57 thereof, subject to compliance with the Commitments set out in the Annex which is an integral part of this Decision.
- (406) This conclusion holds true irrespective of the rescue aid and the restructuring aid mentioned in section VII.G due to the fact that those funds primarily serve the purpose of ensuring the survival of OS and due to their low amount as compared to the overall financial needs of OS and the overall financial strength of LH.

HAS ADOPTED THIS DECISION:

Article 1

The notified concentration whereby Deutsche Lufthansa AG acquires control of Austrian Airlines within the meaning of Article 3(1)(b) of Regulation (EC) No 139/2004 is hereby declared compatible with the common market and the EEA Agreement.

Article 2

Article 1 is subject to compliance with the conditions set out in Sections 1.1.1, 1.1.3 (iii), 1.2.2, 1.2.5, 1.2.8, 1.3.2, 2, 4.1, 5.1, 6.1 and 7.1 of the Annex.

Article 3

Deutsche Lufthansa AG shall comply with the obligations set out in the sections of the Annex not referred to in Article 2.

Article 4

This decision is addressed to:

Deutsche Lufthansa AG
Von-Gablenz-Strasse, 2-6
D-50679 Köln
Germany

To be delivered to:

Wilmer Cutler Pickering Hale and Dorr LLP
Bastion Tower
Place du Champ de Mars 5,
B-1050 Brussels
Belgium

Done at Brussels, 28.8.2009

For the Commission
(*signed*)
Neelie KROES
Member of the Commission

31 July 2009

PHASE II COMMITMENTS PACKAGE

CASE COMP/M.5440 - Lufthansa /Austrian Airlines

Pursuant to Article 8(2) of Council Regulation (EC) 139/2004 (“Merger Regulation”), Deutsche Lufthansa AG (“Lufthansa”) submits the commitments specified below (the “Commitments”) in order to enable the European Commission (“Commission”) to declare the proposed concentration between Lufthansa and Austrian Airlines (“Concentration”) compatible with the common market by means of a decision pursuant to Article 8(2) of the Merger Regulation (“Decision”).

These Commitments shall take effect upon receipt of the Commission’s Decision declaring the Concentration compatible with the common market and will be binding on Lufthansa, its subsidiaries, successors and assigns. These Commitments are offered exclusively in the context of the notified concentration between Lufthansa and Austrian Airlines and are without prejudice to the position of Lufthansa and/or its alliance partners in other cases examined by the European Commission.

This text shall be interpreted in the light of the Decision to which the Commitments are attached as conditions and obligations, and in the general framework of Community law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies.

0 DEFINITIONS

Blocked Space Agreement

An agreement on the purchase of reserved seating capacity by one airline (the marketing airline) on flights operated by another airline (the operating airline).

Brussels Airport

Means Brussels Zaventem Airport (BRU).

Codeshare

Means an enhanced form of interlining that includes one airline (the marketing airline) marketing services on flights operated by the other airline (the operating airline) under its own name and under its own designator code, regardless of whether it is construed in form of a free-flow or blocked space agreement or in other form.

Competitive Air Service

A non-stop scheduled passenger air service that is operated on one or more of the Identified City Pairs.

Consummation of the Concentration

The date on which Lufthansa, through Gomele Beteiligungsverwaltungs GmbH and Sobire Beteiligungsverwaltungs GmbH, acquires at least 75% of the share capital in Austrian Airlines as provided for in the Amendment and Waiver Agreement dated 5 December 2008.

Effective Date

The date of the Decision.

Frequency

Means a roundtrip on an Identified City Pair.

FFP (Frequent Flyer Program)

A program offered by airlines to reward customer loyalty under which airline customers enrolled in the program accrue points for travel on that airline that can be redeemed for free air travel and other products or services, as well as allowing passengers to have increased benefits, such as airport lounge access, or priority bookings.

IATA Scheduling Period or IATA Season

The IATA Summer Scheduling Period (also known as IATA Summer Season) starts on the 4th Sunday in March and ends on the 4th Saturday in October. The IATA Winter Scheduling Period (also known as IATA Winter Season) starts on the 4th Sunday in October and ends on the 4th Saturday in March.

Identified City Pairs

Vienna-Frankfurt, Vienna-Munich, Vienna-Cologne/Bonn, Vienna-Stuttgart, Vienna-Brussels..

Indemnified Party

Has the meaning given to it in Section 8.2.6.

Interline Agreement

An agreement between two or more airlines under which the contracting airlines accept each other's travel documents (tickets).

Intermodal Partner

Has the meaning given to it in Section 6.1.

Lufthansa

Deutsche Lufthansa AG and Austrian Airlines AG, and companies and/or affiliated businesses controlled by these entities after the Consummation of the Concentration.

Misuse

This term will have the meaning provided under Section 1.3.4.

MITA

Multilateral Interline Traffic Agreements Manual published by the International Air Transport Association (IATA).

Monitoring Trustee

Means an individual or institution, independent from Lufthansa and Austrian Airlines, who is approved by the Commission and appointed by Lufthansa and who has the duty to monitor Lufthansa's compliance with the conditions and obligations attached to the Decision as more fully described in Section 8.

New Air Service Provider

Any airline or airlines that are each members of the same alliance (other than the Parties including all airlines controlling it/them or controlled by it/them), that individually, or collectively by Codeshare, provide(s) a new or additional Competitive Air Service.

Parties

Lufthansa, Austrian Airlines and any undertakings controlled by either Lufthansa or Austrian Airlines.

Prospective New Entrant

Any airline or airlines that are each members of the same alliance (other than the Parties, including all airlines controlling either of them or controlled by either of them), able to offer a new or additional Competitive Air Service individually or collectively by Codeshare and needing a slot or slots to be made available by Lufthansa in accordance with the Commitments to operate a Competitive Air Service.

Published Fare

Refers to applicable IATA fares, carrier fares that are distributed to CRS via the public tariff data base of ATPCO (Airline Tariff's Publishing Corporation), and fares marketed on the Internet where such fares are available to the general public, excluding network-wide fuel, passenger or service surcharges.

Review Section

Has the meaning given to it in Section 11.

Slot

Shall mean the arrival and departure at a scheduled time available or allocated to an aircraft movement on a specific date at the airport of origin and destination.

Slot Handback Deadline

15 January for the IATA Summer Scheduling Period and 15 August for the IATA Winter Scheduling Period.

Slot Transfer Agreement

Has the meaning given to it in Section 1.2.6.

Slot Transfer Procedure

Has the meaning given to it in Section 1.2.1.

Standard Slot Allocation Procedure

Has the meaning given to it in Section 1.2.1.

1 SLOTS

1.1 SLOTS FOR CERTAIN IDENTIFIED CITY PAIRS

1.1.1 The Parties undertake to make available Slots at Vienna and/or Frankfurt and/or Munich and/or Cologne/Bonn and/or Stuttgart and/or Brussels to allow one or more Prospective New Entrant(s) to operate a new or additional Competitive Air Service on the following Identified City Pairs. The Parties shall be obliged to make available to Prospective New Entrants the number of Slots needed to support in aggregate:

- **Vienna-Frankfurt:** up to five (5) frequencies per day;
- **Vienna-Stuttgart:** up to three (3) frequencies per day;
- **Vienna-Cologne/Bonn:** up to three (3) frequencies per day, but not more than 18 frequencies per week;
- **Vienna-Brussels:** up to four (4) frequencies per day, but not more than 24 frequencies per week; and
- **Vienna-Munich** up to four (4) frequencies per day.

1.1.2 The number of Slots the Parties to be made available under Section 1.1.1 shall be reduced by the number of Slots already transferred to a Prospective New Entrant except for Slots that have been handed back to the Parties pursuant to Section 1.2.8 or Section 1.3.4. Subject to the provisions in Sections 1.1.3 and 1.1.4 below, Frequencies of a Competitive Air Service already operated by an airline independent of and unconnected to the Parties on an Identified City Pair shall be counted against the number of Slots to be made available by the Parties to that airline under Section 1.1.1 for this Identified City Pair.

1.1.3 Notwithstanding the provisions of 1.1.2, with respect to the Vienna-Frankfurt City Pair, on which Niki Luftfahrtgesellschaft mbH (“Niki”) currently operates a Competitive Air Service with two (2) Frequencies for which it has obtained from Lufthansa two (2) Slots at Frankfurt, and Adria Airways currently operates a Competitive Air Service with three (3) Frequencies for which it has obtained from Lufthansa three (3) Slots at Frankfurt, the following shall apply:

- (i) The two (2) Frequencies currently operated by Niki based on slots leased from Lufthansa (three (3) Frequencies to the extent that Niki obtains a third slot from Lufthansa as from the IATA Winter Seasons 2009/2010), shall be counted against the number of Slots to be made available by the Parties under Section 1.1.1 for the Vienna-Frankfurt City Pair. For the avoidance of doubt, if Niki were to exit from one or more of these frequencies in advance of acquiring grandfathering rights, such frequencies will be made available in accordance with section 1.1.1.

- (ii) In case no Non-Star Alliance Applicant (as defined in Section 3.5) requests Slots for the Vienna-Frankfurt City Pair for the IATA summer season 2010 or the first season for which the procedures for implementation of the present commitments would be in place, whichever is the later, one (1) Frequency operated by Adria Airways shall be counted against the number of Slots to be made available by the Parties under Section 1.1.1 for the Vienna-Frankfurt City Pair until the end of three subsequent IATA seasons, and for every subsequent period of 2 years until such time as a non-Star Alliance Applicant requests such slot. For the avoidance of doubt, this exceptional mechanism shall cease to apply should Adria Airways at any stage cease to operate frequencies on the Vienna-Frankfurt City Pair.
- (iii) Lufthansa undertakes to amend its existing agreements with Niki to reflect the provisions of these Commitments. For the IATA summer season 2010 and IATA winter season 2010/2011, Niki may request to exchange its existing Slots for Slots at different times pursuant to Section 1.2.1 of these Commitments, for these and subsequent IATA seasons, provided that Lufthansa shall not be obliged to transfer to Niki more than one Slot at Frankfurt during each of the time periods defined in the table below. If Niki has already two Slots in one time period, Lufthansa shall be obliged to grant any request by Niki to exchange up to two Slots in that time period, but shall be entitled to ensure that the relevant Slots are at least 105 minutes apart. For the avoidance of doubt, Niki may retain any or all of its existing Slots for which it would not seek an exchange under this paragraph.

Arrival	Departure
05:35 - 08:00	06:30 - 08:15
08:05 - 10:20	08:20 - 11:35
10:25 - 14:00	11:40 - 15:05
14:05 - 15:30	15:10 - 16:15
15:35 - 17:50	16:20 - 19:45
17:55 - 21:50	19:50 - 22:25

The Utilization Period required for the acquisition of grandfathering rights for the two (2) Frequencies currently operated by Niki based on slots leased from Lufthansa (three (3) Frequencies to the extent that Niki obtains a third slot from Lufthansa as from the IATA Winter Season 2009/2010) shall begin with the start of the IATA Winter Season 2009/2010, irrespective of whether Niki exchanges such Slots for Slots at different times in accordance with this paragraph. For the avoidance of doubt any Slot granted by Lufthansa under the present Commitments to Niki in a different time period, as defined in the table above, from the time period for which Niki had requested the Slot shall be deemed to be granted in that latter time period for the purposes of the present paragraph (iii).

- (iv) Lufthansa undertakes to amend its existing agreements with Adria Airways with respect to one (1) slot to reflect the provisions of these Commitments, provided however that Adria Airways shall not acquire grandfathering rights.

1.1.4 Notwithstanding the provisions of 1.1.2, with respect to the Vienna-Munich City Pair, on which Niki Luftfahrtgesellschaft mbH (“Niki”) currently operates a Competitive Air Service with three (3) Frequencies, Niki may request, to exchange these existing Slots for

Slots at different times pursuant to Section 1.2.1 of these Commitments. Niki's Frequencies shall be counted against the number of Slots to be made available by the Parties under Section 1.1.1 for the Vienna-Munich City Pair. For the avoidance of doubt, if Niki were to exit from one or more of the frequencies obtained under these Commitments in advance of acquiring grandfathering rights and/or from one or more of the frequencies currently operated, a corresponding number of frequencies will be made available by Lufthansa in accordance with section 1.1.1.

1.1.5 To the extent that the Parties make available Slots to a Prospective New Entrant for the operation of a new or additional Competitive Air Service on the Identified City Pairs Vienna-Stuttgart and/or Vienna-Cologne/Bonn pursuant to Section 2.1.1 of Lufthansa's commitments in case COMP/M.3940 – *Lufthansa/Eurowings*, these Slots shall be counted against the number of Slots to be made available pursuant to this Section 1.1.1. Conversely, to the extent that the Parties make available Slots to a Prospective New Entrant for the operation of a new or additional Competitive Air Service on the Identified City Pair Vienna-Stuttgart and/or Vienna-Cologne/Bonn pursuant to this Section 1.1.1, these Slots shall be counted against the number of Slots to be made available pursuant to Section 2.1.1 of Lufthansa's commitments in case COMP/M.3940. For the avoidance of doubt, a Prospective New Entrant on these Identified City Pairs shall have the choice of whether to avail itself of the commitments in Case COMP/M.3940 or the present Commitments.

1.1.6 Lufthansa will inform the Monitoring Trustee and the Commission in accordance with Section 8 of the announced commencement by a carrier of a new or additional Competitive Air Service on an Identified City Pair that does not use Slots made available by the Parties as soon as possible following the announcement of that service, and of the amendments to existing agreements in accordance with Section 1.1.3.

1.2 CONDITIONS PERTAINING TO SLOTS

1.2.1 The Prospective New Entrant shall comply with the following procedure to obtain slots from the Parties ("***Slot Transfer Procedure***").

The Prospective New Entrant wishing to commence/increase a new additional Competitive Air Service on one or more of the Identified City Pairs shall notify in writing its request for Slots to (i) the slot coordinator, through the normal slot allocation procedure ("***the Standard Slot Allocation Procedure***"); and (ii) the Monitoring Trustee, within the period provided for in Clause 3.1.

The Prospective New Entrant shall be eligible to receive slots pursuant to these Commitments only if it can demonstrate that all reasonable efforts to obtain slots for the Identified City Pair(s) through the Standard Slot Allocation Procedure before the beginning of the relevant IATA traffic season have failed, including the allocation of Slots by the coordinator from the waitlist following the Slot Handback Date. The Prospective New Entrant shall request slots for use during a full IATA Season unless it can demonstrate a compelling business need to start its services during the Season.

The Prospective New Entrant will be deemed not to have exhausted all reasonable efforts to obtain slots, if:

- (i) slots were obtained through the Standard Slot Allocation Procedure within twenty (20) minutes of the times requested, but such slots have not been accepted by the Prospective New Entrant; and/or
 - (ii) slots were obtained through the Standard Slot Allocation Procedure more than twenty (20) minutes from the times requested and the Prospective New Entrant did not give the Parties the opportunity to exchange those slots for slots within +/- twenty (20) minutes of the times requested.
- 1.2.2** The slots released by the Parties shall be within +/- twenty (20) minutes of the time requested by the Prospective New Entrant, if the Parties have slots available within this time-window. In the event that the Parties do not have slots available within this time-window, they shall offer to release the slots closest in time to the Prospective New Entrant's request. Arrival and departure slots shall be such as to allow for reasonable aircraft rotation taking into account the Prospective New Entrant's business model. The Parties do not have to offer slots, however, if the slots that the Prospective New Entrant can obtain through the Standard Slot Allocation Procedure are closer in time to the Prospective New Entrant's request than the slots that the Parties have available.
- 1.2.3** Any slot transferred on an indefinite basis in accordance with the Slot Transfer Procedure under Section 1.3 shall reduce the maximum number of slots to be transferred in accordance with the Commitments.
- 1.2.4** To ensure that the slots released by the Parties are used in a manner consistent with these conditions, the Prospective New Entrant should inform the Monitoring Trustee in accordance with Section 3.5.
- 1.2.5** Slots made available by the Parties under these Commitments shall be offered without any compensation.
- 1.2.6** The Parties shall enter into a slot transfer agreement with the Prospective New Entrant (the "*Slot Transfer Agreement*"). Such an agreement shall be subject to review by the Monitoring Trustee and approval by the Commission and shall provide for fast-track dispute resolution according to Section 9. The agreement may (i) contain prohibitions on the Prospective New Entrant transferring any slots released by the Parties to a third party, swapping such slots for other slots with a third party, making available such slots in any way to any third party for the use of that third party, or releasing, surrendering, giving up or otherwise disposing of such slots; and (ii) provide for reasonable financial compensation to the Parties in case of Misuse as defined in Sections 1.3.4 and 1.3.5. The duration of the Slot Transfer Agreement shall be the Utilization Period, as defined in 1.3.1 below, except if the Prospective New Entrant is a member of the Star Alliance. If the Prospective New Entrant is a member of the Star Alliance, the agreement shall include the obligations listed in 1.3.6 and, if appropriate, specific conditions imposed on the Prospective New Entrant by the Commission according to Section 3.3. c), and the

Commission's approval of the agreement shall be conditional on the Prospective New Entrant committing to comply with these obligations and conditions.

- 1.2.7** The slot transfer agreement shall provide that the Prospective New Entrant will be able to terminate the slot transfer agreement at the end of each IATA season without penalty, provided the Prospective New Entrant notifies the termination of the agreement to the Parties in writing before the Slot Handback Deadline for the relevant IATA season.
- 1.2.8** Upon termination of the agreement, the slots will be handed back to the Parties and will be available for a new entrant under Section 1.1.1, unless the Prospective New Entrant has acquired Grandfathering rights according to Section 1.3.

1.3 GRANDFATHERING OF SLOTS

- 1.3.1** As a general rule, the slots obtained by the Prospective New Entrant from the Parties as a result of the Slot Transfer Procedure shall be used only to provide a Competitive Air Service on the Identified City Pairs for which the Prospective New Entrant has requested them from the Parties through the Slot Transfer Procedure. These slots can not be used on another city pair unless
- the Prospective New Entrant has operated the Identified City Pair for which these slots have been transferred for a number of full consecutive IATA Seasons ("*Utilization Period*") and
 - the Prospective New Entrant is not a member of the Star Alliance.

The Utilization Periods for the Identified City Pairs Vienna-Frankfurt shall be 8 (eight) consecutive IATA Seasons, and 2 (two) consecutive IATA seasons for all other Identified City Pairs.

- 1.3.2** The slot transfer will become definitive and the Prospective New Entrant will be deemed to have grandfathering rights for the slots once appropriate use of these slots has been made on the Identified City Pair during the Utilization Period. In this regard, once the Utilization Period has elapsed, the Prospective New Entrant will be entitled to use the slot(s) obtained on the basis of these Commitments exclusively for intra-European City Pair operated by the Prospective New Entrant, or operated by one of the Prospective New Entrant's alliance partners and marketed by the Prospective New Entrant on a code-share basis ("*Grandfathering*").
- 1.3.3** Grandfathering is subject to the approval of the Commission, advised by the Monitoring Trustee, in accordance with Section 3.3. The Commission's approval shall be conditional on the Prospective New Entrant committing that if it ceases to use the Slots in question for purposes described in Section 1.3.2, it will return those Slots to the slot coordinator.

1.3.4 During Utilization Period, the Prospective New Entrant shall not be entitled to transfer, assign, sell, swap or charge in breach of these Commitments any Slot transferred by the Parties in the Slot Transfer Procedure. During the Utilization Period, a situation of Misuse shall be deemed to arise where a Prospective New Entrant that has obtained slots released by the Parties decides: (i) not to commence services on a Identified City Pair(s); (ii) to operate fewer daily Frequencies on the Identified City Pair(s) or to cease operating on the Identified City Pair(s) during such period; (iii) to transfer, assign, swap or sell in breach of these Commitments any Slot transferred by the Parties in the Slot Transfer Procedure; (iv) not to use the slots for the Identified City Pair(s); and (v) not to use the slots properly. The Prospective New Entrant does not use the slots properly, if (a) it loses the slots as a consequence of the principle of “*use it or lose it*” in Article 10 of Regulation (EEC) No. 95/93 or (b) it misuses the slot as described and interpreted in Art. 14 (4) of the Slot Regulation 793/2004.

1.3.5 During the Utilization Period, the Prospective New Entrant who has obtained slots under the Slot Transfer Procedure and has been found to or is anticipated to be found in a situation of Misuse as defined in Section 1.3.4 shall immediately inform the Monitoring Trustee and Lufthansa and hand back the Slots. In cases (i) and (ii) identified in Section 1.3.4, the Parties shall then use their best efforts to redeploy the slots in order to safeguard the historic precedents. If despite their best efforts, the Parties are not able to retain the historic precedents for these slots, or in case of a Misuse as defined in (iii), (iv), and (v)(b) of Section 1.3.4, the Prospective New Entrant shall provide reasonable compensation to the Parties as provided for in the Slot Transfer Agreement.

1.3.6 If the Prospective New Entrant is a member of the Star Alliance at the time of the signature of the Slot Transfer Agreement, or becomes a member of the Star Alliance between the signature of the Slot Transfer Agreement and the end of the Utilization Period (Star Alliance New Entrant), the Prospective New Entrant will not acquire grandfathering rights of the slots released.

A Star Alliance New Entrant shall not be entitled to transfer, assign, swap or sell any slot transferred by the Parties. All provisions of Sections 1.3.4 and 1.3.5 foreseen for the Utilization Period apply to a Star Alliance New Entrant without any limitation in time.

Furthermore, the Star Alliance New Entrant shall not enter into a code share agreement with the parties or any other airline that is a member of the Star Alliance with respect to the Identified City Pairs on which it operates a Competitive Air Service, and more generally shall not operate a Competitive Air Service collectively with the Parties or any other airline that is a member of the Star Alliance.

2 DURATION OF THE SLOT TRANSFER

The Parties’ obligations to transfer slots are unlimited in duration and may be invoked at any time by a Prospective New Entrant, subject to the limitations set out in Sections 1 and 11.

3 SELECTION PROCEDURE, ROLE OF THE MONITORING TRUSTEE AND APPROVAL OF THE COMMISSION

- 3.1** Before the deadline for the submission of slot applications to slot coordinators (i.e. currently 35 days before the IATA Scheduling Conference)(the “*Final Slot Request Date*”), any airline wishing to obtain Slots from the Parties pursuant to the Transfer Procedure shall send a slot request to (i) the slot coordinator; and (ii) the Monitoring Trustee.
- 3.2** At latest three (3) weeks before the IATA Scheduling Conference of the relevant season, the Monitoring Trustee forwards the slot requests to Lufthansa and asks, if necessary, which slots the Parties would release within +/- twenty (20) minutes of the time a Prospective New Entrant requested. Lufthansa’s proposal shall refer to IATA’s Slot Preliminary Allocation List (SAL). Lufthansa will respond to the Monitoring Trustee within two (2) weeks upon the Monitoring Trustee’s request.
- 3.3** Between the Final Slot Request Date and the beginning of the IATA Scheduling Conference the Commission, advised by the Monitoring Trustee:
- (a) assesses whether each applicant would qualify as a Prospective New Entrant and whether the service to be provided by the Applicant qualifies as a Competitive Air Service;
 - (b) if there is more than one applicant, ranks the applicants by order of preference;
 - (c) if the Prospective New Entrant is a member of the Star Alliance, or is anticipated to become a Member of the Star Alliance, assesses whether specific conditions should be imposed on the Prospective New Entrant; and
- 3.4** In its assessment according to Section 3.3 (a), the Commission shall decide after considering the advice of the Monitoring Trustee whether it considers the applicant to be a Prospective New Entrant pursuant to the following criteria:
- the Prospective New Entrant is independent of and unconnected to the Parties;
 - the Prospective New Entrant is a viable existing or potential competitor, with the ability, resources and commitment to operate the Identified City Pair in the long term as a viable and active competitive force.
- 3.5** In its assessment according to Section 3.3. (b), the Commission shall decide, after considering the advice of the Monitoring Trustee, how to rank the applicants by order of preference using notably the following criteria:
- Preference shall be given to applicants that are not members of the Star Alliance or anticipated to become members of the Star Alliance (Non Star Alliance Applicants) over applicants that are members of the Star Alliance or anticipated to become members of the Star Alliance (Star Alliance Applicants), regardless of the

number of Identified City Pairs or Frequencies the Star Alliance Applicant(s) is/are proposing to operate.

- If there is more than one Non Star Alliance Applicant, preference shall be given to the Non Star Alliance Applicant that intends to operate the greatest numbers of Identified City Pairs.
 - If there is more than one Star Alliance applicant, preference shall be given to the Star Alliance Applicant that intends to operate the greatest number of Identified City Pairs.
- 3.6** In its assessment according to Section 3.3 (c), the Commission shall decide, after considering the advice of the Monitoring Trustee, whether specific conditions should be imposed on a Star Alliance Applicant in order to guarantee the independence of the Star Alliance Applicant from the Parties.
- 3.7** To assist the Monitoring Trustee in the preparation of his advice and/or the Commission in taking its decision, the Monitoring Trustee and/or the Commission shall request the Prospective New Entrant to provide to the Monitoring Trustee and/or the Commission with a detailed business plan. This plan shall contain a general presentation of the company including its history, its legal status, the list and a description of its shareholders and the two most recent yearly audited financial reports. The plan shall provide information on the plans that the company has in terms of development of its network, fleet etc, and detailed information on its plans for the Identified City Pairs on which it wants to operate. The company should specify in detail planned operations (size of aircraft, number of frequencies operated, planned time-schedule of the flights) and expected financial results (expected traffic, revenues, profits) on the Identified City Pairs on which it wants to operate during the Utilization Period for the respective Identified City Pair. The Monitoring Trustee and/or the Commission may also request a copy of all co-operation agreements the Prospective New Entrant may have with other airlines. Business secrets and confidential information will be kept confidential by the Commission and the Monitoring Trustee and will not become accessible to other undertakings or to the public.
- 3.8** Upon receiving the SAL messages from the slot coordinator, and in advance of the beginning of the IATA Scheduling Conference, the Monitoring Trustee informs each applicant not having received slots within the time-window of +/-twenty (20) minutes as indicated through the SAL and the slot coordinator:
- (i) whether it qualifies for the Slot Commitment;
 - (ii) whether it is:
 - a) The only applicant or the preferred applicant; or
 - b) Not the preferred applicant

(iii) whether specific conditions are imposed by the Commission under Section 3.3
(c)

(iv) the exact Slot(s) that the Parties would release through the Slot Transfer Procedure.

In any case, the applicant shall go to the IATA Scheduling Conference and try to improve its slots.

3.9 At the end of the IATA Scheduling Conference, it will be clear, also for the Monitoring Trustee, for instance through the *European Union Airport Coordinators Association* (EUACA) database, whether each Prospective New Entrant will have received slots within the window of +/- twenty (20) minutes through the Standard Slots Allocation Procedure.

3.10 Within two (2) weeks of the end of the IATA Scheduling Conference, the preferred applicant informs the Monitoring Trustee and Lufthansa whether it will commit to operate the slots offered eventually by the Parties, in case the Standard Slot Allocation Procedure does not provide for them. If not, the Monitoring Trustee offers the slots to the next applicant (if any) by order of preference.

3.11 Within one (1) week of the confirmation that the applicant will operate the slots, the Parties offer the dedicated slots for transfer to the preferred applicant. The Slot Transfer Agreement shall be signed and the slot transfer performed within three weeks after the Slot Handback Deadline, and the slot coordinator is informed of the transfer in order to get the required confirmation.

4 INTERLINING AGREEMENTS

4.1 At the request of a New Air Service Provider, the Parties shall enter into an interline agreement concerning any Identified City Pair operated by the New Air Service Provider.

4.2 Any such interline agreement shall be subject to the following restrictions:

- it shall apply to the business and economy class only;
- it shall provide for interlining on the basis of the Parties' published one-way fares when a one-way ticket is issued or half of the Parties' published round-trip fares when a round-trip ticket is issued;
- it shall be limited to true origin and destination traffic on the Identified City Pair operated by the New Air Service Provider;
- it shall be subject to the MITA rules and/or normal commercial conditions;

- it shall include the possibility for the New Air Service Provider, or travel agents, to offer a return trip comprising services provided one-way by the Parties and one-way by the New Air Service Provider.
- 4.3** Subject to seat availability in the relevant fare category, the Parties shall carry a passenger holding a coupon issued by a New Air Service Provider for travel on an Identified City Pair. However, to avoid abuse, the Parties may require that the New Air Service Provider or the passenger, where appropriate, pay the (positive) difference between the fare charged by the Parties and the fare charged by the New Air Service Provider. In cases where the New Air Service Provider's fare is lower than the value of the coupon issued by it, the Parties may endorse its coupon only up to the value of the fare charged by the New Air Service Provider. A New Air Service Provider shall enjoy the same protection in cases where the Parties' fare is lower than the value of the coupon issued by it.
- 4.4** All interline agreements entered into pursuant to this Section 4 for a particular Identified City Pair shall lapse automatically in the event that the New Air Service Provider ceases to operate that City Pair.

5 SPECIAL PRORATE AND CODE SHARE AGREEMENTS

- 5.1** At the request of a Prospective New Entrant, the Parties shall enter into a special prorate agreement with the Prospective New Entrant for traffic with a true origin and destination in either Austria and/or Germany or Austria and/or Belgium, provided part of the journey involves the Vienna-Frankfurt, Vienna-Munich, Vienna-Cologne, Vienna-Stuttgart, or Vienna-Brussels routes. The conditions for a special prorate agreement shall be on terms such that the New Air Service Provider shall have equal treatment with Lufthansa's Star Alliance partners on the same Identified City Pair. Financial conditions will be reasonable and in particular reflect the average conditions agreed upon with Lufthansa's alliance partners. The conclusion of the special prorate agreement is subject to the approval of the Commission, advised by the Monitoring Trustee. The Commission will in particular assess whether the financial conditions of the special prorate agreement are reasonable.

6 COMMITMENT TO FACILITATE INTERMODAL SERVICES

- 6.1** At the request of a railway or other surface transport company operating between Austria, Belgium, and/or Germany (an Intermodal Partner), the Parties shall enter into an intermodal agreement whereby they provide passenger air transport on their services on any of the Identified City Pairs as part of an itinerary that includes surface transportation by the Intermodal Partner.
- 6.2** Any intermodal agreement entered into pursuant to this Section 6 shall be based on the MITA principles (including the Intermodal Interline Traffic Agreement - Passenger and IATA Recommended Practice 1780e) and normal commercial conditions. The Parties shall accept full pro-rating according to the terms applied by MITA members, including on routes where only rail services are provided. No restrictions shall apply to fare

combinations between carriers that are IATA intermodal MITA members and the most restrictive conditions rule shall apply only for the applicable segment and its carrier. The Parties and the Intermodal Partner may waive minimum stay requirements on any fare and any City Pair they operate. Such decisions are respected and published reciprocally. Where the Intermodal Partner requires notification of a sector mileage, a location identifier or an add-on fare, the Parties shall make such a request to IATA under normal IATA procedures.

- 6.3** At the request of a potential Intermodal Partner, the Parties shall make efforts in good faith to reach an agreement on conditions comparable to those granted to other Intermodal Partners, provided that the necessary requirements are met especially with regard to safety, quality of service, insurance coverage and liability limits. The conditions of such an agreement shall override the general obligations arising pursuant to this Section 6.

7 FREQUENT FLYER PROGRAM

- 7.1** At the request of a New Air Service Provider that does not participate in Lufthansa's frequent flyer program ("Miles&More"), Lufthansa shall allow it to be hosted in Miles&More for the Identified City Pairs operated by the New Air Service Provider. The agreement with the New Air Service Provider shall be on terms such that the New Air Service Provider shall have equal treatment with Lufthansa's alliance partners. Financial conditions will reflect the average conditions agreed upon with Lufthansa's alliance partners.
- 7.2** Any agreement relating to a particular Identified City Pair and entered into pursuant to this Section 7 shall lapse automatically in the event that the New Air Service Provider ceases to operate that City Pair.

8 MONITORING TRUSTEE

8.1 APPOINTMENT OF MONITORING TRUSTEE

- 8.1.1** A Monitoring Trustee shall be appointed in accordance with the procedure described in Section 8.1.2. The Monitoring Trustee must be familiar with the airline industry and have the experience, competence and independence necessary for this appointment. The Monitoring Trustee will have had no direct or indirect employment, consultancy or other relationship with Lufthansa or Austrian Airlines during the past two years and will have no such relationship with Lufthansa for the three years following the completion of its mandate.
- 8.1.2** The Parties shall ensure that the Monitoring Trustee's remuneration shall be sufficient to guarantee the effective and independent compliance of its mandate.

Within one (1) week of the Effective Date, Lufthansa, in agreement with Austrian Airlines, shall submit a list of one or more persons whom Lufthansa proposes to appoint as the Monitoring Trustee to the Commission for approval.

The proposal shall contain sufficient information for the Commission to verify that the proposed Monitoring Trustee fulfils the requirements set out in Section 8.1.1 and shall include:

- (i) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Monitoring Trustee to fulfil its duties under these Commitments;
- (ii) the outline of a work plan which describes how the Monitoring Trustee intends to carry out its assigned tasks.

The Commission shall have the discretion to approve or reject the proposed Monitoring Trustee and to approve the proposed mandate subject to any modifications it deems necessary for the Monitoring Trustee to fulfil its obligations. If only one name is approved, Lufthansa shall appoint or cause to be appointed the individual or institution concerned as Monitoring Trustee. If more than one name is approved, Lufthansa shall be free to choose the Trustee to be appointed from among the names approved. The Monitoring Trustee shall be appointed within one (1) week of the Commission's approval, in accordance with the mandate approved by the Commission. Lufthansa commits not to close the notified transaction before the appointment of the Monitoring Trustee.

If all the proposed Monitoring Trustees are rejected, Lufthansa shall submit the names of at least two more individuals or institutions within one (1) week of being informed of the rejection, in accordance with the requirements and the procedure set out in Section 8.1.1.

If all further proposed Monitoring Trustees are rejected by the Commission, the Commission shall nominate a Monitoring Trustee, whom Lufthansa shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

8.2 MONITORING TRUSTEE'S MANDATE

8.2.1 The Monitoring Trustee's mandate shall include, in particular, the following responsibilities:

- (i) to monitor the satisfactory discharge by the Parties of the obligations entered into in these Commitments in so far as they fall within the scope of these Commitments;
- (ii) to propose to the Parties such measures as the monitoring Trustee considers necessary to ensure the Parties' compliance with the conditions and obligations attached to the Decision;

- (iii) to advise and make a written recommendation to the Commission as to the suitability of the Slot Transfer Agreement and any Prospective New Entrant submitted for approval to the Commission under Section 1 and 3;
- (iv) to provide written reports to the Commission on the progress of the discharge of its mandate, identifying any respects in which the Parties have failed to comply with these Commitments and in which the Monitoring Trustee has been unable to discharge its mandate;
- (v) to mediate any disagreements relating to these Commitments;; if mediation is agreed to by the other party or parties to the agreement in question, and submit a report upon the outcome of the mediation to the Commission; and
- (vi) at any time, to provide to the Commission, at its request, a written or oral report on matters falling within the scope of these Commitments;
- (vii) to review and report on the amendments to the agreements referred to in Section 1.1.3.
- (viii) to grant adequate publicity in trade journals and by any other appropriate means sufficiently in advance of the beginning of the slot allocation procedure for each IATA Season to those remedies under the present Commitments which have not yet been taken up by competitors or which may become available.

8.2.2 The Parties shall receive simultaneously a non-confidential version of any written recommendation made by the Monitoring Trustee to the Commission (as provided for in Section 8.2.1(iii)).

8.2.3 The reports provided for in Section 8.2.1(iii) to (vii) shall be prepared in English. The reports provided for in Section 8.2.1(iv) shall be sent by the Monitoring Trustee to the Commission within ten (10) working days from the end of every IATA season following the Monitoring Trustee's appointment or at such other time(s) as the Commission may specify, and shall cover developments in the immediately preceding IATA season. The Parties shall receive simultaneously a non-confidential copy of each Monitoring Trustee report.

8.2.4 The Parties shall provide the Monitoring Trustee with such assistance and information, including copies of all relevant documents, as the Monitoring Trustee may reasonably require in carrying out its mandate and shall pay reasonable remuneration for its services.

8.2.5 The Monitoring Trustee shall have full and complete access to any of the Parties' books, records, documents, management or other personnel facilities, sites, technical information necessary for fulfilling its duties.

8.2.6 The Parties shall indemnify the Monitoring Trustee (and, where appropriate, its employees and agents) (each an Indemnified Party) and hold each Indemnified Party

harmless, and hereby agrees that an Indemnified Party shall have no liability to the Parties for any liabilities arising out of the performance of the Monitoring Trustee's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Monitoring Trustee (or, where appropriate, its employees, advisors and agents).

8.2.7 At the expense of the Parties, the Monitoring Trustee may appoint advisors, subject to the Commission's prior approval, if the Monitoring Trustee considers the appointment of such advisors necessary for the performance of its duties under the mandate, provided that any fees incurred are reasonable and upon consultation of the Parties.

8.3 TERMINATION OF MANDATE

8.3.1 If the Monitoring Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Monitoring Trustee to a conflict of interest:

(i) the Commission may, after hearing the Monitoring Trustee, require the Parties, to replace the Monitoring Trustee; or

(ii) the Parties, with the prior approval of the Commission, may replace the Monitoring Trustee.

8.3.2 If the Monitoring Trustee is removed the Monitoring Trustee may be required to continue in its function until a new Monitoring Trustee is in place to whom the Monitoring Trustee has affected a full hand over of all relevant information. The new Monitoring Trustee shall be appointed in accordance with the procedure referred to Section 8.1.2.

8.3.3 Aside from being removed in accordance with Section 8.3.1, the Monitoring Trustee shall cease to act as Monitoring Trustee only after the Commission has discharged it from its duties. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the Commitments might not have been fully and properly implemented.

9 FAST TRACK DISPUTE RESOLUTION

9.1 In the event that a Prospective New Entrant or a New Air Services Provider has reason to believe that the Parties are failing to comply with the requirements of the Commitments vis-à-vis that party, the fast track dispute resolution procedure described in this Section 9 will apply.

9.2 Any Prospective New Entrant or New Air Services Provider who wishes to avail itself of the fast track dispute resolution procedure ("Requesting Party") must notify the Parties in writing setting out in detail the reasons leading that party to believe that the Parties are failing to comply with the requirements of the Commitments ("Notice"). The Requesting Party and the Parties will use their best efforts to resolve all differences of opinion and to

settle all disputes that may arise through co-operation and consultation within a reasonable period of time not to exceed fifteen (15) business days after receipt of the Notice.

- 9.3 Should the Requesting Party and the Parties fail to resolve their differences of opinion through cooperation and consultation as provided for in Section 9.2, the Requesting Party shall nominate an arbitrator.
- 9.4 The Parties shall, within two (2) weeks of receiving notification in writing from a Requesting Party of the appointment of the Requesting Party's arbitrator, nominate its arbitrator and provide to the Requesting Party in writing detailed reasons for its challenged conduct.
- 9.5 The arbitrators nominated by the Parties and the Requesting Party shall, within one (1) week from the nomination of the former, agree to appoint a third arbitrator. If the arbitrators nominated by Lufthansa and the Requesting Party cannot agree on the nomination of a third arbitrator, they shall ask the President of the International Chamber of Commerce ("ICC") to appoint the third arbitrator.
- 9.6 The arbitrators shall be instructed to establish an arbitration tribunal and to make a preliminary ruling on the contested issues within one (1) month of the appointment of the third arbitrator, which may be extended, if necessary, by the unanimous agreement of all arbitrators. The preliminary ruling shall be applicable immediately and until the final decision is issued. The final decision shall be taken by the arbitrators within six (6) months of the appointment of the third arbitrator, which may be extended, if necessary, by the unanimous agreement of all arbitrators.
- 9.7 In their preliminary ruling and their final decision, the arbitrators shall also decide the action, if any, to be taken by the Parties in order to ensure compliance with the Commitments vis-à-vis the Requesting Party, including making a preliminary or final binding determination of the disputed contractual conditions.
- 9.8 Any of the arbitrators will be entitled to request any relevant information from the Parties or the Requesting Party in order to enable the arbitrators to reach a decision.
- 9.9 The burden of proof in any dispute under this fast track dispute resolution procedure shall be borne as follows: i) the Requesting Party must produce evidence of a *prima facie* case, and ii) if the Requesting Party produces evidence of a *prima facie* case, the arbitrator must find in favour of the Requesting Party unless the Parties can produce evidence to the contrary.
- 9.10 The arbitrators shall be instructed not to disclose confidential information and to apply the standards attributable to confidential information and business secrets by European Community competition law.

- 9.11** The arbitration shall be in English and conducted pursuant to the ICC rules. The arbitration award shall, in addition to dealing with the merits of the claim, impose the fees and costs of the prevailing party upon the party that is unsuccessful. The arbitration award shall be final and binding on the parties.
- 9.12** In the event of disagreement between the parties to the arbitration regarding the interpretation of the Commitments, the arbitrators shall inform the Commission and may seek the Commission's interpretation of the Commitments before finding in favour of any party to the arbitration. The Commission may, at any time, issue a submission during the arbitration procedure.
- 9.13** Nothing in the arbitration procedure shall affect the powers of the Commission to take decisions in relation to the Commitments in accordance with its powers under the Merger Regulation and the EC Treaty.

10 GENERAL PROVISIONS

- 10.1** If the Concentration is abandoned, abrogated, unwound, not approved or disapproved by a relevant Government Authority, or otherwise terminated, then these Commitments shall automatically cease to apply.
- 10.2** If the approval of the Concentration by another governmental authority is made subject to requirements that are potentially inconsistent with these Commitments, Lufthansa may request a review and adjustment of these Commitments in order to avoid such inconsistencies.

11 REVIEW SECTION

- 11.1** The Commission may, if appropriate, in response to a request from Lufthansa duly justified and provided together with the relevant report prepared by the Monitoring Trustee, in exceptional circumstances, waive, modify or substitute one or more of the obligations stated in these Commitments, in particular as regards the necessity of making available a fifth slot to a Non-Star Alliance Applicant to ensure effective competition on the Vienna-Frankfurt route.

11.2 The Commission may, if appropriate, in response to a request from Lufthansa duly justified and provided together with the relevant report prepared by the Monitoring Trustee, grant an extension of the terms foreseen in these Commitments. In case Lufthansa asks for any term extension, such a request shall be filed no later than one (1) month before the end of the period. Only in exceptional circumstances shall Lufthansa be entitled to request an extension within the last month of any period.

31 July 2009

Deutsche Lufthansa Aktiengesellschaft

Armin Herzwurm
Vice President Corporate Strategy &
Group Development

Michael Niggemann
Deputy General Counsel
Vice President

EN

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A summary of this decision is published in all EU languages in the Official Journal of the European Union.

***Case No COMP/M6286 -
SÜDZUCKER/ ED&F MAN***

Only the English text is authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 8 (2)

Date: 16/05/2012

EN

EN



EUROPEAN COMMISSION

Brussels, 16.5.2012
C(2012) 3145 final

PUBLIC VERSION

COMMISSION DECISION

of 16.5.2012

addressed to:

SÜDZUCKER AG MANNHEIM/OCHSENFURT

**declaring a concentration to be compatible with the internal market
and the functioning of the EEA Agreement**

Case M.6286-SÜDZUCKER/ ED&F MAN

(Only the EN text is authentic)

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COMMISSION DECISION

of 16.5.2012

addressed to:

SÜDZUCKER AG MANNHEIM/OCHSENFURT

**declaring a concentration to be compatible with the internal market
and the functioning of the EEA Agreement
(Case M.6286-SÜDZUCKER/ ED&F MAN)**

(Only the English text is authentic)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings¹, and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 9 November 2011 to initiate proceedings in this case,

Having given the undertakings concerned the opportunity to make known their views on the objections raised by the Commission on 14 February 2012,

Having regard to the opinion of the Advisory Committee on Concentrations,

Having regard to the final report of the Hearing Officer in this case,

WHEREAS:

1. INTRODUCTION

- (1) On 19 September 2011, the Commission received a notification of a proposed concentration pursuant to Article 4 of Regulation (EC) No 139/2004 (the "Merger Regulation")² by which the undertaking Südzucker Holding GmbH, controlled by Südzucker AG Mannheim/Ochsenfurt ("Südzucker", Germany), acquires within the

¹ OJ L 24, 29.1.2004, p.1.

² OJ L 24, 29.1.2004, p.1.

meaning of Article 3(1)(b) of the Merger Regulation control of ED&F Man Holding Limited ("EDFM", United Kingdom) by way of purchase of shares (the "proposed transaction"). Südzucker and EDFM are designated hereinafter as the "Parties" while Südzucker is the "notifying party".

2. THE PARTIES

- (2) Südzucker is a German food company active in the areas of sugar production and marketing, food additives, frozen food, portioned food articles, bioethanol production and fruit juices concentrates and preparations. The sugar segment covers white sugar production from beet as well as the refining of raw cane sugar and marketing of sugar and by-products. Südzucker produces sugar in 29 beet sugar factories and three refineries in Germany, Belgium, Bosnia-Herzegovina, France, Poland, Austria, Slovakia, the Czech Republic, Hungary, Moldova and Romania.
- (3) EDFM is primarily a commodity trading company. Its product portfolio comprises sugar, liquid by-products of sugar production such as molasses (liquid-products segment), coffee, tropical oils and biofuels (primarily biodiesel, ethanol is not supplied in the EEA). The company also provides logistic services (storage and transportation) and financial services.

3. THE OPERATION AND THE CONCENTRATION

- (4) Pursuant to a Subscription Agreement and the New Articles of Association of EDFM (as amended by a Deed of Variation signed on 24 August 2011), Südzucker will acquire 24.99% of EDFM's share capital. Pursuant to paragraphs 54 to 57 of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (the "Jurisdictional Notice")³ sole control may be acquired *de jure* by a minority shareholder if it obtains the ability to exercise decisive influence over the other undertaking's strategic commercial behaviour⁴. The Subscription Agreement and the Articles of Association grant Südzucker strong veto rights in particular over the annual budget, business plan and appointment of directors^{5*}. No other shareholder will enjoy such veto rights⁶.

³ OJ C/95, 16.4.2008, p. 1.

⁴ See Jurisdictional Notice, paragraph 54: "*Sole control is acquired if one undertaking alone can exercise decisive influence on an undertaking. Two general situations in which an undertaking has sole control can be distinguished (...) Second, a situation also conferring sole control 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 (the so-called negative sole control).*" And paragraph 57: "*Even in the case of a minority shareholding, sole control may occur on a legal basis in situations where specific rights are attached to this shareholding. These may be preferential shares to which special rights are attached 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. 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 on the basis of the organisational structure*".

⁵ For instance [...]*.

* Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

⁶ The current major shareholders of EDFM are [...]* of EDFM's shares, [...]* of the shares and [...]*.

Therefore, the proposed transaction will lead to negative sole control within the meaning of paragraph 54 of the Jurisdictional Notice⁷.

- (5) The proposed transaction thus constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

4. UNION DIMENSION

- (6) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5,000 million [...]*. Each of them has a Union-wide turnover in excess of EUR 250 million [...]*. Neither of the undertakings achieves more than two-thirds of its aggregate Union-wide turnover within one and the same Member State.
- (7) The proposed transaction therefore has a Union dimension within the meaning of Article 1(2) of the Merger Regulation.

5. THE PROCEDURE

- (8) Based on its first phase investigation, the Commission raised serious doubts as to the compatibility of the proposed transaction with the internal market and adopted a decision to initiate proceedings pursuant to Article 6(1)(c) of the Merger Regulation on 9 November 2011 (the "Article 6(1)(c) decision").
- (9) The notifying party submitted its written comments on the Article 6(1)(c) decision on 17 November 2011.
- (10) A non-confidential version of certain key statements of third parties collected during the first phase investigation was provided to the Parties on 24 November 2011.
- (11) On 14 February 2012, the Commission adopted a Statement of Objections (the "SO") pursuant to Article 18 of the Merger Regulation.
- (12) By submission of 28 February 2012 Südzucker responded to the Statement of Objections and asked for an Oral Hearing.
- (13) On 5 March 2012 an Oral Hearing took place. As a third party, Società Fondiaria Industriale Romagnola SpA ("SFIR") attended the Oral Hearing.
- (14) The meeting of the Advisory Committee took place on 25 April 2012.

⁷ See Jurisdictional Notice, paragraph 54: "*Sole control is acquired if one undertaking alone can exercise decisive influence on an undertaking. Two general situations in which an undertaking has sole control can be distinguished (...) Second, a situation also conferring sole control 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 (the so-called negative sole control).*"

6. ASSESSMENT

- (15) The proposed transaction concerns the acquisition of sole control by Südzucker, the largest European sugar producer, of EDFM, the second largest sugar trader worldwide. EDFM is also active in the production of sugar in Europe via two refineries; the SFIR Raffineria di Brindisi ("SRB" or the "Brindisi refinery") in the South of Italy and the Sociedade de Desenvolvimento Agro-Industrial, S.A. (the "DAI refinery") in Coruche, Portugal.
- (16) The proposed transaction results in potentially affected markets for (i) the supply of white sugar in Italy and Greece, (ii) the supply of preferential raw cane sugar in the EEA, and (iii) the supply of molasses in several Member States, mainly in Central Europe. The competitive assessment will therefore focus on the markets for sugar and molasses, which are elaborated separately in the following sections of this Decision.

6.1. THE SUPPLY OF WHITE SUGAR TO ITALY AND GREECE

6.1.1. INTRODUCTION TO THE SUGAR INDUSTRY

6.1.1.1. The production of sugar

- (17) Sugar (the proper term is sucrose⁸) is the most common sweetener. It can be found in many natural foods (e.g. fruits and vegetables) but can only be extracted from sugar beet and sugar cane.
- (18) Sugar is a relatively homogeneous product. Although some variations of sugar exist on the market, such as liquid or specialty sugars, the vast majority of sugar sold is so-called "granulated white sugar".
- (19) Sugar has many different uses in industrial processing. It can be used as: a sweetener, a preservative, a flavour enhancer, a bulking agent in other foods, a food for yeast to aid fermentation in baking and brewing, a means to raise boiling or lower freezing points (e.g. in ice cream) and as an enhancer of the texture and shelf-life of certain foods (sugar absorbs moisture and provides a crunchy feel). Only around 30% of all sugar used in Europe is destined for direct consumption⁹.
- (20) Sugar is produced either from sugar beet, which is grown in Europe and elsewhere and processed into sugar locally, or from sugar cane, grown in more tropical climates.
- (21) Both sugar cane and sugar beet are increasingly used in the production of bio-fuels. Due to higher oil prices in recent years, Brazil is currently streaming more sugar cane yields into the ethanol industry in order to lower gasoline prices. In the Union, the use of bio-fuels in gasoline is also increasing, due to regulation at both Union and Member State levels calling for decreases in CO₂ emissions.

⁸ Sucrose may be hydrolisated into two molecules: glucose and fructose which are also sweeteners.

⁹ See CBI report on sugar, June 2009.

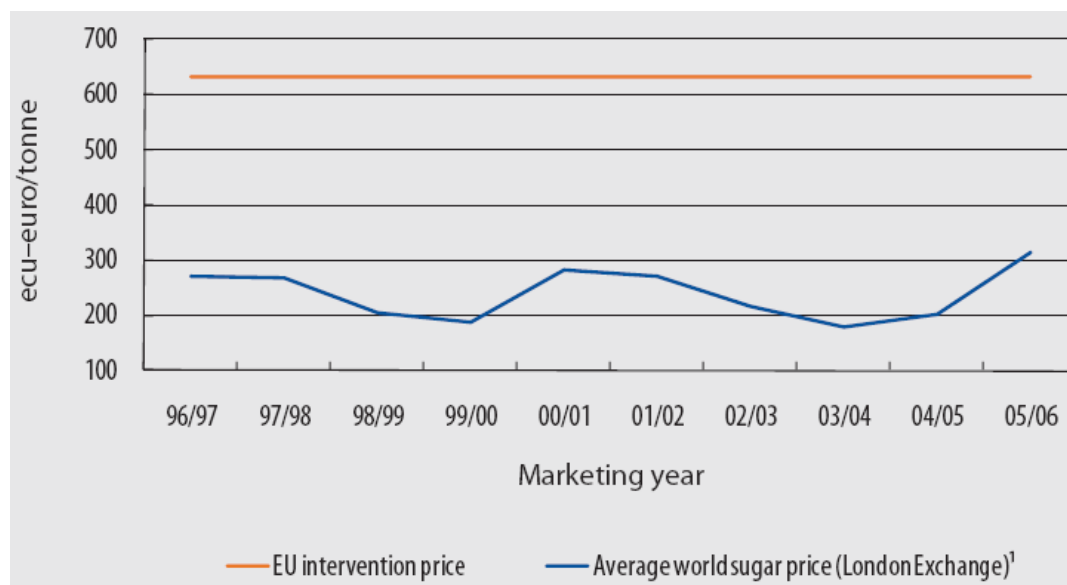
- (22) Currently, 80% of world sugar production is based on cane, while most of the sugar consumed in the Union is still beet sugar. However, since the reform of the sugar regime in the Union in 2006 a higher percentage of Union production is based on raw cane sugar.
- (23) Sugar production from beet involves extracting the beet sugar content with water into a raw juice solution which is then filtered, purified and evaporated to remove moisture and impurities and then concentrated until crystallisation occurs. This juice is in turn put through a centrifugal process to which small crystals are added in order to act as a nucleus for the crystallisation process. At the end of this process, crystallised sugar is dried, stored and packed according to end-use markets, i.e. generally in bulk, 1 tonne and 50 kg bags for industrial and merchant customers and in 1 kg or smaller packets for retail customers.
- (24) Sugar cane is a tropical grass which is harvested mechanically or by hand. Unprocessed cane sugar is not imported into the Union. Indeed, the sugar content per unit of weight is much lower for unprocessed sugar cane than for semi-processed raw cane sugar. Therefore, the import of unprocessed sugar cane would not be economical compared with the import of semi-processed raw cane sugar. Rather, the sugar cane is processed at a mill in the country of origin and the resulting raw cane sugar is then shipped to the Union as a product for further processing (refining). Alternatively, raw cane can be refined into the final product locally.
- (25) The first stage of processing cane sugar is carried out in factories close to or in the growing area. The cane is cleaned, crushed and shredded and sprayed with hot water in order to extract the juice. The juice is then further processed to create "raw cane" or raw cane sugar, which is an off-white sugar that is partly purified and is in a concentrated, crystallised, microbiologically stable form (so-called "semi-processed form") suitable for bulk handling, storage and transportation to refineries.
- (26) At the sugar refinery, the remaining impurities in the raw cane are removed through a second onward processing/refining stage which in itself is a complex process comprising various distinct stages (including affination and melting; carbonation and filtration; decolourisation; evaporation and crystallisation; and separation and drying).
- (27) White sugar production from raw cane sugar is mainly done in specialised refineries, i.e. refineries that are optimised for raw cane sugar and in which sugar cannot be produced from processing sugar beet. This is the case for EDFM's refinery in Brindisi as well as Südzucker's refinery in Marseille.
- (28) It is also possible to refine raw cane sugar in factories that are mainly dedicated to beet processing but this requires some significant modifications¹⁰. In the Union some beet sugar factories have been equipped in such way. This is the case for example in a factory of the Eridania group in Minerbio (Italy) and Südzucker group in Romania.

¹⁰ An ion exchanger for decolourization would have to be added. The crystallization process would have to be modified, but the same machinery (crystallizers, pumps, centrifuges, sugar drier etc.) can be used. Some equipment like flow transport devices or tubes, the automation systems and some other devices must be modified.

6.1.1.2. The Union regime prior to the sugar reform of 2006

- (29) The sugar common market organisation (CMO) was set up in 1967¹¹ to ensure a fair income to Community producers and to stabilise the market. Union producers could sell sugar at guaranteed prices, i.e. intervention prices which in the period 1996–2006 were significantly higher than the international market price.

Graph 1: Prices for white sugar from 1996 to 2006¹²



- (30) Production quotas distributed amongst the Member States kept the overall production within certain limits. Levies were applied on imports and sugar surpluses were exported. Sugar which had been produced within the quotas but in excess of internal market requirements was exported with export refunds (or stored). No export refunds were granted for the export of sugar which had been produced in excess of the quotas.
- (31) Prior to the 2006 sugar reform, the Union was the third largest sugar producer in the world with annual production in excess of 20 million tonnes and was the second largest consumer¹³ [...] ¹⁴.

¹¹ CMO was set up by Regulation No 1009/67/EEC of the Council of 18 December 1967 on the common organisation of the market in sugar (OJ 308, 18.12.1967, p. 1). Currently CMO is governed by Council Regulation (EC) No 1234/2007 of 22 October 2007 establishing a common organisation of agricultural markets and on specific provisions for certain agricultural products (Single CMO Regulation) (OJ L 299, 16.11.2007, p. 1).

¹² Special report n°6 from the European Court of Auditors – "Has the reform of the sugar market achieved its main objectives?" - 2010.

¹³ In 2005 the Union produced 20.3 million tonnes of sugar and consumed 15.6 million tonnes. The Union imported 2.3 million tonnes of raw sugar while exports of white sugar amounted to 7.5 million tonnes, of which 2.5 million tonnes were subsidized by the EU through export refunds.

¹⁴ The Union also had a limited production of isoglucose which is derived from processing starch usually extracted from maize or from wheat or potatoes. Isoglucose is largely used in the food industry and in many cases, for instance in soft drinks, is a potential substitute for sugar. Union production of isoglucose has been limited by the establishment of a quota of marginal magnitude. Quotas of limited importance also exist for the production of inulin syrup, a sweetener obtained from a fibre extracted from the chicory root.

(32) In the years preceding the 2006 sugar reform, the Union came under increasing pressure to avoid exporting surplus quantities of sugar at subsidised rates on the world market. This pressure finally resulted in a World Trade Organisation ruling in 2005 which obliged the Union to include out-of-quota sugar exports and re-exports of ACP imports in its sugar export limit. Thus, since 2006 the Union cannot export more than 1.37 million tonnes of subsidised white sugar, instead of the previous annual average exports of 6.5 million tonnes¹⁵.

6.1.1.3. The regime put in place by the sugar reform of 2006

(33) Following the negative WTO ruling condemning in particular the export subsidies, the Union sugar regime was reformed in 2006 in order to increase the competitiveness in the sugar sector, stabilise the markets, guarantee the availability of sugar supplies and improve the market orientation of the sector by reducing some of the regulatory barriers.

(34) Therefore the Union sugar regime was reformed in 2006 and final changes took place in October 2009.

(35) Some of the main regulatory instruments remained unchanged, such as the allocation of beet sugar production quota to Member States, which in turn allocate the quotas to sugar beet processors as a precondition for the obligation to pay the minimum beet price (reference price). Whereas the 2006 sugar reform abolished intervention prices, it still maintained a system of minimum, albeit reduced, prices to be paid to beet growers. The sugar reform also suspended export refunds for sugar as of September 2008 onwards.

(36) The main features of the sugar reform were as follows¹⁶:

- (a) Significant reduction of the overall European sugar beet production through massive quota renunciation. In the first two years of the sugar reform, the expected level of voluntary quota renunciations was not achieved, as only 2.2 million tonnes instead of the targeted 6 million tonnes were renounced, indicating that the incentives offered were not deemed to be sufficiently attractive. Therefore, in 2007 several modifications were made to the reform process creating a stronger incentive for all producers to renounce at least a certain percentage of their quota. These amendments aimed at achieving the desired Union sugar market balance through a 6 million tonnes reduction of the production of sugar, isoglucose and inulin syrup. As a direct consequence of these changes, in 2008 and 2009 producers renounced around 3.6 million tonnes quotas. By 2009, total renunciations reached 5.77 million tonnes, of which 5.23 million tonnes relates to the sugar quota.
- (b) Abolition of intervention prices: reference prices, which replaced intervention prices, have been reduced by 36% over four years starting from 2006/07. The

¹⁵ Special report n°6 from the European Court of Auditors – "Has the reform of the sugar market achieved its main objectives?" - 2010 p. 9.

¹⁶ Special report n°6 from the European Court of Auditors – "Has the reform of the sugar market achieved its main objectives?" - 2010 p. 13 et seq.

2006/07 white sugar support price of EUR 631.9 per tonne was therefore reduced to EUR 404.4 per tonne by the end of the transition period in 2009/10.

- (c) Suspension of export refunds for sugar as from September 2008 on, and only limited out-of-quota exports permitted. Following to WTO sugar panel, exports of out-of-quota sugar are limited to 1.37 million tonnes.
- (d) Establishment of a temporary restructuring fund to finance compensatory payments for voluntary production quota renunciations. A restructuring fund paid a basic EUR 730 per tonne in the first two years for producers, renouncing their quotas and quitting the industry, with at least EUR 73 per tonne going to ex-growers (the fund would be paid for by a levy on continuing processors).
- (e) Tariff-free market access for sugar from the Least Developed Countries ("LDC") and from the African, Caribbean, Pacific ("ACP") countries sugar as from 1 October 2009 on (see section 5.1.1.5).

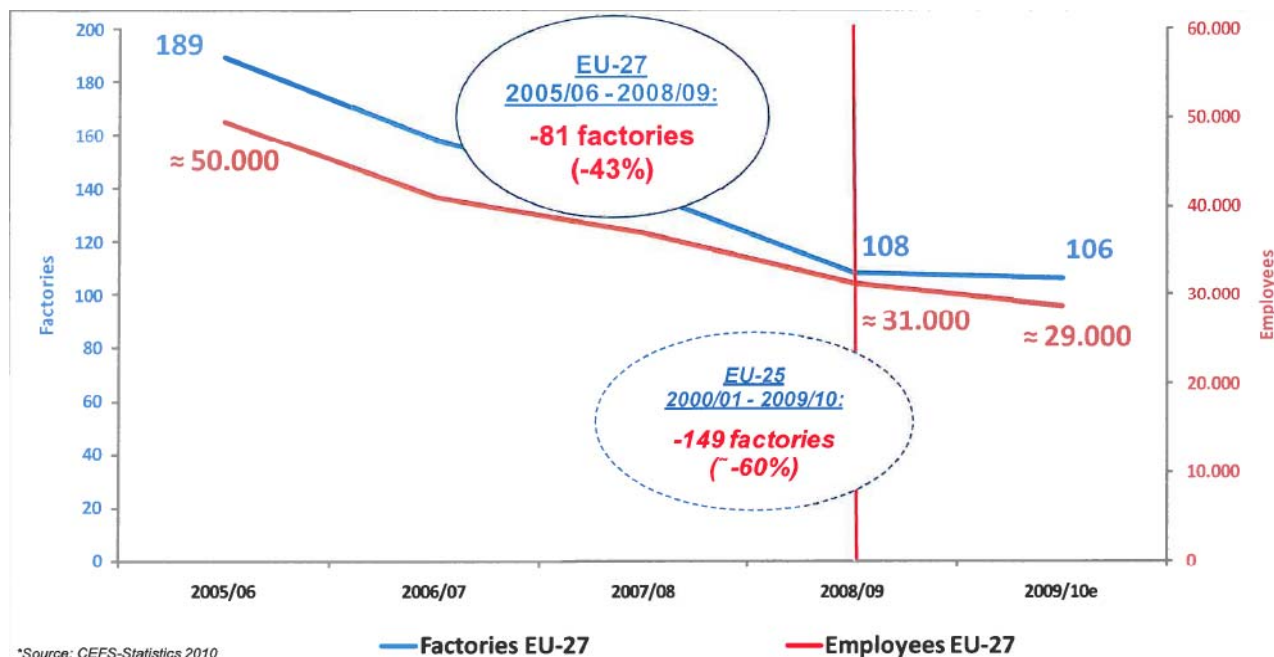
6.1.1.4. Consequence of the reform on the sugar production in the Union (internal dimension of the new regime)

- (37) From being a net leading exporter the Union has become the 2nd largest importer in the world. Quota renouncements have changed the Union market supply from a level of sugar production significantly above the internal consumption to a level of production (beet quota sugar production is currently of 13.3 million tonnes) markedly below consumption (Union domestic demand is approximately 16.7-17.1 million tonnes per year), the EU thus becoming a net importer, with Union production covering 85% of its consumption.
- (38) Those quota renouncements led to (i) a significant reduction of the Member States producing sugar, (ii) a limited number of large Union sugar producers (iii) which grew and are still growing by the way of horizontal and vertical integrations.
- (39) The Union accounts for around 9% of global sugar production¹⁷. Within the Union, France was, in 2009, the largest refined white sugar producer, accounting for almost 25% of the Union sugar production. The second largest sugar producer is Germany, accounting for approximately 22% of the Union sugar production.
- (40) The quota renouncements led to a significant reduction of the number of Member States producing sugar. While before the sugar reform 23 out of 27 Member States produced sugar from beets, after the reform five Member States stopped sugar production entirely (namely Ireland, Portugal, Slovenia, Bulgaria, Latvia), while six further Member States renounced 50% or more of their respective quota (namely Italy, Hungary, Slovakia, Greece, Finland and Spain).
- (41) Since 2000/2001, 149 sugar factories (more than 60%) have been closed, of which alone 81 sugar factories were closed between 2005/06 and 2007/08. Sugar production is now concentrated in six Member States (France, Germany, Poland,

¹⁷ Global sugar consumption reached over 162 million tonnes for the year 2007/2008 and grew to 166 million tonnes in 2008/2009, indicating a growth of 2.2% (International Sugar Organisation, 2009).

United Kingdom, Netherlands and Belgium) to which approximately 75% of the quota is allocated¹⁸.

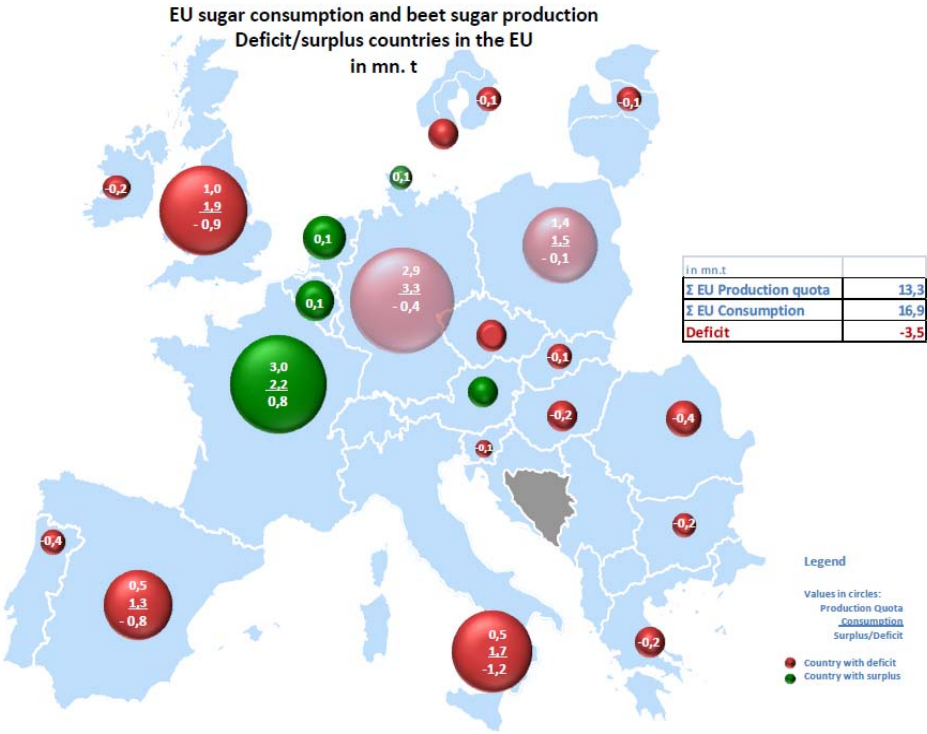
Sugar Factory closure 2001-2010



- (42) Furthermore, a large number of Member States have become sugar deficit countries in the Union with consumption exceeding domestic beet sugar production. These deficit regions are in particular southern Europe and the United Kingdom. Italy is the biggest deficit Member State followed by the United Kingdom and Spain.

¹⁸ See for instance Special Court of Auditors Report Nr 6/2010, Annex II.

Union Sugar consumption and beet sugar production



(43) As shown by the table below¹⁹, amongst the Member States which were still important sugar producers before the sugar reform, the impact has been greatest on Italy, which lost 67% of its sugar production quota between 2006 and 2009 (which represents more than 1 million tonnes).

¹⁹ Court of Auditors Report, page 49, Annex II.

Evolution of the Union sugar quotas from 2006 to 2010

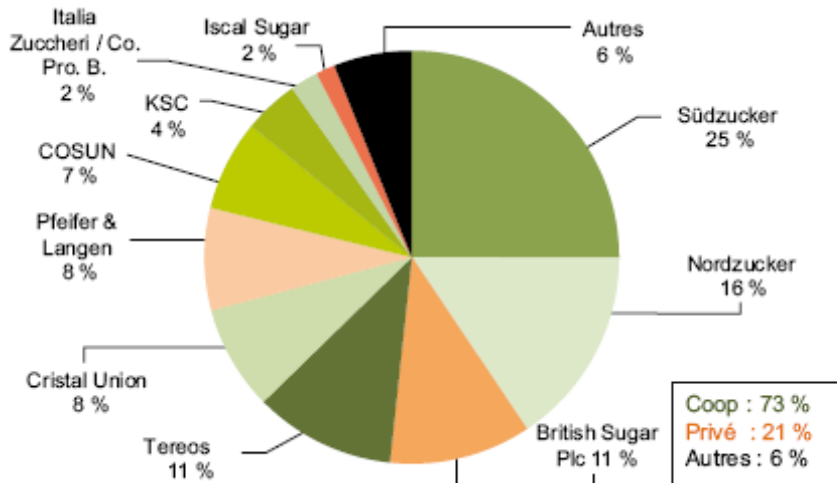
Member State	Initial quotas ¹	Quota renounced for given marketing year				Quotas available from marketing year 2009/10	Percentage of total quotas renounced
		2006/07	2007/08	2008/09	2009/10		
	(A)	(B)	(C)	(D)	(E)	(F) = (A+B+C+D+E)	(G) = $\Sigma(B+C+D+E)/A$
France ²	4 120 687			-683 655		3 437 032	16,6%
Germany	3 655 456			-757 200		2 898 256	20,7%
Poland	1 772 477			-366 869		1 405 608	20,7%
United Kingdom	1 221 474			-165 000		1 056 474	13,5%
Netherlands	931 435			-126 547		804 888	13,6%
Belgium	882 301			-206 066		676 235	23,4%
Italy	1 557 443	-778 737	-24 861	-245 467		508 378	67,4%
Spain	996 961	-93 119	-16 679	-256 578	-132 106	498 479	50,0%
Czech Republic	474 932		-102 473			372 459	21,6%
Denmark	452 466			-80 083		372 383	17,7%
Austria	405 812			-54 785		351 027	13,5%
Sweden	385 984	-42 562		-50 236		293 186	24,0%
Greece	317 502		-158 800			158 702	50,0%
Slovakia	216 037		-70 133	-33 584		112 320	48,0%
Hungary	406 684		-108 093	-193 171		105 420	74,1%
Romania ³	109 164			-4 475		104 689	4,1%
Lithuania	111 010			-20 758		90 252	18,7%
Finland	146 087		-56 087	-9 001		80 999	44,6%
Portugal ⁴	79 671	-35 218	-19 500	-15 000		9 953	87,5%
Slovenia	52 973		-52 973			0	100,0%
Latvia	66 505		-66 505			0	100,0%
Ireland	199 260	-199 260				0	100,0%
Bulgaria ³	4 752			-4 752		0	100,0%
TOTAL	18 567 073	-1 148 896	-676 104	-3 273 227	-132 106	13 336 740	28,2%

(i) Union sugar production is concentrated in a few large companies

(44) The 2006 sugar reform has led to a reduction of the number of players, thus reinforcing the concentrating pre-existing trend in the Union sugar sector. Today, five corporate alliances, namely Südzucker, Nordzucker, British Sugar, Tereos and Pfeifer & Langen account for over 80% of Union sugar beet processing capacity and 72% of the Union sugar market²⁰.

²⁰ Cf Special Agritrade report, May 2010 - <http://agritrade.cta.int/Resources/Agritrade-documents/Special-reports/Corporate-restructuring-in-the-EU-sugar-sector-Implications-for-the-ACP>

The 10 main Union sugar producers – 95% of the EU quota²¹



- (45) **Südzucker AG** is the largest sugar producer in Europe with a Union sugar quota of around 25% and a yearly sugar production of 4.2 million tonnes. Südzucker produces sugar in 29 sugar factories and three refineries in Germany, Belgium, Bosnia-Herzegovina, France, Poland, Austria, Slovakia, the Czech Republic, Hungary, Moldova and Romania.
- (46) **Nordzucker** is the second largest sugar manufacturer in Europe with an estimated Union-wide quota of 16%. The company runs five sugar beet processing factories in Germany. These are located in Sachsen-Anhalt and Niedersachsen. Additionally, there are sugar factories in Denmark, Finland, Lithuania, Poland, Slovakia and Sweden, and raw cane sugar refineries in Sweden and Finland.
- (47) **British Sugar plc** is a subsidiary of Associated British Foods and the sole British producer of sugar from sugar beet. British Sugar processes all sugar beet grown in the United Kingdom and produces about half of the United Kingdom's quota of sugar, with the remainder covered by Tate & Lyle and imports. They hold around 11% of the Union quota with four beet processing plants in the United Kingdom, three beet processing plants in northern Spain and cane sugar refinery in the South of Spain.
- (48) **Tereos** has an estimated sugar production quota of 11% in the Union and is the largest sugar manufacturer in France. The company operates nine sugar factories in France, two in the Czech Republic, and one raw cane sugar refinery in Spain. Outside the Union Tereos operates two sugar factories in La Reunion, one in Mozambique and seven in Brazil. Refineries are located in Mozambique and Brazil.
- (49) **Pfeifer & Langen** has an estimated sugar production quota of 8% in the Union and produces around 100,000 tonnes of beet molasses p.a. in Germany. It has sugar-related operations in Germany, Czech Republic, Poland, Italy, Slovenia, Croatia, Ukraine, Romania, Hungary and Greece. The company runs six sugar factories in Germany, four of which are located in the very western part of Germany close to the

²¹ Graph available on the "Rapport d'activité 2011 from Confédération Générale des planteurs de betteraves" <http://www.cgb-france.fr/IMG/pdf/RapportDactivite-2011-Web.pdf> p.6.

Dutch and Belgian border. P&L is also the third largest sugar manufacturer in Poland with four beet sugar factories. It also operates a sugar factory in Romania.

(50) In its decision on the merger *Nordzucker/Danisco* (B2-46/08), the Bundeskartellamt considered that the German sugar market was dominated by an oligopoly of Nordzucker and Südzucker and that those companies created "sealed off" regional distribution areas, which they mutually respected. Sugar companies agreed on avoiding price competition within Germany by increasing activities in deficit countries regardless of high transport costs. The Bundeskartellamt has finally cleared the acquisition of Danisco by Nordzucker under the condition that Danisco's production plant in northern Germany (Anklam/Mecklenburg-Western Pomerania) is sold to a suitable purchaser before the acquisition is realized. The purchaser proposed by the parties, the Dutch sugar producer Royal Cosun ("Cosun"), has been accepted by the Bundeskartellamt.

(ii) The increasing trend towards horizontal and vertical integrations

(51) Due to the impact of the 2006 Union sugar reform, many Member States have become sugar deficit countries in the Union. In these countries where the demand is much higher than local production, the leading sugar producers in the Union have used different ways in order to be present. For instance, Nordzucker acquired the Scandinavian producer Danisco while ABF acquired the Spanish refiner Azucarera. In Italy, the traditional Italian sugar manufacturers, such as Eridania-Sadam, Italia Zuccheri S.p.A. ("Italia Zuccheri") and SFIR, have been trying to keep their "pre-reform" market share. In that context, they have established joint ventures mainly with manufacturers from surplus Member States, in order to satisfy the demand of their customers.

(52) Thus, the German sugar manufacturer Pfeiffer & Langen acquired 49.9% of Italia Zuccheri, while Tate & Lyle (recently replaced by Cristal Union) established a joint venture with Eridania for the marketing and sales of all sugar products. SFIR has taken a different approach by building a new refinery in a joint venture with EDFM in the South of Italy. SFIR also bought white sugar from other players, such as Eurosugar (Nordzucker, Sucre Union, and EDFM) in order to satisfy the demand of its customers. Other sugar manufacturers, such as Tereos, entered the market by establishing local distribution companies. Finally Südzucker, the leading supplier in Italy, markets and sells refined sugar through the joint venture Maxi Srl – a well-known Italian wholesaler, which Südzucker jointly controls together with Podini Holding S.p.A ("MAXI").

(53) To balance the lower sugar production, a few European beet sugar producers have tried to secure their own raw cane sugar supplies from ACP and LDC countries either by creating powerful integrated players – (e.g. ABF through Illovo which controls a significant amount of raw cane in Malawi, Zambia, Swaziland, Mozambique and Tanzania) – or through strong partnerships with players in those

countries (e.g. Südzucker in Mauritius, Tereos in Mozambique, Tate & Lyle in Barbados, Belize, Cambodia, Fiji, Guyana and Laos)²².

6.1.1.5. Consequence of the reform on the trade between the Union and third countries (external dimension)

- (54) Since the reform of the Union sugar industry was initiated in 2006/07, it was expected that the Union domestic demand of approximately 16.7-17.1 million tonnes per annum would be covered by Member State beet quota sugar production of 13.3 million tonnes, with the remainder covered by imported sugar from traditional preferential trade partners²³. However, between then and now this has not been the case notably because expected imports from LDC/ACP-countries have been below the Commission's expectations, with the result that quota stock levels have progressively fallen.
- (55) At the moment, raw cane sugar for refining may be imported into the Union from third countries under the following customs schemes:
- (i) Sugar imports from ACP/LCP countries - Everything But Arms initiative and Economic Partnership Agreements
- (56) On 26 February 2001, the "Everything But Arms" (EBA) amendment to the EU's Generalised Scheme of Preferences (GSP) was adopted. EBA extended duty and quota free access to all products originating in Least Developed Countries (LDCs), except arms and ammunition. However, three sensitive products, namely sugar, bananas and rice were not liberalised until 1st October 2009.
- (57) On 23 June 2000, a new Partnership Agreement between the 77 ACP countries and the then 15 Member States was signed in Cotonou. The ACP-EU Sugar Protocol was annexed to Annex V of the Cotonou Partnership Agreement. Compared with the Lomé Conventions, the Cotonou trade regime paved the way for a profound transformation, preserving non-reciprocal tariff preferences until 31st December 2007, but replacing them as from 2008 with trade arrangements agreed in reciprocal Economic Partnership Agreements (EPAs) compatible with the rules of the World Trade Organisation (WTO).
- (58) From 2001 until 2009, imports of sugar from LDCs were restricted by an annual first-come-first-served quota. In the 2001/02 marketing year, the quota was fixed at

²² See answer of Südzucker to the third request of information. See also <http://agritrade.cta.int/en/Welcome-to-Agritrade> (Agritrade is the website for ACP-EU agriculture and fisheries trade issues).

²³ Even though the Commission decided to suspend export refunds for sugar from September 2008, the Union still exports between 500,000 tonnes and 1 million tonne of sugar/year, see Commission Regulations (EC) No 900/2007 of July 2007 on a standing invitation to tender to determine refunds on exports of white sugar until the end of the 2007/2008 marketing year (OJ L 196, 28.7.2007, p. 26), Commission Regulation (EC) No 947/2008 of 25 September 2008 suspending the export refunds on white and raw sugar exported without further processing (OJ L 258, 26.9.2008, p. 60), Commission Regulation (EC) No 948/2008 of 25 September 2008 suspending the export refunds on syrups and certain other sugar products exported without further processing (OJ L 258, 26.9.2008, p. 61) and Commission Regulation (EC) No 951/2008 of 25 September 2008 fixing the rates of refunds applicable to certain products from the sugar sector exported in the form of goods not covered by Annex I to the Treaty (OJ L 258, 26.9.2008, p. 66).

74,185 tonnes w.s.e., and was increased by 15% (compound) per annum until 2008/09. The EBA quota did not increase the raw sugar access or availability to the Union market because that quantity reduced tonne-for-tonne the amount of SPS/CQ required from the ACP suppliers.

- (59) With the tacit approval of the Commission, the LDC Ambassadors based in Brussels agreed a “EBA Sugar Framework Agreement” which allocated the overall annual EBA quantity on the basis of a formula (based one third on GDP per capita, one third sugar production and one third in equal shares) which ensured that every LDC sugar supplier which wanted to ship to the Union in any year could register and would be allocated a meaningful share by the Ambassadors in accordance with the agreed formula.
- (60) As from 1 October 2009, in accordance with the provisions of the EPAs, the ACP and the Union agreed to duty-free-quota-free (“DFQF”) access for ACP sugar to the Union markets, subject to a the transitional safeguard mechanism for sugar of 3.5 million tonnes per annum fixed in Article 9 (1)(b) of Council Regulation (EC) No 1528/2007 of 20 December 2007 applying the arrangements for products originating in certain States which are part of the African, Caribbean and Pacific (ACP) Group of States provided for in agreements establishing, or leading to the establishment of, Economic Partnership Agreements²⁴. At the same time, the DFQF for sugar was also extended to the LDCs under the EBA initiative with a non-automatic safeguard clause. Taking into account the number of ACP countries involved, the EPA regime applies to almost half the ACP countries (36 countries), and the EBA regime applies to 31 countries. All 19 ACP beneficiaries of the Sugar Protocol will come either under the EPA (17 countries) or the EBA regime (2 countries). The only ACP countries excluded from the preferential regime are the 10 non-LDCs that have neither signed nor initialed an EPA with the Union.

(ii) CXL quotas

- (61) In the wake of the accession of Austria, Finland and Sweden, and in the context of the conclusion of the negotiations under Article XXIV of the General Agreement on Tariffs and Trade (GATT), the Union undertook to import from third countries, from 1st January 1996, a quantity of raw cane sugar for refining, known as the CXL sugar quota, at a rate of duty of EUR 98 per tonne. The quota was originally set at 85,463 tonnes (of which 58,969 tonnes was assigned to Cuba and 23,930 tonnes to Brazil).
- (62) The quota was further expanded to its current level in 2007 following the accession of Bulgaria and Romania to the Union and negotiations under Article XXIV:6 of the GATT. The current CXL quotas are presented in the table below.

²⁴ OJ L 348, 31.12.2007, p. 1.

Country	Access
Australia	9,925
Brazil	334,054
Cuba	68,969
Erga Omnes (3rd Countries)	253,977
India	10,000
TOTAL	676,925

(iii) Exceptional tariff rate quotas

- (63) Special rules have been agreed for exceptional tariff rate quotas (TRQs) for sugar, these exceptional quotas being deemed necessary from time to time by the Commission in case of exceptional market conditions (Article 186 and/or 187 of Council Regulation (EC) No 1234/2007 of 22 October 2007 establishing a common organisation of agricultural markets and on specific provisions for certain agricultural products²⁵ (the "Single CMO Regulation")).

(iv) Other sugar import custom schemes

- (64) Sugar can also be imported from the world market under most favoured nation (MFN) conditions on payment of the appropriate import duties, notably EUR 419 per tonne for white and direct consumption sugars and EUR 339 per tonne for raw sugar for refining, plus additional special safeguard (SSG) duties.

- (65) The system of import licenses is regulated by framework rules set by the Commission²⁶.

(v) However the volumes available of raw cane sugar are insufficient for the Union refineries

- (66) The access to raw sugar from ACP/LDC countries or under CXL quotas is crucial and strategic for Union sugar producers since it is the only raw cane sugar that can be imported without prohibitive duties and quantities into the Union.

- (67) In the sugar marketing year 2010/11 the expected use of sugar in the Union was around 17.2 million tonnes. Thereof 13.8 million tonnes were supplied by beet quota sugar production of the marketing year and 1.1 million tonnes by CXL and Balkan import quotas. The 700,000 tonnes under CXL quotas consisted almost exclusively of raw cane sugar for refining while the 400,000 tonnes imported from the Balkans was white sugar for direct consumption.

²⁵ OJ L 299, 16.11.2007, p. 1.

²⁶ Commission Regulation (EC) No 376/2008 of 23 April 2008 laying down common detailed rules for the application of the system of import and export licenses and advance fixing certificates for agricultural products. In addition, for ACP/LDC and CXL sugar from a named origin, an export licence is required in order to apply for an EU import licence. These export licences must be certified and authenticated by the competent authorities of the originating country, thereby giving the exporting country the wherewithal and moreover the obligation (under customs cooperation agreements) to control the export marketing of the sugar originating in its territory.

- (68) The remaining 2.3 million tonnes were partially covered by [...] * tonnes of imports from ACP/LDC producers, [90-100] *% of which being raw cane sugar for refining and [10-20] *% white sugar for direct consumption²⁷.
- (69) Therefore, for the marketing year 2010/2011, about 2.5 million tonnes of preferential raw cane sugar for refining (including raw sugar from ACP/LDC countries and raw sugar under CXL quotas) were imported into the EEA. This is less than what was necessary to close the gap with European demand. One reason for that gap was that international market prices²⁸ increased significantly relative to Union prices. Another reason was that the ACP and LDC countries were not able to expand their sugar production as fast as initially expected.
- (70) Due to unavailability of raw cane sugar, cane sugar refineries are currently operating well below capacity in the EEA as shows the figure below.

Estimated supply and demand for raw cane sugar for refining in the Union²⁹

[...] *

6.1.1.6. Significant price increase in the Union

- (71) European prices for sugar, at least initially, fell drastically. At the beginning of the 2010/11 marketing year (starting from 1 October 2010) the international market price for sugar were even at a higher level than the Union sugar price as a consequence of shortfalls in important sugar producing countries, such as Mauritius, Fiji, Guyana, Swaziland and Brazil. Whereas one of the recommendations of the special report of the European Court of Auditors was that "[t]he Commission and the Member States must ensure that competition law is correctly enforced in the sector thus ensuring the Treaty objective that supplies reach consumers at reasonable prices"³⁰, the press in several Member States has recently reported however significant price rises in particular of retail sugar. In some Member States such price rises seem to reach 30 to 40 %. [...] *.

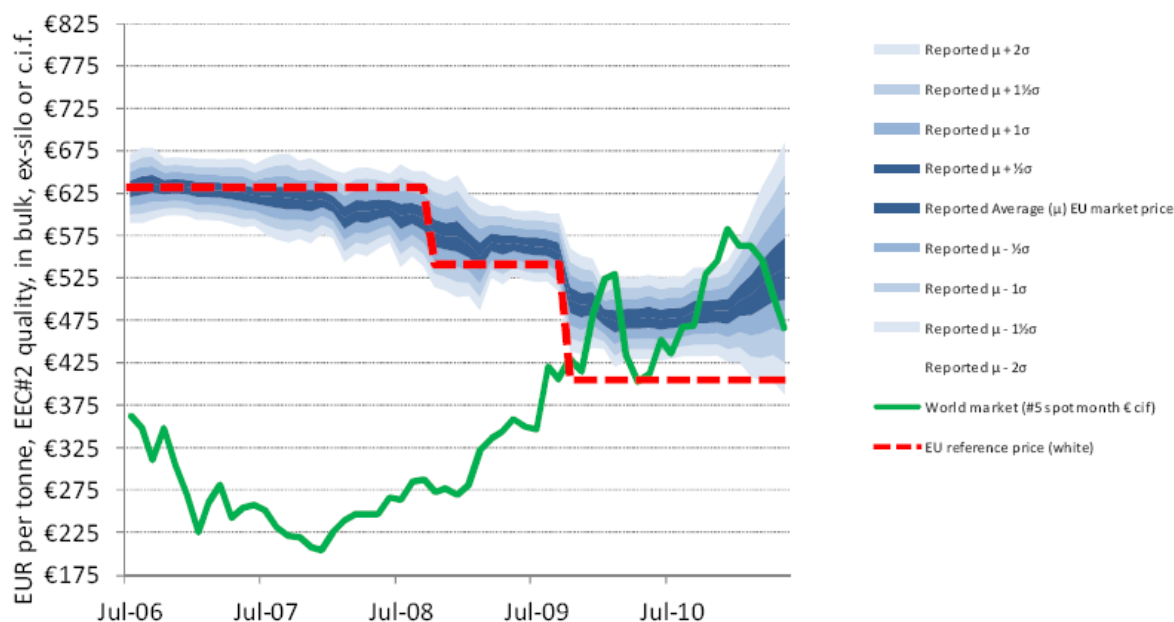
²⁷ See 3rd request for information to EDFM. 10/12/2011.

²⁸ The spot prices determined for raw sugar on the two main futures markets, London (LDP) and New York (NY spot price), are considered to be indicators of the world price. The International Sugar Organisation spot price is calculated daily from these two prices. The key indicator price for refined white sugar is the London LIFFE Contract Number 5.

²⁹ Estimates from EDFM in the submission entitled "The European Union market for raw cane sugar for refining and the place of ED&F Man in that market".

³⁰ Court of Auditors Report, paragraph 102, Recommendation IV.

Union and international market white sugar prices³¹



- (72) Article 187 of Council Regulation (EC) No 1234/2007 states that, in the event of sugar prices reaching a level that disrupts or threatens to disrupt the availability of supply on the Union market and where that situation is likely to continue or to deteriorate, the Commission may, in particular, suspend the usual MFN import duties in whole or in part for certain quantities.
- (73) In the Union sugar sector, such an event was recorded during the 2010/11 season, when it became clear that high international market prices were leading to a very low level of Union sugar stocks. Given the situation in March 2011, the Commission opened an 'exceptional' import quota for 300,000 tonnes at zero duty for raw and white sugar. When it became clear that this quantity would not be enough to cover a projected shortfall in the Union market, a second 'exceptional' import quota for 200,000 tonnes was opened at the end of May 2011.
- (74) The rule for allocating licences was the "simultaneous examination method"³², and given the high margins that were available at the time, each quota was heavily oversubscribed (for example, for the first quota a final allocation coefficient of 1.8053% was fixed, implying that import licences for applications for 16.6 million tonnes were received). According to the Parties, a consequence of this was that the final awarded tonnages were small (for example, if an operator had applied for the full first 300,000 tonne quota, they ended up receiving just 5.400 tonnes).

³¹ Annex 7.8 e) Form CO.

³² In the case of tariff quotas, e.g. for CXL sugar, applications are administered according to the "simultaneous examination method". In accordance with the rules of this method, applicants may not lodge more than one import licence application for the same quota order number each week; where an applicant lodges more than one application per order number per week, none of his applications will be admissible. An application may not relate to a quantity exceeding the total quantity of the quota. If the Commission receives more applications than total quota available in any week, it will fix an allocation coefficient to apply to each licence application. The allocation coefficient will be calculated as follows: [(available quantity/requested quantity) × 100] %.

- (75) Against this backdrop, and with Union supply shortages still not alleviated, the Commission opened a third ‘exceptional’ import quota on 29th June 2011. However, the mechanism for allocating import licences to Union operators was not the same; instead the Commission decided on a tendering procedure for raw and white sugar imports. Under this scheme, five tenders were opened between July and September, during each of which tenderers could apply for between 20 - 45,000 tonnes and the proposed amount of customs duty they were willing to pay. It was then at the Union's discretion as to the quantities and duties that were awarded after each tender. The table below shows the quantities of sugar that was awarded at each of the tenders:

EU - Results of the Tendering Scheme, 2010/11

Tender	Date	Raw Sugar for Refining		Direct Consumption Raws		White Sugar		TOTAL	
		Total Bids	Awarded	Total Bids	Awarded	Total Bids	Awarded	Total Bids	Awarded
1	14/07/2011	260,800	55,000	1,644	1,644	127,976	7,720	390,420	64,364
2	28/07/2011	n.a.	141,960	n.a.	200	n.a.	10,048	n.a.	152,208
3	24/08/2011	n.a.	83,535	n.a.	775	n.a.	27,440	n.a.	111,750
4	15/09/2011	n.a.	0	n.a.	1,160	n.a.	7,509	n.a.	8,669
5	29/09/2011	176,040	14,500	2,721	827	106,407	4,266	285,168	19,593
Total			294,995		4,606		56,983		356,584

Note: n.a. = not announced

- (76) Under those five tenders in 2010/11, a total of 356,584 tonnes was awarded, 85% of which was for raw sugar for refining.

- (77) As the situation of high and volatile international market prices has continued, in November 2011 the Commission once again agreed to open an exceptional import quota to be allocated under a tendering scheme for the 2011/12 marketing year. The Commission announced that it aims to allow about 300,000 tonnes to enter into the Union through the import tenders in order to cover an estimated shortfall of 700,000 tonnes (the rest being covered by the release of out-of quota sugar into the Union domestic market).

6.1.1.7. A new sugar reform is currently discussed

- (78) On 12 October 2011 the Commission published its legislative proposal for the Common Agricultural Policy (CAP) after 2013. The Commission's stated intention is to finalise the legislation and implementing rules so that the revised CAP can enter into force on 1 January 2014.

- (79) The potential expiry of quotas should not take place before September 2015 as evidenced by the document "Prospects for agricultural markets and income 2011-2020" published in December 2011 by DG AGRI³³.

- (80) At the moment, the outcome of this reform is uncertain and the end of sugar quotas faces considerable opposition as is illustrated by the press releases of the last European Council for Agriculture stating that "[t]he Council took note of the request from the Hungarian delegation on the extension of the sugar quota regime to 2020. This received varied support from the Belgian, Czech, German, Spanish, French, Lithuanian, Austrian, Portuguese, Slovak, Finnish and Romanian delegations"

³³

http://ec.europa.eu/agriculture/publi/caprep/prospects2011/fullrep_en.pdf

(14/11/2011)³⁴ and "many delegations mentioned that the end of sugar quotas scheduled for 2015 should be postponed" (28/01/2012)³⁵.

- (81) Furthermore, in his report, the MEP Albert Dess "advocates that the 2006 sugar market regime be extended at least to 2020 in its existing form and calls for suitable measures to safeguard sugar production in Europe and to allow the EU sugar sector to improve its competitiveness within a stable framework; to allow the sector to better adapt"³⁶.
- (82) Given the number of uncertainties, the reform of the CAP cannot be considered as a relevant counterfactual in the assessment of the competitive effect deriving from the proposed transaction.

6.1.1.8. Background of the Italian sugar industry

- (83) Italy is the second largest sugar consumer in the Union after Germany. In Italy, the annual demand amounts to 1.73 million tonnes of sugar³⁷. Italy is also the market with the largest sugar deficit in the Union.
- (84) In Italy the sugar is mainly sold to two types of customers: industrial processors and retailers. The following [...] ³⁸ presents the most important Italian sugar consumers:

Sugar consumers type in Italy

[...]*

- (85) Around 60% of all sugar is consumed in the North of Italy, to where sugar from closely located regions can be economically transported. Central Italy and southern Italy are in a more disadvantageous situation. According to internal documents of EDFM based on an internal logistics model, the average transportation costs in Italy amount to EUR [...] * per tonne, while the transportation costs to Central Italy and southern Italy amount to EUR [...] * per tonne.
- (86) The local production after the 2006 quota reform and prior to the launch of the Brindisi refinery covered less than 50% of the Italian demand. In Italy 15 out of 19 sugar beet factories closed after the reform and the limited domestic beet sugar production was carried out by three companies until the jointly controlled Brindisi refinery became operational in January 2011. Those three Italian producers are Eridania Sadam [description of Eridania' production]*, CO.PRO.B. s.c.a. ("COPROB")/Italian Zuccheri [description of COPROB's production]* and Zuccherificio del Molise ["ZDM"]. The rest of the Italian sugar demand is satisfied *via* imports mainly from the closely located surplus countries, in particular from

³⁴ See press release – 3123rd Council meeting - Agriculture and Fisheries.

³⁵ See press release - 3140th Council meeting - Agriculture and Fisheries.

³⁶ See Report "the CAP towards 2020: meeting the food, natural resources and territorial challenges of the future" Albery Dess, 31 May 2011.

³⁷ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 12, sent by e-mail of 1 December 2011 (19:33).

³⁸ Answer to the 6th request for information to EDFM of 11 October 2011, internal document on "Italian Market" (undated).

South-East France and especially the French producer Tereos and from southern Germany from the Südzucker.

- (87) Major European sugar producers have considered the deficit in the Italian market as a real opportunity to enter a key market. However, except Tereos which entered at a very early stage by establishing a sales office in Italy, they all teamed up with an existing Italian player in order to sell their sugar in Italy: Südzucker with MAXI, Pfeifer & Langen with Italia Zuccheri, Cristal Union with Eridania³⁹.
- (88) Other characteristics and aspects of the Italian sugar market will be analysed in more detail in the market definition and in the competitive assessment parts.

6.1.1.9. Background of the Greek sugar industry

- (89) The Greek sugar market is characterized by the presence and strength of the incumbent sugar producer, Hellenic Sugar. It is the only sugar supplier in Greece having sugar production facility in Greece⁴⁰. [description of Hellenic Sugar's production plants]*. The Hellenic Sugar's production quota amounts to [...] tonnes per year⁴¹. That quota does not cover domestic demand; therefore Greece is a sugar deficit Member State like Italy.
- (90) Other market players are, nevertheless, present in Greece via sugar imports, namely Südzucker, Tereos, Nordzucker and Pfeifer & Langen (Sugartia).

6.1.2. RELEVANT PRODUCT MARKET

6.1.2.1. Description of white sugar

- (91) The supply of sugar in the Union is regulated by the Common Market Organization (CMO), the principles of which are set out in Regulation (EC) No 1234/2007.
- (92) Depending on the sucrose content, Regulation No 1234/2007 distinguishes between "white sugar" and "raw sugar": while both refer to "*not flavoured or coloured or containing any other added substances*" sugar, "white sugar" must contain, in the dry state, 99.5 % or more by weight of sucrose. Sugar with less than 99.5 % of sucrose is considered as "raw sugar".

6.1.2.2. White sugar as compared to industrial sugar

- (93) Under the Union sugar regime, the white sugar market is divided into two segments; for quota sugar and out-of-quota sugar utilization. Different regulations apply to each segment. There are approximately 16 to 17 million tonnes of quota sugar available to the Union consisting of white sugar produced within the Union as well as white sugar imported under various quota arrangements into the Union, including quota allocated to Brazil, the Balkan countries, LDC and ACP countries (accounting for approximately 2.5 to 3 million tonnes). Quota sugar is primarily used for food

³⁹ Tate & Lyle had until last year a partnership with Eridania.

⁴⁰ Reply by Hellenic Sugar to question 65 of the Questionnaire to Sugar Suppliers/Producers in Greece – Phase II.

⁴¹ Reply by Hellenic Sugar to question 46 of the Questionnaire to Sugar Suppliers/Producers in Greece – Phase II.

applications. In contrast, out-of-quota sugar (also referred to as "industrial sugar") cannot be sold on the market for food applications but only for certain defined purposes such as alcohol, yeast production or in the chemical and pharmaceutical industry⁴². Therefore, there are significant differences between the commercialisation of quota sugar and the out-of quota sugar. The quota sugar market is regulated to a certain extent, including some elements of price regulation, whereas the out-of-quota market is less regulated and adheres more to international developments and conditions⁴³.

- (94) As the proposed transaction does not lead to any overlap or any other reason for competition concerns with respect to the supply of out-of-quota sugar in Italy or in Greece⁴⁴, this Decision will only assess the Parties' activities in the supply of quota sugar for food applications (hereinafter white sugar).
- (95) The notifying party considers that it is not necessary to further segment the white sugar market according to the origin (beet or cane), the type (such as granulated, liquid, industry specialities, etc.), or the distribution channel (food industry or retail) of sugar. According to the notifying party, the market should include all types of sugar intended for food consumption⁴⁵.

6.1.2.3. Different origins of sugar

- (96) On the basis of the market investigation, the Commission considers that, with regard to both Italy and Greece, no distinction is necessary as regards the origin of white sugar. Although, according to respondents, for very limited applications refined beet and cane sugar are not interchangeable, their vast majority considers the two types of sugar to be interchangeable. Therefore, for the purpose of this Decision, the Commission concludes that it is not appropriate to distinguish between beet sugar and cane sugar.

6.1.2.4. Different forms of white sugar

- (97) White sugar is available on the market under various forms: granulated sugar, liquid sugar, industry specialities etc.
- (98) Granulated sugar is the most common type of sugar sold in the Union, the basic product used in all industries. Liquid sugar is obtained by mixing granulated sugar with a liquid. Liquid sugar is used mainly in the beverage/soft drink industry in technically highly developed Member States, where smaller beverage producers dominate the market structure⁴⁶. The category of industry specialities refers to sugar processed for special clients' use. For example, one type of industry specialities sugar, fondant, is based on granulated sugar with the addition of glucose and various other elements.

⁴² Article 62(2) of the Regulation (EC) No1234/2007.

⁴³ Form CO, p.48.

⁴⁴ Südzucker reply to the 7th Request for Information ("RFI") in Phase II.

⁴⁵ Form CO p. 48.

⁴⁶ Form CO p.49.

- (99) The Commission and national competition authorities ("NCAs") have considered the sugar market in several cases⁴⁷. In its most recent decision⁴⁸ the Commission left open whether different types of sugar belong to the same market indicating that "*for different types of sugar there is limited substitutability from the customer's point of view since each type of sugar tends to fulfil a certain requirement and each type differs as to the texture, colour and flavour. However, from a supply-side perspective, in the market investigation most sugar producers indicated that they can easily switch production between different types of sugar without significant cost as well as within a short period of time (i.e. significantly less than one year) in order to meet the demands of customers*".
- (100) The notifying party submitted in the present case that the appropriate product market to assess the proposed transaction in this case encompasses all types of sugar (granulated, liquid etc). It refers to the Commission previous findings, as well as to the United Kingdom Competition Commission's findings in the case *James Budgett Sugars Ltd and Napier Brown Foods PLC*⁴⁹, according to which, although different sugar products may not be close substitutes for each other in certain industrial processes, there is, on the supply side, a high degree of substitutability between different types of sugar.
- (i) *Italy*
- (101) In Italy, Südzucker sells a variety of sugar products derived from further processing of white sugar. [...] ⁵⁰. Therefore, a distinction between granulated, liquid and other types of sugar is immaterial for the assessment of the proposed transaction. The Commission will therefore not consider a further segmentation according to the different types of sugar, as also put forward by the notifying party.
- (ii) *Greece*
- (102) EDFM has no overall sales of sugar in Greece, and thus also no sales of liquid sugar or industry specialities sugar to end-customers⁵¹. Therefore, a distinction between granulated, liquid and other types of sugar is immaterial for the assessment of the proposed transaction in Greece. The Commission will thus not consider a further segmentation according to the different types of sugar, as also put forward by the notifying party.

⁴⁷ Commission Decision 2003/259/EC in Case No COMP/M.2530 - Südzucker/Saint Louis Sucre (OJ L 103, 24.4.2003, p. 1); Commission Decision 97/624/EC of 14 May 1997 in Case IV/F 3/M.34.621 Irish Sugar (OJ L 258, 22.9.1997, p. 1); Commission Decision 1999/210/EC of 14 October 1998 in Case IV/F 3/33.708 British Sugar (OJ L 76, 22.3.1999, p. 1).

⁴⁸ Commission Decision of 30 March 2009 in Case No COMP/M.5449 – ABF / AZUCARERA (OJ C 97, 28.4.2009, p. 2).

⁴⁹ United Kingdom Competition Commission *James Budgett Sugars Ltd and Napier Brown Foods PLC*, 2005.

⁵⁰ [...]*.

⁵¹ Südzucker's reply to the 3rd RFI in Phase II, Annex 35-1 Form CO Greece, page 15.

6.1.2.5. Distinction according to customer types

Commission previous findings

- (103) In its previous decisions, the Commission considered a potential segmentation of the sugar supply market by distribution channel. The Commission has consistently confirmed a distinction between industrial and retail sugar in its decisions⁵²: industrial sugar is sold in large quantities to industrial customers mainly in the food and beverage industry ("white sugar sold to industrial processors"), while retail sugar is sold in small packages to end-customers primarily via retail chains ("white sugar sold to retailers").
- (104) In the case *Südzucker/Saint Louis Sucre*⁵³, the Commission concluded that in Germany a third additional market for the sugar supply can be distinguished according to the distribution channel, namely sugar for distributors' private labels. The Commission acknowledged, however, that this category is less familiar among businesses in other Member States such as France, where on the downstream retail market very little sugar is sold under distributors' private labels. Such a third distinction (i.e. to consider private label sugar as a distinct product market) was not considered by the Commission to be necessary in the case *ABF/AZUCARERA*⁵⁴.

View of the notifying party

- (105) With regard to the proposed transaction, the notifying party considers that white sugar sold to industrial processors and white sugar sold to retailers may constitute separate market segments, although they also point out the "*great degree*" of supply-side substitutability between these two categories. Indeed, the notifying party explained⁵⁵ that sugar production is a two steps process. In a first step bulk sugar is produced which is stored in most cases in sugar silos. In a second step this bulk sugar is directly sold or can be further processed and/or packed depending on the customers' demands. The ability of a producer to switch between white sugar sold to industrial processors and white sugar sold to retailers depends on the availability of free capacities for the - compared to the standard product bulk sugar - additional steps.

Commission findings in the case at hand

(i) Italy

- (106) In the Commission's view, the replies to its requests for information show that switching production from white sugar sold to industrial processors to white sugar sold to retailers may not be as easy as described by the notifying party. Although some competitors of the Parties answered positively, when asked whether, in case of a permanent price increase of 10% in Italy for white sugar sold to retailers they could

⁵² See Commission Decision 97/624/EC of 14 May 1997 in Case IV/F 3/M.34.621 Irish Sugar, OJ L 258, 22.09.1997, p. 1, recital 90, and Commission Decision 1999/210/EC of 14 October 1998 in Case IV/F 3/33.708 British Sugar, OJ L 76, 22.3.1999, p. 1, recital 59.

⁵³ Commission Decision 2003/259/EC in Case No COMP/M.2530 – Südzucker / Saint Louis Sucre.

⁵⁴ Commission Decision of 30 March 2009 in Case No COMP/M.5449 – *ABF / AZUCARERA*.

⁵⁵ Answers to 3rd Request for Information to Südzucker, Form CO – Italy, pages 6 and 7, sent by e-mail of 1 December 2011 (19:33).

switch their production, the largest player in the retail market replied that it would not switch.⁵⁶ Furthermore, when asked to elaborate on their position, those competitors explained that, when switching production from white sugar to be sold to industrial processors to white sugar to be sold to retailers, several elements have to be considered.⁵⁷ In addition to the technical investments in order to install a packaging line, the supplier must consider the costs involved in designing the packaging, the listing fees in each Italian store and the promotion in stores which is necessary in order to become established as a retail sugar supplier. This could require significant investments (up to several millions of euros)⁵⁸.

- (107) From a demand side perspective there is also limited substitutability between products sold to retail and industrial customers. The great majority of customers responding to the market investigation consider the Commission's previous market segmentations⁵⁹ in which sugar for industrial processors and for retailers constitute separate markets to be appropriate⁶⁰. The main reason the majority of respondents consider such product market segmentation as the appropriate way to assess the competition in the sugar industry is because distribution through industrial and retail channels follows different market logics (for example in terms of marketing and packaging).
- (108) Concerning the packaging, industrial processors require their sugar delivered in bulk or large bags, whereas retail customers tend to prefer smaller packets of 1 kilogram or less.
- (109) Different competitors adopt different market positioning and, as a result, the market shares in the two markets differ significantly (see in particular recitals (336) and (337) of this Decision which discusses market shares). In particular, Eridania, which is seen as one of the most recognised brands of white sugar sold in the retail channel in Italy, has market shares several times higher in the market for white sugar sold to retailers compared to the market for white sugar sold to industrial processors. In contrast, the notifying party has significantly higher market shares for white sugar sold to industrial processors than for white sugar sold to retailers.
- (110) Some respondents to the market investigation also explained that colour or quality differences may exist between industrial and retail users⁶¹.
- (111) Overall, these differences in the packaging, distribution and customer profiles for industrial and retail sugar are also manifested by different pricing structures, with white sugar sold to retailers persistently being more expensive than white sugar sold

⁵⁶ Questionnaire to Sugar Competitors Italy, Phase II, question 24.

⁵⁷ Follow-up questions to Sugar Competitors in Italy sent on 17 January 2012.

⁵⁸ SFIR's reply to Question 9 of the 2nd RFI in Phase II; [...] reply to Question 20 of the Questionnaire to Sugar Competitors Italy, Phase II.

⁵⁹ See Commission Decision 2003/259/EC in Case No COMP/M. 2530 - Südzucker/Saint Louis Sucre, Commission Decision 97/624/EC in Case No IV.F-3/M34.621 Irish Sugar 1997, Commission Decision 1999/210/EC in Case No IV/F-3/33.708 British Sugar but also the Decisions from the British, French and Spanish competition authorities: (i) Acquisition of Illovo Sugar Limited by ABF Overseas Limited, OFT, 31 July 2006. (ii) Decision C 2005-113 du Ministre de l'Economie, des Finances et de l'Industrie en date du 18 janvier 2006. (iii) Decision N-07012 Azucarera Ebro/Negocio de azucar de DAI. 22 March 2007.

⁶⁰ Questionnaire to Sugar Customers Italy, Phase II, question 15

⁶¹ Questionnaire to Sugar Customers Italy, Phase II, question 13; Questionnaire to Sugar Competitors Italy, Phase II, question 21.

to industrial processors⁶². Moreover, the review of Südzucker's internal documents shows that the price difference between the white sugar sold to industrial processors and the white sugar sold to retailers is not stable [...] ⁶³.

[...]*

- (112) The Commission also notes that the distinction between white sugar for industrial processors and for retailers is also a standard industry practice. [...] ⁶⁴. [...] ⁶⁵. Moreover, the investigation shows that the split between industrial and retail customers is in line with the market segmentation used in the sector, such as the Parties' competitors, the economics studies or the business intelligence services (notably the F.O.Licht's reports⁶⁶).
- (113) For these reasons, the Commission takes the view that, for the assessment of the proposed transaction, the supply of white sugar to industrial processors and the supply of white sugar to retailers constitute separate relevant product markets.
- (114) Concerning a possible further distinction within white sugar sold to retailers, and in particular whether sugar for distributors' private labels constitutes a separate market, the market investigation has not brought to light any substantial elements supporting such a conclusion. On the contrary, it rather supports the notifying party's submission that, in Italy, the retail market is driven by price and availability rather than brand⁶⁷. If end-users may be "brand sensitive" for some other products sold in the retail chains, this seems not to be the case for sugar.
- (115) In addition, the review of Südzucker's internal documents shows that, when assessing the market dynamics in Italy, [...] ⁶⁸.
- (116) Therefore, for the purpose of this Decision, no distinction is made between private and brand label products.

(ii) *Greece*

- (117) EDFM has no sales of sugar in Greece, and thus no sales of white sugar to either industrial processors or to retailers⁶⁹. Therefore, a distinction between white sugar

⁶² Questionnaire to Sugar Competitors Italy, Phase II, question 19-24.

⁶³ See document submitted as "Monthly Report Maxi. 5 October 2011", Annex 8 to Südzucker' reply to the 3rd RFI, Phase I.

⁶⁴ See document submitted as "Monthly Report Maxi. 5 October 2011", Annex 8 to Südzucker' reply to the 3rd RFI, Phase I; the agendas of Südzucker' Group Sales function ("GSF") meetings where its commercial policy is discussed/decided provided as Annex Q3-1 to Südzucker's reply to the 1st RFI Phase I; document submitted as "ED&F Man and SFIR S.p.A. Competitive analysis of supplying sugar to the Italian market".

⁶⁵ See document submitted as "Status Contracts CY 11/12", Annex Q1-c to Südzucker's reply to the 5th RFI, Phase II.

⁶⁶ F.O. Licht is a soft commodity analyst, reporting on a wide range of commodities, including sugar, grain, coffee, tea, molasses, ethanol and biofuels, with reports online and in print.

⁶⁷ Südzucker' reply to the 8th RFI, Phase II.

⁶⁸ See document submitted as "Monthly Report Maxi. 5 October 2011", Annex 8 to Südzucker' reply to the 3rd RFI, Phase I as well as the agendas of Südzucker' Group Sales function ("GSF") meetings where its commercial policy is discussed/decided provided as Annex Q3-1 to Südzucker's reply to the 1st RFI Phase I.

⁶⁹ Südzucker's reply to the 3rd RFI in Phase II, Annex 35-1 Form CO Greece, page 15.

sold to industrial processors or to retailers is immaterial for the assessment of the proposed transaction in Greece. The Commission will thus not consider, in respect of Greece, a further segmentation according to the different types of sugar, or according to customer types.

6.1.2.6. Conclusion

- (118) For the reasons elaborated above, the Commission takes the view that, for the purpose of this Decision, the relevant product markets are the market for the supply of white sugar to industrial processors and the market for the supply of white sugar to retailers with regard to Italy, while with regard to Greece such distinction is immaterial.

6.1.3. RELEVANT GEOGRAPHIC MARKET

(i) Italy

- (119) The relevant geographic market for the assessment of the effects of the proposed transaction on competition in Italy is national.

6.1.3.1. General framework on the definition of the relevant geographic market

- (120) The general framework for the definition of the relevant geographic market is provided for in the Merger Regulation and the Commission notice on the definition of the relevant market for the purposes of Community competition law⁷⁰ (the "Notice on the definition of the relevant market").
- (121) Article 9(7) of the Merger Regulation states that "*[t]he geographical reference market shall consist of the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because, in particular, conditions of competition are appreciably different in those areas. This assessment should take account in particular of the nature and characteristics of the products or services concerned, of the existence of entry barriers or of consumer preferences, of appreciable differences of the undertakings' market shares between the area concerned and neighbouring areas or of substantial price differences*".
- (122) As regards the supply side, paragraph 13 of the Notice on the definition of the relevant market states that "*from an economic point of view, for the definition of the relevant market, demand substitution constitutes the most immediate and effective disciplinary force on the suppliers of a given product, in particular in relation to their pricing decisions*".
- (123) As regards the demand side, paragraph 17 of the Notice on the definition of the relevant market states that "*[t]he question to be answered is whether the parties' customers would switch to [...] suppliers located elsewhere in response to a hypothetical small (in the range 5 % to 10 %) but permanent relative price increase in the [...] areas being considered. If substitution were enough to make the price*

⁷⁰ OJ C 372 of 9.12.1997, p. 5.

increase unprofitable because of the resulting loss of sales, additional [...] areas are included in the relevant market. This would be done until the set of [...] geographical areas is such that small, permanent increases in relative prices would be profitable".

- (124) Also, in accordance with paragraph 8 of the Notice on the definition of the relevant market, the relevant geographic market comprises *"the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those areas"*.
- (125) In order to gain evidence for the purposes of market definition, the Commission takes *"a preliminary view of the scope of the geographic market on the basis of broad indications as to the distribution of market shares between the Parties and their competitors, as well as a preliminary analysis of pricing and price differences at national and EEA level. [...] The initial working hypothesis will [...] be checked against an analysis of demand characteristics (importance of national or local preferences, current patterns of purchases of customers, product differentiation/brands, other) in order to establish whether companies in different areas do indeed constitute a real alternative source of supply for consumers. [...] The Commission will identify possible obstacles and barriers isolating companies located in a given area from the competitive pressure of companies located outside that area, so as to determine the precise degree of market interpenetration at national, European or global level"*.⁷¹
- (126) The Notice on the definition of the relevant market states also that, after the demand side has been analysed, *"If necessary a further check on supply factors will be carried out to ensure that those companies located in differing areas do not face impediments in developing their sales on competitive terms throughout the whole geographic market. This analysis will include an examination of requirements for a local presence in order to sell in that area the conditions of access to distribution channels, costs associated with setting up a distribution network [...]"*⁷².
- (127) Concerning basic demand characteristics, paragraph 46 of the Notice on the definition of the relevant market states that *"[t]he nature of demand for the relevant product may in itself determine the scope of the geographical market. Factors such as national preferences or preferences for national brands, language, culture and life style, and the need for a local presence have a strong potential to limit the geographic scope of competition"*, while paragraph 48 states that *"an examination of the customers' current geographic pattern of purchases provides useful evidence as to the possible scope of the geographic market"*.
- (128) In addition, *"[t]rade flows, and above all, the rationale behind trade flows provide useful insights and information for the purpose of establishing the scope of the geographic market but are not in themselves conclusive"*⁷³.

⁷¹ Notice on the definition of the relevant market, paragraphs 28, 29 and 30.

⁷² Notice on the definition of the relevant market, paragraph 30.

⁷³ Notice on the definition of the relevant market, paragraph 49.

- (129) Moreover, according to paragraph 50 of the Notice on the definition of the relevant market, *"The absence of trans-border purchases or trade flows, for instance, does not necessarily mean that the market is at most national in scope. Still, barriers isolating the national market have to be identified before it is concluded that the relevant geographic market in such a case is national. Perhaps the clearest obstacle for a customer to divert its orders to other areas is the impact of transport costs and transport restrictions arising from legislation or from the nature of the relevant products"*. The same paragraph also states that: *"access to distribution in a given area, regulatory barriers still existing in certain sectors, quotas and custom tariffs might also constitute barriers isolating a geographic area from the competitive pressure of companies located outside that area"*.
- (130) Paragraph 52 clarifies and concludes that *"[t]he paragraphs above describe the different factors which might be relevant to define markets. This does not imply that in each individual case it will be necessary to obtain evidence and assess each of these factors. Often in practice the evidence provided by a subset of these factors will be sufficient to reach a conclusion, as shown in the past decisional practice of the Commission"*.

6.1.3.2. Geographic definition of the market for the supply of white sugar in previous cases

- (131) In a number of previous decisions⁷⁴, the Commission considered that the relevant geographic market for the supply of sugar was national in scope or even sub-national, at least for Germany.
- (132) In *Südzucker / Saint Louis Sucre*⁷⁵ the Parties claimed that the market for sugar in general should be Union-wide. However, the Commission concluded in line with previous decisions⁷⁶ on a market that is even smaller than national in Germany. The main reason for this was the location of the production sites in Germany. Whereas, for example, in France the production sites were located in the northern and north-eastern parts of the country, the production sites of the different competitors in Germany were located in different parts of Germany. Due to transport costs, longer distances between customers and suppliers played an important role for the final price of the sugar. This resulted in Südzucker having large market shares (over 80 %) in the campaign year 1999/2000, as in the previous years, in Bavaria, Baden-Württemberg, Saarland, Hessen and Rheinland-Pfalz, whereas Nordzucker had comparable market shares in Schleswig-Holstein, Hamburg, Bremen and Niedersachsen and Pfeifer & Langen had comparable market shares in Nordrhein-Westfalen. The market shares were comparable only in Eastern Germany. The Commission also found that this effect was strengthened on the German market due to different market acting strategies of the producers. Most of the customers had confirmed during the market investigation that proximity to the customer is a major factor affecting customer choice. Sugar is only supplied for "free-house-prices" in a certain radius around the production site. Longer distances are not be supplied at all or only for much higher costs.

⁷⁴ Commission Decision 2003/259/EC in Case No COMP/M.2530 - Südzucker / Saint Louis Sucre and Commission Decision of 30 July 1991 in Case No IV.M.062 - Eridania / ISI 30 July 1991.

⁷⁵ Commission Decision 2003/259/EC in Case No COMP/M.2530 - Südzucker / Saint Louis Sucre.

⁷⁶ Commission Decision 1999/210/EC in Case No IV/F-3/33.708 British Sugar plc, paragraph 65; Commission Decision 97/624/EC in Case IV/F-3/M. 34.621 Irish Sugar, paragraph 98.

- (133) In the most recent decision after the 2006 sugar reform, *ABF/Azucarera*⁷⁷, the Parties argued that the relevant geographic market was, at the very least, wider than national, and is increasingly becoming EEA-wide in scope, because the dynamics of competition in the supply of sugar in the EEA have changed following reforms to the Sugar Regime and the anticipated removal of quotas and tariffs on imports from ACP countries and LDCs, together with the elimination of restitution payments for exports to third countries. They submitted that the reforms to the sugar regime have led and will continue to lead, to an intensification of intra-EEA trade with sugar producers increasingly selling across national borders and a significant increase in imports from third countries.
- (134) The Commission reported that on the basis of the market investigation most customers were still sourcing their supply from sugar producers located close-by and only within deficit areas⁷⁸, cross-border sales could be observed. While the Commission ultimately left the market definition open, it also stated expressly that *the results of the market investigation have generally not confirmed this view*⁷⁹, i.e. that the reforms of the sugar regime had led to wider than national markets.
- (135) Some NCAs, including Bundeskartellamt⁸⁰ and the Autorità Garante della Concorrenza e del Mercato⁸¹, have come to the conclusion that the geographic market is national, whilst other NCAs have left the final definition open without an own assessment⁸². The Dirección General de Defensa de la Competencia, although ultimately leaving open the definition of the relevant geographic market, conducted its assessment under different alternative geographic delineations which included national markets as well as the (larger than national) regional market, consisting of Iberia together with France⁸³.
- (136) In Case C5151 – SECI – CO.PRO.B. – Finbieticola / Eridania, the Italian Competition Authority (ICA) considered the geographic market for the production and supply of sugar to be national in scope with respect to Italy, regardless of imports as high as 26% in 2001. The decision was however partially annulled by the Italian High Administrative Court ("Consiglio di Stato") insofar as the commitments attached to the approval decision were concerned.
- (137) In 2005, the ICA readopted the decision in Case C5151. The 2005 decision does not include a separate relevant market definition. However, the ICA concluded that the competitive conditions in the market had not changed since 2001. In particular, the reasons for a very significant increase in the imports between 2001 and 2005 (up to

⁷⁷ Commission Decision of 30 March 2009 in Case No COMP/M.5449 - ABF/Azucarera. This case mainly dealt with the sugar supply in Spain.

⁷⁸ Paragraph 43 of the ABF/Azucarera decision refers to Spain and Italy as "deficit areas", although Italy was not specifically considered in that case.

⁷⁹ Commission Decision of 30 March 2009 in Case No COMP/M.5449 - ABF/Azucarera, paragraph 43.

⁸⁰ Bundeskartellamt, Beschluss *Nordzucker/Danisco* of 17 February 2009.

⁸¹ Provvedimento n. 11040 (C5151) - SOCIETÀ ESERCIZI COMMERCIALI INDUSTRIALI-S.E.C.I.-CO.PRO.B.- FINBIETICOLA/ERIDANIA, de 1 de agosto de 2002.

⁸² The United Kingdom Office of Fair Trading has stated that the regulatory changes affecting the EU sugar market may cause imports to be a stronger competitive constraint in the future (Acquisition of Illovo Sugar Limited by ABF Overseas Limited, OFT decision of 31 July 2006).

⁸³ Case N 07012 Azucarera Ebro/Negocio de azucar de DAI of 22 March 2007.

50%) were not structural in nature and appeared to depend mainly on isolated events such as a crop failure in Italy.

- (138) Further to a request by the parties to review the commitments because of the new competitive conditions in the market, a new decision in the same case was adopted in 2006. In that decision, the ICA did not explicitly depart from its relevant geographic market definition of the sugar market as national. The ICA considered, however, that the change in the European regulation would have been likely to make structural the increase of imports in Italy already noted in the 2005 decision. As a result, the constraints on the merger entity had been modified and the commitments were no longer necessary. The ICA therefore decided to revoke the remedies attached to its conditional decisions of 2002 and 2005.
- (139) Concerning the case *Nordzucker/Danisco*,⁸⁴ which was decided almost four years after the sugar reform, the German Bundeskartellamt concluded that markets were national pointing to continued price differences between Member States. The Bundeskartellamt regarded the German market as national, because (i) there were only small chances of accessing the market, (ii) transport costs were relatively high, (iii) imports were small, (iv) in order to compete in Germany a strong local presence was necessary due to the fact that customers did not have their own storage capacities but were dependent on just-in-time deliveries, (v) there were different national market conditions regarding prices and the market structure on the supply-side in different Member States.
- (140) The Bundeskartellamt stressed that potential importers need to have a strong national presence, including in particular important storage facilities, since industrial food processors require security of supply and flexible adaptation of sugar supplies according to their factories' needs.

6.1.3.3. View of the notifying party

- (141) The notifying party puts forward that the relevant geographic market for the supply of white sugar is at least larger than national if not EEA-wide, since the Commission's decisional practice indicating national geographic markets should be re-assessed, in the light of the intensified intra-Union trade post-2006. In particular, the notifying party points to the quota renuncements that transformed the Union into a net importer of sugar and the abolishment of quantitative restrictions on LDC imports as of 1 October 2009.
- (142) More specifically, the notifying party argues that (i) already today, 50% of the Italian demand is satisfied through imports, and (ii) the fact that customers mention a practice of nationwide contracting and do generally not source directly from abroad does not say anything with respect to the trade flows in the sugar industry.
- (143) Therefore, the notifying party is of the opinion that the relevant geographic market should be EEA-wide. In this regard, the notifying party has submitted that the European sugar market experiences an intensification of the sugar trade flows as (i) regional consumer preferences disappear more and more, (ii) contracts are increasingly based on international tenders for key accounts, since retailers and other

⁸⁴ Bundeskartellamt, Beschluss *Nordzucker/Danisco* of 17 February 2009.

sugar customers increasingly change to European sourcing strategies, and (iii) the new sugar market regime reduced the entry barriers. Concerning in particular the supply of white sugar in Italy, the notifying party points to the fact that the white sugar sold in Italy originates from Austria, Germany, France, but also from the United Kingdom, Spain, the Netherlands, Poland, Serbia, Croatia, ACP/LDC-countries and other third countries.

- (144) Therefore, the notifying party considers that for the assessment of the proposed transaction with respect to the supply of white sugar in Italy the relevant geographic market should include at least southern Europe, including southern Germany and southern France⁸⁵.

6.1.3.4. Assessment

- (145) Despite the sugar reform of 2006 and subsequent market developments in Italy and the EEA, the relevant geographic market for the supply of white sugar to industrial processors in Italy remains national essentially for the following reasons analysed in detail below:

- (1) On the demand side, (i) industrial customers in the vast majority of cases buy from suppliers based in Italy, have national contracts and do not source directly from abroad; (ii) the few large players which do buy transnationally from transeuropean players have to pay "Italian" prices for their purchases; (iii) the vast majority of industrial customers buy nationally, because security and regularity of supply and thus closeness to storage facilities are crucial factors for industrial processors and retailers; and (iv) while customers multisource they rarely switch their main supplier. These demand-side characteristics mean that suppliers who want to compete successfully in the overall market for industrial customers in Italy need to have access to an established customer base, possess a developed distribution and logistics network and have a good knowledge of local and national market conditions, as analysed below under point (2).
- (2) On the supply-side, (i) producers of beet sugar in Italy are constrained by non-tradable fixed production quotas which are set on a national basis; (ii) the large quantity of imports in Italy is the direct consequence of the quota system which limits beet sugar production in Italy and does not as such indicate competitive pressure exercised upon Italian producers by foreign players; (iii) foreign producers operate in Italy mainly through joint ventures with well-established Italian players; this tends to show that the Italian market has characteristics distinct from other markets in Europe, otherwise the big European producers would simply sell directly into Italy and not engage in joint venture agreements which force them to share profits; (iv) in recent years Südzucker's strategy in Italy has been to compete with low prices and thus is markedly different from its strategy in Germany or France where it maintained high prices; in a market wider than national transnational arbitrage would have defeated such separate strategies; (v) internal documents of the Parties indicate national marketing strategies per Member State; (vi) internal documents of the Parties indicate

⁸⁵ Annex 16-1 of Südzucker's reply to the 3rd RFI in Phase II (Form CO Italy, page 10).

sales programs and price-setting at a national level; (vii) market boundaries along national borders are both reflected and reinforced by non-compete clauses based on Italy as reference territory in joint-venture agreements; and (viii) a submission by the Bundeskartellamt also points towards national market definition for Germany, with arguments which are by analogy relevant for the Italian market and coherent with a national definition of the market.

- (3) Price data collected by the Directorate General for Agriculture of the Commission ('DG AGRI') show that (i) during the last years significant price differences between Italy and Germany/France have not been arbitrated away as would be expected to happen in the same geographic market, (ii) Italian market price changes co-move less strongly with its neighbouring and exporting Member States than these neighbouring Member States' price changes co-move amongst each other and (iii) in recent years where Europe experienced scarcity of sugar supply the price differences between Member States actually increased which is incompatible with the claim that the market is increasingly EEA-wide.
- (4) Persistent significant divergences in market shares from one Member State to another, even when those Member States are neighbouring, point towards the continued existence of national markets, since market share differences are not competed away.

(1) DEMAND SIDE CHARACTERISTICS

- (146) According to paragraph 13 of the Notice on the definition of the relevant market, *"from an economic point of view, for the definition of the relevant market, demand substitution constitutes the most immediate and effective disciplinary force on the suppliers of a given product, in particular in relation to their pricing decision"*. More specifically, the Commission will conduct an analysis of the demand characteristics, such as the importance of national or local preferences, current pattern of purchase of customers (paragraph 29 of the Notice).
 - (i) Industrial and retail customers in the vast majority of cases buy from suppliers based in Italy, have national contracts and do not source directly from abroad
- (147) According to paragraph 48 of the Notice on the definition of the relevant market, *"an examination of the customers' current geographic pattern of purchases provides useful evidence as to the possible scope of the geographic market"*.
- (148) In the case at hand, the main part of commercial relationships between customers and suppliers is national. The market investigation revealed that most of the customers purchase on a national level and do not import into Italy (only 4 out of 35 customers buy from abroad). Even some large customers [...] have only national wide contracts. [A large customer]* argued that, because of national contracts, an Italian producer delivers only to Italy⁸⁶ indicating that Italian customers cannot source

⁸⁶ Reply by [...] (replied to question 28) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

directly from producers active outside that Member State. Also, [a large customer]*⁸⁷ explains that their contracts are exclusively national.

(ii) The few big players which do buy transnationally have to pay "Italian" prices for their purchases

(149) Only a few very large customers [...] indicate that they have both EEA and national wide contracts while another important customer, [a large customer]* underlines that negotiations take place regionally (cross-border) and the contracts are signed locally⁸⁸. However, even in the few cases where the overall negotiations take place on a wider than national level (regional or EEA), the majority of customers replied that prices are set for each Member State separately, according to the market situation in the Member State of supply. With respect to Italy, the market participants explained that the scarcity of sugar is the most important factor determining the Italian prices they have to pay⁸⁹.

(150) On the basis of the above, it is considered that the market investigation has shown that even in the few cases where contracts were negotiated centrally for several countries, the prices and market characteristics differed between Italy and other countries. Transnational purchases are therefore not able to exercise a meaningful constraint on pricing in Italy.

(151) The existence of national prices in Italy different from prices in other Member States is evidenced in more detail by the analysis in recitals (215) to (250) of this Decision.

(iii) Industrial and retail customers buy nationally because security and regularity of supply and thus closeness to storage facilities are crucial factors for industrial processors and retailers

(152) In the customers' view⁹⁰, the availability of sugar is fundamental for their business. All customers questioned during the second phase market investigation considered that security of supply is a determining factor for their activities with regard to their purchases of sugar in Italy, both in terms of quantity and quality. Apart from other disadvantages of sourcing abroad - such as high transport costs, longer delivery period resulting from long-distance transportation - the need to maximise security of supply and minimise the risk of disruption are essential for their choices regarding the sourcing of sugar. Sugar is an essential product for the food and beverage industries (e.g. producers of biscuits, ice-cream, sweets, soft drinks) as well as for the retailers which cannot be substituted by other products.

(153) This is not contested by the notifying party which agrees that security of supply is one of the main characteristics that industrial customers (in the food and beverage industry) and retailers are seeking from their suppliers. The notifying party has further explained that its own strategy for ensuring security of supply for its customers in sugar deficit countries is based on two pillars: (i) sufficient storage

⁸⁷ Reply by [...] (replied to question 28) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁸⁸ Questionnaire to sugar customers in Italy – Phase II, question 28.

⁸⁹ See replies to the Follow-up questions to Sugar Customers sent on 17 January 2012.

⁹⁰ Questionnaire to sugar customers in Italy – Phase II.

facilities close to the customers and (ii) sound management decisions about allocation of sales to a specific destination (including stock levels required)⁹¹.

- (154) In order to ensure security of their sugar supplies, customers generally conclude long-term (annual and/or 3-8 months) contracts with suppliers⁹². Furthermore, the vast majority of those contracts are concluded under "Italian" prices and conditions.
- (155) The contractual and established commercial relationships in the different markets also do not allow producers in other Member States to effectively constrain sugar prices in Italy. For example, even the notifying party suggests that there is "*no incentive and/or possibility for Südzucker to redirect sugar supply that is originally destined for other markets to deficit countries such as Italy unless prices in Italy would exceed considerably the price levels in other markets thereby covering the extra logistics costs [...]**⁹³. [...]*⁹⁴.
- (156) Customers also acknowledge the importance of regular deliveries, which may even have to take place on a daily basis. This is even more true for small customers who - in contrast to the notifying party - lack their own storage facilities and are therefore dependent on in time supply of relatively small quantities. Therefore, customers seek suppliers which control storage and distribution sites geographically close to their own facilities in order to minimize the risk of supply disruptions and delays.
- (iv) Low price elasticity of demand confirms dependence of customers on suppliers
- (157) The importance of regular and uninterrupted sugar supplies for industrial processors is further confirmed by the low price elasticity of demand of industrial customers. In an internal document EDFM describes the sugar consumption within the Union as relatively static and thus independent of price fluctuations. In the same document it also states that both the industrial and retail demand is income and price inelastic. "*The total EU-27 sugar consumption is relatively static at around 16.5 million tonnes, and moreover, sugar demand, both industrial demand and retail demand, in the EU is markedly income and price inelastic*"⁹⁵.
- (158) The statement suggests that customers will buy similar quantities of sugar independently of price levels and thus also when prices are very high. It also suggests that customers have limited leverage to negotiate prices below market price levels and that they cannot choose to switch to alternative suppliers.
- (159) In view of the above elements, combined with the customers' need for security of supply, customers have no leverage to deviate from Italian contracts. This element also suggests that there is a national market for Italy.

⁹¹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 58, sent by e-mail of 1 December 2011 (19:33).

⁹² Questionnaire to sugar customers in Italy – Phase II.

⁹³ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 15, sent by e-mail of 1 December 2011 (19:33).

⁹⁴ EDFM's reply to the 6th request for information of 11 October 2011, internal document on "Italian Market" (undated), slide 12.

⁹⁵ European Sugar Logistics Study prepared for the Ethiopian Sugar Development Agency from 16 February 2010, provided by ED&F Man, p.17.

- (v) Many customers who view the market as wider than national base their opinion on the fact that Italy imports sugar.
- (160) In its response to the Statement of Objections the notifying party stated that "*[a]ll competitors and 27 out of 47 customers stated in response to the market testing that they view the relevant geographic market is wider than Italy*".
- (161) A more careful reading of the replies to the market investigation shows however a different and much more nuanced picture.
- (162) With regard to competitors, only 5 out of 10 considered that the market was not confined to Italy but was wider. By contrast 4 out of 10 competitors considered that the relevant geographic market for the supply of sugar was still national while one of the competitors did not answer this question.
- (163) Concerning the customers, out of a total of 50 customers who replied, 25 consider that the market is wider than national, while 25 customers do not consider the market to be wider than national.
- (164) In addition, out of 25 customers considering the market wider than national, 18 justified their answer by pointing towards the large import quantities entering into Italy due to the deficit nature of the Italian sugar market.
- (165) The Notice on the definition of relevant market (paragraph 49) emphasizes in this respect that "*trade flows, and above all, the rationale behind trade flows provide useful insights and information for the purpose of establishing the scope of the geographic market but are not in themselves conclusive*".
- (166) In the case at hand, these large quantities of sugar imports are the direct result of market regulation, that is to say the radical reduction of Italian production quotas after the sugar reform of 2006, which limits Italian internal production and thus has created an important but artificial gap between Italian supply and consumption. Therefore, large quantities of imports of sugar into Italy do not as such illustrate competitive pressure exercised upon Italian producers by foreign players and do not evidence a market wider than the Italian market. The fact that imports result from regulation means that they do not come into the market as a response to relatively higher prices but to an artificially created gap.
- (167) Thus, the 18 customers, concluding that the market was wider than national on the basis of significant imports, did not take into account that the rationale for the imports was not well-functioning cross-border competition, but an output restriction in Italy imposed by regulation.
- (168) Of the remaining 7 customers who stated that the market is wider than national, 6 stated that they purchase sugar exclusively on a national basis and do not purchase sugar directly from abroad.
- (169) Accordingly, (i) around half of the competitors and customers consider that the market is national and (ii) a significant proportion of the other half's replies have to be read bearing in mind that they did not take into account the regulatory rationale of the large amounts of imports and/or did not themselves engage in any cross border sales.

- (vi) Customers have not switched to non-Italian suppliers in the recent past despite significant price increases
- (170) Even if a majority of contacted customers stated that in the case of a price increase of 5% to 10%, they would consider buying sugar directly from abroad, such replies need to be read in the light of the replies which the same customers gave to other questions and in particular those concerning their actual market behaviour.
- (171) Only about 4 of 35 end customers which replied to the questionnaire seem to buy directly from abroad⁹⁶. Therefore, the prevailing pattern for end-customers is to purchase through national (Italian) sales offices, thus under Italian prices and conditions.
- (172) Those 4 exceptional customers are particularly large and sophisticated multinationals [...] and cannot serve as a proxy for the average industrial sugar customer in Italy.
- (173) In addition, even within that group of 4 customers, at least 2 of them stated that for such purchases prices were different between Member States and that such price differences apply in particular for Italy. Therefore, even the sugar supply contracts of those 2 customers reflect the different pricing patterns in the Member States, which points towards national markets.
- (174) In addition, as stated in paragraph 47 of the Notice on the definition of the relevant market, where appropriate the views of customers on the boundaries of the geographic market, as well as most of the factual information it requires to reach a conclusion on the scope of the market, have to be sufficiently backed by factual evidence. Furthermore, as evidenced by paragraph 38 of the Notice on the definition of the relevant market "*in certain cases, it is possible to analyse evidence relating to recent past events or shocks in the market that offer actual examples of substitution between two products (...) if there have been changes in relative prices in the past (all else being equal), the reactions in terms of quantities demanded will be determinant in establishing substitutability*".
- (175) Therefore, taking this into account, the actual behaviour of the customers in the past under comparable market conditions as outlined in the questionnaire⁹⁷ becomes as important as their opinion as to how they would react under the outlined conditions. The conditions outlined in the questionnaire were a significant price increase in Italy. While this very same situation actually took place in the last years in Italy, a vast majority of the customers, as indicated above, did not actually start sourcing sugar from abroad.
- (176) Furthermore, according to all customers, responding to the questionnaire⁹⁸, in the last five years and despite recent significant price increases in Italy which were much

⁹⁶ Questionnaire to sugar customers in Italy – Phase II, question 22. Three end-customers were not included for calculating the previous percentage of 15% referred to in the Statement of Objections. The total responding customers are in fact 35, the 3 additional ones not sourcing from abroad.

⁹⁷ Questionnaire to sugar customers in Italy – Phase II.

⁹⁸ Questionnaire to sugar customers in Italy – Phase II.

higher than 5% to 10 %, no customer responded by purchasing sugar directly from abroad in the last 5 years⁹⁹.

- (177) The above considerations support the conclusion that (i) the prices are set at the Member State level for the Italian market, and (ii) customers cannot/do not source directly from abroad even when they are faced with significant price rises.

(2) SUPPLY SIDE PERSPECTIVE

(i) Production quotas are still national and non-tradable

- (178) In its reply to the Statement of Objections, the notifying party has argued that the Commission should not rely on its previous decision-practice due to the fact that all previous decisions deal with the situation prior to the sugar reform or still influenced by the previous regime¹⁰⁰. In support of its argument, Südzucker points to paragraph 32 of the Notice on the definition of the relevant market, which states that "*the Commission also takes into account the continuing process of market integration*" when defining geographic markets.
- (179) The continuing process of market integration has been taken into account in this Decision. Nevertheless, paragraph 32 of the Notice on the definition of the relevant market does not necessarily mean that the Commission will define markets as Union-wide or EEA-wide for each product which is covered by internal market legislation. The Commission analyses, on the basis of the facts in every individual case, to what extent the process of market integration has actually led to Union-wide or larger than national markets.
- (180) As regards the sugar regime following the 2006 reform, the Court of Auditors in its 2010 report¹⁰¹ found that the currently applicable sugar regime had similar consequences as the regime in force before 2006, namely limited possibilities of transferability of quotas and rigidity of production capacity. The Court of Auditors stressed that: "*The Court's previous special report on the sugar CMO) drew attention to the rigidities linked to the quotas system and concluded that 'national quotas have prevented production moving to the most efficient areas', 'normal competitive forces do not operate and in several cases sugar companies have been fined for abuses of competition' and stated that the existence of barriers to entry for new sugar beet growers warranted consideration by the Commission. In this regard a 2004 Commission Communication initially proposed a sugar sector reform based on a uniform cut in quotas and intended to foster quotas transferability between producers in the EU. However, this proposal was not adopted because a majority of Member States opposed the idea of intra-Community quota transfers. In terms of sugar industry processing efficiency, the maintenance of rigidities and constraints incorporated into the current quota system, i.e. such as the establishment of quantitative quotas per individual grower in certain Member States, the absence of tradability of quotas and the limited possibilities for their transferability, results in undue rigidity of production capacity and reduces scope for both growers and*

⁹⁹ Questionnaire to sugar customers in Italy – Phase II, question 38(e).

¹⁰⁰ Südzucker's reply to the Statement of Objections, para. 32.

¹⁰¹ Special report n°6 from the European Court of Auditors – "Has the reform of the sugar market achieved its main objectives?" – 2010.

producers to increase efficiency. The audit confirmed that in some of the audited Member States, quota restrictions hamper the entry of possible new growers and delivery rights of existing growers may not be changed without their consent. This entails significant constraints in the sugar production market."

(181) In this context, the 2001 Commission reasoning in *Südzucker/Saint Louis Sucre*¹⁰² stating that *"the existence of an EU-wide regulation for a certain economic branch would not necessarily lead to an EU-wide market but rather, on the contrary, prevent an EU-wide market due to national quota"* is still valid under the current regime.

(182) Therefore, the reform of 2006 did not change one of the main rigidifying factors why sugar markets are still national, namely the attribution of quotas on a national basis to established national players without possibility to trade quotas.

(ii) Imports do not imply a wider than national market

(183) According to paragraph 49 of the Notice on the definition of the relevant market *"trade flows, and above all, the rationale behind trade flows provide useful insights and information for the purpose of establishing the scope of the geographic market but are not in themselves conclusive"*.

(184) In addition, paragraph 50 of the Notice on the definition of the relevant market states: *"The absence of trans-border purchases or trade flows, for instance, does not necessarily mean that the market is at most national in scope. Still, barriers isolating the national market have to [be] identified before it is concluded that the relevant geographic market in such a case is national [...]** access to distribution in a given area, regulatory barriers still existing in certain sectors, quotas and custom tariffs might also constitute barriers isolating a geographic area from the competitive pressure of companies located outside that area".

(185) It follows that although trade flows often provide useful insights and information for the purpose of establishing the scope of the geographic market, under paragraph 49 of the Notice on the definition of the relevant market, they are not in themselves conclusive and it is necessary to look carefully at their *rationale*, as well as at other elements.

(186) As discussed above, in the present case the existence of large imports as such does not indicate a larger than national market, because the need for such a large amount of imports is a direct consequence of the significant reduction of Italian production quotas after the sugar reform of 2006, which limits beet sugar output in Italy and thus has created an important gap between supply and demand in Italy which can only be filled by imports.

(187) Moreover, the nature of the imports in question needs to be taken into account¹⁰³. The market investigation has shown that the vast majority of these imports are intra company supplies by the big northern European players [...]*

to their Italian sales joint ventures or organisation¹⁰⁴. By contrast there seems to be hardly any direct

¹⁰² Case COMP/M. 2530 – *Südzucker / Saint Louis Sucre* of 20 December 2001, para. 34.

¹⁰³ See paragraph 49 of the Notice on the Definition of the Relevant Market.

¹⁰⁴ Questionnaire to sugar competitors – Phase I & Phase II.

imports from players active outside Italy directly to customers in Italy. Such intra company imports do not exercise any direct competitive pressure on the big suppliers active in Italy.

- (188) Thirdly, it is important to bear in mind that the prevailing pattern for large scale sugar operations of northern European sugar producers in Italy remains that of a joint venture between an Italian and a foreign player (e.g. Südzucker with MAXI, Pfeiffer & Langen with COPROB, Cristal Union with Eridania and in a certain way EDFM with SFIR). This shows first of all that Italian producers limited in their output by the quota system need to co-operate with foreign producers in order be able to supply the necessary quantities in the Italian market. Furthermore and more importantly, it also shows the lack of direct competitive pressure exercised by sugar producers with no established presence in Italy on prices in Italy. If it were easy to react to high prices in Italy with direct imports, then foreign producers would have no reason to engage into joint ventures with Italian players and share profits with the Italian joint venture partner. In fact, the profit-sharing of the joint venture structures is the "price" that foreign players have to pay because it is not easy for them to establish themselves during a short period of time as independent competitors in Italy on their own.
- (189) Fourthly, while Tereos is [Description of Tereos' market strategy]*, its case also shows that there is no direct pressure from imports leading to price arbitrage between the rest of Europe and Italy. Tereos entered the Italian market in 2005/2006, at a moment when the sugar reform led to a particularly large sugar deficit in Italy and other foreign players were only starting to enter the market through joint ventures with Italian players. [...]*. Moreover, Tereos [Description of Tereos' market strategy]*.
- (190) In line with the above [a large Italian sugar producer]* describes Tereos as a player on the Italian white sugar market with very good access to input, no infrastructure in Italy, very light national sales office, non-existent regional sales office, no partnership on the Italian white sugar market¹⁰⁵, poor customer relationship¹⁰⁶ and in addition without ability to expand its sugar output¹⁰⁷.
- (191) In view of the above, the quantities of the imports of white sugar to Italy by other Member States do not point towards a wider than national geographic market. Rather, the nature of those imports actually militates in favour of a national definition of the market.
- (iii) Foreign producers operate in Italy through joint ventures with Italian players
- (192) The Notice on the definition of the relevant market states that the Commission analysis on supply factors will include "*an examination of requirements for a local*

¹⁰⁵ Reply by [...]* ([...]* (reply to question 58) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

¹⁰⁶ Reply by [...]* ([...]* (reply to question 69) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

¹⁰⁷ Reply by [...]* ([...]* (reply to question 59) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

*presence in order to sell in that area the conditions of access to distribution channels, costs associated with setting up a distribution network [...]**¹⁰⁸.

- (193) The need for security of supply pushes Italian customers towards a strong preference for local suppliers. For example, internal documents of Südzucker show that "*Italian customers appreciate national partners more than customers of other countries*"¹⁰⁹. This leads to the necessity for foreign suppliers to establish partnerships with local players in Italy.
- (194) The notifying party itself argued that prior to its acquisition of MAXI, [...]*. Those statements stress the necessity for a foreign producer to establish a partnership with a player already active in Italy in order to be an effective competitor.
- (195) The other non-Italian players also had to team up with well-known Italian players in order to enter the Italian market in a large-scale:
- (a) the German sugar manufacturer Pfeifer & Langen has acquired 49.9% of the sales subsidiary of COPROB/Italia Zuccheri;
 - (b) the British sugar manufacturer Tate & Lyle had established a joint-venture with Eridania for the marketing and sales of all their sugar products. In the course of 2011, Tate & Lyle left the Italian market, [...]*
 - (c) subsequently the French sugar manufacturer Cristal Union via CristalCo had to step in and replaced Tate & Lyle in the joint-venture with Eridania; and
 - (d) EDFM has built a new refinery through a joint-venture with SFIR in the South of Italy (Brindisi - SRB).
- (196) Although the French sugar manufacturer Tereos is [Description of Tereos' market strategy]*, this does not break the pattern of joint-venture entry, because: (i) Tereos' entry took place in 2006, thus very early in the reform at a period when producers still disposed significant volumes of sugar; and (ii) Tereos' market share in Italy [...]* over the past years and is [...]* that of other foreign players, such as Südzucker who teamed up with MAXI the same year and increased significantly its presence over the last 5 years.
- (197) Therefore the prevailing pattern for foreign producers' operations in Italy is through joint ventures with Italian players or at the very least through a national sales organisation.
- (iv) Südzucker's pricing strategy [...]*
- (198) [...]*
- (199) During the oral hearing the Parties submitted a graph¹¹⁰, which was meant to show a convergence of prices between Germany, France and Italy. However, first of all, the prices shown are Südzucker prices only and it is not clear whether they correspond to

¹⁰⁸ Commission Notice on the definition of the relevant market, paragraph 30.

¹⁰⁹ Annex 23 of Südzucker's answer to the 2nd RFI in Phase I, at page 13.

¹¹⁰ Slide 13 of Südzucker's presentation in the hearing of 5 March 2012.

market prices. Secondly, the alleged convergence in 2011/2012 appears to be mainly driven by the forecasted data inserted for 2011/2012 on the basis of 'contracted prices' instead of 'invoiced prices'¹¹¹. The Commission is of the view that the data from DG AGRI used in the Commission's analysis below offers a more reliable view on price differences between Member States.

- (200) However, even assuming that some conclusion can be drawn from the price figures given for the years 2006 to 2011¹¹², those price figures would actually confirm significant price differences between Member States which cannot be explained by transport costs. According to the graph in question from campaign year 2006/2007 to 2008/2009, price differences between [...] are in the range of EUR [...] and between [...] in the range of EUR [...]. In campaign year 2009/2010, price differences between [...] are in the range of EUR [...] and between [...] in the range of EUR [...]. Even in campaign year 2010/2011, price differences between [...] are in the range of EUR [...].
- (201) These price differences are higher than the transport costs between those Member States. If those Member States belonged to the same geographic market, these price differences would not exist since arbitrage would equalise prices through sales of low-priced Italian white sugar to high-priced Germany and France.
- (202) Furthermore, statements by competitors indicate that the conditions of competition are substantially different in the (more competitive) Italian market than in Germany or France. For example, [a large sugar producer]* stated that *"MAXI, Südzucker's distributor in Italy, may have managed to deter potential entrants by significantly reducing its prices during the last 3 to 4 years in Italy. It appears that Südzucker via MAXI were selling at lower prices in Italy than in surplus markets in the last few years. Normally, the market price in Italy should reflect the high transport costs involved when sugar is imported into the Italian market from France, Germany and the United Kingdom. However, MAXI's prices in Italy during the last couple of years were lower than the ones in the abovementioned countries."*¹¹³. In addition, [a large Italian sugar producer]* stated: *"Tate & Lyle had not enough raw sugar to supply their refineries. Nordzucker concentrated its commercial action in North of Europe, given the fixed quantity at their disposal and the low level of pricing in Italy not sufficient to cover logistic costs to arrive in Italy. However, we can assume that the dumping were made in that period by Südzucker was aimed to discourage the competitors to play in Italy"*¹¹⁴.

(v) Internal documents of the Parties indicate national strategies

- (203) Internal documents of the Parties show that they develop their strategies on [...].
- (204) Südzucker's internal documents show that it monitors the production and prices for sugar [...]. For example, Südzucker's presentation for the acquisition of MAXI

¹¹¹ See recitals (246) to (249) of this Decision which explain in more detail why the data are not reliable.

¹¹² Slide 13 of Südzucker's presentation in the hearing of 5 March 2012.

¹¹³ Minutes of the conference call with [...] on 30 November 2011.

¹¹⁴ [...] reply to question 60 of the Questionnaire to sugar producers/suppliers in Italy.

performs an analysis of the conditions of competition [...]*, while it also concludes that [...]***¹¹⁵. [...]***¹¹⁶.

(205) With respect to EDFM, the preparatory documents for the construction of the Brindisi refinery in 2009 also analyse extensively [...]***¹¹⁷.

(vi) Internal documents of the Parties indicate sales, marketing and price-setting at a national level

(206) A review of internal documents submitted by the notifying party shows that it [...]*** that sales, marketing and price-setting are elaborated¹¹⁸. [...]***¹¹⁹.

(207) Furthermore, Südzucker's "planning tool"¹²⁰ makes reference to [...]*** programs with regard to [...]***. Therefore, the "planning tool" shows that the notifying party establishes strategies for [...]***.

(208) The monthly reports of MAXI submitted by Südzucker also report prices [...]***¹²¹.

(209) As to the Brindisi refinery, [...]*** analysis is also conducted [...]***¹²².

(vii) National boundaries are reflected and reinforced by nationwide non-compete clauses in joint-venture agreements

(210) The Italian white sugar market is widely characterised by the existence of nationwide non-compete clauses in the joint-venture agreements for the supply of white sugar.

(211) [...]***¹²³. [...]***¹²⁴.

(212) Those [...]*** clauses both reflect and reinforce the segmentation of sugar supply and demand in Italy along national boundaries because [...]***.

(viii) The findings of the Bundeskartellamt also point towards a national market definition

(213) The Bundeskartellamt in a letter¹²⁵ to the Commission makes reference to the behaviour and market strategy of Südzucker in Germany indicating the existence of a national market with regard at least to Germany.

¹¹⁵ Annex 23 of Südzucker's answer to the 2nd RFI in Phase I, at page 13.

¹¹⁶ Annex 23 of Südzucker's answer to the 2nd RFI in Phase I, at page 13.

¹¹⁷ "Information Memorandum", "Project Overview" and "Competitive Analysis of supplying Sugar to the Italian Market" submitted respectively as Annexes 4, 5.a and 5.b of EDFM's answer to the 2nd RFI in Phase I.

¹¹⁸ See document submitted as "Sales policy SZ Group 2011/2012", Annex Q1c to Südzucker's reply to the 5th RFI Phase II. See also the agendas of Südzucker Group Sales function ("GSF") meetings between 1 January 2010 until November 2011 mentioned above.

¹¹⁹ See documents submitted as Annex Q1-a, Q1-b and Q1-c to Südzucker's reply to the 5th RFI Phase II.

¹²⁰ Annex 6 of Südzucker's reply to the 3rd RFI in Phase I.

¹²¹ Annex 5 of Südzucker's reply to the 5th RFI in Phase I.

¹²² Annex 17 of EDFM's reply to the 6th RFI in Phase I.

¹²³ Article 12 of the "RAHMENVERTRAG" signed on 6 December 2006 in Bolzano.

¹²⁴ Annex 1.a of EDFM's reply to the 2nd RFI in Phase I.

- (214) The Bundeskartellamt's letter is, inter alia, based on a [...] ¹²⁶. This shows that Südzucker is likely to be capable of segmenting the market in Italy and Germany along national lines.

(3) WHITE SUGAR PRICE DIVERGENCES BETWEEN THE DIFFERENT MEMBER STATES

DG AGRI data points towards the existence of national markets

(i) DG AGRI data description

- (215) In order to verify the boundaries of the geographic market the Commission has also analysed a database collected by DG AGRI on monthly Member State price data for the period April 2008 to November 2011, as well as aggregate price data at Union level for the period June 2006 to October 2011.
- (216) Union beet producers submit their ex-works prices and quantities sold every month and DG AGRI computes (i) the weighted Union and national average price levels for sugar and (ii) the standard deviations, a measure of price dispersion, thereof (i.e. in the database DG AGRI computes the standard deviation both within a given Member State and also across the Union). Data on average price levels and standard deviation at the Union level, but not at Member State level, are publicly available.
- (217) There are some general clarifications on what is included in the data collected by DG AGRI. First, the pricing data are collected from beet producers while pricing information from raw cane refiners are not included in the database. This issue however should not be material to the analysis as prices of white sugar produced either from beet or from raw cane sugar should be very similar within the same geographic market ¹²⁷. Second, the pricing data provided by beet producers refer to homogeneous granulated crystal, standard quality, in bulk or big bags and in particular exclude bag for retailers ¹²⁸. Therefore, as the data collected specify the quality of sugar they are comparable across Member States.

¹²⁵ Letter from the BKA dated 07.10.2011 addressed to [Commission official].

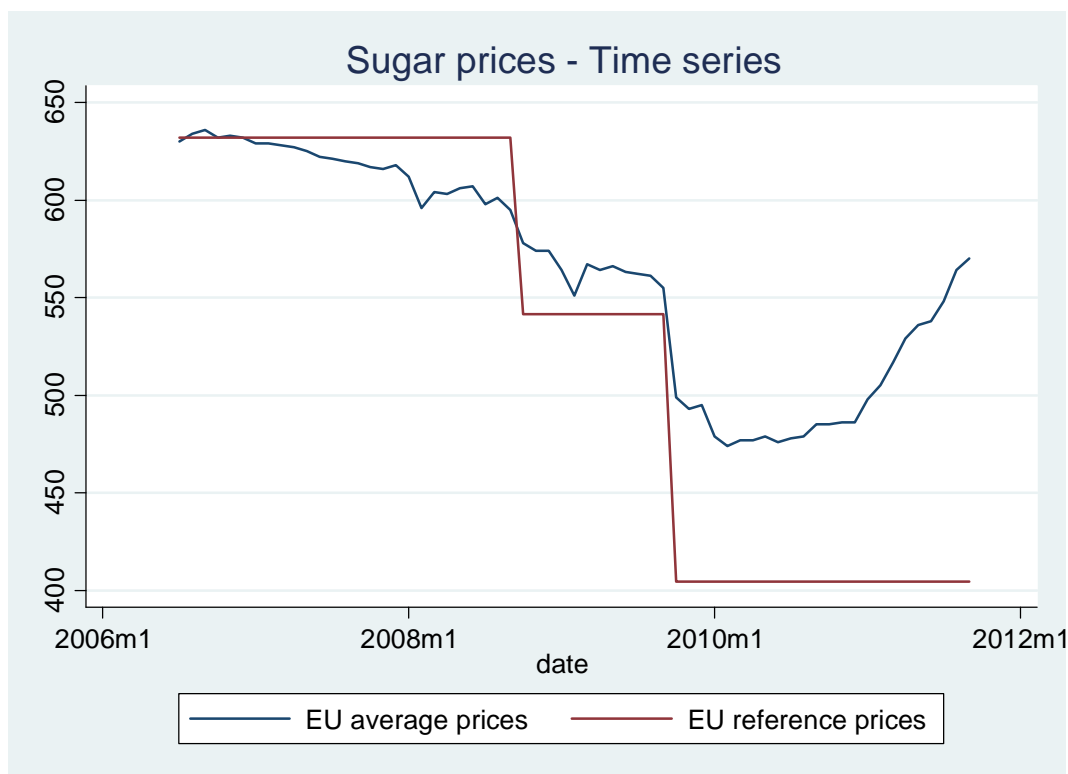
¹²⁶ "[...] * Danach respektieren Nordzucker und Südzucker ihre jeweiligen Vertriebsgebiete in Deutschland. Dies hat schon in der Vergangenheit zu Preissteigerungen und zur Zurückhaltung von Zuckermengen geführt. Wesentliche Abnehmer von Industriezucker haben vorgetragen, trotz wiederholter Nachfrage kein Angebot von anderen Zuckerproduzenten als dem Stammlieferanten zu erhalten. Quotenzucker [...] * wird offenbar unter Inkaufnahme hoher Transportkosten in Defizitgebiete, insbesondere Italien, exportiert. Dadurch konnte ein vergleichsweise hohes Preisniveau für Verarbeitungszucker in Deutschland etabliert und aufrecht erhalten werden. Diese Probleme haben sich im Jahr 2011 nach den Marktrecherchen des "Infozentrum Zuckerverwender" als einer Interessenvertretung der Industriekunden, weiter verschärft." [Letter from the BKA from 07.10.2011 p. 2-3]

¹²⁷ White sugar produced either from beet or from raw cane is entirely substitutable as shown by the replies in Questionnaires to Competitors in Phase I.

¹²⁸ See price reporting system regulation (EC) No 1234/2007, Article 9, update: March 2011.

(ii) Price evolution

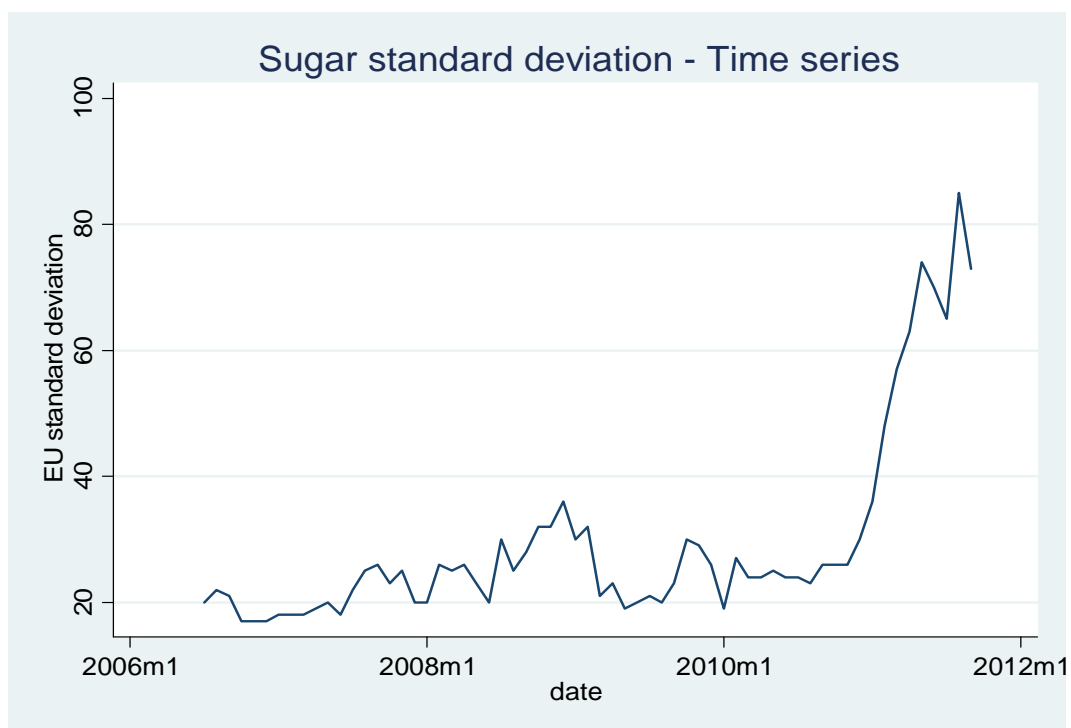
Figure 1: Union average price



- (218) DG AGRI computes the Union average prices based on those Member State data. As shown in Figure 1, the Union average price has decreased until 2010 but since then the average Union price for white sugar has increased substantially, despite the decrease in the reference price introduced by the 2009 reform. DG AGRI also computes the evolution of the weighted standard deviations across the Union¹²⁹. Those data show that while price dispersion has remained relatively stable up to the end of 2010, it has increased significantly during 2011. This finding is likely to illustrate that the variation of sugar prices in the Union has increased during 2011, instead of converging.

¹²⁹ Computing the weighted average standard deviation across Member States yields a very similar pattern.

Figure 2: Union standard deviation weighted by quantities



- (219) These aggregate level trends are also evident at the Member State level. In particular, while prices in different Member States follow similar overall patterns, the differences across Member States in levels have been increasing, especially during 2011, as shown in the following graphs of Member States prices and within Member State standard deviation¹³⁰.

¹³⁰ Due to the confidentiality of the Member State data collected by DG AGRI there are no labels provided for the different Member States prices and standard deviations. The countries shown in the graphs are Austria, Belgium, Bulgaria, Czech Republic, Denmark, Germany, Spain, Finland, France, United Kingdom, Greece, Hungary, Italy, Lithuania, Netherlands, Poland, Portugal, Romania, Sweden and Slovakia.

Figure 3: Member States prices

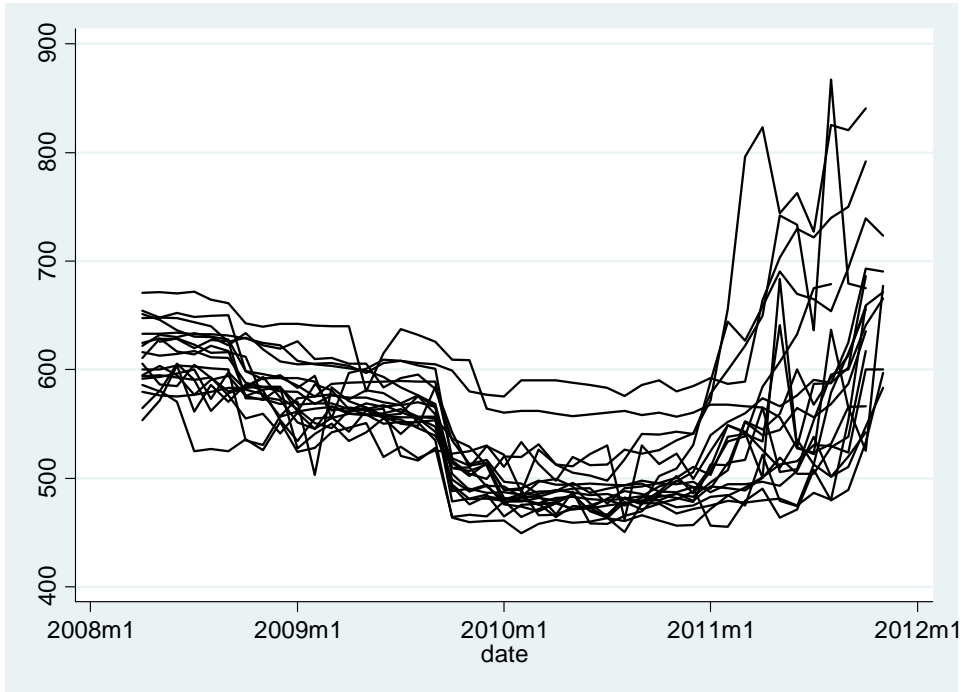
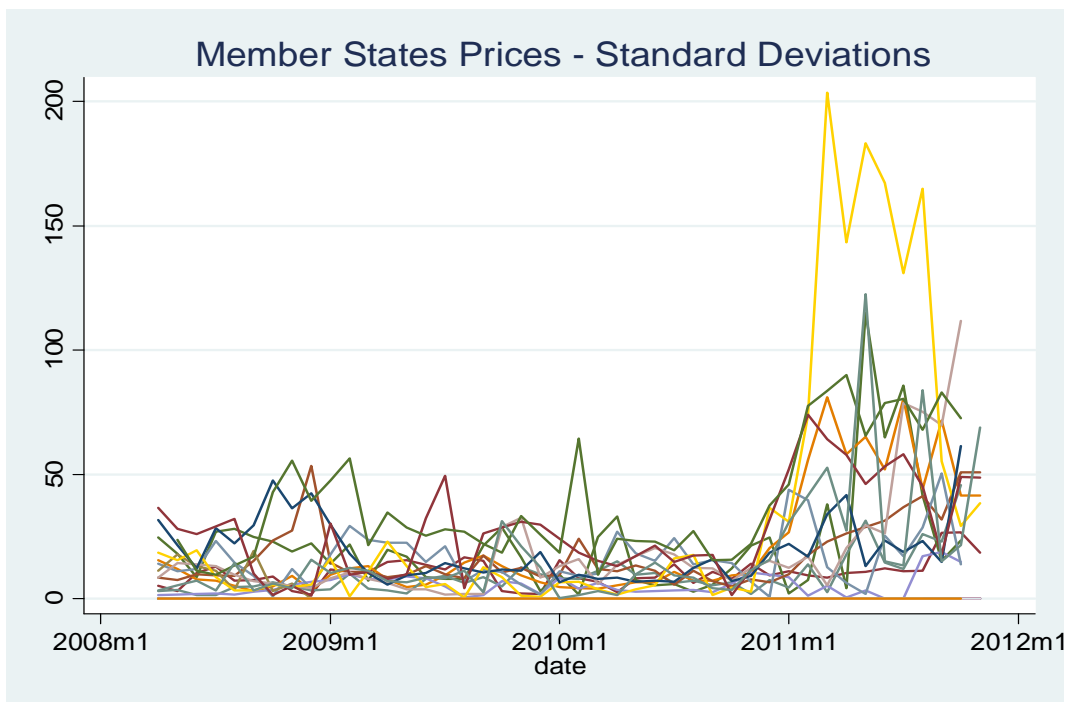


Figure 4: Member States prices - Standard Deviations

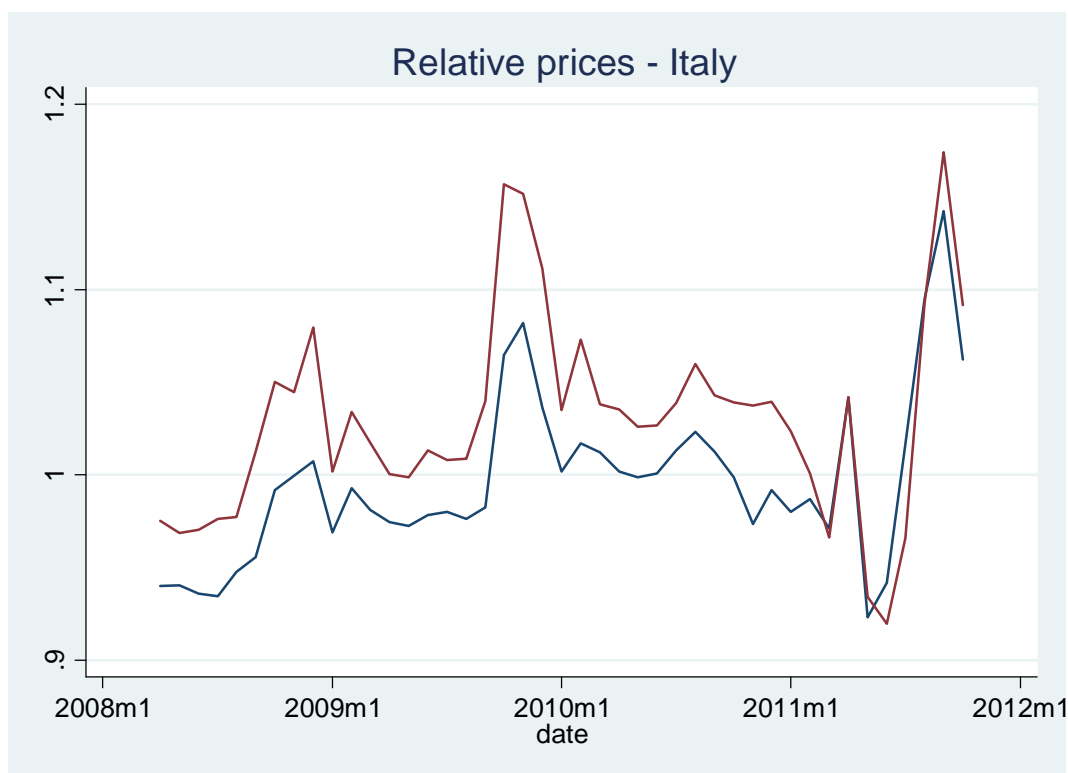


- (220) Focusing on the Italian market, two patterns at the end of the period under consideration appear. First, the prices in Italy have risen relatively more than in other main Union markets, such as Germany and France (see Figure 5 on relative prices of Germany and France compared to Italy). The prices in Italy have risen from levels that were below German and French prices, by around 8%, in the second quarter of 2011 to more than 15% higher in the third quarter of 2011. Secondly, during 2011

the variability observed within Italy is much greater than the variability in the two large surplus Member States, Germany and France (the standard deviation in the Italian market even reached above EUR 100 in 2011). This finding implies that price differences well in excess of 15% (but also well below 15%) were observed between Italy and France and Italy and Germany¹³¹.

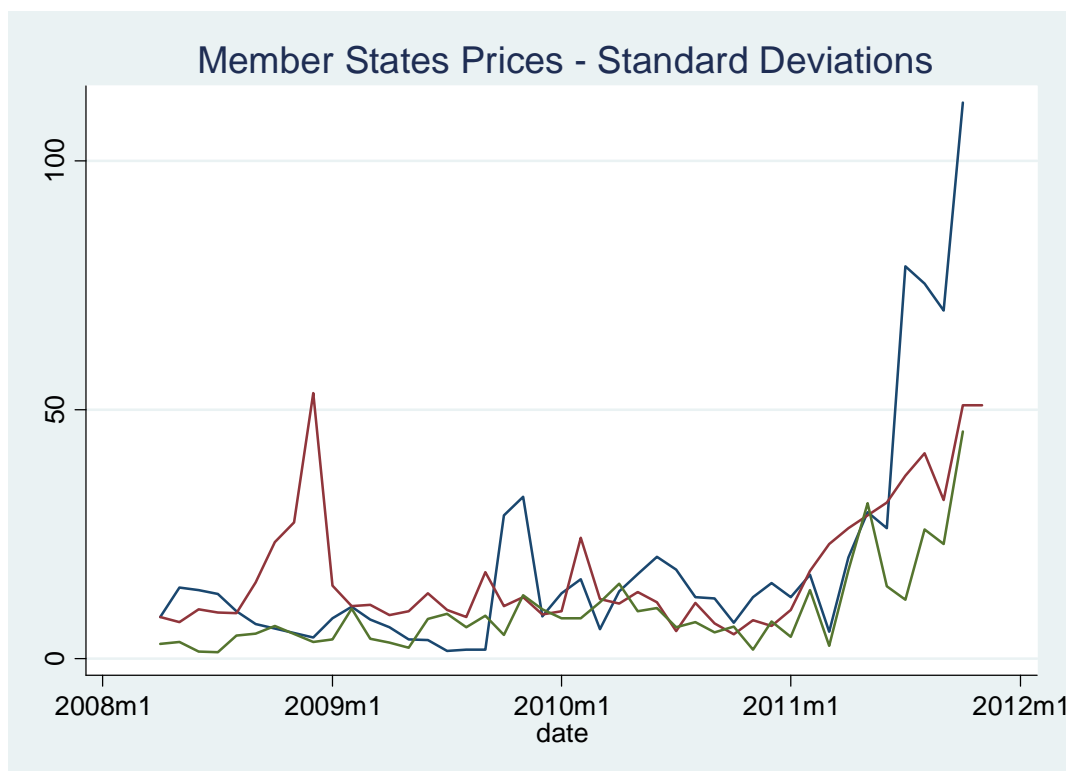
- (221) In the presence of one geographic market, however, one would expect that prices for a homogeneous product do not diverge significantly from each other as arbitrage opportunities will "correct" any pricing difference (and any divergence would only reflect differences in transportation costs). The two figures however suggest that the German and French markets are not likely to be in a position to constrain, at least to a significant level, the increase in the variability observed in the Italian market, in a period where Italian prices have increased significantly compared to the German and French levels.
- (222) In summary, the price dispersion across Member States goes up as the Union price level goes up (during 2011 when sugar becomes scarce overall). As regards Italy, the price level as well as the price dispersion within Italy goes up by relatively more than in its neighbouring Member States. This suggests that price differences are not arbitrated away as should be expected to happen in the same geographic market.

Figure 5: Member States relative prices – Italy



¹³¹ The swings in the relative prices of Italy vs Germany and Italy vs France, as depicted in Figure 5, shows that prices in Italy can diverge from German and French prices.

Figure 6: Member States prices Standard Deviations - Italy



(223) Overall, as far as Italy is concerned, the above Figures of the pricing data collected by DG AGRI are consistent with the qualitative evidence that does not support the definition of a supra-national geographic market.

(iii) Correlation analysis

(224) A correlation analysis on the Member States price series has also been performed in order to explore the pricing patterns across Member States further. Price correlation analysis is based on the idea that in the absence of common (demand or supply side) shocks the extent of co-movement in the prices of different Member States will provide information about the substitutability amongst them. This is because price competition results in an alignment of prices in the two Member States if they belong to the same relevant market¹³². Hence, if two Member States are considered to be part

¹³² For example for two Member States that were to belong to the same market, if a *country specific* cost shock (such as labour costs) were to lead to a price rise in Member State *i*, then consumers would substitute their purchases away from this Member State and purchase instead from Member State *j*. As a result of the increase of the demand in Member State *j* the price in this Member State should increase and so a co-movement (measured by a positive correlation) between the changes in the prices in the two Member States is expected. The Commission acknowledges that price correlation analysis is not a perfect measure for the purposes of market definition and the results of this analysis should be interpreted with caution and in parallel with the pricing evolution and the qualitative evidence collected during the market investigation. A main caveat of correlation analysis is that common shocks (such as fuel costs) can induce spurious correlation and therefore high correlations could be driven by factors which can cause a co-movement but are still unrelated to consumer/producer substitution. Similarly, two price series may be found to be correlated only because each of them has a trend (again, leading to spurious correlation). To address these concerns, correlation analysis is performed on stationary series, i.e. series with constant mean and variance. A series is non stationary if it fails to satisfy any part of this

of the same geographic market then the price movements should be correlated. If the prices of the two geographic areas move perfectly in line with each other, the correlation coefficient is equal to one and if there is no relationship the correlation is equal to zero.

- (225) To assess whether the prices are sufficiently correlated, as one of the elements to consider the two geographic areas to belong to the same market, it is typical to use as a benchmark some other correlations (for which one has strong indications on whether they belong to the same market or not). Therefore, the most useful source of information from this correlation analysis comes from a comparison of correlations among different pairs. For the purpose of this Decision, correlation analysis has been carried out on price changes amongst Member States.
- (226) The results of the correlation analysis are provided in Annex I. The results show that price correlations between Italy and its "neighbouring" and main exporting Member States (notably France and Germany)¹³³ are significantly lower than amongst these Member States, suggesting that the Italian market is more isolated. Therefore, the significant imports from Germany and France to Italy have not led to higher correlation between the price changes in Italy and each of those Member States than between the changes in prices amongst Germany and France¹³⁴.
- (227) Price correlation analysis measures the contemporaneous adjustments in the price changes¹³⁵. The comparative results mentioned above are relatively robust when we consider a (moving average correlation) specification of the tests that captures adjustments in the price changes over a three month period¹³⁶.

definition. In the current case it is found that the Member State price series in levels are non stationary and therefore correlation analysis on the levels is not meaningful. Taking the first difference of the price series though yields stationary series and therefore correlation analysis was conducted on first differences. The economic interpretation when calculating correlations in differences measures whether the price changes rather than price levels would be potentially correlated or not (and therefore the interpretation would be of relative convergence). A high correlation indicates that price changes co-vary.

¹³³ The correlation coefficient between Italy and Austria is higher than Italy and Italy's other "neighbouring countries" but still lower than other pairs of "neighbouring countries", in particular of the main exporting Member States (i.e. Germany and France).

¹³⁴ The Commission has also tested whether the differences in the correlation coefficients are statistically significant following the *cortesti* command in Stata. These tests show that the correlation coefficients between Italy-Germany and Italy-France are significantly smaller (even at the 1 percent significance level) than the correlation coefficient between Germany-France.

¹³⁵ Annex I of this Decision provides the correlation results for a quarterly moving average. Even though the correlations between Italy and its neighbouring/exporting Member States are in most instances higher than the simultaneous correlation they are still relatively lower than the correlations amongst these neighbouring Member States (notably France and Germany). Furthermore, the correlation coefficients between Italy-Germany and Italy-France are found to be statistically significantly smaller (the former at the 5 percent and the latter at the 1 percent) than the correlation coefficient between Germany-France.

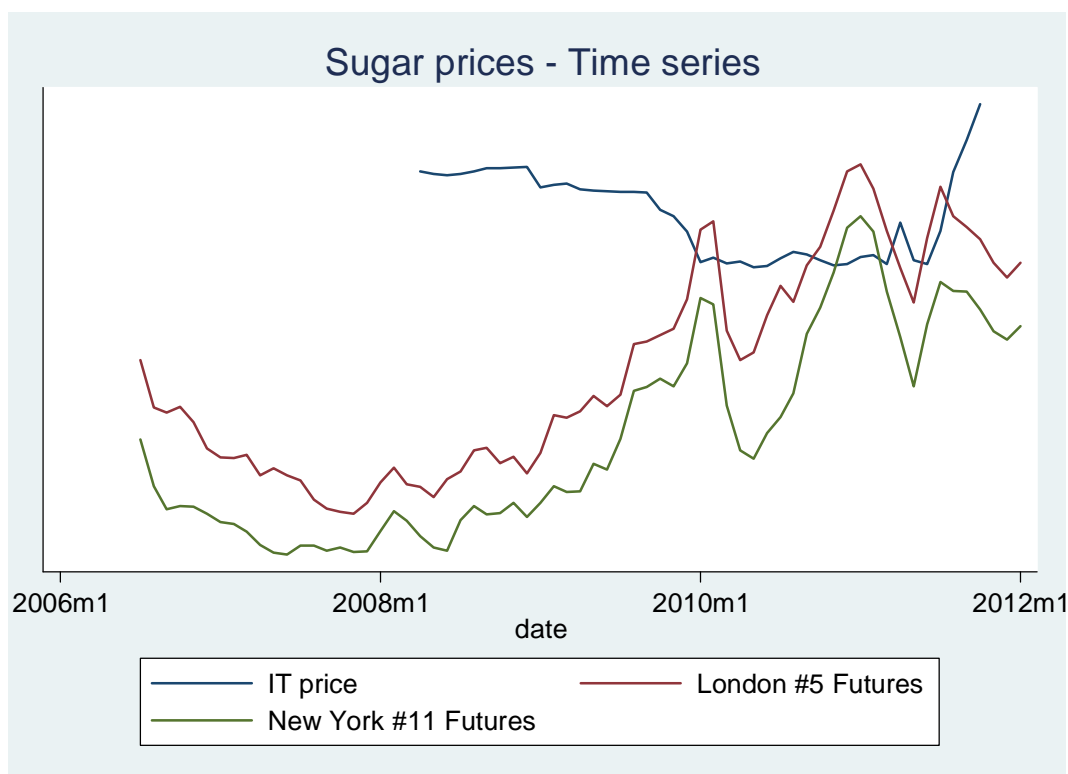
¹³⁶ Furthermore, the Commission notes that much larger movements in prices were recorded during the 2010/2011 campaign compared to previous campaigns, largely due to the regime change and the general shortage of white sugar in the market (as evidenced by the market investigation). These larger shifts in prices would be an interesting source of variation for the purposes of price correlation analysis. However, even if the correlations for this subsample for Italy and its "neighbouring countries" are relatively lower than correlations between other "neighbouring countries", the time period is particularly short to draw any meaningful estimates on correlations for this specific subsample.

- (228) Overall, it is concluded that the correlation analysis is consistent with the qualitative evidence collected during the market investigation showing that the Italian market price changes co-move less strongly with its neighbouring and exporting Member States than those neighbouring Member States' price changes co-move amongst each other.

White sugar price divergences between Italian and world price

- (229) The notifying party also claims that the Italian market adheres to world price market conditions. It claims that any increase in market prices in Italy is simply the consequence of increasing world market prices and not capable of being influenced materially by Südzucker. However, the notifying party has not provided evidence to this effect. On the contrary, the evolution of future contracts for white sugar and raw cane sugar (measured by the London #5 and New York #11 futures respectively) and the Italian price do not follow each other closely, as shown in Figure 7.

Figure 7: Italian sugar prices and futures prices

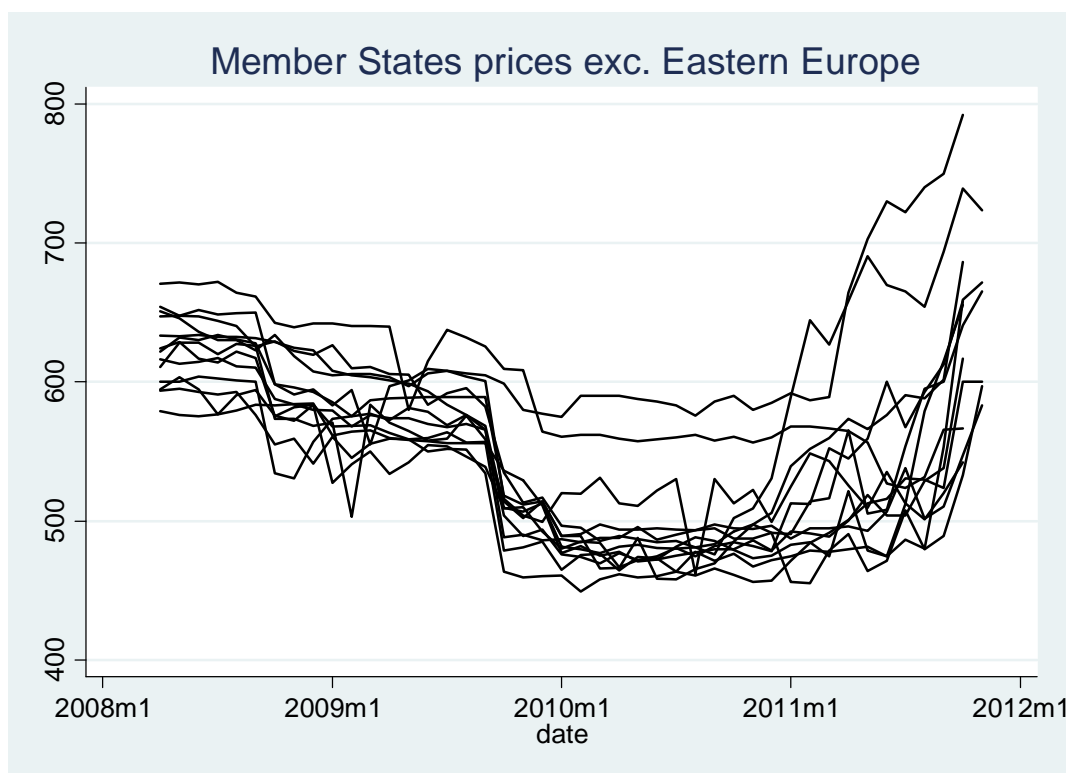


The concerns raised by the notifying party on the comparability of the DG AGRI data are either incorrect or do not affect the main conclusions of the analysis

- (230) The notifying party has raised several arguments on the comparability of the DG AGRI data (see paragraphs 76 to 90 of the reply to the Statement of Objections). The arguments can be grouped into three groups.
- (231) First, the notifying party raises concerns on the usefulness of the analysis and the data due to the differing product mix and the differing contract duration across

Member States. It suggests that "any nationwide analysis of prices also had to include the mix between bulk and retail sugar in that country"¹³⁷. However, as explained above and as acknowledged by the Parties during the Oral Hearing, the DG AGRI data exclude retail sugar and therefore that argument is not relevant for those data. The notifying party also alleges the differing contract duration across Member States to bias the comparability of the data. However, it argues that its contracts are usually shorter in Italy for the retail segment and in Eastern European countries¹³⁸. As retail prices are not included in the data, the price evolution and price correlation analysis is at least valid for all non-Eastern European countries and thus the main findings that compare Italy with France and Germany remain unaffected¹³⁹. Besides, and for sake of completeness, Figures 8 and 9 representing Member States prices and standard deviations excluding Eastern European countries show that the main findings based on Figures 3 and 4 that include all Member States still apply. The Parties contest the similarity of the graphs and claim that "it is unclear for the Parties how these deviations can be explained"¹⁴⁰. The Commission notes that the only difference between the two sets of graphs is the exclusion of the Eastern European Member States. Also the graphs show an increase in the price level differences across Member States and an increase in the Member State standard deviations.

Figure 8 : Member States prices excluding Eastern Europe



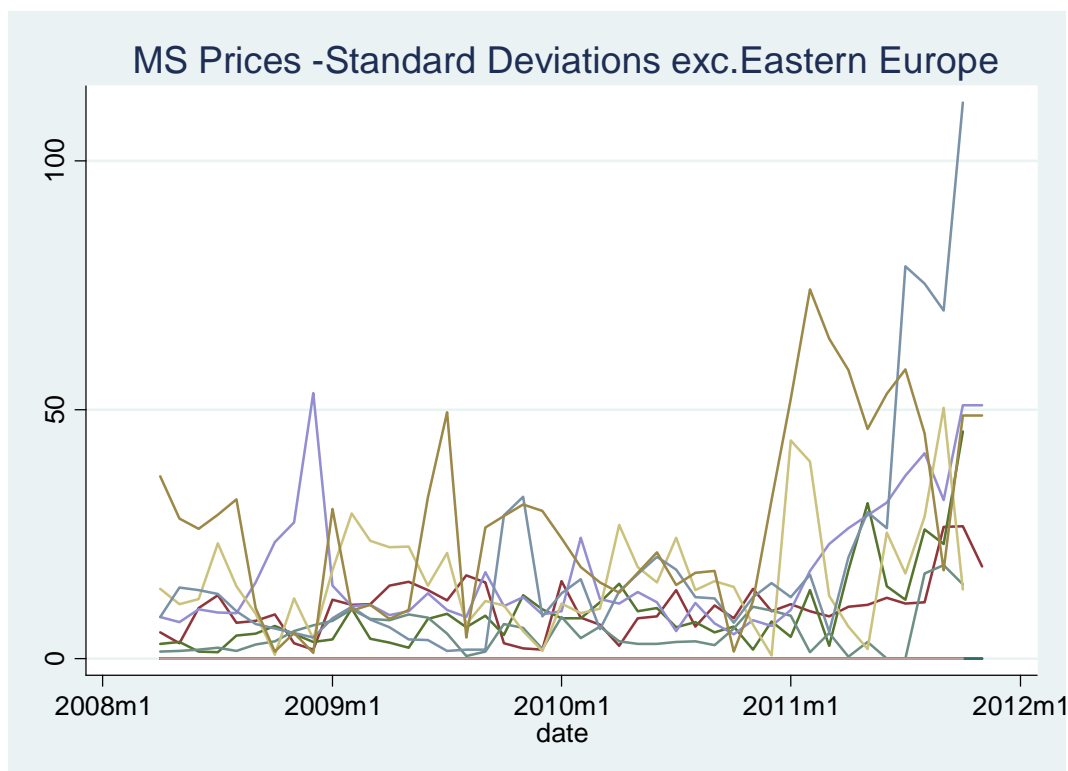
¹³⁷ See reply to the SO, paragraph 87.

¹³⁸ See reply to the SO, paragraph 79.

¹³⁹ The possibility of different contract durations in different Member States is also addressed by the robustness check of moving average correlation analysis. A moving average analysis relaxes the assumption of contemporaneous price correlation but captures also price adjustments with a lag.

¹⁴⁰ Reply to the Letter of Facts, paragraph 31.

Figure 9: Member States standard deviation excluding Eastern Europe



- (232) Second, the notifying party claims that "reported prices relate to ex-factory prices causes any price analysis to be strongly biased in the sense that large exports from e.g. France and Germany to Italy will not be reflected adequately in the reported prices. i.e. amounts and prices of sugar exported to Italy are included in the German average price and the Italian average price is calculated only on the basis of local Italian production which represents much less than 50% of the market"¹⁴¹. The Commission understands this argument to acknowledge that different ex works prices (i.e. prices that exclude any transport cost) are set for different Member States for a given factory. This would imply that the "law of one price"¹⁴² would not hold and a country specific "margin" (unrelated to transport costs) would be set.
- (233) Otherwise, namely if ex works prices are the same irrespective of the destination country then this bias cannot be present in the dataset and therefore the analysis above is not affected in any way. Under the assumption that ex works prices depend on the destination country, the Commission notes the following:
- (1) Given that the notifying party does not put forward that the geographic market for Italy is narrower than national, nor does it result from the market investigation, it is not obvious why the price of factories located in Italy would not be representative of the average Italian prices. Imports into Italy would need to compete with Italian producers (therefore no bias would be present in the data for importing countries, such as Italy).

¹⁴¹ Reply to the SO, paragraph 78.

¹⁴² The Law of one price suggests that all identical products should have only one price.

- (2) The Commission is aware of the German data in the DG AGRI data also comprises ex works prices of German exports to Italy. Indeed, the ex works average prices for exporting Member States are calculated on the basis of data that also include the price of exports from that Member State in other Member States. The exporting structure (as well as the share of exports compared to production sold domestically) is important to understand the impact that the method used to calculate prices may have on exporting countries' prices, as computed in the DG AGRI dataset and on the resulting correlation analysis. For this purpose, the Commission has consulted the Comext database collected by Eurostat on intra-Union white sugar flows¹⁴³. During the period of correlation analysis, from April 2008 to November 2011, the sugar exports from Germany to Italy have been consistently between 43-51% of the German exports and therefore represent the vast majority thereof. As these German exports to Italy are part of the German ex works price, the estimated correlation coefficient for Italy-Germany would be higher than the correlation coefficient of Italy-Germany that would result if the prices of these German exports were instead allocated to Italy. Conversely, if German data did not contain the prices of these exports, the correlation between Italy-Germany would be lower than the estimated correlation¹⁴⁴. Hence, the impact of the effect that the notifying party alleges leads to lower correlation between Germany and Italy which therefore suggests that Italian prices are likely to be even more isolated compared to Germany and, similarly, to other exporting Member States. This would therefore be an element militating not against but, to the contrary, in favour of the national dimension of the market for the supply of white sugar to industrial processors in Italy.
- (234) The third argument raised by the notifying party suggests that "*the price correlation between Italy and Germany resp. France has been significantly affected by the explained special events*"¹⁴⁵ such as the unlimited access of sugar from LDC/ACP countries in October 2009 and the temporary low price level in Italy immediately after the reform in 2006. The Commission, however, notes that the correlation analysis performed was based on the first difference of the series. As a result the effect of common shocks, such as EEA wide regulation, would be accounted for in the Commission's correlation analysis.
- (235) The notifying party provided supplementary comments following the Oral Hearing. In this submission the notifying party claims that the price variation analysis is flawed for three reasons which are discussed and dismissed in turn¹⁴⁶.
- (236) First, the notifying party considers that the time intervals chosen for correlation/price evolution/dispersion analyses yields irrelevant results. The Commission does not accept that the extraordinary economic situations, as described by the notifying party,

¹⁴³ The data refer to codes 1701 99 10 and 90.

¹⁴⁴ As to the question whether the relative high correlation between France and Germany is driven by a similar exporting structure, the Commission notes that this is not the case. Indeed, the trade flows suggest a markedly different exporting structure between the two Member States as shown in Appendix 3.

¹⁴⁵ Reply to the SO, paragraph 90.

¹⁴⁶ Südzucker Supplement Comments following Oral Hearing, 12 March 2012. The Parties have repeated the same concerns in their Reply to the Letter of Facts, paras 24 to 30 without providing any further explanations.

imply that prices in this time interval cannot provide useful insights. The explanation provided by the notifying party for persistent differences in prices across Member States may provide the reasons for such movements, however, to the Commission's view they confirm that prices in different Member States do not move closely together.

- (237) The notifying party admits that due to higher stock levels at the beginning of the transition significant quantities had to be redirected and made "*the sugar producers compete aggressively for customers in Italy. Strong price competition resulted temporarily in attractive offers for Italian customers compared to existing customers in neighbouring countries*"¹⁴⁷. The Commission considers that this explanation cannot be reconciled with one EEA-wide geographic market, especially in the light of the fact that those price differences lasted for several years. On the contrary, the fact that the German and French prices were shielded from the alleged very low prices in Italy is an indication that there is no arbitrage between Italy and these Member States. This is also confirmed by the results of the price correlation analysis which shows that the arbitrage between Italy and its neighbouring/exporting Member States is lower than amongst these Member States. The presence of asymmetric shocks (such as the reduction in Italian domestic quota) does not render price correlation analysis irrelevant but on the contrary such shocks provide useful source of information for detecting whether two Member States belong to the same market (i.e whether prices adjust through arbitrage). The Commission also notes that the starting period of the analysis is April 2008 well after the start of the post 2006 regime¹⁴⁸.
- (238) Second, the notifying party claims that the inclusion of ex-works prices for exports from Germany/France into Italy in Italian ex-works prices would lead to lower price differences and higher price correlation. The Commission accepts the notifying party's point that the ex-work prices in Italy would normally be lower than what is reported in the DG AGRI data as it is likely that the ex-works prices of the exports from Germany/France into Italy have to incur higher transport costs than Italian domestic production (and since the final price of sales in Italy should be similar to the ex-works prices of the exports from Germany/France into Italy would be lower)¹⁴⁹. However, this argument does not affect the results of the analysis. Even if the level of Italian ex-works prices would be somewhat lower than indicated in the DG AGRI data, the evolution of the adjusted ex works prices would be identical to the one observed in the dataset (in particular as in the period under consideration the distribution of imports per Member State into Italy are rather stable). The only effect would be a horizontal shift of the Italian prices series downwards to reflect the lower ex work prices for the quantities sold from Germany to Italy. The relative prices (Figure 5) would also fall by the same amount, however the relative swings in the prices would remain and the Italian prices would have increased the most during the last period compared to French and German prices (and as a result there would not be lower price differences as the notifying party suggests).

¹⁴⁷ Supplementary Comments following Oral Hearing, p2.

¹⁴⁸ The Commission also notes the fact that intervention stocks were sold in Italy is not relevant. Besides, the sale of this intervention stocks was sold through EEA tenders.

¹⁴⁹ The Commission notes that exporters from Germany and France may often have to incur transport costs of EUR 30-40 to sell in northern Italy.

- (239) The correlation analysis would also largely remain unaffected. As the correlation analysis focuses on the price changes, it is irrelevant whether the German exports to Italy are included in the Italian dataset. The price changes of the Italian producers and German exports to Italy are expected to be basically the same. Also, the Commission notes that the results of the correlation analysis contradict the conditional statement of the Parties that "*ex-works prices for sugar exports from Germany are comparable to ex-works prices for sugar sales within Germany when the market is balanced. Otherwise, it would be more profitable to sell sugar to other destinations*"¹⁵⁰. This is precisely the price arbitrage (price alignment) hypothesis tested by the correlation analysis. If the tested hypothesis of a common geographic market is true the correlation between the two countries' prices should be very strong. If, on the other hand, the estimated correlation is weak (and especially in comparison with the correlations of other country pairs, such as Germany-France) the hypothesis is rejected, and this is interpreted (in this Decision) as evidence consistent with the national market hypothesis. If Germany and Italy were to belong to the same geographic market, the ex-works price of a German factory would be identical irrespective of the destination of the quantities. An increase in the ex-works price for domestic German sales would also be followed by an increase in the ex-works price for exports to Italy which in turn would also be followed by an equivalent increase in the ex-works price of Italian domestic producers. Therefore, the correlation between German and Italian ex work prices as captured by DG AGRI data would be very high, which is however not supported by the data. On the other hand, if one assumes that the two Member States belong to separate geographic markets then the estimated correlation would be an upper bound of the correlation between the two Member States, given the high share of German exports directed into Italy.
- (240) Besides, as Mr Wolfgang Heer claimed in the Oral Hearing "*We have defined the volume of quota sugar which we have to sell in Europe countries and we decide where to sell this sugar. And the price, that is done by the market. [...]*"¹⁵¹.
- (241) This statement shows that ex work prices are not necessarily the same for a given factory. [...]*¹⁵².
- (242) Third, the notifying party suggests that a comparison of biased ex-works prices is unfit to determine whether the competitive situation differs across Member States. However, this view is not explained and is in stark contrast with the reasoning of the Commission as set out above.
- (243) Therefore, the Commission concludes for the reasons described above that overall, the findings of the analysis based on DG AGRI data, which support the qualitative evidence in favour of a separate national market for Italy, remain largely unaffected by the arguments raised by the notifying party.

¹⁵⁰ Supplementary Comments following Oral Hearing received on 12 March 2012, p3.

¹⁵¹ Statement by Wolfgang Heer, Speaker of the Board ('Vorstandssprecher'), during the Oral Hearing of 5 March 2012, minute 43:55 to 44:36 of recording C-15.50-16.42.

¹⁵² [...]*.

Exchange of arguments on Südzucker's own pricing data

- (244) With respect to prices that Südzucker sets in different Member States, the Commission argued in the SO, on the basis of Südzucker's internal documents, that its average sugar prices differ between the different Member States it supplies¹⁵³.
- (245) In its reply to the SO, the notifying party has provided a table with its invoiced prices with inclusion of data from Agrana and Südzucker Polska¹⁵⁴. The resulting differences in levels are lower, notably in Member States where Agrana is active such as [...]*. However, even the revised tables show significant differences in average prices between e.g. Italy and [...]*.
- (246) The notifying party also acknowledges other deficiencies of the data, namely the inclusion of transportation costs and different mixes of products in different Member States to cast doubts on the comparability of the data across Member States. The Commission has concerns that those deficiencies are such that those data are not suitable for an analysis for the purposes of geographic market definition. In particular the Commission considers that the possibly different mix of industrial vs retail sugar sales of Südzucker in different Member States may have an impact on the comparability of the data across Member States. As a result, the Commission considers that those aggregate data are not sufficiently reliable for the purposes of the definition of the geographic market for sugar sold to industrial processors. On the contrary, DG AGRI data, which only consider prices of sugar sold to industrial processors, are much more reliable for the purposes of the geographic market definition.
- (247) The notifying party, while strongly criticising the reliability of Südzucker's pricing data for the purposes of geographic market definition, also provides a graph based on these data on the prices between France, Italy and Germany. On the basis of that graph, the notifying party argues that there is national average price convergence amongst those three Member States. According to the notifying party *"the price increases in Italy in 2010/2011 and 2011/2012 are not the result of limited competitive pressure but of convergence process following years of relatively low prices in Italy not even covering transport costs"*¹⁵⁵. Furthermore, these graphs only include five annual prices and one estimate of prices based on contracted prices for 2011/2012. In this respect, the Commission notes that the *"greater convergence"* of prices takes place in 2011/2012 when contracted and not invoiced prices are graphed, which creates an inherent incomparability¹⁵⁶.

¹⁵³ Annex Q10 Südzucker's reply to the 4th RFI, Phase II. The Commission notes that this data do not include volumes sold by Agrana (Austria and Slovenia) and SZ Polska (Poland, Baltics and partly Scandinavia). At the Commission's request, Südzucker also provided data including all consolidated Südzucker's group companies sales, although stressing that the data is available only on high cumulated levels. In any event, this does not change the fact that the prices differ between the different Member States supplied.

¹⁵⁴ Table 2 of reply to the SO, p. 43.

¹⁵⁵ Figure 2, reply to the SO, p. 47.

¹⁵⁶ The Parties in para 12 their Reply to the Letter of Facts claim that the Commission had in its possession the data underlying the graph. The Parties only hide in their last sentence that the Commission's point in the Letter of Facts (para 20) only relate to the use of contracted data for 2011/2012 as opposed to invoiced data for previous years. The Parties only further submit that contracted prices are extracted

- (248) Even if the data provided by the notifying party in this context were reliable, they would still not support the geographic market definition as being national. Even if the graph was based on comparable data it would merely show a starkly different evolution of prices in different Member States.
- (249) First, the notifying party acknowledges that prices in Italy were for several years lower than in Germany and in particular in France. For several years there has been a difference of prices of around EUR [...] between the sales of the notifying party notably in [...] and Italy. This is even more striking as the transport costs for the notifying party are higher for Italy than in [...] (as in Italy, in contrast to [...]). Assuming comparable sales in different Member States, the graph would show that the arbitrage opportunities between Member States are not exploited which can lead to persistent price differences well above transport costs (this arbitrage argument would need to hold also in cases of asymmetric shocks across Member States, as described by the notifying party¹⁵⁷). Second, even the evolution of prices as shown by the notifying party's graph shows a greater co-movement between Germany and France than between these two Member States and Italy, which is also consistent with the result of the correlation analysis described before.
- (250) Therefore, while acknowledging that the data have several limitations, it has to be noted that if the data were considered at face value they show that the notifying party's prices may well differ across Member States for a persistent period. Contrary to the Parties' claim in the Letter of Facts that these differences were due to the transitory period post 2006 reform, such sustained differences show a clear lack of arbitrage amongst Member States.
- (251) In view of the above, the Commission considers, on the basis of DG AGRI data, that the price differences between Italy and its neighbouring Member States are not arbitrated away. In addition, the price changes in the Italian market co-move less strongly with its neighbouring (exporting) Member States than these neighbouring Member States' price changes co-move amongst each other. This finding suggests that the Italian market is relatively more isolated than its neighbouring countries. The arguments raised by the notifying party on the comparability of DG AGRI data do not affect the above conclusions of the analysis. Finally, the Südzucker aggregate pricing data is not sufficiently reliable for the purpose of the geographic market definition of sugar sold to industrial processors in Italy.

(4) MARKET POSITIONING OF COMPETITORS DIFFERS SIGNIFICANTLY ACROSS MEMBER STATES

- (252) The presence of the same major suppliers or producers in a number of countries or regions provides initial evidence suggestive of a market comprising those countries or areas. However, the Commission will also seek to determine whether there are material deviations in those countries or regions¹⁵⁸.

form ordinary course of business data and invoiced prices at the end of the year "do not usually significantly differ" without providing any further evidence.

¹⁵⁷ In their Reply to the Letter of Facts, the Parties also provide a list of reasons pointing to asymmetric (i.e. only relevant for Italy) and symmetric shocks (EEA wide shocks) during the transitory period.

¹⁵⁸ See Commission Decision of 27 July 2001 in Case No IV/M.2337 - Nestlé/Plaston Purina, OJ C 239, 25.8.2001, p. 8; Commission Decision of 8 January 2002 in Case No COMP/M.2621 - Seb/Moulinex,

- (253) Generally, the Commission views significant national market share differences as evidence that the conditions of competition are not sufficiently homogeneous to support a wider geographic market definition¹⁵⁹.
- (254) In the case at hand, even more than 6 years after the latest reform, the market shares of all European players are very different depending on the Member States in which they sell sugar. This is illustrated by the presence of Südzucker, the main European sugar producers, in the various Member States.
- (255) Indeed, Südzucker held the following market shares (for the sales of white sugar to industrial processors) for the marketing year 2010/2011 of: [70-80]*% in Austria, [30-40]*% in Germany, [20-30]*% in France, [60-70]*% in Belgium, [0-5]*% in the Netherlands, [40-50]*% in Hungary, [5-10]*% in Denmark and [5-10]*% in the United Kingdom.
- (256) Similarly, Nordzucker, the second main sugar producer in Europe, held on the same product market and the same year market shares of [30-40]*% in Germany, [60-70]*% in Finland (through Nordic Sugar AB), [40-50]*% in Latvia and [5-10]*% in Poland and has almost no presence in France, Italy and Spain.
- (257) Such significant divergences in market shares from one Member State to another, in particular where those Member States are neighbouring, point towards the existence of national markets in this case.

(i) *Greece*

- (258) The market investigation conducted in this case has demonstrated that Greece is a deficit country like Italy. Therefore, the existence of imports itself does not suggest that those imports pose competitive constraints on competitors in Greece because such imports simply derive from the regulatory environment. The demand and supply patterns are similar to those in Italy; similar price and market share differences are also observed in Greece like in Italy. Therefore, although Greece is a deficit Member State and imports are important in order to fulfil the domestic sugar needs, from a customer and organisation of supplies perspective the market is likely to be national. However, as the likelihood of entry of EDFM in Greece is low and as the proposed transaction would not lead to any significant impediment of effective competition under the narrowest possible market definition, there is no need to conclude on the precise scope of the geographic market as regards Greece.

¹⁵⁹ OJ C 49, 22.2.2002, p. 18; *Summary of Commission Decision in Case No COMP/M.4513 - Arjowiggins/M-real Zanders Reflex*, OJ C 96, 25.4.2009, p. 10. In Commission Decision 2003/777/EC in Case No COMP/M.2861 - Siemens/Drägerwerk/JV, OJ L 291, 8.11.2003, p. 1, the Commission identified national markets for therapy equipment, inter alia because of wide variations of market shares (ranging from 65-75% in some countries to 5-15% in others). In Commission Decision of 29/06/2007 in Case No COMP/M.4540 - Nestlé/Novartis, OJ C 229, 29.9.2007, p. 1, the Commission identified national markets for nutrition products inter alia, because of "significant unexplained price differences among Member States" and "considerable" differences of the parties and their competitors.

6.1.3.5. Conclusion

- (259) For the reasons illustrated above, the Commission takes the view that with regard to Italy and for the purposes of the assessment of the proposed transaction the geographic market for the supply of white sugar to industrial processors and the market for the supply of white sugar to retailers is national in scope.

6.1.4. *EFFECTS ON COMPETITION / COMPATIBILITY WITH THE INTERNAL MARKET*

(i) Supply of white sugar to industrial processors in Italy

- (260) The following competitive assessment presents a number of factors on the basis of which the Commission concludes that the proposed transaction results in non-coordinated effects in the market for the supply of white sugar to industrial processors in Italy. The Parties' combined market shares are significant in this relevant market for the supply of white sugar to industrial processors in Italy. As a first illustration for the markets for the supply of white sugar to industrial processors and to retailers in Italy, a table below presents the market shares for these two relevant markets as defined by this Decision. It also shows the market shares of the main competitors. The presentation then examines, first, the elements pointing towards price rises before discussing possible expansion of output by competitors, potential buyer power of industrial processors and likely, timely and sufficient entry of new competitors into the relevant market post-merger, in line with the framework for analysing non-coordinated effects in the Guidelines on the Assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings¹⁶⁰ (the "Horizontal Merger Guidelines")¹⁶¹.
- (261) The proposed transaction has the following characteristics and consequences: (i) Südzucker is the most important player on the Italian market for the supply of white sugar to industrial processors, (ii) EDFM is an important player on the same market, (iii) the increment added by the proposed transaction is significant (conservatively estimated at [10-20]*%), (iv) the post-merger market shares are very high (superior to [50-60]*%), (v) Südzucker and EDFM are close competitors and are the two competitors that can most easily adapt their quantities/sales in the Italian market, (vi) post-merger the merged entity would have the incentive and ability to withdraw quantities from Italy, thereby raising prices, (vii) the competitors of the merged entity, established in Italy or outside Italy, face capacity constraints and therefore are unlikely to increase supply if prices increase, and therefore to counteract such market behaviour, (viii) countervailing buyer power appears unlikely to constrain the ability of the merged entity to increase prices post transaction, especially in periods of overall shortage of sugar supply, and (ix) entry post-merger in the relevant market is not likely, sufficient and timely. As a result of all the elements enumerated above, it is concluded that the proposed transaction would significantly impede effective competition, in particular as a result of the creation of a dominant position.

¹⁶⁰ OJ C 31, 5.2.2004, p. 5.

¹⁶¹ Pages 5 – 18 of the Horizontal Merger Guidelines.

6.1.4.1. Introduction

- (262) Italy is the second largest sugar consumer after Germany. In Italy, the annual demand amounts to approximately 1.73 million tonnes of sugar¹⁶², with sugar sold to industrial processors accounting for around 70% of that demand. Italy is one of the largest deficit sugar markets in the Union.
- (263) Prior to the 2006 sugar reform, Italy was mainly supplied with sugar by local producers; COPROB/Italia Zuccheri had a market share of 30%, Eridania Sadam 30%, SFIR 18% and Zuccherificio del Molise 4%. Approximately 18% of Italy was supplied by sugar imports¹⁶³.
- (264) However, as already mentioned, in Italy 15 out of 19 sugar beet factories closed following the 2006 sugar reform. Therefore, prior to the launch of the Brindisi refinery in December 2010, less than half of Italian demand was covered by domestic (beet sugar) production. Apart from the Brindisi refinery, Italian sugar production in 2011 consisted of beet sugar production carried out by three companies:
- (a) Eridania: one beet factory in San Quirico (Parma) with a capacity of [...] tonnes per year¹⁶⁴.
 - (b) COPROB/Italia Zuccheri: one beet factory in Minerbio with a capacity of [...] tonnes per year and one beet factory in Pontelongo with a capacity of [...] tonnes per year¹⁶⁵.
 - (c) Zuccherificio del Molise: one beet factory in Termoli with a capacity of [...] tonnes per year¹⁶⁶.
- (265) If the [...] tonnes per year¹⁶⁷ of cane sugar production capacity of the Brindisi refinery are also taken into account, it follows that at least 875,000 tonnes of the 1.73 million tonnes per year of Italian sugar demand have to be satisfied via imports mainly from the closely located surplus Member States, such as France and Germany.
- (266) Around 60% of all sugar is consumed in the North of Italy. The Centre and South of Italy are in a more disadvantageous situation, as they are located further away from production facilities, with the exception of Brindisi and Termoli, and from the exporting countries. According to internal documents of EDFM, based on an internal logistics model¹⁶⁸, the average transportation costs for imports (mainly from Germany, Austria and France) in the whole of Italy amount to EUR [...] per tonne, while the transportation costs to the Centre and South of Italy amount to EUR [...] per tonne.

¹⁶² See below the reconstructed table of market shares in recitals (336) and (337) of this Decision.

¹⁶³ SFIR's answer to Question 3 of the 2nd RFI in Phase II.

¹⁶⁴ Eridania's reply to the Questionnaire to competitors in Italy.

¹⁶⁵ COPROB's reply to the Questionnaire to competitors in Italy.

¹⁶⁶ Zuccherificio del Molise's reply to the Questionnaire to competitors in Italy.

¹⁶⁷ "Brindisi capacity paper" submitted by EDFM on 2 December 2011. This figure has also been confirmed by SFIR on the cover letter of SFIR addressed to the Commission dated 30 January 2012 (DG 08/2012).

¹⁶⁸ Annex 5b of Südzucker's answer to the 2nd RFI in Phase I.

6.1.4.2. The Italian sugar market structure prior to the proposed transaction

Role of Südzucker

- (267) Südzucker, the leading supplier in Italy, markets and sells refined sugar through the joint venture Maxi Srl (an Italian sugar trader), which Südzucker jointly controls together with Podini Holding S.p.A.
- (268) Even at the beginning of its commercial activity in Italy, direct sales from Südzucker to industrial processors or to retailers had always been very rare¹⁶⁹. Until the end of the 1990s, Südzucker used to sell sugar to various traders in Italy. However, in 2000 Südzucker entered into a cooperation agreement with MAXI, and thus Südzucker's sales in Italy became more and more channelled through MAXI. At the end of 2006, the cooperation agreement between Südzucker and MAXI was substituted by a joint-venture through the acquisition of a 50% stake by Südzucker in MAXI¹⁷⁰.
- (269) [Description of MAXI]*¹⁷¹. [Description of MAXI]*
- (270) As a result, MAXI has been integrated into the overall Union sugar marketing of Südzucker [...]*¹⁷² [Description of MAXI]*¹⁷³.
- (271) Since Italy is the second largest consumer of white sugar in the Union and has a substantial deficit, over the past five years Südzucker has had a clear commercial strategy [Description of Südzucker's strategy]*.
- (272) Südzucker has admitted that the main reason for its focus on the Italian market has been the expectation that Italy would become a large deficit market after the closure of large parts of its domestic beet production¹⁷⁴. Furthermore, Südzucker submitted that it had envisaged supplying to Italy up to [...]* tonnes of sugar per year to Italy¹⁷⁵. Indeed, a presentation from 2006 shows that Südzucker was aiming at supplying approximately [...]* tonnes/year to the Italian market¹⁷⁶.
- (273) In fact, Südzucker has increased its sales volume drastically from approximately [...]* tonnes in 2008¹⁷⁷ to approximately [...]* tonnes in 2010¹⁷⁸ following a very conscious expansion strategy.
- (274) Therefore, today Südzucker is the largest and fastest growing player in Italy.

¹⁶⁹ Südzucker's answer to Question 17 of the 3rd RFI in Phase II.

¹⁷⁰ Südzucker's answer to Question 17 of the 3rd RFI in Phase II.

¹⁷¹ Südzucker's answer to Question 19 of the 3rd RFI in Phase II. See also [...]* presentation in Annex 23 of 2nd RFI and SZ's reply to the 6(1c) Dec. [...]*.

¹⁷² Südzucker's answer to Question 19 of the 3rd RFI in Phase II. See also [...]* presentation in Annex 23 of 2nd RFI and SZ's reply to the 6(1c) Dec.

¹⁷³ Südzucker's answer to Question 17 of the 3rd RFI in Phase II.

¹⁷⁴ Südzucker's answer to Question 17 of the 3rd RFI in Phase II.

¹⁷⁵ Südzucker's answer to Question 17 of the 3rd RFI in Phase II.

¹⁷⁶ Presentation of Commercial Director [...]* dated 17 July 2006, chart 6, provided as Annex 23 of Südzucker's reply to the 2nd RFI in Phase I.

¹⁷⁷ Annex Q16-1 (chart at p. 16) of Südzucker's answer to the 3rd RFI in Phase II.

¹⁷⁸ Annex Q16-7.3.a of Südzucker's answer to the 3rd RFI in Phase II.

Role of EDFM

- (275) In 2008, EDFM engaged in a [...] joint-venture with SFIR. The joint-venture was the Brindisi refinery and its purpose was to build and operate a new raw cane refinery in Brindisi, in the south of Italy.
- (276) Both EDFM and SFIR made considerable investments in SRB. The whole project was originally budgeted at EUR [...] million¹⁷⁹, but an additional contribution of EUR [...] million¹⁸⁰ was made in September 2010.
- (277) Both EDFM and SFIR exercise control over SRB. The voting shares in SRB are held [...] between the two partners. [Description of SRB]¹⁸¹. [Description of SRB]¹⁸².
- (i) EDFM jointly controls with SFIR the sales of white sugar from the Brindisi refinery to industrial processors in Italy
- (278) According to the Parties, ESI, a 100% subsidiary of SFIR in charge of [...], buys in principle [...] white sugar produced by SBR. From December 2010 to October 2011, SRB sold [...] tonnes to ESI, while exporting [...] tonnes to [...] and [...] tonnes to [...]¹⁸³.
- (279) The Parties claim that EDFM [...] the sugar produced in the Brindisi refinery¹⁸⁴ and thus SRB is in their view [...] of the sugar produced. They argue that sugar originating in the refinery is sold [...] to ESI, who then relying on its historical customer relationships and storage facilities [Description of SRB and ESI].
- (280) However, the investigation with regard to the role of EDFM in the sales and marketing of the white sugar produced by SRB does not confirm the Parties' claim. In fact, internal documents show that [Description of SRB].
- (281) The SRB joint-venture agreement between EDFM and SFIR states that the purpose of the joint-venture is to *refine, sell and distribute* sugar¹⁸⁶. Indeed, the partners even agreed [Description of SRB]¹⁸⁷. [Description of SRB].
- (282) Furthermore, in the markets for the supply of white sugar it is the supplied quantity that directly determines the price. This has been illustrated by Südzucker in the Oral Hearing of 5 March 2012: [...] ¹⁸⁸. Given that it is the Brindisi refinery that

¹⁷⁹ Answer to the 2nd request for information to EDFM of 27 September 2011, "Information Memorandum SFIR/ED&F Man Brindisi Project" of 4 June 2009.

¹⁸⁰ Answer to the 2nd request for information to EDFM of 27 September 2011, SFIR Raffineria di Brindisi Spa - Operational Progress Report of 15th April 2011.

¹⁸¹ Article 5 of the Brindisi Joint Venture Agreement.

¹⁸² See for instance "White paper on Brindisi" submitted on 19 October 2011.

¹⁸³ Annex Q16-1 (p. 19) of Südzucker's answer to the 3rd RFI in Phase II.

¹⁸⁴ Form CO, p.27.

¹⁸⁵ EDFM's answer to the 1st RFI of 26 September 2011 and answer to the 2nd RFI of 27 September 2011.

¹⁸⁶ Article 3 of the Brindisi Joint Venture Agreement (Annex 1.a of EDFM's reply to the 2nd RFI in Phase I), which states that the business of SRB is [...].

¹⁸⁷ Article 14 of the Brindisi Joint Venture Agreement submitted as Annex 1.a of EDFM's reply to the 2nd RFI in Phase I.

¹⁸⁸ Statement by Wolfgang Heer, Südzucker, during the Oral Hearing of 5 March 2012 (minute 43:55 to 44:36 of recording C-15.50-16.42).

determines the quantities that ESI can sell in Italy, necessarily it is also the Brindisi refinery that determines the price at which those quantities will be sold.

- (283) In the Brindisi refinery, the production output and sales of the refined sugar are discussed [Description of SRB]*¹⁸⁹, where there is [Description of SRB]*¹⁹⁰. [Description of SRB]*. In this respect, the argument of the Parties that [Description of SRB]* is immaterial. The fact that [Description of SRB]* indicates its influence on marketing.
- (284) The internal documents submitted by EDFM also demonstrate that [Description of SRB]*¹⁹¹. In particular, the internal document entitled as [...] *¹⁹² indicates that [Description of SRB]*.
- (285) Moreover, the [...] * minutes of [...] * state that [Description of SRB]*¹⁹³. According to the minutes of [...] *,¹⁹⁴. During that meeting, the participants also agreed [Description of SRB]*¹⁹⁵.
- (286) The minutes of meetings of [...] * further demonstrate that, [Description of SRB]*¹⁹⁶. [Description of SRB]*¹⁹⁷, [Description of SRB]*. This is also demonstrated by the sale of [...] * tonnes to [...] * and [...] * tonnes to [...] * by SRB¹⁹⁸.
- (287) The minutes of the meeting of [...] * of [...] * indicate that [Description of SRB]* and further support that ESI acts [Description of SRB and ESI]* as [Description of SRB and ESI]* for the joint venture rather than [Description of SRB and ESI]*¹⁹⁹.
- (288) The reason for EDFM's active participation in the value created through refining and production of white sugar can be found in the business case study for Brindisi, which EDFM conducted prior to the creation of SRB. This study did not solely concern the supply of raw cane sugar, but also covered extensively the economics of the Italian white sugar market²⁰⁰.
- (289) Indeed, EDFM has a strong financial interest to control the selling activity of SRB. The total capital expenditure for the Brindisi refinery project is quite substantial, amounting to approximately EUR [...] * million. The raw cane supplies to the Union are currently particularly tight and the [...] *. As the initial business case study

¹⁸⁹ Annex 5.b in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I; Annex 5.c in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

¹⁹⁰ EDFM's reply to the 6th RFI in Phase I.

¹⁹¹ Annex 15 of EDFM's answer to the 6th RFI of 11 October 2011.

¹⁹² Annex 17 of EDFM's answer to the 6th RFI in Phase I.

¹⁹³ Annex 5.b in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

¹⁹⁴ Annex 5.c in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

¹⁹⁵ Annex 5.c in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

¹⁹⁶ See for instance the minutes of the Board meeting of 19 May 2009 in Annex 7.b of EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

¹⁹⁷ EDFM's reply to Question 9 of the 6th RFI in Phase I.

¹⁹⁸ Annex Q16-1 (p. 19) of Südzucker's answer to the 3rd RFI in Phase II.

¹⁹⁹ Annex 5.b in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

²⁰⁰ See, for example, the "Information Memorandum", the "Project Overview" and the "Competitive Analysis of supplying Sugar to the Italian Market", submitted respectively as Annexes 4, 5.a and 5.b of EDFM's answer to the 2nd RFI in Phase I.

indicates [Description of SRB]*²⁰¹. [Description of SRB]*²⁰². [Description of SRB]*²⁰³ [Description of SRB]*.

- (290) In its reply to the Statement of Objections²⁰⁴, Südzucker claimed that the sales of white sugar produced by SRB should not be attributed to EDFM.
- (291) First, according to Südzucker, SRB is in charge of "wholesale" sales to ESI, whereas ESI is in charge of the "retail" sales to the industrial processors and retailers. [Description of SRB]* Südzucker believes that the mention in the [...] minutes of [...] is a normal mechanism when a production company sells to a marketing and sales company. In this context, ESI's sales of white sugar (quality, quantity and prices) were discussed on [...] and a discussion on the creation of [...] took place. [Description of SRB]*.
- (292) Second, the plan that ESI would [Description of SRB and ESI]* was a proposal that was never implemented²⁰⁵.
- (293) Third, Südzucker submitted that the purpose of the [...] clause in the Brindisi Joint-Venture Agreement (the "JV Agreement")²⁰⁶ was only to [Description of SRB]*.
- (294) Fourth, the documents in preparation of the SRB project²⁰⁷, where EDFM and SFIR discuss extensively the economics of white sugar sales in Italy and average prices that could be achieved, are not evidence that SRB would market white sugar in Italy.
- (295) The above arguments put forward by the notifying party cannot be accepted. The sales of white sugar produced by SRB should be attributed to EDFM, [Description of SRB and ESI]*.
- (296) First, ESI's sales to industrial customers and to retailers cannot constitute "retail" sales, since these customers are still supplied at the wholesale level. It is retailers that then sell at the retail level to the end-customers. [Description of SRB and ESI]* this argument does not alter the conclusion that it is SRB [Description of SRB and ESI]* for the white sugar produced in Brindisi. In that regard, SRB does not need to know individual clients and prices of ESI.
- (297) For SRB to make [Description of SRB and ESI]*²⁰⁸ [Description of SRB and ESI]* is sufficient. On the basis of [Description of SRB and ESI]*, SRB can set the price at which it sells white sugar to ESI [Description of SRB and ESI]*.
- (298) [Description of SRB and ESI]*.

²⁰¹ See the "Information Memorandum" submitted as Annex 4 of EDFM's answer to the 2nd RFI in Phase I.
²⁰² "Operational Progress Report" submitted as Annex 5.c of EDFM's answer to the 2nd RFI.
²⁰³ EDFM's answer to the 3rd RFI in Phase I.
²⁰⁴ Paragraphs 108 *et seq.*
²⁰⁵ Annex 5.b in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.
²⁰⁶ Article 3 of the Brindisi Joint Venture Agreement, which states that the business of SRB is [...]*.
²⁰⁷ See, for example, the "Information Memorandum", the "Project Overview" and the "Competitive Analysis of supplying Sugar to the Italian Market", submitted respectively as Annexes 4, 5.a and 5.b of EDFM's answer to the 2nd RFI in Phase I.
²⁰⁸ As demonstrated *inter alia* in the document "ESI transfer price analysis" submitted as Annex 17 of EDFM's answer to the 6th RFI in Phase I.

- (299) Second, even if the plan that ESI [Description of SRB and ESI]* was an unimplemented proposal²⁰⁹, the fact that this proposal was discussed and almost implemented in the SRB [...] shows that SRB [Description of SRB]* and that EDFM [Description of SRB]*.
- (300) Third, if SRB were [Description of SRB]* and each party to the joint venture wanted to ensure that [Description of SRB]*, a [...] clause would be unnecessary and irrelevant, since [Description of SRB]*. In fact, if SRB were [Description of SRB]* it would not be conceivable that [...]. Nevertheless, the [...] clause of the Joint Venture Agreement states that [Description of SRB]*²¹⁰.
- (301) Fourth, if SRB were a [Description of SRB]*, EDFM and SFIR would have only analysed the ways to efficiently produce white sugar from raw cane. Nevertheless, the fact that [Description of SRB]*²¹¹ also points towards the conclusion that [Description of SRB]*.
- (302) In the light of the above and, in particular, EDFM's active participation in [Description of SRB]* and the [Description of SRB]*, the refined sugar sales of the refinery should be attributed to EDFM. Therefore, EDFM controls SRB, which markets the white sugar it produces, and thus the sales of white sugar produced by SRB should be attributed to EDFM.
- (ii) EDFM has secured the supply of raw cane sugar input to the Brindisi refinery
- (303) SRB benefits from three [...] contracts [...]²¹²: [contracts with Supplier A, Supplier B and Supplier C]*
- (304) Therefore, in times of scarcity of raw cane sugar for refineries in the Union, the Brindisi refinery has secured the input of at least [...] tonnes [...].
- (305) Moreover, EDFM has also concluded two other [...] contracts: (i) the contract with [...] in [...], which gives [...], and (ii) the contract with [...] in [...]²¹³.
- (iii) EDFM's participation in the DAI refinery
- (306) SFIR does not only depend on EDFM with respect to the [...] supply contracts secured for the Brindisi refinery, but also with respect to the operation of the DAI refinery, which is situated in Coruche (Portugal) located approximately 65km from the Port of Setubal. The current shareholders of the DAI refinery are EDFM with [...]*%, SFIR with [...]*%, "Sociedade Industrial de Açúcar" with [...]*% and "Caixa de Crédito Agrícola Mútuo de Coruche" with [...]*%. Originally a sugar beet factory, since 2007 the DAI refinery has re-focused its operations on refining due to the sugar reform. Over the first three years of the sugar reform, DAI has renounced its entire

²⁰⁹ Annex 5.b in EDFM's answer to the 5th RFI of 7 October 2011 in Phase I.

²¹⁰ Annex 1.a of EDFM's reply to the 2nd RFI in Phase I.

²¹¹ See, for example, the "Information Memorandum", the "Project Overview" and the "Competitive Analysis of supplying Sugar to the Italian Market", submitted respectively as Annexes 4, 5.a and 5.b of EDFM's answer to the 2nd RFI in Phase I.

²¹² Annexes 3a, 3b and 3c of EDFM's answer to the 3rd RFI in Phase I.

²¹³ EDFM's answer to the 3rd RFI in Phase I.

beet quota to the Union restructuring fund and is concentrating on achieving maximum refinery output and sales, in line with the refinery's designed capacity of [...] tonnes/year²¹⁴.

Role of other sugar suppliers

- (307) Due to the negative impact of the 2006 sugar reform in Italy in terms of sugar production, the traditional Italian sugar manufacturers, such as Eridania, COPROB/Italia Zuccheri and SFIR, have been trying to maintain their "pre-reform" market share. In that context, they have established joint-ventures mainly with manufacturers from surplus Member States, and/or are building raw cane refining facilities, in order to satisfy the demand of their customers.
- (308) In that context, the following developments have taken place:
- (a) the German sugar manufacturer Pfeifer & Langen has acquired 49.9% of the sales subsidiary of COPROB/Italia Zuccheri ;
 - (b) the British sugar manufacturer Tate & Lyle had established a joint-venture with Eridania for the marketing and sales of all their sugar products. In the course of 2011, Tate & Lyle left the Italian market (because it did not have sufficient raw sugar input) and subsequently the French sugar manufacturer Cristal Union via CristalCo stepped in and replaced it in the joint-venture with Eridania;
 - (c) SFIR has gone into a different direction by building a new refinery in a joint-venture with EDFM in the South of Italy (SRB). Meanwhile, SFIR also bought white sugar from other players, such as EuroSugar (Nordzucker, Sucre Union, EDFM) in order to satisfy the demand of its customers;
 - (d) the French sugar manufacturer Tereos has entered the market by establishing its own national sales office for Italy. However, this does not break the pattern of joint-venture entry in Italy for the following reasons: (i) Tereos' entry took place in 2006, thus very early in the reform at a period when producers still disposed significant volumes of sugar; and (ii) Tereos' market share in Italy has remained stable over the past years and is way below that of other foreign players, such as Südzucker who teamed up with MAXI the same year and has increased its presence significantly over the last 5 years.

Wholesalers

- (309) In the Form CO and in the first two Requests for Information, the Parties did not mention wholesalers as a competitive force in the Italian market. In the market shares submitted in the 2nd Request for Information²¹⁵, the Parties only identified Eridania/Tate & Lyle, Pfeifer & Langen/COPROB/Italia Zuccheri, SFIR and Tereos as competitors in the markets for sales of white sugar to industrial processors and to retailers in Italy.

²¹⁴ EDFM's answer to Question 4 of the 3rd RFI in Phase I.

²¹⁵ Annex 19 of Südzucker's answer to the 2nd RFI in Phase I.

- (310) However, when the issue of EDFM's control over the Brindisi refinery was raised, and thus that its sales should be attributed to EDFM, the Parties submitted new market share estimations²¹⁶. These new estimations included a new category of suppliers, the "wholesalers", to whom the Parties attributed 20% of the market for sales to industrial processors and 18% of the market for sales to retailers in Italy.
- (311) According to Südzucker, wholesalers constitute a significant competitive factor in the Italian sugar market. Wholesalers have a multitude of sources which they can easily change and the volume that they trade amounts to approximately 20% of total consumption. It is also put forward by the notifying party in this context that wholesalers fulfil transparency and arbitrage functions in a perfectly competitive Italian market. Finally, according to Südzucker, wholesalers have very good relationships with the customers, and the supplier's brand is irrelevant in the Italian sugar market.
- (312) However, Südzucker acknowledged that wholesalers obtain a large proportion of their sales volumes from the same producers and/or importers who are selling also directly to industrial processors and retailers in Italy²¹⁷. SFIR has also stated that wholesalers are mostly active in servicing customers (industrial processors and retailers) who need special service requirements or who require only small volumes, in particular hotels, restaurants, catering, bars, bakeries, patisseries²¹⁸.
- (313) According to the second phase market investigation²¹⁹, only 6 out of 33 customers consider wholesalers as a significant competitive constraint on white sugar producers/suppliers in Italy, whereas more than half of the customers do not have any business relationship with wholesalers. Furthermore, only 5 out of 12 wholesalers consider themselves to constitute competitive constraints on existing producers/suppliers in Italy. Moreover, with one exception, none of the producers/suppliers who are active in Italy considers wholesalers as a competitive constraint on them.
- (314) During the second phase market investigation²²⁰, approximately 1/3 of customers were of the view that wholesalers import part of their sugar supplies from sources different from the existing producers/suppliers in Italy. On their part, all wholesalers replied that they purchase from 2/3 to 100% of their supplies from existing producers/suppliers in Italy, with the exception of one wholesaler who purchases approximately 1/3 of its supplies from existing producers/suppliers in Italy. In any event, even under the broadest interpretation of the data from the market investigation, the wholesalers' total sugar supplies from sources different than the existing producers/suppliers in Italy would not exceed 50,000-70,000 tonnes per year.

²¹⁶ Annex 4 of Südzucker's answer to the 3rd RFI in Phase I.

²¹⁷ Südzucker's answer to Question 25 of the 3rd RFI in Phase II.

²¹⁸ SFIR's answer to Question 58 of the 2nd RFI in Phase II.

²¹⁹ Questionnaire to sugar customers – Phase II.

²²⁰ Questionnaire to sugar customers – Phase II.

- (315) Moreover, internal documents of the Parties only distinguish between sales to [...] while not even mentioning sales to wholesalers as a distinct category of sales²²¹. Therefore, the Parties themselves regard the wholesalers as pure intermediaries that cannot exercise arbitrage.
- (316) When the Parties were requested to present internal documents supporting that wholesalers are perceived as competitors for the sale of white sugar in Italy, the Parties admitted that they were unable to provide such documents²²². The only such document that the Parties could provide at a much later stage²²³ was the presentation held by Mr [...] on the acquisition of a 50% stake in MAXI, where wholesalers MAXI, Inagra and Csapo were allegedly presented on equal footing with the sugar producers Italia Zuccheri/COPROB, Eridania/Saddam and SFIR.
- (317) However, that presentation was dated on 17 July 2006. Such a document of more than five years ago cannot reflect the (drastically altered) situation in the Italian white sugar markets post-reform. Indeed, prior to the 2006 sugar reform, wholesalers might have had a different role because of the different market structure in the Italian sugar market. Until 2006, sugar wholesalers might have been able to have an impact on the Italian white sugar markets, since Italian and Union production were higher and wholesalers could buy from different sources. Thus, it cannot be excluded that until 2006 wholesalers might have played an arbitrage role and thus possibly contributed to a price decrease. Today, however, the lack of available sugar supply as well as the sales agencies put in place by the large sugar market producers/suppliers, such as MAXI, certainly leave very little room for manoeuvre for wholesalers in the Italian deficit markets²²⁵.
- (318) Furthermore, Südzucker does not systematically monitor wholesalers (if it does so at all), since the abovementioned presentation was the one and only internal document that Südzucker could invoke as evidence for the wholesalers' alleged role as competitors in the Italian sugar markets. In particular, this presentation analyses [...] and therefore its focus was on alternative wholesalers active in the market, irrespective of their ability to set/constrain prices in the market.
- (319) The presentation also demonstrates that [...]. It also shows that all important wholesalers are systematically coupled with an important sugar producer²²⁶. Indeed, MAXI, Inagra and Csapo are clearly indicated to be wholesalers as opposed to producers and in particular MAXI is portrayed as a partner of [...] Csapo as a partner of [...] and Inagra as [...] and delivered by [...]. Therefore, this presentation also stresses the economic dependency of these wholesalers from producers.
- (320) Moreover, when contacted during the market investigation²²⁷, the Autorità Garante della Concorrenza e del Mercato, the Italian NCA, also confirmed the Commission's

²²¹ See, for example: Annex 8 of Südzucker's answer to the 3rd RFI in Phase I; Annex 17 of EDFM's answer to the 6th RFI in Phase I.

²²² Südzucker's answer to Question 2.e of the 5th RFI in Phase I.

²²³ Südzucker's answer to Question 25 of the 3rd RFI in Phase II.

²²⁴ Annex 23 of Südzucker's answer to the 2nd RFI in Phase I.

²²⁵ See, for instance, minutes of the conference call with Achard Italia on 15 December 2011.

²²⁶ Annex 23 of Südzucker's answer to the 2nd RFI in Phase I, at pages 9-10.

²²⁷ Conference call on 1 December 2011.

understanding that wholesalers do not exercise a competition constraint in the Italian sugar markets.

- (321) In its reply to the Statement of Objections²²⁸, Südzucker restated its views on the competitive role of wholesalers.
- (322) First, the notifying party claimed that wholesalers source quantities of sugar from sources different from the existing suppliers in the Italian sugar markets. Wholesalers source on average 1/3 of their requirements abroad, which amounts to more than 110,000 tonnes of white sugar. Moreover, seven wholesalers import sugar from Croatia and Serbia.
- (323) Second, it was claimed that the majority of customers view wholesalers as a competitive force in Italy and five out of twelve wholesalers consider themselves as competitive constraint on sugar producers in Italy.
- (324) Third, wholesalers account for [20-30]*% of total consumption and without them Südzucker would have never reached sales of [...]* tonnes/year. Südzucker has named [...]* wholesalers that could sell more sugar in Italy. Half of the customers have business relationships with wholesalers. Südzucker's internal documents do not mention wholesalers because they are an Italian particularity and, in any event, Südzucker's internal documents do not mention much about other competitors either.
- (325) The above arguments put forward by the notifying party cannot be accepted. For the following reasons, wholesalers cannot be regarded as competitors in the markets for the supply of white sugar to industrial processors in Italy and to retailers.
- (326) First, Südzucker's claim that wholesalers source on average 1/3 of their requirements abroad is not based on any evidence. On the contrary, during the market investigation all wholesalers replied that they purchase from 2/3 to 100% of their supplies from existing producers/suppliers in Italy, with the exception of one wholesaler who purchases approximately 1/3 of its supplies from existing producers/suppliers in Italy²²⁹.
- (327) Even under the broadest interpretation of the data from the market investigation, the wholesalers' total sugar supplies from sources different than the existing producers/suppliers in Italy would not exceed 50,000-70,000 tonnes per year. This quantity is very small compared to total Italian consumption of 1.73 million tonnes/year. Furthermore, imports from Croatia to the Union are expected to significantly decrease post-accession as analysed in recitals (509) to (514) of this Decision.
- (328) Second, only five out of twelve wholesalers consider themselves as competitive constraint on sugar producers in Italy and the majority of wholesalers do not share that view. Most importantly, with one exception, none of the producers/suppliers who are active in Italy considers wholesalers as a competitive constraint on them.

²²⁸ Paragraphs 203 *et seq.*

²²⁹ Statement of Objections, para. 195.

- (329) Third, the fact that 20% of sales in Italy might be passing through wholesalers as pure intermediaries does not render wholesalers competitors, since the existing producers/suppliers remain in full control of these quantities and, in essence, the prices at which they are sold. If wholesalers played such an important competitive role in Italy, as the Parties claim, there should be at least one internal document of Südzucker, MAXI or EDFM mentioning the allegedly special role of wholesalers in Italy.
- (330) Therefore, the arguments submitted by Südzucker for the attribution of sales to Italian "wholesalers" in the Italian markets for the sale of white sugar to industrial processors and to retailers cannot be accepted within the course of the assessment of the proposed transaction.
- (331) In view of the above, it is concluded that wholesalers are not regarded as competitors in the Italian markets for sales of white sugar to industrial processors and to retailers.

Market shares of the Parties and their competitors

- (332) In the Form CO, the notifying party submitted that the Parties' activities did not overlap in Italy, where only Südzucker was allegedly active as a supplier of white sugar with market shares of [40-50]*% (regarding sales to industrial processors) and [10-20]*% (regarding sales to retailers). In particular, the Parties submitted the following table,²³⁰ where Südzucker's sales and market shares were calculated over the period from March 2010 to February 2011, whereas EDFM's sales and market shares were calculated over the period from October 2009 to September 2010. The notifying party thus attributed no sales to EDFM in Italy, where the Brindisi refinery had started operating in December 2010.

²³⁰ Annex 7.3.a of the Form CO.

	White sugar sales to industrial processors, including liquefied white sugar, refined cane sugar		White sugar sales retailers	
	Qty in mt	Market share in % of Qty	Qty in mt	Market share in % of Qty
Total market 2009/2010 (without sales to Ethanol industry)	[...]*	[90-100]*	[...]*	[90-100]*
Südzucker 2010/2011	[...]*	[40-50]*	[...]*	[10-20]*
[...]*	[...]*			
ED&F MAN 2009/2010		-		-
[...]*	[...]*	[40-50]*	[...]*	[10-20]*
Eridania / Tate & Lyle	[...]*	[20-30]*	[...]*	[30-40]*
Italia Zuccheri / Pfeifer & Langen	[...]*	[10-20]*	[...]*	[20-30]*
SFIR	[...]*	[10-20]*	[...]*	[10-20]*
Tereos	[...]*	[10-20]*	[...]*	[10-20]*

(333) When the issue of EDFM's control over the Brindisi refinery was raised, and in particular that its sales should be attributed to EDFM, the notifying party submitted new market share estimates.²³¹ As explained above, the new data included a new category of suppliers, the "wholesalers",²³² to whom the Parties attributed 20% of the market for sales to industrial processors and 18% of the market for sales to retailers in Italy. Furthermore, the notifying party attributed a significant amount of sales to "others",²³³ although Südzucker admitted that it could not provide accurate estimates of companies and quantities supplied in Italy under this vague category.²³⁴ In particular, for the period from January 2011 to September 2011, the Parties submitted the following table:

²³¹ Südzucker's reply to the 4th RFI in Phase I.

²³² This category has been highlighted in red in the table that follows.

²³³ This category has been highlighted in red in the table that follows.

²³⁴ Südzucker's answer to Question 1 of the 5th RFI in Phase I.

	White sugar sales to industrial processors		White sugar sales retailers	
	Qty in mt	Market share in % of Qty	Qty in mt	Market share in % of Qty
Jan - Sep 11 (without sales to Ethanol industry)	[...]*	[90-100]*%	[...]*	[90-10]*%
Südzucker	[...]*	[20-30]*%	[...]*	[10-20]*%
ED&F MAN incl Brindisi	[...]*	[10-20]*%	[...]*	[10-20]*%
[...]*	[...]*	[30-40]*%	[...]*	[20-30]*%
Eridania / Tate&Lyle	[...]*	[10-20]*%	[...]*	[20-30]*%
Italia Zuccheri / Pfeifer & Langen	[...]*	[10-20]*%	[...]*	[10-20]*%
SFIR (exc. Brindisi)	[...]*	[0-5]*%		[0-5]*%
Tereos	[...]*	[5-10]*%	[...]*	[0-5]*%
[...]*	[...]*	[5-10]*%	[...]*	[0-5]*%
Zuccherificio del Molise	[...]*	[0-5]*%	[...]*	[0-5]*%
[...]*	[...]*	[20-30]*%	[...]*	[20-30]*%

(334) However, the market shares submitted by the Parties were not considered credible, in particular for the following reasons:

- (a) The volumes of sales attributed to specific competitors were only the Parties' estimates without any concrete and objective basis for such allegations.
- (b) Wholesalers were attributed a volume of sales as an alleged category of sellers, whereas no sales were attributed individually to each of them. Moreover, the sales attributed to wholesalers were only the Parties' estimates without any concrete and objective basis for such allegations.
- (c) Most importantly, for the reasons analysed under recitals (309) to (331) of this Decision, wholesalers cannot be regarded as competitors in the Italian markets for sales of white sugar to industrial processors and to retailers, and thus no market share should be attributed to them.

(335) Therefore, a market reconstruction on the basis of credible data was necessary. In that market reconstruction, producers' sales to wholesalers were attributed either to industrial processors or to retailers, according to who was the final customer. The fact that producers were able to give precise estimates of the percentage of their sales to wholesalers which is finally sold to industrial processors or to retailers confirms that wholesalers are not competitors in the Italian sugar markets, but pure intermediaries between producers and customers, in line with the reasoning under recitals (309) to (331) of this Decision.

(336) The following table shows the sales of white sugar (in metric tonnes) to industrial processors and to retailers in Italy from 1 January 2011 to 31 October 2011:

	sales to industrial processors		sales to retailers		sales to industrial processors and retailers	
	volume	market share	volume	market share	volume	market share
Südzucker ²³⁵	[...]*	[30-40]*%	[...]*	[10-20]*%	[...]*	[30-40]*%
EDFM (incl. Brindisi) ²³⁶	[...]*	[10-20]*%	[...]*	[10-20]*%	[...]*	[10-20]*%
Südzucker/EDFM combined	[...]*	[40-50]*%	[...]*	[30-40]*%	[...]*	[40-50]*%
COPROB/Italia Zuccheri/Pfeifer & Langen ²³⁷	[...]*	[20-30]*%	[...]*	[10-20]*%	[...]*	[20-30]*%
Tereos ²³⁸	[...]*	[10-20]*%	[...]*	[5-10]*%	[...]*	[10-20]*%
Eridania/Cristal Union ²³⁹	[...]*	[5-10]*%	[...]*	[30-40]*%	[...]*	[10-20]*%
Zuccherificio del Molise ²⁴⁰	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Société Vermandoise ²⁴¹	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Sunoko ²⁴²	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%

²³⁵ Südzucker's answer to the 6th RFI in Phase II. This is a conservative basis for the calculation of Südzucker's share in the market for the supply of white sugar to industrial processors. As a way of example, Annex Q21-1 of Südzucker's reply to the 3rd RFI in Phase II shows that from January 2011 to September 2011 the ratio of sales to industrial processors over sales to retailers was [...]*, as opposed to a ratio of [...]* on the basis of Südzucker's answer to the 6th RFI in Phase II.

²³⁶ Confidential information provided by SFIR.

²³⁷ Questionnaire to sugar competitors – Phase II.

²³⁸ Questionnaire to sugar competitors – Phase II.

²³⁹ Questionnaire to sugar competitors – Phase II.

²⁴⁰ Questionnaire to sugar competitors – Phase II.

²⁴¹ Questionnaire to sugar competitors – Phase II.

²⁴² Questionnaire to sugar competitors – Phase II.

	sales to industrial processors		sales to retailers		sales to industrial processors and retailers	
	volume	market share	volume	market share	volume	market share
Total volume of competitors	[...]*	[40-50]*%	[...]*	[60-70]*%	[...]*	[50-60]*%
Total market volume	1,013,039	100%	363,182	100%	1,377,028	100%

(337) The following table shows the forecasted sales of white sugar (in metric tonnes) to industrial processors and to retailers in Italy for the campaign year 2011/2012 (from October 2011 to September 2012):

	sales to industrial processors		sales to retailers		sales to industrial processors and retailers	
	volume	market share	volume	market share	volume	market share
[...]* ²⁴³	[...]*	[30-40]*%	[...]*	[20-30]*%	[...]*	[30-40]*%
[...]* ²⁴⁴	[...]*	[10-20]*%	[...]*	[10-20]*%	[...]*	[10-20]*%
[...]*	[...]*	[50-60]*%	[...]*	[30-40]*%	[...]*	[40-50]*%
COPROB/Italia Zuccheri/Pfeifer & Langen ²⁴⁵	[...]*	[20-30]*%	[...]*	[10-20]*%	[...]*	[20-30]*%
Tereos ²⁴⁶	[...]*	[10-20]*%	[...]*	[0-5]*%	[...]*	[10-20]*%
Eridania/Cristal Union ²⁴⁷	[...]*	[5-10]*%	[...]*	[30-40]*%	[...]*	[10-20]*%
Zuccherificio del Molise ²⁴⁸	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Société Vermandoise ²⁴⁹	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%

²⁴³ The forecast of overall sugar sales of [...]* tonnes for the campaign year 2011/2012 is based in the internal document submitted as Annex 6 in Südzucker's answer to the 3rd RFI in Phase I. This figure is then attributed between sales to industrial processors and sales to retailers on the basis of the ratios provided in Südzucker's answer to the 6th RFI in Phase II (including the clarification received by email on 13 January 2012).

²⁴⁴ Internal document entitled as "ESI's sales forecast for 2012" and submitted by EDFM on 13 January 2012.

²⁴⁵ Questionnaire to sugar competitors – Phase II.

²⁴⁶ Questionnaire to sugar competitors – Phase II.

²⁴⁷ Questionnaire to sugar competitors – Phase II.

²⁴⁸ Questionnaire to sugar competitors – Phase II.

	sales to industrial processors		sales to retailers		sales to industrial processors and retailers	
	volume	market share	volume	market share	volume	market share
Sunoko ²⁵⁰	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Total volume of competitors	[...]*	[40-50]*%	[...]*	[60-70]*%	[...]*	[50-60]*%
Total market volume	1,278,112	100%	453,827	100%	1,731,939	100%

- (338) Therefore, on the basis of the market reconstruction the Parties appear to have high combined market shares, especially in the market for sales of white sugar to industrial processors in Italy. According to the estimates of the 2011/2012 campaign for sales of white sugar to industrial processors, the pre-transaction clear market leader (Südzucker) joins forces with the 3rd largest player in the market (EDFM including SRB) post-merger. As a result, it is likely that the merged entity would have market shares above [50-60]*% ([50-60]*%) on a market that is already concentrated. The next largest competitor COPROB would have market shares slightly above [10-20]*%. Tereos ([10-20]*%) and Eridania ([5-10]*%) follow with no other player having more than 5%.
- (339) Furthermore, the two tables above are a conservative reconstruction of the Parties' market shares, given that according to the Horizontal Merger Guidelines "*[n]ormally, the Commission uses current market shares in its competitive analysis. However, current market shares may be adjusted to reflect reasonably certain future changes, for instance in the light of exit, entry or expansion*"²⁵¹.
- (340) The combined market shares of the Parties as illustrated in the two tables above should be considered to reflect conservative estimations of their market position, since SRB is still in the initial stages of its start-up period. [Description of SRB]*.²⁵²
- (341) Furthermore, Südzucker's forecasted sales for campaign year 2011/2012 are based on internal planning documents²⁵³, which constitutes the most detailed and substantiated source for this forecast. The Parties themselves have not contested the validity of these internal planning documents or the figures contained therein. The use of the 2011/2012 forecasted sales contained in these planning documents is still a conservative basis, since Südzucker's actual sales tend to exceed its planned sales in a given campaign year²⁵⁴.

²⁴⁹ Questionnaire to sugar competitors – Phase II.

²⁵⁰ Questionnaire to sugar competitors – Phase II.

²⁵¹ Horizontal Merger Guidelines, para. 15.

²⁵² Draft Form RM submitted by the Parties on 16 January 2012, paras 16 and 37.

²⁵³ Annex 6 in Südzucker's answer to the 3rd RFI in Phase I.

²⁵⁴ See, for example, the actual sales of MAXI in campaign year 2010/2011, which exceeded by approximately [...]* tonnes its planned sales for that same year (Annex 8 of Südzucker's reply to the 3rd RFI in Phase I).

- (342) Even on the basis of such conservative estimations, post-transaction the Parties would become the clear leader in the market for white sugar sold to industrial processors with a combined market share of [50-60]*% for the campaign year 2011/2012, while the remaining competitors would have significantly lower market shares.
- (343) In addition, according to the Horizontal Merger Guidelines and settled case-law, *"very large market shares - 50 % or more - may in themselves be evidence of the existence of a dominant market position"*²⁵⁵. Since the Parties' combined market share post-transaction in Italy would reach at least [50-60]*%, this also evidences the creation of a dominant position of the Parties which would allow them to behave independently of competitors and customers.
- (344) Furthermore, the Parties' market shares should be seen dynamically, in order to obtain a more realistic estimation of their market power post-transaction. First, the production of the Brindisi refinery will be at least [...] tonnes per year of white sugar, after its start-up period, as analysed under recitals (361) to (364) of this Decision. Secondly, Südzucker can easily expand in Italy by reallocating sugar across different Member States, since it benefits from the highest quota in the Union of approximately [...] tonnes per year²⁵⁶, which amounts to around [...] of total sugar quota production in the Union. For example, in 2010 Südzucker managed to direct [...] tonnes of white sugar into Italy from other Member States.²⁵⁷ At the same time, all other competitors have limited abilities and no incentive to expand in Italy, as analysed under recitals (393) *et seq.* of this Decision. Thus, in the near future the merged entity could sell [...] tonnes/year of white sugar out of the approximately 1.73 tonnes/year of Italian consumption (for industrial processors and retailers combined).
- (345) In its reply to the Statement of Objections, Südzucker claimed that the combined market share of the Parties amounted to [40-50]*%, i.e. [20-30]*% for Südzucker and [10-20]*% for ESI/SFIR/EDFM, on the basis of a market volume of 1.73 million tonnes per year.
- (346) Nevertheless, Südzucker's calculation of the combined market share of the Parties is manifestly incorrect. First and most importantly, Südzucker calculated and provided an "overall" combined market share, since it took into account the volumes both in the market for the supply of white sugar to industrial processors and in the market for the supply of white sugar to retailers in Italy. However, as noted above in section 6.1.2 of this Decision, these are two different product markets and Südzucker should have calculated the respective market shares separately.
- (347) In view of the above, the Parties have high combined market shares of at least [50-60]% in the market for sales of white sugar to industrial processors in Italy. Therefore, in an already concentrated industry, further consolidation would take place and the proposed transaction would create a market leader unmatched by its competitors.

²⁵⁵ Horizontal Merger Guidelines, para. 17, citing Case T-221/95, *Endemol v. Commission*, [1999] ECR II-1299, para. 134, and Case T-102/96, *Gencor v. Commission*, [1999] ECR II-753, para. 205.

²⁵⁶ Annex 16-1 of Südzucker's reply to the 3rd RFI in Phase II.

²⁵⁷ Annex Q16-7.3.a of Südzucker's answer to the 3rd RFI in Phase II.

6.1.4.3. The effects of the proposed transaction on the Italian sugar market structure

Elimination of competition between Südzucker and EDFM

(i) Role of Südzucker

- (348) Already before the acquisition of 50% of MAXI's capital by Südzucker, Südzucker and MAXI had entered into a cooperation agreement in which Südzucker *inter alia* agreed to supply MAXI with white sugar. However, at that time, Südzucker was not the only supplier of MAXI. MAXI did not produce sugar itself and storage capacities were not necessary due to the lower sugar sales. MAXI's white sugar sales mainly covered northern Italy and industrial processors (beverage, chocolate, biscuits, etc)²⁵⁸. Already in 2006, Südzucker had foreseen the potential benefits from a closer cooperation with MAXI²⁵⁹.
- (349) After the acquisition of 50% of MAXI's capital by Südzucker, MAXI has become Südzucker's [...] sales arm in Italy, following which Südzucker's sales increased in the Italian markets of white sugar to industrial processors and to retailers.
- (350) MAXI currently has [...] storage facilities in [...] ([...] tonnes), [...] ([...] tonnes), [...] ([...] tonnes) and [...] ([...] tonnes). According to Südzucker, stocks are used for packed goods and the facilities are currently used [...] ²⁶⁰.
- (351) The following maps indicate for 2011 the areas served by each of MAXI's storage facilities in [...] ²⁶¹:

[...] ^{*}

The following table shows the distance of deliveries for each of MAXI's storage facilities: ²⁶²

[...] ^{*}

- (352) According to Südzucker, sugar storage has two main purposes: (i) bringing sugar into sales areas during campaign periods (external warehousing), and (ii) ensuring continuous deliveries to clients. The extent to which Südzucker uses external warehousing during campaign periods for bringing sugar into the sales areas depends on the produced quantity. Security of supply is one of the main characteristics industrial processors and retailers seek from suppliers ²⁶³.
- (353) Südzucker's strategy for ensuring security of supply for its customers in Italy is based on two pillars: (i) sufficient storage facilities, and (ii) sound allocation of sales and required stock levels to a specific destination ²⁶⁴.

²⁵⁸ Südzucker's answer to Question 1 of the 3rd RFI in Phase II.

²⁵⁹ Annex 23 of Südzucker's answer to the 2nd RFI in Phase I, at page 13.

²⁶⁰ Südzucker's answer to Question 5 of the 3rd RFI in Phase II.

²⁶¹ Annex 5-1 of Südzucker's answer to the 3rd RFI in Phase II.

²⁶² Südzucker's answer to Question 8 of the 3rd RFI in Phase II.

²⁶³ Südzucker's answers to Questions 12 and 30 of the 3rd RFI in Phase II.

²⁶⁴ Südzucker's answer to Question 29 of the 3rd RFI in Phase II.

- (354) In order to ensure continuous supply to customers, Südzucker works with an average stock in Italy that covers approximately [...] weeks of sales, i.e. around [...] tonnes. This quantity is split into [...] tonnes packed goods (circa [40-50]%) and [...] tonnes bulk (circa [60-70]%)²⁶⁵.
- (355) Moreover, Südzucker is perceived by other sugar producers/suppliers as an aggressive competitor in Italy. In that regard, [large sugar producer] stated: *"since the Italian sugar market is significantly deficit, it should have normally attracted new players. However, [large sugar producer]* believes that MAXI, Südzucker's distributor in Italy, may have managed to deter potential entrants by significantly reducing its prices during the last 3 to 4 years in Italy. It appears that Südzucker via MAXI were selling at lower prices in Italy than in surplus markets in the last few years. Normally, the market price in Italy should reflect the high transport costs involved when sugar is imported into the Italian market from France, Germany and the United Kingdom. However, MAXI's prices in Italy during the last couple of years were lower than the ones in the abovementioned countries. [...] [large sugar producer]* believes that the competitors of MAXI could not follow its example since this strategy would not be economically viable for them. Therefore, there is a risk that once all players are driven out of the market, MAXI would be able to increase its prices higher without facing any competitive constraint"*²⁶⁶. In addition, [another large sugar producer]* stated: *"Tate & Lyle had not enough raw sugar to supply their refineries. Nordzucker concentrated its commercial action in North of Europe, given the fixed quantity at their disposal and the low level of pricing in Italy not sufficient to cover logistic costs to arrive in Italy. However, we can assume that the dumping were made in that period by Südzucker was aimed to discourage the competitors to play in Italy"*²⁶⁷.
- (356) Following this expansion strategy in the Italian market illustrated by the acquisition of MAXI and the subsequent increase of market presence in Italy, Südzucker has managed to become the market leader in the market for white sugar for industrial processors and currently manages to sell approximately [...] tonnes of white sugar per year in Italy of which [...] tonnes to industrial processors.

(ii) *Role of EDFM and the Brindisi refinery*

(a) *EDFM*

- (357) EDFM entered the Italian market as a producer of white sugar through its SRB joint-venture with SFIR. The background of the business decision to establish SRB was the reaction to the effects of the 2006 sugar market reform in Italy. As explained above, between 2006 and 2008, Italy gave up 67% (1,049,000 tonnes/year), of its 2005 quota, which amounted to 1,557,000 tonnes/year. As a result, 15 out of 19 beet factories in Italy had to close. Facing a relatively stable demand for white sugar and the limited Italian beet quota, the four remaining beet sugar factories in Italy (located

²⁶⁵ Südzucker's answer to Question 12 of the 3rd RFI in Phase II.

²⁶⁶ Minutes of the conference call with [...] on 30 November 2011.

²⁶⁷ [...] reply to question 60 of the Questionnaire to sugar producers/suppliers in Italy.

in San Quirico (Parma), Minerbio, Termoli and Pontelongo) could not satisfy demand²⁶⁸.

(b) *EDFM and SFIR partnership*

- (358) In the past, SFIR was one of the historical Italian beet sugar producers²⁶⁹ in need of a reorientation of its business after the closure of its sugar production. EDFM was part of the dissolved EuroSugar joint-venture, a sugar distribution joint-venture operating between 2007 and 2009. EDFM and SFIR, thus decided to establish an Italian refinery to process raw cane sugar. EDFM assumed a strategic role in the supply of raw cane to the refinery, whereas SFIR had the customer relations and knowhow to serve the Italian market.
- (359) The main business consideration behind the Brindisi project was precisely the large Italian deficit, in particular in the South of Italy. According to the project plans, the refinery would supply customers within a radius of [...] km covering [20-30]*% of the Italian domestic consumption²⁷⁰. On this business *rationale* EDFM and SFIR built up the Brindisi refinery, which started operating in December 2010.

(c) *Production capacity of the Brindisi refinery*

- (360) EDFM's internal documents of 2007 and 2009 indicate that SRB would have a maximum capacity of [...] tonnes per year and that SRB would reach a production of: (i) under a worst-case scenario [...] tonnes/year, (ii) under a base-case scenario [...] tonnes/year, and (iii) under a best-case scenario [...] tonnes/year.²⁷¹ A further internal document of 2009 plans EDFM's and SFIR's strategy in Italy on the assumption that SRB will be producing [...] tonnes per year²⁷².
- (361) The Brindisi refinery is the second largest raw cane sugar refinery in the Union with a maximum capacity of [...] tonnes²⁷³. In 2011, the projected production for the refinery was around [...] tonnes to industrial processors and [...] tonnes to retailers covering roughly [20-30]*% of the entire Italian sugar demand²⁷⁴.
- (362) Contrary to all the above mentioned internal documents, in the second phase the Parties suddenly claimed that EDFM had reduced its planned production for the Brindisi refinery to [...] tonnes/year²⁷⁵. However, EDFM was unable to submit internal documents that could substantiate its allegedly modified estimation for a production of [...] tonnes instead of [...] tonnes per year (under the base-case

²⁶⁸ "Information Memorandum" and "Competitive Analysis of supplying Sugar to the Italian Market" submitted as Annexes 4 and 5.b of EDFM's answer to the 2nd RFI in Phase I.

²⁶⁹ SFIR owned and operated four sugar beet factories in Italy prior to the sugar reform.

²⁷⁰ "Information Memorandum" and "Project Overview" submitted respectively as Annexes 4 and 5.a of EDFM's answer to the 2nd RFI in Phase I.

²⁷¹ "Information Memorandum" and "Project Overview" submitted respectively as Annexes 4 and 5.a of EDFM's answer to the 2nd RFI in Phase I.

²⁷² "Competitive Analysis of supplying Sugar to the Italian Market" submitted as Annex 5.b of EDFM's answer to the 2nd RFI in Phase I.

²⁷³ Form CO, p. 135 and answer to the 2nd RFI to EDFM of 27 September 2011, "Information Memorandum SFIR/ED&F Man Brindisi Project" of 4 June 2009.

²⁷⁴ Form CO, p. 27.

²⁷⁵ Südzucker's reply to the Commission's Decision under Article 6(1c) of the Merger Regulation, paragraph 15.

scenario) by the Brindisi refinery²⁷⁶. On 2 December 2011, the Parties submitted a paper²⁷⁷ claiming that in reality the Brindisi refinery could only produce up to [...] tonnes per year.

- (363) In view of the above and taking into account the base-case scenario as well as the paper submitted on 2 December 2011, the production of the Brindisi refinery should be at least [...] tonnes per year in the future.

(d) *Supply area of Brindisi*

- (364) The Brindisi refinery will not only be a substantial relief for the South of Italy, where there are no other sugar factories at all but according to internal documents of EDFM made in preparation of the refinery²⁷⁸, [Description of SRB's supplies]*.

(e) *Storage facilities*

- (365) The main Italian distribution hubs for the Brindisi refinery are the four former (no more operational) sugar beet factories of SFIR located in Forlimpopoli (close to Ravenna), in San Pietro in Casale (close to Bologna), in Pontelagoscuro (close to Ferrara) and Foggia in the South of Italy²⁷⁹. SRB also owns white sugar storage facilities in Brindisi with capacity of [...] tonnes²⁸⁰. The following table and map²⁸¹ show SFIR's (rented or owned) storage facilities, which are used to store white sugar from the Brindisi refinery:

[...]*

- (366) The locations of these storage facilities cover the whole Italian market from North to South. EDFM acknowledges that SFIR has maintained a good distribution network and the necessary structures (storage and packing facilities), relationships and customer contacts in Italy²⁸².

- (367) [Description of SRB's supplies]*. These storage facilities enable SFIR to minimize time of delivery and to offer better service to the final customer. SFIR considers such storage facilities as very important, in order to deliver bulk sugar to final customers and to feed packaging facilities. [Description of SRB's supplies]*²⁸³.

(f) *Perception by competitors and customers*

- (368) With regard to SFIR, respondents have largely emphasized the competitive advantage linked to the Brindisi refinery in terms of access to input (raw cane sugar),

²⁷⁶ Südzucker's answer to Question 15 of the 3rd RFI in Phase II.

²⁷⁷ "Brindisi capacity paper" submitted by EDFM on 2 December 2011.

²⁷⁸ "Competitive Analysis of supplying Sugar to the Italian Market" submitted as Annex 5.b of EDFM's answer to the 2nd RFI in Phase I. Zuccherificio del Molise is located in the centre of Italy and in any event only has a limited capacity of approximately 85,000 tonnes/year.

²⁷⁹ "Information Memorandum" submitted as Annex 4 of EDFM's answer to the 2nd RFI in Phase I.

²⁸⁰ Annex 5 of EDFM's answer to the 2nd RFI in Phase II.

²⁸¹ SFIR's answers to Questions 17 and 18 of the 2nd RFI in Phase II.

²⁸² "Information Memorandum" submitted as Annex 4 of EDFM's answer to the 2nd RFI in Phase I.

²⁸³ SFIR's answers to Questions 22 and 25 of the 2nd RFI in Phase II.

geographic position of the refinery²⁸⁴ or the excellent established customer relationship of SFIR²⁸⁵. Besides, according to an internal document on the competitive analysis of supplying sugar to the Italian market, it is acknowledged that Brindisi has a "*EUR [...]** logistic premium to the average of imported and Italian beet supplied sugar"²⁸⁶.

(iii) *Closeness of competition between Südzucker and EDFM*

- (369) The main competitors of Südzucker and EDFM, as identified in the reconstructed market shares table in recitals (336) and (337) of this Decision, have their storage facilities located in the north of Italy, such as Eridania and COPROB, or do not have any, like Tereos.
- (370) On the contrary, as analysed above, both Südzucker and EDFM have storage facilities and make sales of white sugar to industrial processors and to retailers in the whole territory of Italy. Südzucker and EDFM are geographically close competitors in the sense that they operate in the same areas in Italy. The following two maps illustrate the sales activities and storages for Südzucker and for EDFM/SFIR respectively²⁸⁷:

[...]*

- (371) The proposed transaction would thus bring together two of the largest Italian suppliers with nation-wide presence, contrary to their main competitors. Post-transaction, the new entity would no longer be exposed to the competitive constraint they exercised to each other. Absent the proposed transaction, the recently introduced SRB could offer a competitive alternative to Südzucker (due to its logistics cost advantage and stable supply) in the Italian market for the supply of white sugar to industrial processors.

(iv) *Post-transaction Südzucker and EDFM would have the incentive and ability to withdraw quantities and raise prices in Italy*

- (372) Südzucker and EDFM post-transaction would have the incentive and ability to withdraw quantities from Italy, thereby raising prices.
- (373) Indeed, the proposed transaction would bring together the two most dynamic and fastest growing players in Italy as analysed above and further explained below.
- (374) Also, as admitted by Südzucker and as stated in its internal documents, Südzucker has a clear commercial strategy [Südzucker's strategy]*. Südzucker has increased its

²⁸⁴ Reply by Tate & Lyle (2011/132417) (reply to question 53) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

²⁸⁵ Reply by COPROB (2011/132649) (reply to question 51) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

²⁸⁶ Annex 5.b of EDFM's reply to the 2nd RFI in Phase I, p.13.

²⁸⁷ Annex 5-1 of Südzucker's answer to the 3rd RFI in Phase II; SFIR's answer to Question 17 of the 2nd RFI in Phase II.

sales volume from approximately [...] tonnes in 2008²⁸⁸ to approximately [...] tonnes in 2010²⁸⁹:

[...]*

- (375) As shown in the Commission's reconstructed table of market shares²⁹⁰, today Südzucker is the biggest player in Italy with at least [30-40]*% of the market for sales of white sugar to industrial processors. However, most importantly, Südzucker is able to reduce the quantities it sells in Italy either by reallocating part of these quantities to other Member States or by increasing its stocks of white sugar. Südzucker can easily reallocate sugar from Italy to other Member States, since it benefits from the highest quota in the Union of approximately [...] million tonnes per year²⁹¹, which amounts to around [...] of total sugar quota production in the Union. Südzucker's internal documents indicate that [Südzucker's strategy]*²⁹².
- (376) On the other hand, with a realistic future production of at least [...] tonnes²⁹³, the Brindisi refinery has produced [...] tonnes during the first ten months of 2011²⁹⁴, and it is expected to produce [...] tonnes in 2012, according to internal documents²⁹⁵. Therefore, only in its first year, the Brindisi refinery represents approximately [10-20]*% of the market for the supply of white sugar to industrial processors in Italy²⁹⁶. In the absence of the proposed transaction, the Brindisi refinery would have both the ability and the incentives to supply an even larger part of the Italian market, [Description of SRB]*. The following graph depicts the quantities produced by the Brindisi refinery (i) in the first ten months of 2011, (ii) in campaign year 2011/2012, (iii) under the worst-case scenario of production, (iv) under the base-case scenario of production, (v) under the best-case scenario of production, and (vi) in terms of theoretical capacity, as analysed in recitals (361) to (364) of this Decision.

[...]*

- (377) Also, in the market for sales of white sugar to industrial processors, the closest competitors in terms of size would be significantly smaller than the merged entity, with market shares of around [10-20]*%.
- (378) In the internal documents preparing the proposed transaction, EDFM and SFIR themselves analyze their competitors²⁹⁷. They indicate that [Description of SRB's supplies]*²⁹⁸ [...] ²⁹⁹.

²⁸⁸ Annex Q16-1 (chart at p. 16) of Südzucker's answer to the 3rd RFI in Phase II.

²⁸⁹ Annex Q16-7.3.a of Südzucker's answer to the 3rd RFI in Phase II.

²⁹⁰ See recitals (336) and (337) of this Decision.

²⁹¹ Annex 16-1 of Südzucker's reply to the 3rd RFI in Phase II.

²⁹² Annex 6 of Südzucker's reply to the 3rd RFI in Phase I.

²⁹³ See recitals (360) to (363) of this Decision.

²⁹⁴ See recital (336) of this Decision.

²⁹⁵ Excel table entitled "The Brindisi Project", provided in EDFM's reply to Question 1 of the 4th RFI in Phase I.

²⁹⁶ See recital (336) of this Decision.

²⁹⁷ Answer to the 2nd request for information to EDFM of 27 September 2011, "ED & F Man and SFIR S.p.A – Competitive Analyses of Supplying to the Italian Market" p. 13-19.

²⁹⁸ *Ibid*, at pp.13 and. 17.

- (379) As the stability of the demand in Italy and the responses of market participants indicate, for all the customers sugar is a crucial input product, therefore security of supply is essential and demand is inelastic. Respondents systematically see Brindisi as an important improvement for the Italian sugar market holding significant competitive advantages in terms of its position, infrastructure and access to preferential raw cane sugar.
- (380) Indeed, in the absence of the Brindisi refinery, Südzucker and other suppliers from northern Italy and Member States north of Italy would not face any significant competitive constraint from the South in setting their commercial strategy in Italy, including pricing. Moreover, when the Brindisi refinery will reach its maximum production capacity, it will alone be able to supply approximately [30-40]*% of the current Italian deficit (approximately 1 million tonnes/year). Since white sugar for industrial processors is a homogeneous product, where the quantity supplied determines its final price, the additional quantities expected in the near-future from the competitive Brindisi refinery will play an important role in the determination of white sugar prices in Italy.
- (381) The maps below³⁰⁰ taken from the preparatory documents of EDFM before investing in the Brindisi refinery, reflect the supply patterns and logistics costs in Italy before the start of production in the Brindisi plant and the predictions for after that moment. They illustrate that the refinery has a strong logistics cost advantage over its competitors and could strongly reduce logistics costs in the South of Italy, including Sardinia and Sicily (from EUR [...]*/tonne previously to EUR [...]*/tonne with the Brindisi refinery), but also in the North of Italy (overall logistics costs to supply Italy falls from EUR [...]*/tonne to EUR [...]*/tonne).

Trade flows and transport costs for sugar in Italy prior the start of production of the Brindisi refinery

[...]*

Predicted trade flows and transport costs for sugar in Italy after the inauguration of the Brindisi refiner

[...]*

- (382) Another internal document also demonstrates the effects of the sugar supplies in Italy indicating that [Description of SRB's supplies]*³⁰¹.

[...]*

- (383) According to an EDFM internal document analysing the Italian market and the Brindisi project, [Description of SRB's supplies]*.³⁰²

²⁹⁹ *Ibid*, at p. 17.

³⁰⁰ 2nd request for information to EDFM of 27 September 2011, "Information Memorandum SFIR/ED&F Man Brindisi Project" of 4 June 2009.

³⁰¹ Answer to the 6th request for information to EDFM of 11 October 2011, internal document on "Italian Market" (undated), slide 12.

³⁰² Answer to the 2nd request for information to EDFM of 27 September 2011, "ED & F Man and SFIR S.p.A – Competitive Analyses of Supplying to the Italian Market" p. 12.

- (384) Furthermore, the Brindisi refinery has secured approximately [...] tonnes of raw cane sugar per year [...] through the three contracts mentioned at recital (303) of this Decision, as also confirmed by the Parties. In particular, the [Supplier A] contract has secured [...] tonnes per year [...], whereas the [Supplier B] and [Supplier C] contracts have together secured [...] tonnes per year [...]. These contractually secured quantities of raw cane sugar are an important element towards SRB's base-case scenario production of [...] tonnes of white sugar per year.
- (385) The analysis in another document also shows that SRB can ensure substantially lower transport costs than imports from France or Germany³⁰³:
- [...]
- (386) Therefore, in the absence of the proposed transaction there would be intense competition in Italy between Südzucker and the Brindisi refinery and the latter would bring even stronger competition in the future [...].
- (387) However, post-transaction Südzucker would have negative control over EDFM, which in turn controls the Brindisi refinery jointly with SFIR. Therefore, the merged entity could exercise negative decisive influence over the commercial policy and the strategic decisions of the Brindisi refinery, irrespective of SFIR's position. In fact, the merged entity would have a veto right with respect to decisions and plans of the Brindisi refinery that could impose competitive constraints upon Südzucker in Italy.
- (388) Parent companies can generally be presumed to have an incentive to co-ordinate their competitive behaviour in the decision-making process of the respective company when it is likely to be profitable and thus economically rational. There are many factors which could influence the incentives of the parents to compete outside the joint venture. The most important factor is the joint venture's ownership and control structure. Under the assumption of rational economic behaviour, the greater the parent's stake in the joint venture, (i) the less likely the parent is to compete with it, and (ii) the easier it is for the parent to control the joint venture. In that regard, the acquisition or strengthening of significant market power is relevant, as the ability to raise prices or exclude competitors, on their own or together with third parties, will most likely eliminate the incentive to compete.
- (389) As a result of the proposed transaction, the merged entity will benefit from a dominant position in the market for white sugar to industrial processors in Italy reinforcing the risk of co-ordinate the competitive behaviour between the parent companies.
- (390) Also, the merged entity could compensate SFIR for any short-term loss of revenue caused by a decision to withhold quantities of sugar from being sold on the Italian market. In the long run, SFIR would in all probability not object to such practices if they lead to higher sugar prices, as the merged entity and SFIR would thus achieve joint profit maximisation.

³⁰³ EDFM's reply to the 6th request for information of 11 October 2011, internal document on "Italian Market" (undated), slide 12.

- (391) Given the above, in the absence of the proposed transaction the Brindisi refinery would bring significantly stronger competition to the largest deficit market in the Union, Italy. On the contrary, post-merger the competitive force exercised by the Brindisi refinery in the Italian market for the supply of white sugar to industrial processors would disappear.

Other competitors currently active in Italy are unlikely to increase supply if prices increase

- (392) In accordance with the Horizontal Merger Guidelines, when market conditions are such that the competitors of the merging parties are unlikely to increase their supply substantially if prices increase, the merging firms may have an incentive to reduce output below the combined pre-merger levels, thereby raising market prices³⁰⁴. A merger such as the proposed transaction leading to a significantly increased market shares increases the incentive to reduce output by giving the merging firms a larger base of sales on which to enjoy higher margins resulting from an increase in prices induced by the output reduction³⁰⁵.
- (393) If market conditions are such that competitors do not have enough capacity and do not find it profitable to expand output significantly, the Commission is likely to find that the merger will create or strengthen a dominant position or otherwise significantly impede effective competition³⁰⁶.
- (394) In other words if competitors have the ability and incentive to significantly increase their supplies and market shares in reaction to a price increase, the merger should not raise competition concerns³⁰⁷.
- (395) In this context, such output and market share expansion is in particular unlikely when competitors face binding capacity constraints and the expansion of capacity is costly or if existing excess capacity is significantly more costly to operate than capacity currently in use³⁰⁸. At the same time, it should be also pointed out that "*[n]on-merging firms in the same market can also benefit from the reduction of competitive pressure that results from the merger, since the merging firms' price increase may switch some demand to the rival firms, which in turn, may find it profitable to increase their prices*" and the "*reduction in these competitive constraints could lead to significant price increases in the relevant market*"³⁰⁹.
- (396) This section therefore analyses the positioning of each competitor of the Parties in the market for supply of white sugar to industrial processors in Italy and examines in particular whether they (a) are in a position and (b) have incentive to increase their sugar supplies on the Italian white sugar market for industrial processors in case of price increase³¹⁰.

³⁰⁴ Paragraph 32 of the Horizontal Merger Guidelines.

³⁰⁵ Paragraph 32 of the Horizontal Merger Guidelines.

³⁰⁶ Paragraph 33 of the Horizontal Merger Guidelines.

³⁰⁷ Paragraphs 17 and 33 of the Horizontal Merger Guidelines.

³⁰⁸ Paragraph 34 of the Horizontal Merger Guidelines.

³⁰⁹ Paragraph 24 of the Horizontal Merger Guidelines.

³¹⁰ The Horizontal Merger Guidelines.

(i) Lack of ability or incentive for competitors of Südzucker and EDFM to expand in Italy: assessment of generally prevailing market conditions

- (397) The Italian sugar market is characterized by low production capacities due to fixed limited white sugar production quotas, therefore Italian competitors, including [...]*, [...]* and [...]*, are capacity constrained. Indeed, half of the Italian white sugar demand (1.73 million tonnes/year³¹¹) is satisfied from domestic production fixed on the basis of the Italian production quota (855,000 tonnes/year)³¹². Therefore, the Italian white sugar market is highly import dependent since half of its domestic consumption has to be satisfied from imports. At the same time, the sugar stocks in the Union are very low³¹³ and significant shortage of access to preferential raw cane sugar is commonly known by the industry³¹⁴. All these elements taken together significantly limit the ability of sugar producers that are already established in Italy to reallocate capacities in Italy.
- (398) Therefore, in response to a price increase, those producers would have to reallocate white sugar quantities which are in principle destined to already existing customers in other Member States. Therefore, such reallocation of sugar quantities would be quasi impossible without withdrawing sugar from other customers with whom the producer has already a well-established relationship. That is different from the 2005/2006 market conditions where surplus country producers with stocks were in a position to reallocate quantities without disrupting already existing customer relationships³¹⁵.
- (399) In particular, in times of scarcity other significant European players with sales organisations in the Italian market such as [...]*, [...]* and [...]*, have limited capacities and also no incentives to redirect substantial additional sugar quantities from other Member States to Italy on the basis of the elements above and below. In addition, such reallocation of quantities would also imply additional transport costs leading to lower margins for sales in Italy than for sales in the country of origin of the white sugar.
- (400) Reallocation of sales with a view to expanding market shares in Italy would also entail the risk that Südzucker will protect its market shares in Italy in a selective manner as it is in a position to do so, in particular post-merger, by giving selective and pre-emptive price reductions to those customers which a supplier would like to acquire.
- (401) A further factor which needs to be taken into account is that a failure of an expansion strategy on the Italian market would entail high costs, because it requires to accept for the additional quantities low prices and thus margins, transport costs to bring the sugar from abroad and the loss of high margins in the country of origin. According to

³¹¹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 12, sent by e-mail of 1 December 2011 (19:33).

³¹² Production capacities of [...]*

³¹³ Recital 2 of Commission Regulation (EU) No 222/2011 of 3 March 2011 laying down exceptional measures as regards the release of out-of-quota sugar and isoglucose on the Union market at reduced surplus levy during marketing year 2010/2011 (OJ L 60, 5.3.2011, p. 6).

³¹⁴ See recitals (69) to (73) of this Decision.

³¹⁵ Reply by [...]* (reply to questions 7 and 8) (Non-Confidential Version – Questionnaire to [...]* – Phase II) (received by e-mail of 9 January 2012 at 18:15).

the Horizontal Merger Guidelines high risks and high costs of failed entry or expansion make entry or expansion less likely³¹⁶.

- (402) Last but not least, [...]*, [...]*and [...]* all indicated to the Commission that they will not expand their white sugar supplies in Italy even in reply to a price increase.
- (403) Against this background, in paragraph 181 of its reply to the SO, the notifying party argued the following: "*[t]he fact that producers are capacity constrained does not mean that they will not sell more sugar to industrial customers in Italy if there is a permanent price increase as postulated by the Commission's theory of harm. The postulated higher Italian sugar prices resulting from withholding of volumes will necessarily change the incentives of the sugar producers and suppliers in Europe – sales to industrial customers in Italy will be relatively more profitable making it profit-maximising for producers to commence sales in Italy or to divert a higher proportion of their sales to Italy*".
- (404) [...]*³¹⁷ [Description of Südzucker's market strategy]*.
- (405) [Description of Südzucker's market strategy]*. The analysis of Südzucker stops there, however as explained above, on top of the high risk of losing home market customers and facing additional transport costs, as rightly pointed out by Südzucker, a re-allocation of sugar quantities to Italy would also imply the risk of facing an incumbent operator who would protect its market shares in a selective manner by offering long-term contracts or giving targeted pre-emptive price reductions to those customers that the given supplier would try to acquire³¹⁸. That would lower the profitability of such sugar reallocation, and is especially relevant for the Italian sugar market where such market behaviour has already taken place.
- (406) Indeed, [a large Italian sugar producer]* indicated to the Commission in the following terms that "*Tate & Lyle had not enough raw sugar to supply their refineries. NZ concentrated its commercial action in North of Europe, given the fixed quantity at their disposal and the low level of pricing in Italy not sufficient to cover logistic costs to arrive in Italy. However we can assume that the dumping [was] made in that period by SDZ was aimed to discourage the competitors to play in Italy*". [a large sugar producer]* took the view that "*[f]urthermore, since the Italian sugar market is significantly deficit, it should have normally attracted new players. However, [a large sugar producer]* believes that MAXI, Südzucker's distributor in Italy, may have managed to deter potential entrants by significantly reducing its prices during the last 3 to 4 years in Italy. It appears that Südzucker via MAXI were selling at lower prices in Italy than in surplus markets in the last few years. Normally, the market price in Italy should reflect the high transport costs involved when sugar is imported into the Italian market from France, Germany and the United Kingdom. However, MAXI's prices in Italy during the last couple of years were lower than the ones in the abovementioned countries*"³¹⁹.

³¹⁶ Paragraph 69 of the Horizontal Merger Guidelines.

³¹⁷ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 15, sent by e-mail of 1 December 2011 (19:33).

³¹⁸ Paragraph 69 of the Horizontal Merger Guidelines.

³¹⁹ Reply by [...]* ([...]*) (reply to question 60) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) and Non-confidential version of the Minutes of the

- (407) In paragraph 148 of its reply to the SO the notifying party qualifies these quotes being "*anecdotes*" by simply objecting that "*many other European sugar producers had expansion strategies and directed significant quantities of sugar to Italy*" before however qualifying these anecdotes "*evidence*" which would reflect "*the existence of functioning competition*".
- (408) Also, during the Hearing of 5 March 2012, the notifying party produced a table³²⁰ with Südzucker's national average invoiced sugar prices [Information about Südzucker's prices in Italy between 2006/2007 and 2010/2011]*. In this respect, the notifying party explains that such strategy only took place because during the transitional period from the old regime to the full effects of the 2006 sugar regime Südzucker had surplus sugar to reallocate in other Member States. [Information about Südzucker's prices in Italy between 2006/2007 and 2010/2011]*. In addition, competitors without stocks could not engage in such strategy which resulted in an increase of Südzucker's market shares on the Italian white sugar markets to the detriment of its direct competitors. Therefore, Südzucker cannot validly argue that evidence of its aggressive market behaviour is only an "*anecdote*" and that competition for market shares did not take place in Italy.
- (409) As for the replies by the competitors whether they would expand in Italy as a reaction to a sugar price increase as a result of the proposed transaction, the notifying party takes the view in its reply to the Statement of Objections that the question in the questionnaire sent to the competitors in Phase II was not precise enough and that the replies of the competitors were flawed as they replied to leading questions in some instances.
- (410) As for the irrelevance of the question in the questionnaire³²¹, the notifying party argued in this respect in its reply to the SO that reference should be made to the two years period as provided for in Paragraph 74 of the Horizontal Merger Guidelines and that price increase should be "*permanent*". However, Paragraph 74 of the Horizontal Merger Guidelines relates to "*entry*" of new competitors and not "*expansion*" of existing competitors and the Horizontal Merger Guidelines do not require the use of reference to a "*permanent*" price increase.
- (411) Also, in its criticism³²² the notifying party overlooks the fact that several follow-up questions were addressed to competitors on that very issue. Indeed, more precise answers were obtained in the course of the follow-up questions. Reference to such exchanges is widely reflected in the Statement of Objections and this Decision.
- (412) As for [a large Italian sugar producer]* for example references to these exchanges are made in footnotes 224, 245, 247 or 248 of the Statement of Objections or the non-confidential version of the Minutes of the conference call with [a large sugar producer]* on 30 November 2011. Concerning [a large Italian sugar producer]*, reference is also made to footnote 265 of the Statement of Objections or the non-

Teleconference with [...] of 30 November 2011, e-mail of Mr [...] of 9 January 2012, at 14:18, paragraphs 4 and 5.

³²⁰ Slide 13 of the presentation by [...] of 5 March 2012, entitled "Effects of the Transaction on the White Sugar Market".

³²¹ Paragraphs 167 – 169 and 175 of the reply of the notifying party to the Statement of Objections.

³²² Paragraphs 172 – 173 of the reply of the notifying party to the Statement of Objections.

confidential version of the Minutes of the Teleconference with [a large sugar producer]* on 8 December 2011. With regard to [a large sugar producer]* reference is made to footnotes 291 or 292 of the Statement of Objections or a specific questionnaire with 10 questions on the ability and incentives of [a large sugar producer]* to expand in the Italian white sugar market to industrial processors entitled "M.6286 – Südzucker / ED&F Man Questionnaire to [...]* – Phase II" or also the Non-confidential Minutes [...]* – 18 November 2011 and several other exchanges.

- (413) Concerning the alleged leading nature of some questions³²³, it must be borne in mind that replies to the questions about the ability and incentive to expand output in the Italian white sugar markets in case of price increases imply highly confidential market strategy information of the competitors subject to the market investigation.
- (414) The Commission has proposed summaries of the confidential information provided by the respondents to them in order for them to be able to agree to the non-confidential summaries being used for the purposes of the investigation. Therefore, the indications by the Commission did not constitute a question on a stand-alone basis but only the non-confidential summary of the confidential answers of the respondents already obtained beforehand.
- (415) Therefore, on the basis of the market investigation, it is concluded that white sugar producers / suppliers would have limited ability and no incentive to expand their white sugar supplies in the market for supply of white sugar to industrial processors in Italy post-merger even in response to a price increase.

(ii) *Eridania / Tate & Lyle / Cristal Union*

(a) *The notifying party*

- (416) According to the notifying party³²⁴, Eridania (Eridania Italia S.p.A.) is one of the incumbent Italian beet sugar manufacturers with two beet factories producing 275,000 tonnes per year. As one of the incumbent Italian beet sugar manufacturers, Eridania has expert knowledge of the Italian market, good client contacts and distribution network. It furthermore profits from being an Italian company, providing a "local touch" for certain customers. In order to maintain its historically strong position on the Italian market despite the reduction of its beet production, Eridania is sourcing sugar from inside and outside the Union. Eridania had a cooperation agreement in place with Tate & Lyle and is now tied to Cristal Union, one of the major French sugar beet manufacturers (the envisaged³²⁵ acquisition of Groupe Vermandoise would make Cristal Union the fifth largest sugar producer in the Union). According to the notifying party, that cooperation agreement will help Eridania get significant sugar supplies from France and is intended to "*reinforce the leadership position of Eridania in Italy and maintain its strong position vis-à-vis*

³²³ For example Paragraphs 189, 194 or 199 of the reply of the notifying party to the Statement of Objections.

³²⁴ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 21, sent by e-mail of 1 December 2011 (19:33).

³²⁵ The "*protocole d'accord*" was signed on 7 January 2012 ("<http://www.cristal-union.fr/1157/conclusion-d%e2%80%99un-protocole-d%e2%80%99accord-avec-cristal-union-pour-l%e2%80%99acquisition-du-controle-du-groupe-vermandoise/>")

industrial clients". The notifying party has also put forward that both Eridania and Cristal Union have significant refinery projects in the pipeline. Cristal Union builds a refinery in Algeria which is expected to start operations in mid-2012 while Eridania announced in April 2011 an agreement with Kenana Sugar Company of Sudan to build a major sugar refinery in Sudan with an initial capacity of 500,000 tonnes of raw sugar which is planned to reach 1 million tonnes in the future. The notifying party suggests that the realisation of the Sudan project³²⁶ will enable Eridania to source for the Italian market within the LDC/ACP preference framework and compete with sugar of Sudan origin in the Italian market.

(b) *Historical background*

- (417) Eridania is a historical operator on the Italian white sugar market. Currently Eridania has a [...] production facility³²⁷. Following the 2006 sugar reform it concluded a cooperation agreement with Tate & Lyle on 28 March 2007.
- (418) Tate & Lyle had been trading in the Italian sugar market for 20-30 years through a local agent before deciding in 2007 to create a joint venture together with Eridania Sadam³²⁸. However, Tate & Lyle exited the Italian sugar market in 2011³²⁹ as [...] ³³⁰.
- (419) On 7 March 2011 Eridania Italia S.p.A. set up a joint-venture ([...]) with [...], CristalCo³³¹. [Shareholder structure of CristalCo]³³².

(c) *Sources of supply and infrastructure*

- (420) Contrary to the indication by the notifying party, Eridania [...] ³³³ and [...] ³³⁴.

³²⁶ Also see Presentation by Südzucker to the Commission on the "Sugar Market in Italy" of 2 December 2011, slide 6 (Sugar Market in Italy Presentation to the Commission (M.6286) Brussels, 2. December 2011).

³²⁷ Reply by [...] ([...]) (reply to question 5) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³²⁸ Non-confidential version of the Minutes of the Teleconference with [...] of 30 November 2011, e-mail of Mr [...] of 9 January 2012, at 14:18, paragraph 1

³²⁹ (http://www.eridaniaitalia.it/media/documents/eridania_italia/PARTE_GENERALE_-_ERIDANIA_ITALIA_SPA_rev290311_INGL.pdf), page 5

³³⁰ Non-confidential version of the Minutes of the Teleconference with Tate & Lyle of 30 November 2011, e-mail of Mr [...] of 7 January 2012, at 1:05, paragraph 2 [...], Reply by [...] ([...]) (reply to question 60) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) and Reply by [...] ([...]) (reply to question 48) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³³¹ (http://www.eridaniaitalia.it/media/documents/eridania_italia/PARTE_GENERALE_-_ERIDANIA_ITALIA_SPA_rev290311_INGL.pdf), page 5

³³² Reply by [...] ([...]) (2012/002468) (reply to question 5) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³³³ Reply by [...] ([...]) (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) and e-mail of Mr [...] of 6 January 2012 at 18:43 entitled "Rif: M.6286 - Clarification of your reply to question 9 of the Questionnaire to sugar suppliers / producers Italy - Phase II".

³³⁴ Reply by [...] ([...]) (reply to question 96) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

(d) *Market positioning*

- (421) Despite Eridania's important sales of white sugar in Italy, its commercial focus is strongly placed on the retail market. This is also evidenced by the fact that Eridania has market shares almost [CONFIDENTIAL] times higher in the market for the supply of white sugar to retailers compared to industrial processors. Eridania holds [5-10]*% market share in the market for the supply of white sugar to industrial processors in Italy.

(e) *Perception by Eridania*

- (422) Eridania describes itself very succinctly as a company with infrastructure, national and regional sales offices and established customer relationship³³⁵.

(f) *Perception by competitors*

- (423) [A large Italian sugar producer]* describes Eridania on the Italian white sugar market with good access to input, very good infrastructure, customer relationship and national sales office and partnership with Cristal Union, however without the ability to expand its output on the Italian market in view of fixed limited production quotas and limited access to preferential raw cane sugar³³⁶.
- (424) [A large Italian sugar producer]* also explains that Tate & Lyle exited the Italian white sugar market because it had not sufficient raw cane sugar to supply the Eridania joint venture. At the same time, [a large Italian sugar producer]* considers that Cristal Union entered the joint venture as it has a surplus of sugar as a result of the recent acquisition of Société Vermandoise Industries and it was necessary to channel sugar into deficit and close market such as Italy³³⁷. [A large Italian sugar producer]* also emphasizes that Cristal Union entered the Italian market as it benefits from a surplus under the French sugar beet quota³³⁸ and [A large Italian sugar producer]* left the Italian white sugar market in the absence of enough raw sugar³³⁹. [A large Italian sugar producer]* explains that one of the reasons for Cristal Union's plan to cooperate with Eridania is the deficit situation of the Italian white sugar market³⁴⁰.
- (425) While [a large Italian sugar producer]* claims that competitors (in general) are able to increase the volumes sold in Italy, such increase would necessitate reallocation of volumes sold in other countries or through imports since no increase of production in

³³⁵ Reply by [...]* ([...]* (reply to question 90) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³³⁶ Reply by [...]* ([...]* (reply to questions 58, 59 and 69) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³³⁷ Reply by [...]* ([...]* (reply to questions 61 and 63) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³³⁸ "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...]* ([...]* (reply to question 64) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³³⁹ Non-confidential version of the Minutes of the Teleconference with [...]* of 30 November 2011, e-mail of Mr [...]* of 7 January 2012, at 1:05, paragraph 2 "[...]*".

³⁴⁰ Reply by [...]* (reply to question 64) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

Italy is possible³⁴¹. [A large Italian sugar producer]* takes the view that Eridania has a fixed quota for beet sugar output and has therefore little flexibility to increase output before adding that at current price levels raw sugar bought on the free market (for example, from Brazil) cannot be sold profitably in the Union because of high duties³⁴². [A large Italian sugar producer]* explains that Italy is a highly deficit country in terms of sugar³⁴³ and states in this respect that no player on the Italian market (including Eridania) is in a position to expand its output in a short period of time as a response to a price increase in view of the fact that "*all the players deal with production quotas which are fixed and with constraints in access to preferential sugar*"³⁴⁴.

(g) *Perception by customers*

- (426) As for customers, [a customer]* indicated that "*ESI/SFIR, MAXI and Italia Zuccheri have more strengths compared to Eridania/Tereos and Zuccherificio del Molise*"³⁴⁵. [A customer]* put forward that Eridania has its own refineries in Italy which constitutes a competitive advantage, however does not have important sugar quantities³⁴⁶. [A customer]* also indicated that Eridania has a favourable geographical situation³⁴⁷. However, [a customer]* indicated that "*Eridania is just a dealer not a producer*"³⁴⁸ while [a large customer]* underlined that Eridania is too small to be competitive on the segment for supply of sugar to industrial processors but has more sugar as a result of the cooperation with Cristal Union but is more present on the retail market via its brand "Zefiro"³⁴⁹.
- (427) Concerning the exit of the Italian white sugar market by Tate & Lyle, [a large customer]* explains that Tate & Lyle left the Italian market because of lack of sugar³⁵⁰. [A large customer]* suggests with regard to Cristal Union's market entry that it is linked to the deficit character of the Italian sugar market with high prices³⁵¹ while [a large customer]* takes the view that with the departure of Tate & Lyle Cristal Union has captured the opportunity to form a joint-venture with Eridania and

³⁴¹ Reply by [...] (reply to question 61) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁴² "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...] ([...]) (reply to question 61) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁴³ Reply by [...] ([...]) (reply to question 112) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁴⁴ Reply by [...] ([...]) (reply to question 59) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁴⁵ Reply by [...] ([...]) (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

³⁴⁶ Reply by [...] ([...]) (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II).

³⁴⁷ Reply by [...] ([...]) (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

³⁴⁸ Reply by [...] ([...]) (reply to question 45) (Non-Confidential and Confidential Versions – Questionnaire to sugar customers in Italy – Phase II).

³⁴⁹ Reply by [...] ([...]) (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³⁵⁰ Reply by [...] ([...]) (reply to question 48) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³⁵¹ Reply by [...] ([...]) (reply to question 50) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

"secure" a straight entry on the market³⁵². In this line, [a large customer]* puts forward that Cristal Union (CristalCo) "*needs to sell its sugar produced in France in other countries*" and Italy constitutes the best option to do it "*in terms of payback*"³⁵³.

(428) In general, Italian customers are very much concerned by the lack of availability of sufficient sugar quantities for Italian sugar producers / suppliers³⁵⁴.

(h) *Assessment*

(429) As already mentioned, it is submitted by the notifying party that both Eridania and Cristal Union have significant on-going refinery project developments. Cristal Union is building a refinery in Algeria which is expected to start operations in mid-2012 while Eridania announced in April 2011 an agreement with Kenana Sugar Company of Sudan to build a major sugar refinery in Sudan with an initial capacity of 500,000 tonnes of raw sugar which is planned to double to 1 million tonnes in the future. According to the notifying party, the realisation of the Sudan project³⁵⁵ will enable Eridania to source for the Italian market, within the LDC/ACP preference framework, and therefore compete with sugar of Sudan origin in the Italian market.

(430) In view of the Commission, the ability and incentives for Eridania/Cristal Union to substantially expand supplies on the market for supply of white sugar in Italy within the timeframe relevant for merger control are unlikely.

(431) As analysed in recitals (398) to (402) of this Decision, the Italian sugar market is production limited, Italian competitors are capacity constrained, sugar stocks in the Union are very low and significant shortage of access to preferential raw cane sugar is commonly known by the industry. In such difficult market conditions of scarcity of sugar, other major players with established presence in Italy such as Cristal Union with its joint venture with Eridania, do not have the capacity and incentives to redirect substantial additional sugar quantities from other Member States to Italy since it would entail commercial risks of losing existing customers, lower margins due to transport costs and the risk of failure of expansion due to the risk of selective reaction of the post-merger entity.

(432) Therefore, competitors such as Eridania and Cristal Union would have limited ability to substantially increase white sugar supplies in Italy post-merger and such strategy

³⁵² Reply by [...]* ([...]* (reply to question 50) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

³⁵³ Reply by [...]* ([...]* (reply to question 50) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³⁵⁴ For example, Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II) or Reply by [...]* ([...]* (reply to question 23) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

³⁵⁵ Also see Presentation by Südzucker to the Commission on the "Sugar Market in Italy" of 2 December 2011, slide 6 (Sugar Market in Italy Presentation to the Commission (M.6286) Brussels, 2. December 2011).

does not appear to be profitable as it would imply the significant commercial risks to lose existing customers in the country of origin of the sugar, to get lower margins due to transport costs and the high risk of failure of expansion of market share due to the risk of selective reaction of the post-merger entity, Südzucker/EDFM.

- (433) The new Sudanese refinery project for the time being is not precise enough and, as described by Südzucker's presentation³⁵⁶ in the most optimistic scenario the project will not commence operations before 2014. First of all, given the size of the project, its limited stage of advancement and the Sudan related political, legal and economic challenges to respect an ambitious calendar, it is at this stage not certain whether that timeframe is realistic. At this stage it is even uncertain whether the project will be realised at all. In this respect, the Commission notes that the project is still at an early stage [...]*. It must also be borne in mind that in the current economic and financial crisis it is difficult to find financing for a project like this. In addition, the Commission notes that the project has been on hold for several years now. Also, the political and economic environment in Sudan does not guarantee the timely implementation of the project. Therefore, there is uncertainty whether this project will materialise and significant doubts whether, if it does, it will come on-line in 2014. Accordingly, the Sudanese refinery project does not constitute a likely plan in view of the uncertainties surrounding the project and the fact that in the most optimistic scenario it is not foreseen to be in a position to provide white sugar on the Italian market prior to 2014.
- (434) Concerning the Algerian refinery, the Commission notes that, notwithstanding the fact that the project is at an advanced stage and is foreseen to operate as of the end of 2012, importing white sugar from Algeria is subject to world market import duties and is thus not currently an economically viable alternative compared to white sugar imported from LDC/ACP countries. [A large Italian sugar producer]*³⁵⁷ puts forward that the [...]*. [A large Italian sugar producer]* also explains that the [...]*. Consequently, the actual TRQs (exceptional tariff rate quotas) will not allow sufficient white sugar imports [...]* from Algeria³⁵⁸. Therefore, even if the Algerian refinery is operational at the end of 2012, it will have no financial incentive to supply white sugar into Italy and therefore does not constrain the Parties from increasing prices in the Italian white sugar market.
- (435) Moreover, [a large Italian sugar producer]* also indicated that it did not plan [...]* during the next 1-2 years³⁵⁹ and most importantly that "[a large Italian sugar producer]*³⁶⁰ while [a large Italian sugar producer]*³⁶¹ also confirmed to the Commission that it [market strategy]*.

³⁵⁶ Presentation by Südzucker to the Commission on the "Sugar Market in Italy" of 2 December 2011, slide 6 (Sugar Market in Italy Presentation to the Commission (M.6286) Brussels, 2. December 2011).

³⁵⁷ E-mails of Mr [...]* on 5 January 2012, at 18:25 and on 6 January 2012 at 08:01 entitled "M.6286 EDFM/Sudzucker - Algerian refinery".

³⁵⁸ E-mails of Mr [...]* on 5 January 2012, at 18:25 and on 6 January 2012 at 08:01 entitled "M.6286 EDFM/Sudzucker - Algerian refinery": "(...) [...]*".

³⁵⁹ Reply by [...]* ([...]* (reply to question 104) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁶⁰ E-mail by Mr [...]* of 12 January 2012 at 11/15, Subject: "Rif: M.6286 - Your reply to question 93 of the Questionnaire to sugar suppliers / producers in Italy - Phase II".

³⁶¹ E-mail of Mr [...]* of 11 January 2012 at 15:26 stating that "[...]*".

- (436) Especially as for the ability and incentive of expansion by Eridania/Cristal Union³⁶², the notifying party, in its reply to the Statement of Objections, without mainly putting forward new elements simply reiterates its arguments of the Form CO.
- (437) The only new element is that it takes the view that expansion of supply of white sugar to industrial processors could result from switching from supply of white sugar to retailers to supply of white sugar to industrial suppliers³⁶³ by Eridania who is an important operator in the field of supply of white sugar to retailers.
- (438) However, replies of the market players to new requests for information depict a different picture. Indeed, the new documents and information collected by the Commission, following the reply to the Statement of Objections by the notifying party, confirm the findings of the Statement of Objections in the sense that competitors do not have the ability or incentive to expand their sales to industrial customers in Italy, since it is not even possible or profitable to switch quantities from retail customers to industrial customers.
- (439) In reply to follow up questions sent by the Commission on 16 February 2012, producers/suppliers of white sugar in Italy indicated that they are not able to expand in Italy and they do not have incentives to do so. As to the claimed ability of suppliers/producers to increase quantities available to industrial processors at the expense of supplying the same sugar to retailers, none of these producers/suppliers finds it feasible and profitable to do so, mainly because of (i) the necessity to keep the loyalty of existing retail customers in the long-term, and (ii) the need to maintain low unit costs of sugar sold to retailers in the long-term taking into account the relevant costs, such as the cost of the marketing structure or the cost of the packaging lines³⁶⁴.

(i) *Conclusion*

- (440) On the basis of the above, it is concluded that notwithstanding the fact that Eridania and Cristal Union seem to be well established sugar suppliers on the Italian sugar market, they would have (a) limited ability and (b) no commercial incentives to substantially expand output post-merger in the Italian market for supply of white sugar to industrial processors even in response to a price increase.

(iii) *Italia Zuccheri / Pfeifer & Langen / COPROB*

(a) *Views of the notifying party*

- (441) According to the notifying party, Italia Zuccheri has expert knowledge of the Italian market, good client contacts and a good distribution network, being one of the incumbent Italian beet sugar manufacturers. Being an Italian company provides it furthermore with a "local touch" certain customers are seeking. Italia Zuccheri owns two beet factories producing around 290,000 tonnes. Italia Zuccheri, moreover, has access to imports from within the Union as it has a cooperation agreement with

³⁶² Paragraphs 185 - 191 of the reply of the notifying party to the Statement of Objections.

³⁶³ Paragraph 191 of the reply of the notifying party to the Statement of Objections.

³⁶⁴ The notifying party was informed about it by a Letter of Facts of 14 March 2012 and was provided with the non-confidential versions of the replies of the competitors.

Pfeifer & Langen, Germany's third largest beet sugar producer. To the further extend of release of out of quota sugar by the Commission additional sugar quantities would be available for the commercialisation in the Italian market. Furthermore, Italia Zuccheri and Pfeifer & Langen are building a refinery in Minerbio with a capacity of 150,000 tonnes, which will start operations in February 2012, allowing them to get access to further quantities of sugar for the Italian market³⁶⁵.

(b) *Historical background*

- (442) Italia Zuccheri is a historical operator on the Italian white sugar market. Via COPROB Italia Zuccheri has created a Joint-venture (Italia Zuccheri Commerciale S.r.l.) with Pfeifer & Langen ([shareholder structure of the joint-venture]*) on 27 November 2006 to share the sales in the Italian market. All the sugar quantities of COPROB and of Pfeifer & Langen intended for sale in Italy are sold via Italia Zuccheri Commerciale S.r.l.³⁶⁶.

(c) *Sources of supply and infrastructure*

- (443) Italia Zuccheri currently has two sugar production facilities: Minerbio ([...]* tonnes/year for beet – [...]* - while [...]* tonnes/year for cane) and Pontelongo COPROB ([...]* tonnes/year for beet, [...]*)³⁶⁷. It has sugar storages in Minerbio, Pontelongo, Argelato, Porto Viro, Finale Emilia and Pontelagoscuro³⁶⁸.

(d) *Market positioning*

- (444) Italia Zuccheri / COPROB / Pfeifer & Langen holds [20-30]*% market share in the market for the supply of white sugar to industrial processors in Italy.

(e) *Perception by COPROB*

- (445) COPROB considers that it has good access to sugar, very good infrastructure, very good national sales office with dedicated staff, good regional sales office with dedicated staff, very good established customer relationship and a specific partnership with Pfeifer & Langen³⁶⁹. However, it considers itself less competitive than Südzucker / EDFM in terms of access to input, price making and location to supply north and south of Italy. It also considers that it has less volume than Südzucker / EDFM³⁷⁰.

³⁶⁵ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 22, sent by e-mail of 1 December 2011 (19:33).

³⁶⁶ Reply by [...]* ([...]* (reply to question 7) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁶⁷ Reply by [...]* ([...]* (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁶⁸ Reply by [...]* ([...]* (reply to question 95) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁶⁹ Reply by [...]* ([...]* (reply to question 88) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁷⁰ Reply by [...]* ([...]* (reply to question 89) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

(f) *Perception by competitors*

- (446) [A large sugar producer]* takes the view that Italia Zuccheri has a fixed quota for beet sugar output and therefore has little flexibility to increase output and at current price levels raw sugar purchased on the free market (for example, from Brazil) cannot be sold profitably in the Union³⁷¹.

(g) *Perception by customers*

- (447) [A large customer]* emphasizes the partnership of Italia Zuccheri with Pfeifer & Langen and the fact that it has the largest Italian production quota and that it will soon start to refine raw sugar which constitutes its most important strength³⁷². [A customer]* indicated in general terms that Italia Zuccheri has more strengths compared to Eridania/Tereos and Zuccherificio del Molise³⁷³ while [a customer]* puts forward that Italia Zuccheri has its own refinery in Italy which constitutes a competitive advantage however it has no important sugar quantities³⁷⁴. [A large customer]* and [a large customer]*³⁷⁵ also underline the fact that the production of Italia Zuccheri is in Italy and the relationship with Pfeifer & Langen³⁷⁶ but, in line with [...]*, it has only small volume quota available (also emphasized by [a customer]*)³⁷⁷.
- (448) As already underlined, in general, Italian customers are very much concerned by the lack of sufficient sugar quantities available for the Italian sugar producers / suppliers³⁷⁸.

(h) *Assessment*

- (449) As already mentioned, the notifying party puts forward that Italia Zuccheri and Pfeifer & Langen have built a refinery in Minerbio with a capacity of 150,000 tonnes, which started operations in February 2012, allowing them to get access to

³⁷¹ "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...]* ([...]* (reply to question 61) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁷² Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³⁷³ Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

³⁷⁴ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II).

³⁷⁵ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II) and Reply by Dr Oetker (2011/129139) (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³⁷⁶ Underlined only by [...]*: Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

³⁷⁷ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II) and Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

³⁷⁸ See paragraph (428) of the present.

further quantities of sugar for the Italian market³⁷⁹. The investment adds refining capacity to an existing sugar beet production site.

- (450) In the Commission's view, it is unlikely that Italia Zuccheri / Pfeifer & Langen / COPROB will have the ability and incentives to substantially expand its supplies on the market for the supply of white sugar in Italy within the timeframe relevant for merger control.
- (451) As analysed in recitals (398) and (402) of this Decision, the Italian sugar market is production limited, Italian competitors are capacity constrained, sugar stocks in the Union are very low and significant shortage of access to preferential raw cane sugar is commonly known by the industry. In such difficult market conditions of scarcity of sugar, other major players with established presence in Italy such as Pfeifer & Langen with its joint venture with Italia Zuccheri, do not have the capacity and incentives to redirect substantial additional sugar quantities from other Member States to Italy since it would entail commercial risks to lose existing customers, lower margins due to transport costs and risk of failure of expansion due to risk of selective reaction of the post-merger entity.
- (452) Therefore, competitors such as Pfeifer & Langen and Italia Zuccheri would have limited ability to substantially increase white sugar supplies in Italy post-merger and such strategy does not appear to be profitable as it would imply the significant commercial risks to lose existing customers in the country of origin of the sugar, to get lower margins due to transport costs and the high risk of failure of expansion of market share due to the risk of selective reaction of the post-merger entity, Südzucker/EDFM.
- (453) To the very contrary Pfeifer & Langen would have the incentive to reallocate sugar quantities back to Germany. Indeed, first, the Commission observes significant scarcity of white sugar in the whole Union and also outside Italy. As a result of historically low stocks and scarcity of white sugar, prices have gone up significantly in all Member States³⁸⁰.
- (454) In this context the German NCA, Bundeskartellamt has indicated to the Commission³⁸¹ that the German white sugar market suffers from white sugar scarcity and historically high market prices. This situation could be a first rationale for a market strategy by Pfeifer & Langen to repatriate its current sugar exports to Italy back to Germany or other neighbouring markets where it could for those quantities compete and achieve higher margins on the basis of lower transport costs.
- (455) Also, [a large Italian sugar producer]* has indicated to the Commission that it is not in a position to expand its output in a short period of time in response to a price increase on the Italian white sugar market given (i) the production quota which is

³⁷⁹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 22, sent by e-mail of 1 December 2011 (19:33) and Presentation by Südzucker to the Commission on the "Sugar Market in Italy" of 2 December 2011, slide 6 (Sugar Market in Italy Presentation to the Commission (M.6286) Brussels, 2. December 2011).

³⁸⁰ Recital 2 of Commission Regulation (EU) No 222/2011 of 3 March 2011 laying down exceptional measures as regards the release of out-of-quota sugar and isoglucose on the Union market at reduced surplus levy during marketing year 2010/2011.

³⁸¹ Letter of the Bundeskartellamt to Mr [...] of 7 October 2011, (2011/107118).

fixed, and (ii) the constraints on sourcing preferential raw cane sugar. Notwithstanding the increase of its production in 2012 due to the investment made to [...]*,[a large Italian sugar producer]* confirmed that as a matter of organisation of their supplies they will not be able to supply additional quantities in the Italian market post-merger³⁸². Indeed, [a large sugar producer]* indicated to the Commission that "[...]*"³⁸³. The Commission considers that this strategy of reorganisation of supplies makes economic sense in the current market circumstances as described above.

- (456) Especially as for the ability and incentive of expansion by Italia Zuccheri / COPROB / Pfeifer & Langen³⁸⁴, the notifying party, in its reply to the Statement of Objections, without hardly putting forward any new elements simply reiterates its arguments in the Form CO.
- (457) The only new element is that it takes the view that expansion of supply of white sugar to industrial processors could result from switching from supply of white sugar to retailers to supply of white sugar to industrial suppliers³⁸⁵ by Italia Zuccheri who is "*also*" an important operator in the market for the supply of white sugar to retailers.
- (458) However, as analysed in recitals (439) and (440) of this Decision, market players indicated to the Commission that such switch would not be feasible and profitable due to (i) the necessity of keeping the loyalty of existing retail customers in the long-term, and (ii) the need to maintain low unit costs of sugar sold to retailers in the long-term taking into account the relevant costs, such as the cost of the marketing structure or the cost of the packaging lines³⁸⁶.

(i) *Conclusion*

- (459) Therefore, after the analysis of the above, notwithstanding the fact that Italia Zuccheri / COPROB and Pfeifer & Langen seem to be well established sugar producers / suppliers on the Italian sugar market, they would have (a) limited ability, and (b) no commercial incentives to substantially expand output post-merger in the Italian market for supply of white sugar to industrial processors, even in the event of a price increase by the merged entity.

³⁸² Reply by [...]* ([...]* (reply to question 91) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) and e-mail of [...]* from [...]* of 13 January 2012 at 15:54, entitled: " M.6286 - Your reply to question 93 of the Questionnaire to sugar suppliers / producers in Italy - Phase II - [...]*" and Reply by [...]* (reply to question 93) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁸³ E-mail of [...]* from [...]* of 13 January 2012 at 15:54, entitled: " M.6286 - Your reply to question 93 of the Questionnaire to sugar suppliers / producers in Italy - Phase II - [...]*".

³⁸⁴ Paragraphs 192 - 198 of the reply of the notifying party to the Statement of Objections.

³⁸⁵ Paragraph 198 of the reply of the notifying party to the Statement of Objections.

³⁸⁶ The notifying party was informed about it by a Letter of Facts of 14 March 2012 and was provided with the non-confidential versions of the replies of the competitors.

(iv) *Tereos*

(a) *Views of the notifying party*

- (460) According to the notifying party, French sugar producer Tereos plays and will continue to play a significant role in Italy. It has gone into a different direction than other sugar producers by having established its own sugar marketing company in Italy. Tereos belongs to the group of five beet sugar producers that according to the Commission account for a combined 80% of the sugar beet processing capacity and 72% of the Union sugar market. Furthermore, Tereos has strong links to a number of raw cane exporting countries, such as Mozambique. This access to sugar combined with a network of local distribution companies in Italy would enable Tereos to readily increase its LDC/ACP supply to Italy in case Südzucker/ESI would increase their prices in Italy following completion of the proposed transaction³⁸⁷.
- (461) Südzucker believes that Tereos is delivering 40% to wholesalers (instead of 20% like the others) because Tereos has established its own marketing company while the other big sugar producers entered into cooperations with local companies, in most cases with a local producer. Absent long-established local contacts, the notifying party considers that it should be more difficult for Tereos to build up and develop a client network in industry and retail. To reach its sales volume, Tereos will therefore probably have to rely to a much greater extent on sales to wholesalers³⁸⁸.

(b) *Historical background*

- (462) Tereos is a cooperative agro-industrial group, specialized in the production and supply of sugar, alcohol, bio-ethanol, sweeteners and by-products. Tereos is mainly a producer of sugar. Tereos sells industrial sugar in almost all Member States while its sales of retail sugar are geographically more restricted³⁸⁹. Tereos Group, which is active at European level, created in 2006/2007 "Tereos Italy", its own commercial office in Milan to facilitate its business in Italy with a [...] sales organisation. This new entity is in charge of the contacts with local customers of Tereos Group and sales in Italy are conducted through it³⁹⁰.

(c) *Sources of supply and infrastructure*

- (463) Tereos has no sugar factory or refinery in Italy and Tereos supplies the Italian market via its sugar factories situated in France³⁹¹.

³⁸⁷ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 22, sent by e-mail of 1 December 2011 (19:33).

³⁸⁸ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 22, sent by e-mail of 1 December 2011 (19:33).

³⁸⁹ Reply by [...] (reply to questions 3 and 5) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁹⁰ Non-confidential Minutes [...] – 18 November 2011

³⁹¹ Reply by [...] (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

(d) *Market positioning*

- (464) Tereos holds [10-20]*% market share in the market for the supply of white sugar to industrial processors in Italy.

(e) *Perception by Tereos*

- (465) With regard to its Italian market entry Tereos puts forward that in the context of the reform of the sugar sector in the Union, Tereos benefited from important volumes of quota sugar to reallocate from France. Tereos therefore increased its sales into other Member States (from France) in 2005/2006 and at the same time carried out investments to develop its commercial presence outside France. In 2005/2006, Tereos reallocated volumes that were initially shipped outside the Union, taking into account pricing, customers requests and logistic aspects. This was the first stage of expansion of Tereos outside France. Since this period Tereos has been increasing its activities all over the Union by creating local subsidiaries. Indeed, Tereos developed a European network notably by creating commercial subsidiaries in various European countries. Tereos has therefore been in a position to satisfy the demand of its industrial clients that were increasingly requesting it to secure the supply of their plants throughout the Union³⁹². In Italy, Tereos sells only white sugar to industrial processors³⁹³.

(f) *Perception by competitors*

- (466) [A large Italian sugar producer]* describes Tereos on the Italian white sugar market as having very good access to input, with no infrastructure in Italy, very light national sales office, inexistent regional sales office and without partnership on the Italian white sugar market³⁹⁴ as well poor customer relationship³⁹⁵ and no ability to expand its sugar output³⁹⁶.
- (467) [A large sugar producer]* takes the view that Tereos (based in France) has a large sugar beet quota thus incurring low production costs and since Italy is close to its domestic market it can export to Italy without bearing high distribution costs³⁹⁷.
- (468) [A large Italian sugar producer]* also explains in respect of Tereos' successful market entry in the Italian white sugar market in 2006 that "*[t]he decrease of Italian production had to be compensated by higher French inflows as forecasted by the*

³⁹² Reply by [...]* (reply to questions 7 and 8) (Non-Confidential Version – Questionnaire to [...]* – Phase II) (received by e-mail of 9 January 2012 at 18:15).

³⁹³ Reply by [...]* (reply to question 1.g) (Non-Confidential Version – Questionnaire to [...]* – Phase II) (received by e-mail of 9 January 2012 at 18:15).

³⁹⁴ Reply by [...]* ([...]* (reply to question 58) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁹⁵ Reply by [...]* ([...]* (reply to question 69) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁹⁶ Reply by [...]* ([...]* (reply to question 59) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁹⁷ "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...]* ([...]* (reply to question 63) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

Commission" and such entry was easy in view of the sugar deficit created by the 2006 sugar reform³⁹⁸.

(g) *Perception by customers*

- (469) In view of [a large customer]*, Tereos represents the largest French sugar producer with big share on the Italian market and "*will definitely increase it*" while it delivers only from factories in the Union with some risk of limited quantities in case of bad crop or other events³⁹⁹ while, according to [a large customer]*, Tereos is not competitive but only follows the policy of Südzucker and it does not "*disturb*" the latter's market approach, its strength being that it has "*huge*" French production but is not flexible and has only a short term approach vis-à-vis the Italian white sugar market coupled with a low degree of services⁴⁰⁰. [A large customer]* describes Tereos without strengths while making echo of its poor customer relationship resulting from lack of trustworthiness⁴⁰¹. [A customer]* also doubts that Tereos is a competitive player on the Italian sugar market since it delivers from the northern part of France to Italy⁴⁰².
- (470) As for the incentives of Tereos to enter the Italian white sugar market, [a large customer]* underlines that Tereos is the largest French sugar producer whose production costs are the lowest interested in entering a deficit market such as Italy⁴⁰³. [A large customer]* or [a large customer]* see in Tereos' market entry only an opportunity to fill the gap in a largely deficit region that is Italy⁴⁰⁴ in order to market their "*surplus French sugar*"⁴⁰⁵ while [a large customer]* puts forward the proximity of the French sugar factories to Italy and such French factories are more competitive than the sugar produced in Italy⁴⁰⁶. From a different angle [a large customer]* would have the same view about the entry of Tereos on the Italian sugar market; it sees indeed that Tereos "*bought the market with low prices. Now, they get their money back!!*"⁴⁰⁷ in other words [a large customer]* seems to indicate that Tereos dumped French sugar on the Italian market in order to obtain market shares and once its market shares stabilised it was no longer necessary for it to maintain relatively low

³⁹⁸ Reply by [...]* ([...]* (reply to question 62) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

³⁹⁹ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁰⁰ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁰¹ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁰² Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁰³ Reply by [...]* ([...]* (reply to question 49) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁰⁴ Reply by B[...]* ([...]* (reply to question 49) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁰⁵ Reply by [...]* ([...]* (reply to question 49) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁰⁶ Reply by [...]* ([...]* (reply to question 49) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁰⁷ Reply by [...]* ([...]* (reply to question 49) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

sugar prices. In this respect, [a customer]* also emphasizes that for the time being Tereos is not competitive and the quantities dedicated to Italy are "too low"⁴⁰⁸.

(h) *Assessment*

- (471) As already indicated, the notifying party puts forward that Tereos has strong links to a number of raw cane exporting countries, such as Mozambique. Moreover, it is also put forward that this access to sugar combined with a network of local distribution companies in Italy would enable Tereos to readily increase its LDC/ACP supply to Italy in case Südzucker/ESI would increase their prices in Italy following completion of the proposed transaction⁴⁰⁹.
- (472) However, Tereos expressly indicated to the Commission that it does not intend to expand its output in the Italian sugar market during the next three years and post-merger⁴¹⁰.
- (473) In the Commission's view, the ability and incentives for Tereos to substantially expand supplies on the market for supply of white sugar in Italy within the timeframe relevant for merger control are limited.
- (474) As analysed in recitals (398) and (402) of this Decision, the Italian sugar market is production limited, Italian competitors are capacity constrained, sugar stocks in the Union are very low and significant shortage of access to preferential raw cane sugar is commonly known by the industry. In such difficult market conditions of scarcity of sugar, other major players with established presence in Italy such as Tereos, do not have the capacities and incentives to redirect substantial additional sugar quantities from other Member States to Italy since it would entail commercial risks to lose existing customers, lower margins due to transport costs and risk of failure of expansion of market share due to risk of selective reaction of the post-merger entity.
- (475) Therefore, competitors such as Tereos would have limited ability to substantially increase white sugar supplies in Italy post-merger and such strategy does not appear to be profitable as it would imply the significant commercial risks to lose existing customers in the country of origin of the sugar, to get lower margins due to transport costs and the high risk of failure of expansion of market share due to the risk of selective reaction of the post-merger entity, Südzucker/EDFM.
- (476) Indeed, Tereos is the one and only non-domestic sugar manufacturer who succeeded in entering the Italian sugar market following the Union sugar reform in 2006/2007 without entering into cooperation with a local player. Indeed, other foreign players entered the Italian market such as Südzucker, Tate & Lyle, Cristal Union or Pfeifer & Langen but only in cooperation with local players such as MAXI, Eridania or Italia Zuccheri/COPROB. Therefore, its unique situation in the Italian sugar market

⁴⁰⁸ Reply by [...] (replied to question 49) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II).

⁴⁰⁹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 22, sent by e-mail of 1 December 2011 (19:33).

⁴¹⁰ See e-mails by the legal representatives of [...], Mrs [...] and Mr [...], of 10 January 2012 at 15:50 and at 16:12 "[w]e confirm that [...] does not intend to increase its presence in Italy in the next three years".

is obvious leading the Commission to pay particular attention⁴¹¹ in its analysis to the incentives of Tereos to enter, to develop its market presence in the Italian white sugar market and also its capacity to do so.

- (477) In the mid 2000 Tereos had at its disposal important sugar quantities to allocate in the Union. Indeed, in the context of the reform of the sugar sector in the Union, Tereos benefited from important volumes of quota sugar to reallocate from France and it therefore increased its sales into other Member States (from France) in 2005/2006 and at the same time carried out investments to develop its commercial presence outside France by having reallocated volumes that were initially shipped outside the Union, taking into account pricing, customers requests and logistic aspects⁴¹². In other words Tereos benefited from important sugar stocks that it could reallocate in deficit markets at commercially interesting price in order to develop its market presence in a given market⁴¹³.
- (478) Its market entry in Italy is thus rather a specific situation than reflection of the sign of significant competition. Indeed, [...] explains that Tereos' successful market entry in the Italian white sugar market in 2006 is due to the fact that "[t]he decrease of Italian production had to be compensated by higher French inflows as forecasted by the Commission" and such entry was easy taken into account the sugar deficit created by the 2006 sugar reform. This view is also acknowledged by Tereos when it explains that Tereos benefited from important volumes of quota sugar to reallocate from France to other Member States following the 2006 sugar reform. Indeed, Tereos therefore reallocated in 2005/2006 volumes that were initially shipped outside the Union and increased its sales into other Member States (from France) for the obvious reason to take advantage of deficit nature of the Italian sugar market. Indeed, Tereos' market entry can be seen as only a specific opportunity in the past to fill the gap in a largely deficit region that is Italy⁴¹⁴ in order to market their "surplus French sugar"⁴¹⁵.
- (479) However, notwithstanding the fact that Tereos entered recently the Italian white sugar market without local partnership, Tereos has remained a player with a light Italian sales organisation and is exclusively focused on supply of white sugar to industrial processors. Also, the market shares of Tereos have remained stable over the last years⁴¹⁶ since its entry and the lacunas in the quality of its customer relationship were also highlighted by some customers. All these elements taken together do not militate in favour of an analysis pointing towards a dynamic maverick entrant able to expand in Italy.
- (480) As for its future market development, in the light of its stable market presence in Italy, it is doubtful that Tereos will develop its sales organisation and will reallocate

⁴¹¹ See also recital (412) of this Decision.

⁴¹² Reply by [...] (reply to questions 7 and 8) (Non-Confidential Version – Questionnaire to [...] – Phase II) (received by e-mail of 9 January 2012 at 18:15).

⁴¹³ Reply by [...] ([...]) (reply to question 49) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴¹⁴ Reply by [...] ([...]) (reply to question 49) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴¹⁵ Reply by [...] ([...]) (reply to question 49) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴¹⁶ See for example recital (189) of this Decision.

additional sugar quantities in Italy even in case of price increase. Indeed, the conditions of its market entry are different from the ones currently applicable in the Union and in Italian sugar markets and do not advocate for an incentive for further expansion. As explained by Tereos itself, its successful market entry in Italy was basically conditioned by two elements: (a) Italy is a deficit market, (b) it had available stocks to reallocate. While Italy is still a deficit market, sugar stocks in the Union are historically low therefore any strategy of expansion for Tereos would be much less profitable as it was in the past in view of the high number of significant risks that such a strategy would imply as described in recitals (398) and (402) of this Decision. In the same line of logic, Tereos expressly indicated to the Commission that it does not intend to expand its output in the Italian sugar market during the next three years, and therefore post-merger⁴¹⁷. The reason behind Tereos' market strategy with regard to Italy appears to be linked to the absence of enough quantities to be allocated in the Italian white sugar market.

(481) Therefore, Tereos would have limited ability and no incentives to expand on the Italian white sugar market, even in the event of price increase following the proposed transaction.

(482) Especially as for the ability and incentive of expansion by Tereos⁴¹⁸, the notifying party, in its reply to the SO, without putting forward new elements simply reiterates its arguments of the Form CO.

(i) *Conclusion*

(483) In light of the above, it is concluded that Tereos would have limited ability and no incentives to substantially expand output in the Italian market for supply of white sugar to industrial processors even in case of a price increase by the merged entity.

(v) *Zuccherificio del Molise*

(a) *Views of the notifying party*

(484) According to Südzucker, Zuccherificio del Molise has one of the four still active beet sugar factories in Italy. The quota allocated to Zuccherificio del Molise is between 60,000 and 70,000 tonnes/year. The production and sugar marketed is estimated to about 72,000-76,000 tonnes/year. Zuccherificio del Molise is located in the South of Italy. Südzucker assumes that most of the sugar produced is sold locally⁴¹⁹.

(b) *Historical background*

(485) Zuccherificio del Molise is a producer and distributor of sugar in the Centre and South of Italy⁴²⁰.

⁴¹⁷ See e-mails by the legal representatives of [...]*, Mrs [...]* and Mr [...]*, of 10 January 2012 at 15:50 and at 16:12 "[w]e confirm that Tereos does not intend to increase its presence in Italy in the next three years".

⁴¹⁸ Paragraphs 199 - 200 of the reply of the notifying party to the Statement of Objections.

⁴¹⁹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 23, sent by e-mail of 1 December 2011 (19:33).

⁴²⁰ Reply by [...]* ([...]* (reply to question 5) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

(c) *Infrastructure*

- (486) Zuccherificio del Molise has a beet sugar factory in Termoli with an annual quota of 84.326tonnes/year⁴²¹.

Market positioning

- (487) Zuccherificio del Molise holds [0-5]*% market share in the market for the supply of white sugar to industrial processors in Italy.

(d) *Perception by competitors*

- (488) [A large Italian sugar producer]* describes Zuccherificio del Molise on the Italian white sugar market with poor access to input, poor infrastructure, poor customer relationship, poor national-regional sales office and without any partnership and in addition without the ability to expand its output on the Italian sugar market⁴²².

(e) *Perception by customers*

- (489) [A large customer]* puts forward that Zuccherificio del Molise is a public sugar producer in a deficit area with low volume produced coupled with financial instability and low market shares⁴²³. [A customer]* indicated that "*ESI/SFIR, MAXI and Italia Zuccheri have more strengths compared to Eridania/Tereos and Zuccherificio del Molise*"⁴²⁴ or [a customer]* putting forward that ESI, Italia Zuccheri, Eridania and Zuccherificio del Molise have their own refineries in Italy which constitutes a competitive advantage. However, none of those sugar producers/suppliers has large sugar quantities⁴²⁵. The description by [a larger customer]* is much less positive since it is put forward that "*they should have disappeared several years ago*" maybe for political reasons they have not⁴²⁶ while [a customer]* explains that it is not a competitive market player⁴²⁷.

(f) *Possibility to expand output*

- (490) The notifying party does not submit that Zuccherificio del Molise would be in a position to expand its sugar output on the Italian white sugar market and it was several times underlined that Italian customers are very much concerned by the lack of sufficient sugar quantities at the disposal of the Italian sugar producers /

⁴²¹ Reply by [...]* ([...]* (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴²² Reply by [...]* ([...]* (reply to questions 58, 59 and 69) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴²³ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴²⁴ Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴²⁵ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II).

⁴²⁶ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴²⁷ Reply by [...]* ([...]* (reply to question 43) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

suppliers⁴²⁸. In this respect, [a large Italian sugar producer]* claims that Italy is a highly deficit country in terms of sugar⁴²⁹ and no player on the Italian market is in a position to expand in a short period of time its output as a reply to a price increase due to the fact that "*all the players deal with production quotas which are fixed and with constraints in access to preferential sugar*"⁴³⁰. [A customer]* underlines also with regard to Zuccherificio del Molise that it does not have large sugar quantities⁴³¹.

(g) *Assessment*

(491) Neither Südzucker or any other competitor nor customers take the view that Zuccherificio del Molise would be a well positioned competitive market player able to expand its white sugar supplies in the event of an increase of white sugar prices following the proposed transaction on the Italian market.

(h) *Conclusion*

(492) Following the analysis of the above, Zuccherificio del Molise does not seem to be a well-positioned market player and does not seem to have the ability and the incentives to substantially expand output in the Italian market for supply of white sugar to industrial processors in the event of a price increase by the merged entity.

(vi) *Others (other Union or Balkan sugar producers / suppliers)*

(493) The notifying party also claims that other sugar producers in the Union or in the Balkans (Serbia and Croatia) also exert competitive constraint on the post-merger entity⁴³². The in-depth market investigation, however, did not confirm this view.

(a) *Views of the notifying party*

(494) Südzucker claims that there are a number of other players from the Union who supply the Italian market. Such producers include Group Vermandoise, Cosun/Suiker Unie, British Sugar/Azucarera Ebro or Krajowa Spolka Cukrowa, Sunoko doo, Kandit Premijer, Viro Tvornica Secera etc.⁴³³.

⁴²⁸ For example, Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II), Reply by Daila (2011/129886) (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II) or Reply by Nestlé (2011/130092) (reply to question 23) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴²⁹ Reply by [...]* ([...]* (reply to question 112) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴³⁰ Reply by [...]* ([...]* (reply to question 59) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴³¹ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II).

⁴³² Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 23, sent by e-mail of 1 December 2011 (19:33).

⁴³³ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 23, sent by e-mail of 1 December 2011 (19:33).

- (495) The notifying party has estimated sales by those "other competitors" (including both other Union and Western Balkan producers) at 78,000 tonnes in 2010 (56,500 tonnes industry and 21,500 tonnes retail), at 79,058 tonnes for 2011 (57,464 tonnes industry and 21,594 retail) and at 67,000 tonnes for 2012 (57,000 industry and 10,000 retail)⁴³⁴.
- (496) In this respect it is also put forward by the notifying party that a significant price increase by Südzucker/ESI, which does not result from the increase of the sugar price on the world market, would provide an incentive for those sugar producers to enter/expand on the Italian market as customers would switch demand away from Südzucker/ESI and towards other sources⁴³⁵.

(b) *Market investigation*

- (497) As for sugar producers established in the Union, within the course of the second phase investigation, [a large sugar producer]* indicated to the Commission that it currently has no activities on the Italian market⁴³⁶, [a large sugar producer]* stated that it does not supply and has not ever supplied Italy from any of its production facilities⁴³⁷ while only [a sugar producer]* indicated to have supplied some quantities in Italy but only limited quantities⁴³⁸.
- (498) Concerning Western-Balkan sugar (Serbia / Croatia), most importantly, in its reply to the Commission in-depth market investigation, [a sugar producer]* indicated to the Commission that it is not able to expand in a short time period its production quantity in response to a price increase or sugar deficit in the Italian sugar market and that it has no competitive advantage in terms of transport costs in Italy⁴³⁹.
- (499) In this respect [a large sugar producer]* takes the view that third countries of the Balkans which are close to Italy can exert a competitive pressure on Italy since imports from these countries have a duty free access to the Union market (equal to 380,000 tonnes)⁴⁴⁰.

⁴³⁴ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 23, sent by e-mail of 1 December 2011 (19:33).

⁴³⁵ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 23, sent by e-mail of 1 December 2011 (19:33).

⁴³⁶ Reply by [...]* ([...]* (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2584).

⁴³⁷ Reply by Associated British Foods (2011/130802) (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2147).

⁴³⁸ Reply by [...]* ([...]* (reply to question 11) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2817). In this regard, it has to be also emphasized that [...] confirmed to the Commission that it does not intend to increase its presence in Italy in the next three years however with the very recent [...] in the Italian sugar market (E-mail of Mr [...] of 11 January 2012, at 15:26).

⁴³⁹ Reply by [...]* ([...]* (reply to questions 93 and 95) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2364).

⁴⁴⁰ Reply by [...]* (reply to question 65) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

- (500) On the other hand [a large sugar producer]* states that it has not observed any competitive constraint from producers in countries such as Serbia or Croatia on the Italian white sugar market⁴⁴¹.
- (501) In the same context [a large Italian sugar producer]* explains that the success of export from the Balkans to Italy was linked to a positive swap of world market sugar, with these countries exporting their production and importing for their domestic consumption needs. Consequently, in the event of an increase in international market prices there is no interest to supply Italy from the Balkans. In addition Eastern European countries which are also deficit countries are closer to the Balkans sugar producers and will therefore (allegedly) be first supplied⁴⁴². The same view is held by [a large sugar producer]* which submits that *"it is generally difficult to bring more white sugar to Italy from the Balkans. Especially for Croatia it is anticipated that there will be a reduction in the available quantity to be exported due to the entry of the country in the EU. Following accession Croatia will have a quota of approximately 190.000 tonnes while currently it exports to the EU 180.000 tonnes and domestic consumption is approximately 70.000 tonnes. White sugar from the Balkans goes mainly to Slovenia, Hungary and Greece"*⁴⁴³.
- (502) Seven Italian wholesalers including [a customer]* indicate that they purchase sugar from the West Balkans (Croatia and Serbia)⁴⁴⁴ and [a customer]* indicates that Serbian and Croatian sugar has been imported in Italy for many years by Italian traders⁴⁴⁵. On the other hand, most customers [a customer]*⁴⁴⁶, [a customer]*⁴⁴⁷, [a customer]*⁴⁴⁸, [a large customer]*⁴⁴⁹, [a large customer]*⁴⁵⁰, [a large customer]*⁴⁵¹, [a large customer]*⁴⁵², [a large customer]*⁴⁵³ or [a large customer]*⁴⁵⁴ indicate that

⁴⁴¹ "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...]* ([...]*) (reply to question 65) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴⁴² Reply by [...]* ([...]*) (reply to question 63) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴⁴³ Non-confidential version of the Minutes of the Teleconference with [...]* on 8 December 2011, paragraph 10.

⁴⁴⁴ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁴⁵ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁴⁶ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁴⁷ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁴⁸ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁴⁹ Reply by [...]* ([...]*) (reply to question 47) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁵⁰ Reply by [...]* Italia ([...]*) (reply to question 47) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁵¹ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁵² Reply by [...]* ([...]*) (reply to question 47) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁵³ Reply by [...]* ([...]*) (reply to question 47) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁵⁴ Reply by [...]* ([...]*) (reply to question 47) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

they have no experience with sugar producers from the Balkans and are not aware of any activities on the Italian sugar market.

(c) *Assessment*

- (503) As for the actual situation, the proportion of sugar imported on the Italian white sugar market by other Union based sugar producers or by Balkan producers is not very high even in the most optimistic scenario as presented by the notifying party. Indeed, the notifying party puts forward that into Italy 78,000 tonnes/year⁴⁵⁵ are imported by other Union and Balkan sugar producers. This would represent approx. 4.5% of Italian annual consumption, which is 1.73 million tonnes per year⁴⁵⁶. Even if this quantity is not large, in addition no element of the market investigation has shown the existence of such a quantity. Indeed, the sugar quantities imported by Vermandoise into Italy constitute only limited quantities. As a result, the estimation put forward by Südzucker as for the imports from other Union sugar producers to Italy seem to be too optimistic. With respect to sugar imported into Italy from the Balkans, [a large sugar producer]* indicated to the Commission that no sugar is imported into Italy from its Balkans sites⁴⁵⁷, while the sugar quantities imported by [a large sugar producer]* in Italy were by far lower⁴⁵⁸ the 78,000 tonnes indicated by the notifying party while another important player also indicated that it had no sales in Italy during the campaign year 2010/2011. As a result, the estimation put forward by Südzucker as for the imports from the Balkans and also for other competitors in the Union to Italy seem to be too optimistic.
- (504) In addition, none of the other Union based sugar producers indicated plans to enter or expand in the Italian sugar market.
- (505) Furthermore, some respondents ([a large Italian sugar producer]*⁴⁵⁹, [a large sugar producer]*⁴⁶⁰) take the view that Eastern Central European Member States such as Slovenia or Hungary are more natural destinations of Balkan sugar than Italy. And anyhow as a result of the Croatian accession to the Union much less sugar from Croatia will be available.
- (506) Therefore, no expansion on the Italian white sugar market is foreseen and available quantities from the Balkans to the Union will also significantly lower as a result of the Croatian accession to the Union.
- (507) As a result of the accession of Croatia in March 2013, the exports from Croatia to the Union (including Italy) will be completely reorganised and the sugar quantities

⁴⁵⁵ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 23, sent by e-mail of 1 December 2011 (19:33).

⁴⁵⁶ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 12, sent by e-mail of 1 December 2011 (19:33).

⁴⁵⁷ E-mail of 13 February 2012 by H[...] *entitled "RE: Sales in Italy" received at 14:55.

⁴⁵⁸ Reply by [...] * ([...] *) (reply to question 13) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2364).

⁴⁵⁹ Reply by [...] * ([...] *) (reply to question 63) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁴⁶⁰ Non-confidential version of the Minutes of the Teleconference with [...] * on 8 December 2011, paragraph 10.

currently exported to the Union (also Italian) white sugar market from Croatia will be reverted to domestic use.

- (508) In particular, the two main principles behind the determination of Croatia's post-accession sugar production quota were (i) that this quota should not add a surplus to sugar balance in the Union, and (ii) that this quota should not exceed Croatia's domestic consumption. Thus, Croatia's sugar production quota was set at 192,877 tonnes/year based on the level of domestic consumption in the reference period 2004-2008.
- (509) At present, Croatia produces 260,000 tonnes/year, while its domestic consumption is approximately 193,000 tonnes/year. Given Croatia's current export quota of 180,000 tonnes/year to the Union, 180,000 out of 260,000 tonnes are exported to the Union, whereas 80,000 out of these 260,000 tonnes are consumed in Croatia. The remaining 113,000 tonnes of Croatian consumption are satisfied through duty-free imports.
- (510) Following accession, Croatia will benefit from a production quota of approximately 192,877 tonnes/year and a preferential import quota of 40,000 tonnes/year.⁴⁶¹ The present Croatian sugar import regime will be substituted by the Union sugar import regime, thus erasing Croatia's possibility to import unlimited duty-free quantities and exporting almost all its domestic production to the Union. These 40,000 tonnes will partly satisfy the 193,000 tonnes of Croatian consumption. The remaining 153,000 tonnes of Croatian consumption will be satisfied by the three Croatian factories, which will produce on the basis of the quota of 192,877 tonnes/year. This leaves 40,000 tonnes/year for export to the rest of the Union, significantly less than the 180,000 tonnes/year exported today.
- (511) As for the Serbian sites, the most important sugar producer in Serbia in terms of production and storage capacities according to the notifying party is by far [a large sugar producer]*. However, as already mentioned [a large sugar producer]* indicated to the Commission that it was not in a position to expand in a short time period its production quantity in response to a price increase or sugar deficit in the Italian sugar market and that it has no competitive advantage in terms of transport costs in Italy⁴⁶².
- (512) Consequently, significant additional sugar imports from the West-Balkans (Croatia and Serbia) to Italy cannot be considered as likely. To the contrary, as a result of the expected Croatian accession to the Union much lower quantities of sugar will be available to the Union and thus West Balkan sugar producers cannot constitute a viable and foreseeable competitive pressure on the Italian white sugar producers / suppliers including the Parties.
- (513) In its extensive reply to the Statement of Objections, the notifying party does not contest the analysis of the Commission on the point that following the accession of Croatia to the Union in 2013 less sugar will be available to the Union from Croatia. The notifying party only puts forward with regard to the competitive constraints by West-Balkan sugar producers that sugar prices adhere to the international market

⁴⁶¹ The preferential import quota will be valid only for a period of up to three marketing years following Croatia's accession at an import duty of EUR98 per tonne.

⁴⁶² Reply by [...]* ([...]* (reply to questions 93 and 95) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) ([...]*).

price and in consequence there is a "*high competitive pressure*" from the Balkans without however putting forward new element as compared to the Form CO.

(d) *Conclusion*

- (514) Following the detailed examination of the arguments put forward by the Parties and the results of the market investigation, it is concluded that the sugar producers / suppliers established outside Italy (in the Union or Balkans) are not able to expand their output in Italy and following the Croatian accession to the Union further scarcity in sugar will be observed in the Union potentially leading to higher prices.

(vii) *Others (wholesalers)*

- (515) The notifying party puts forward that⁴⁶³ there is an additional category of suppliers, the "wholesalers", to whom the Parties attributed 20% of the market for sales to industrial processors and 18% of the market for sales to retailers in Italy.

- (516) However, as extensively explained above the arguments submitted by Südzucker for the attribution of sales to Italian "wholesalers" in the Italian markets for the sale of white sugar to industrial processors and to retailers cannot be accepted within the course of the assessment of the proposed transaction. First, the second phase market investigation largely infirmed the notifying party's view. Second, wholesalers in principle do not source sugar from suppliers which are outside the normal Italian supply circle. In the limited occasions that they do so, it is for limited quantities and, even then, wholesalers still depend on existing Italian players for the vast majority of their supplies. Third, no internal documents of the Parties present wholesalers as a competitive force. On the contrary, internal documents of the Parties present wholesalers as pure intermediaries between them and the end-customers⁴⁶⁴.

(viii) *Imports from ACP/LDC countries and regulatory measures*

- (517) The notifying party puts forward in its reply to the Statement of Objections that additional competitive pressure can be exercised by ACP/LDC countries and in times of significant scarcity the Commission "*may*" release out-of-quota sugar and authorise additional imports in the Union.
- (518) In particular, the notifying party argues⁴⁶⁵ that in the hypothesis of the European sugar price inferior to international market price ACP/LDC exporters would have incentive to export more raw cane sugar into the Union.
- (519) In this respect it has to be underlined that it is a hypothetical scenario. Currently, the Union and Italian sugar markets are characterized by significant sugar scarcity.⁴⁶⁶ The alleged hypothetical market condition is not evidenced to be likely to take place and under current market conditions there is no ability and incentive for the

⁴⁶³ Annex 4 of Südzucker's answer to the 3rd RFI in Phase I.

⁴⁶⁴ See recitals (309) to (331) of this Decision.

⁴⁶⁵ Paragraphs 216 – 218 of the reply of the notifying party to the Statement of Objections.

⁴⁶⁶ Paragraphs 73 or 75 of the Statement of Objections.

APC/LDC producers to import more sugar into the Union. This is precisely one of the reasons for the current significant sugar shortage in the Union⁴⁶⁷.

- (520) As for the regulatory measures the notifying party submits⁴⁶⁸ that the Commission constantly monitors prices and quantities in the sugar market and that the producers have to report prices and three months in advance their expected sales. Imbalances are instantly traced and the Commission can react to any perceived scarcity of supply by using its regulatory instruments. According to Article 186 of Regulation (EC) No 1234/2007 the Commission "*may*" take the necessary measures in situations disturbing or threatening to disturb the markets with regard to among others sugar, where the prices on the Community market rises or falls significantly.
- (521) In fact, in accordance with Article 186 of the Regulation (EC) No 1234/2007, "*The Commission may take the necessary measures in the case of the following situations, when those situations are likely to continue, thereby disturbing or threatening to disturb the markets: (a) with regard to the products of the sugar (...), where the prices on the Community market for any of those products rise or fall significantly (...)*" (emphasis added).
- (522) In this respect it has to be emphasized that the Commission is not obliged to systematically take such measures, it has the possibility to do so but it does not mean that it proceeds systematically this way. Then, any exceptional Commission intervention would be only for a limited duration and quantities while it concerns price falls and increases in the Community as a whole and not necessarily in Italy.
- (523) Therefore, Article 186 of the Regulation 1234/2007 does not constitute a sufficient legal protection in order to systematically counteract on a permanent basis the continuous negative effects of the proposed transaction on the market for the supply of white sugar to industrial processors in Italy.

Conclusion

- (524) In the light of the above, the Commission takes the view that notwithstanding the fact that some market players are well established in terms of infrastructure, customer relationship or specific partnership with a sugar supplier, they are unlikely to increase supply in the event of price increases by the merged entity on the market for the supply of white sugar to industrial processors in Italy. Indeed, the Italian sugar market is a highly deficit market coupled with fixed production quotas. Moreover, as a result of the Croatian accession expected for 2013 further important input quantities will disappear while no additional quantities are foreseen to be imported from Algeria or Sudan in the foreseeable future. Most importantly, all major competitors in Italy ([sugar producers]*) or outside Italy ([sugar producers]*) have expressly indicated to the Commission that they are not in a position to expand in the Italian sugar market in case the proposed transaction takes place, while wholesalers would not constitute a competitive constraint on the post-merger entity.
- (525) On the basis of the above, the arguments invoked by the notifying party do not amount to significant competitive pressure within the meaning of paragraphs 32 – 35

⁴⁶⁷ Recitals (69) and (70) of this Decision.

⁴⁶⁸ Paragraphs 228 and 229 of the reply of the notifying party to the Statement of Objections.

of the Horizontal Merger Guidelines to counteract the negative effects of the proposed transaction.

6.1.4.4. Countervailing buying power

Views of the notifying party

- (526) In the notification, the notifying party does not invoke the existence of countervailing buying power to argue that despite the high market shares of the Parties on the market for supply of white sugar in Italy, the proposed transaction does not raise competition concerns.
- (527) However the notifying party refers to certain elements indicating countervailing buyer power. Indeed, it submits that with respect to the customers' size, some customers both in the industry and retail segments are big multinational companies with considerable buyer power. Furthermore, it is argued that the customers' European scope allows them to negotiate package deals and they have intimate knowledge of European and world sugar markets, making them powerful and sophisticated procurers of sugar. On the other hand, it is put forward that smaller customers are more inclined to source sugar from "Italian sources"⁴⁶⁹.
- (528) The notifying party therefore makes the distinction between large and smaller customers in terms of buyer power before adding that security of supply is one of the main characteristics that industrial customers and retail customers are seeking from suppliers. Südzucker assumes that its main competitors in Italy can guarantee security of supply to a similar extent as itself. It is put forward that Südzucker's strategy for ensuring security of supply for its customers in sugar deficit countries is based on two pillars: (i) sufficient storage facilities and (ii) sound management decisions about allocation of sales to a specific destination (including stock levels required)⁴⁷⁰.
- (529) Concerning switching, the notifying party also puts forward that there are no specific purchasing patterns according to customer groups. Across customer groups, contracts are usually negotiated on a year's basis, allowing customers to switch between suppliers whenever they deem it profitable and/or necessary to avoid dependency on one supplier. Customers are highly price-sensitive and therefore willing to switch suppliers if the current contractual partner intends to raise prices above the competitive level. Since brands do not play a role in the sugar business, industry and retail customers find it easy to switch between suppliers. Moreover, sugar is a commodity and supply sources are therefore easily replaceable. Furthermore, many customers, even small customers, employ multisourcing strategies by splitting their demand among several suppliers to avoid dependency on one supplier⁴⁷¹.

⁴⁶⁹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 59, sent by e-mail of 1 December 2011 (19:33).

⁴⁷⁰ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 58, sent by e-mail of 1 December 2011 (19:33).

⁴⁷¹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, pages 58 - 59, sent by e-mail of 1 December 2011 (19:33).

No buyer power of customers

- (530) Amongst other elements, as discussed below, the result of the second phase market investigation indicates that customers do not consider that they have buyer power in the negotiations with their sugar suppliers. Even the biggest multinational customers underlined that fact. Customers stress that on a high deficit market such as Italy customers need security of supply above all and are therefore dependent on their suppliers.
- (531) In this respect the significant scarcity of white sugar is emphasized by [a large customer]* in the following terms: *"all refineries in Europe will struggle to compete on a lasting basis given the current restrictions on the import of raw cane sugar. Supply from preferential regions/CXL is not enough to fulfil the refining capacity in Europe"*⁴⁷² or *"there is clearly a big deficit between supply and demand"*⁴⁷³.
- (532) The lack of countervailing buyer power mainly results from the significant lack of white sugar available to industrial processors the fact that industrial processors do not switch suppliers and the fact that industrial processors need to multi-source for reasons of security of supply.
- (533) As a result of the 2006 sugar reform, Italy has become a largely deficit Member State⁴⁷⁴.
- (534) All the respondents to the in-depth market investigation indicated to the Commission that security of supply is important irrelevant the size and economic weight of the customer. Respondents underline the deficit character of the Italian sugar market and that security of supply constitutes a clear factor. To depict only one or two quotations from the largest customers: ([a large customer]*) *"[y]es there is clearly a big deficit between supply and demand [...] security of supply is of key importance"*⁴⁷⁵ or ([a large customer]*) *"[y]es, [security of supply]* is really critical"*⁴⁷⁶. Large customers such as [a large customer]*⁴⁷⁷ or [a large customer]*⁴⁷⁸ underline the possibility of concluding long-term contracts (annual) while others underline the importance of having several sugar suppliers⁴⁷⁹.
- (535) The results of the in-depth second phase market investigation have also confirmed that customers consider that they have very limited buyer power in respect of their

⁴⁷² Paragraph 389 of the Statement of Objections.

⁴⁷³ Reply by [...]* ([...]* (reply to question 23) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁷⁴ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, pages 4 and 5, sent by e-mail of 1 December 2011 (19:33).

⁴⁷⁵ Reply by [...]* ([...]* (reply to question 23) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁷⁶ Reply by [...]* ([...]* (reply to question 23) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁷⁷ Reply by [...]* ([...]* (reply to question 23) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁷⁸ Reply by [...]* ([...]* (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁷⁹ Reply by [...]* ([...]* (reply to question 23) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II) or Reply by [...]* ([...]* (reply to question 23) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

sugar suppliers irrespective of their size, economic power or geographic situation essentially due to the absence of raw material. Some large customers or smaller customers⁴⁸⁰ (approximately 20% of the respondents) indicated that they have buyer power to a limited extent; however the majority of the customers, including both large⁴⁸¹ and smaller customers⁴⁸², made reference to no negotiation power at all or to a very limited one. [...]*, an Italian wholesaler, underlined that they cannot even negotiate on "*total final volume*"⁴⁸³ while [a large customer]* also indicates that it does not get any discount⁴⁸⁴.

No switching by customers

- (536) The results of the in-depth second phase market investigation have also indicated that customers do not switch suppliers.
- (537) Indeed, customers replying to the market investigation affirmed that, given the significant sugar scarcity on the Italian sugar market, they multisource while they do not often switch suppliers and, in any event, they would not be able to source from abroad.
- (538) Against that background, in its reply to the Statement of Objections the notifying party questions the results of the market investigation⁴⁸⁵.
- (539) According to paragraph 67 of the Horizontal Merger Guidelines: "*Countervailing buyer power cannot be found to sufficiently off-set potential adverse effects of a merger if it only ensures that a particular segment of customers, with particular bargaining strength, is shielded from significantly higher prices or deteriorated conditions after the merger*". In the case at hand, 89% of the end-customers that replied to the market investigation indicated that they do not purchase directly from abroad⁴⁸⁶; moreover, in the last five years no customer responded to a price increase by 5-10% on the Italian sugar market by purchasing sugar directly from abroad⁴⁸⁷. In

⁴⁸⁰ Reply by [...]* ([...]* (reply to question 69) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II) or Reply by [...]* ([...]* (reply to question 69) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁸¹ For example Reply by [...]* ([...]* (reply to question 69) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

⁴⁸² Reply by [...]* ([...]* (reply to question 69) (Non-Confidential and Confidential Versions – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 45) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 69) (Confidential and Non-Confidential Versions – Questionnaire to sugar customers in Italy – Phase II), Reply by [...]* ([...]* (reply to question 69) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁸³ Reply by [...]* ([...]* (reply to question 69) (Non-Confidential Version – Questionnaire to sugar customers in Italy – Phase II).

⁴⁸⁴ Reply to Question 71 of the Questionnaire to sugar customers in Italy – Phase II. See exchange of emails between Mr [...]* and Mr [...]* on 30 March 2012, at 08:44.

⁴⁸⁵ Paragraph 237 of the reply of the notifying party to the Statement of Objections.

⁴⁸⁶ Questionnaire to sugar customers in Italy – Phase II, question 22.

⁴⁸⁷ Questionnaire to sugar customers in Italy – Phase II, question 38(e). When asked whether, in case of a price increase of 5 to 10% by the main sugar suppliers in Italy, they would consider buying sugar directly from abroad (question 38(a), the majority of customers replied positively. However, their reply has to be nuanced. If customers would be willing to source directly from abroad, some explain that this would be very difficult to achieve or even unlikely, notably because of the logistics/transport costs. Almost one third of the customers who replied positively would be willing to do so provided they

this respect it has to be underlined that the outlined conditions in the questionnaire were a significant price increase in Italy.

- (540) Against this background, the notifying party in its reply to the Statement of Objections underlines that multisourcing means, in the context of the Italian sugar market, that the customer 'changes its supplier' without actually switching⁴⁸⁸ since it implies that by keeping several suppliers it is possible to select occasionally between those several suppliers. Therefore, according to the notifying party, no importance should be attributed to the replies on 'switching', prices are lower in Italy than in other deficit countries and it is so because of competitive pressure from competitors and countervailing buyer power⁴⁸⁹ and some customers buy from outside Italy, in particular [a large customer]*⁴⁹⁰.
- (541) On the other hand the notifying party did not contest that even significant customers negotiating transnationally are required to pay Italian prices for their purchases in Italy as described in recital (173) of this Decision: "*even in the rare cases that the overall negotiations take place in a regional or EEA level, prices are set for each Member State separately, according to the market situation in each case (with respect to Italy, the market participants explained that the scarcity of sugar is the most important factor determining the prices they have to pay)*" and even [a large customer]* indicates that it does not get any discount⁴⁹¹.
- (542) The notifying party does not contest either that in the past Italian sugar customers have not switched sugar suppliers.
- (543) The notifying party does not contest that sugar demand is price inelastic. On the contrary EDFM's internal document states that "*Total EU-27 sugar consumption is relatively static at around 16.5 million tonnes, and moreover, sugar demand, both industrial demand and retail demand, in the EU is markedly income and price inelastic*"⁴⁹² (emphasis added).
- (544) And most importantly, the notifying party does not even contest the significant sugar scarcity in the Union and in Italy. On the contrary it indicates that this scarcity is only due to the regulatory measures taken by the Commission and that "*every ton of quota sugar finds its way to the customers*"⁴⁹³.

Conclusion

- (545) Since the Italian sugar market is in deficit, the Italian sugar prices are high as compared to sugar prices in other Member States and security of supply is crucial for customers in terms of both quantity and quality, Italian sugar customers do not hold

would be able to conclude long term contracts. However, no customer responded by purchasing sugar directly from abroad to a price increase by 5-10% on the Italian sugar market.

⁴⁸⁸ Paragraph 233 of the reply of the notifying party to the Statement of Objections.

⁴⁸⁹ Paragraph 235 of the reply of the notifying party to the Statement of Objections.

⁴⁹⁰ Paragraph 232 of the reply of the notifying party to the Statement of Objections.

⁴⁹¹ Reply to Question 71 of the Questionnaire to sugar customers in Italy – Phase II. See exchange of emails between Mr [...] and Mr [...] on 30 March 2012, at 08:44.

⁴⁹² Page 17 of the European Sugar Logistics Study prepared for the Ethiopian Sugar Development Agency by ED&F Man, 16 February 2010.

⁴⁹³ Paragraph 202 of the reply of the notifying party to the Statement of Objections.

important buyer power vis-à-vis their sugar suppliers and their possibilities of switching sugar suppliers are very limited.

- (546) On the basis of the considerations above, the Commission takes the view that very little, if any, countervailing buyer power can be attributed to Italian sugar customers in the relationship with their sugar suppliers and they therefore do not exercise competitive pressure on the Italian sugar producers / suppliers including the Parties within the meaning of paragraphs 64 to 67 of the Horizontal Merger Guidelines.

6.1.4.5. No sufficient competitive constraint from entry

- (547) According to paragraph 68 of the Horizontal Merger Guidelines, *"entry analysis constitutes an important element of the overall competitive assessment. For entry to be considered a sufficient competitive constraint on the merging parties, it must be shown to be likely, timely and sufficient to deter or defeat any potential anti-competitive effects of the merger"*.

High barriers to entry

- (548) According to paragraph 71 of the Horizontal Merger Guidelines, barriers to entry can take various forms, including regulatory barriers, tariff and non-tariff trade barriers⁴⁹⁴, difficulties to obtain essential input materials or the closeness of relationships between suppliers and customers⁴⁹⁵. Entry barriers are elements that are likely to expose potential competitors to risks and costs sufficiently high to deter them from entering the market or make entry particularly difficult for them⁴⁹⁶.

Views of the notifying party

- (549) The notifying party argues there are no relevant barriers to enter the markets for the supply of white sugar in Italy.
- (550) The notifying party takes the view that the regulatory entry barriers have been reduced with the new sugar market regime since the European sugar market experiences an intensification of the trade flows since its adoption⁴⁹⁷.
- (551) It is also put forward that no unusual non-tariff barriers apply to the Italian sugar market. Indeed, it is argued that only the usual challenges of cross border trade, such as language barriers, different legal systems, cultures and habits apply. Most customers prefer to have a local partner to communicate with and to solve logistical issues⁴⁹⁸.

⁴⁹⁴ Commission Decision 2002/174/EC in Case COMP/M.1693 — Alcoa/Reynolds, OJ L 58, 28.2.2002, recital 87

⁴⁹⁵ Commission Decision 2002/156/EC in Case COMP/M.2097 — SCA/Metsä Tissue, OJ L 57, 27.2.2002, p. 1, recitals 83-84

⁴⁹⁶ Case T-282/02 Cementbouw v Commission [2006] ECR II-319, paragraph 219

⁴⁹⁷ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 8, sent by e-mail of 1 December 2011 (19:33).

⁴⁹⁸ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 40, sent by e-mail of 1 December 2011 (19:33).

- (552) However, the in-depth market investigation does not confirm the notifying party's views.

Results of the market investigation

- (553) According to the competitors of the Parties, the main market entry barriers are the access to input⁴⁹⁹, the necessary infrastructure⁵⁰⁰, established customer relationship⁵⁰¹ or distribution network⁵⁰² while the sugar supply business is a highly capital intensive market⁵⁰³.

High investments costs

- (554) As already pointed out, the market investigation largely confirmed that the sugar market necessitates high investments costs and the importance of logistics. Some market players also indicated that it is possible to enter the Italian sugar market without Italian production and storage facilities, like did Tereos. However, Tereos supplies the Italian sugar market through its French facilities⁵⁰⁴.

Importance of local knowledge and distribution channels and access to input

- (555) The market investigation also confirmed that the sugar market necessitates local knowledge and distribution channels, while access to input is the most crucial element.

⁴⁹⁹ Reply by [...] ([...]) (reply to question 127) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2817), Reply by [...] (reply to questions 126 and 127) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), Reply by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), Reply by [...] ([...]) (reply to question 125) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...] ([...]) (reply to questions 126 and 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) or Reply by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2584).

⁵⁰⁰ Reply by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), Reply by [...] ([...]) (reply to question 127) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) ([...]).

⁵⁰¹ Reply by [...] ([...]) (reply to question 125) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁵⁰² Reply by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), Reply by [...] ([...]) (reply to question 125) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), "Phase II - reply to RFI – raw cane sugar – IT and Greece Market – conf and non conf" by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II), Reply by [...] ([...]) (reply to question 128) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) ([...]).

⁵⁰³ Reply by [...] ([...]) (reply to question 127) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) or Reply by [...] ([...]) (reply to question 127) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) (ID 2364)

⁵⁰⁴ Reply by [...] (reply to question 9) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

Reply of the notifying party to the Statement of Objections and assessment

- (556) The notifying party submits that the Commission should have "*chased up*" more the respondents which have not replied to the questions in the questionnaire because they are not active on the Italian market. Special reference is made to [a sugar producer]* and [a sugar producer]*. However, it is observed that even though [a sugar producer]*, it is not active on the Italian white sugar market, it replied to the questions about market entry as the notifying party itself notes in paragraph 202 of its reply to the Statement of Objections. Indeed, [a sugar producer]* indicated that it is not aware of any entry plans in the Italian sugar market for the next two years and that entering the Italian white sugar market is difficult without local infrastructure, local market position and local know-how⁵⁰⁵.
- (557) The replies to the questions about market entry appear plausible and are provided by well-established players with experience on the Italian market.
- (558) In general, the notifying party argues⁵⁰⁶ that market entry barriers are low since it is enough to enter the Italian white sugar market as Tereos did in the mid-2000 alone or by teaming up with a wholesaler, as Südzucker has done with MAXI or with an incumbent sugar producer as Pfeifer & Langen has done.
- (559) As already mentioned, according to paragraphs 68 to 75 of the Horizontal Merger Guidelines a "*potential entry*" must be likely, timely and sufficient. In the case at hand all market players have credibly indicated that they see no ability or incentive to enter the Italian white sugar market (see recital (566) of this Decision). Therefore, there is no likely potential market entry in the market for supply of white sugar to industrial processors in Italy. In addition to the main market entry barriers identified above (necessary infrastructure, established customer relationship, or distribution network, the sugar supply business being a highly capital intensive market) **access to input** is considered to be an important market entry barrier. While it is true that Tereos entered the Italian white sugar market, in particular the market for supply to industrial processors, from France in the mid-2000, Tereos itself expressly stated that such market entry was possible only with sufficient sugar quantities while, under the current market conditions, especially taken into account the severe scarcity of sugar in the Union and Italy, "*access to input*" constitutes a high market entry barrier.
- (560) In this context it has to be emphasized once again that Tereos' Italian market entry stemmed from the fact that "*[t]he decrease of Italian production had to be compensated by higher French inflows as forecasted by the Commission*" and such entry was easy in view of the sugar deficit created by the 2006 sugar reform.⁵⁰⁷ while Tereos is not considered to be a competitive player, for example, by [a sugar producer]* as it is indicated to only follow the policy of Südzucker and without "*disturb[ing]*" the latter's market approach⁵⁰⁸.

⁵⁰⁵ Reply by [...]* ([...]*) (reply to questions 127 and 130) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II) ([...]*).

⁵⁰⁶ Paragraph 222 of the Reply to the Statement of Objections.

⁵⁰⁷ Reply by [...]* ([...]*) (reply to question 62) (Non-Confidential Version – Questionnaire to sugar suppliers / producers Italy – Phase II).

⁵⁰⁸ Reply by [...]* ([...]*) (reply to question 45) (Confidential and Non-Confidential Versions - Questionnaire to sugar customers in Italy – Phase II).

Conclusion

- (561) Contrary to the notifying party's submission the Italian white sugar market for the supply of white sugar to industrial processors is characterized by relatively high market entry barriers within the meaning of paragraphs 71 to 75 of the Horizontal Merger Guidelines.

Entry unlikely to occur

Views of the notifying party

- (562) The notifying party only submitted a single example of entry, by Tereos⁵⁰⁹.
- (563) In the context of possible entries in the Italian white sugar market, the notifying party also takes the view that further expansion, and not entry, is possible on the Italian white sugar market by the operators already having supplies on the Italian market (Eridania/Cristal Union, Italia Zuccheri/COPROB/Pfeiffer & Langen or Tereos); as a result of the Minerbio development by Eridania/Cristal Union; by the Cristal Union Algerian refinery which is to be launched at the end of 2012, by the 2014 Sudanese refinery with a capacity of 500,000 tonnes/year by Eridania; other sugar producers in the Union such as Suiker Unie or Vermandoise; or by the Balkan producers. In this context, as already mentioned, entry of new competitors is not to be confused with expansion of existing ones. The examples quoted above are related to expansion and not to market entry.

Results of the market investigation: entry unlikely to occur

- (564) The notifying party does not indicate that any economic entity is considering entering the Italian white sugar market post-merger following the proposed transaction.
- (565) The market test has not revealed either any entity able to or interested in entering the Italian market for the supply of white sugar to industrial processors post-merger.
- (566) On the contrary, the Italian white sugar market is rather characterized by market exits, in particular the exit of Nordzucker or the one of Tate & Lyle in 2011, due to scarcity of essential input.
- (567) Against this background, the notifying party in its reply to the Statement of Objections, therefore, puts forward new entry plans in the market for supply of white sugar to industrial processors in Italy.
- (568) Indeed, the notifying party puts forward⁵¹⁰ that it is furthermore "*widely expected*" that imports will increase during the next years. The high international market prices have fostered and sped up the building-up of new sugar production facilities, even in the context of the worldwide financial crisis, and capacity increases especially in the ACP/LDC-countries (cf. the project of Eridania in Sudan with an initial capacity of 500,000 tonnes and ultimately 1 million tonnes or the expansion plans of Tongaat

⁵⁰⁹ Answers to 3rd Request for Information to Südzucker 1/2 [GL-AM.FID10603463], Form CO – Italy, page 62, sent by e-mail of 1 December 2011 (19:33).

⁵¹⁰ Paragraph 22§ of the reply of the notifying party to the Statement of Objections.

Hullet which plans to expand production in Zimbabwe by 225,000 by 2014/15 and in Mozambique by 200,000 tonnes by 2014/15). Union-wide, ACP/LDC countries will be likely to reach an expected import level of up to 3.1 million tonnes "*with a large part expected to go into deficit areas such as Italy*". In addition, the Union has agreed to a new free trade agreement with Central and South American countries which will lead to additional imports of 300,000 tonnes, probably already from 2012/13 on.

- (569) As for the expansion plans of Tongaat Hullet in Zimbabwe and in Mozambique, these plans, only based upon a presentation available on the internet website of Tongaat Hullet, would seem to be realised in a timeframe outside the scope of the definition of timeliness within the meaning of Paragraph 74 of the Horizontal Merger Guidelines (i.e 2 years).
- (570) As for the agreement with the Central and South American countries leading to additional imports of 300,000 tonnes in the Union, it has to be recalled that for the time being this plan is a Commission proposal only, which still needs to be adopted by the Council and the European Parliament before ratification by the competent legislative assemblies of the concerned Central and South American countries (Panama, Colombia and Peru). However, even if the entry into force of such an agreement were to be considered likely⁵¹¹ and timely, and even in the extreme case that that all of these new volumes could be secured by producers / suppliers willing to import into Italy, it is to be noted that the effect of these new volumes would, to a significant extent, be offset by a reduction of volumes by the impact of the Croatian accession to the Union in March 2013 as analysed and explained in recitals (510) and (511) of this Decision leading to question the sufficiency of these quantities.

Conclusion

- (571) Therefore, market entry is not likely, timely and sufficient to offset the anticompetitive effects of the proposed transaction in the Italian white sugar market in the near future within the meaning of paragraphs 69 – 71 of the Horizontal Merger Guidelines.

6.1.4.6. Conclusions on the Italian market for the supply of sugar to industrial processors

- (572) The Commission concludes that the proposed transaction has the following characteristics and consequences: (i) Südzucker is the most important player on the Italian market for the supply of white sugar to industrial processors, (ii) EDFM is an important player on the same market, (iii) the increment added by the proposed transaction is significant⁵¹², (iv) the post-merger market shares are very high (superior to [50-60]*%)⁵¹³, (v) Südzucker and EDFM are close and dynamic competitors and are the two competitors that can most easily adapt their quantities/sales in the Italian market⁵¹⁴, (vi) post-merger the merged entity would have the incentive and be in a position to withdraw quantities from Italy, thereby

⁵¹¹ As for the likelihood of the agreement it has to recall that for the time being this plan is a Commission proposal, therefore the Commission proposal still needs to be adopted by the Council and the European Parliament before ratification by the competent legislative assemblies of the concerned Central and South American countries (Panama, Colombia and Peru).

⁵¹² Horizontal Merger Guidelines, paragraph 27.

⁵¹³ Horizontal Merger Guidelines, paragraph 27.

⁵¹⁴ Horizontal Merger Guidelines, paragraphs 28-30.

raising prices, (vii) the competitors of the merged entity, established in Italy or outside Italy, face capacity constraints and therefore are unlikely to increase supply if prices increase, and therefore to counteract such market behaviour⁵¹⁵, (viii) countervailing buyer power appears unlikely to constrain the ability of the merged entity to increase prices post transaction, especially in periods of overall shortage of sugar supply⁵¹⁶, and (ix) following the market investigation, entry in the relevant market is not likely and timely and sufficient to offset the anticompetitive effects of the proposed transaction⁵¹⁷. The Commission concludes that as a result of all the elements enumerated above, the proposed transaction would also result in the creation of a dominant position.

(i) *Supply of white sugar to retailers in Italy*

- (573) With respect to the market for the supply of white sugar to retailers, it has to be examined whether the proposed transaction creates competitive concerns in Italy as it leads to the creation of a market leader. The market investigation has however demonstrated that these competition problems do however not reach the threshold of significant impediment of effective competition.
- (574) In particular, the following table below shows the sales of white sugar (in metric tonnes) to industrial processors and to retailers in Italy from 1 January 2011 to 31 October 2011:

⁵¹⁵ Horizontal Merger Guidelines, paragraphs 32-35.

⁵¹⁶ Horizontal Merger Guidelines, paragraphs 64-67.

⁵¹⁷ Horizontal Merger Guidelines, paragraphs 68-70.

	sales to industrial processors		sales to retailers		sales to industrial processors and retailers	
	Volume	market share	volume	market share	Volume	market share
Südzucker ⁵¹⁸	[...]*	[30-40]*%	[...]*	[10-20]*%	[...]*	[30-40]*%
EDFM (incl. Brindisi) ⁵¹⁹	[...]*	[10-20]*%	[...]*	[10-20]*%	[...]*	[10-20]*%
Südzucker/EDFM combined	[...]*	[40-50]*%	[...]*	[30-40]*%	[...]*	[40-50]*%
COPROB/Italia Zuccheri/Pfeifer & Langen ⁵²⁰	[...]*	[20-30]*%	[...]*	[10-20]*%	[...]*	[20-30]*%
Tereos ⁵²¹	[...]*	[10-20]*%	[...]*	[5-10]*%	[...]*	[10-20]*%
Eridania/Cristal Union ⁵²²	[...]*	[5-10]*%	[...]*	[30-40]*%	[...]*	[10-20]*%
Zuccherificio del Molise ⁵²³	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Société Vermandoise ⁵²⁴	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Sunoko ⁵²⁵	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Total volume of competitors	[...]*	[40-50]*%	[...]*	[60-70]*%	[...]*	[50-60]*%
Total market volume	1,013,039	100%	363,182	100%	1,377,028	100%

(575) Moreover, the following table below shows the forecasted sales of white sugar (in metric tonnes) to industrial processors and to retailers in Italy for the campaign year 2011/2012 (i.e. from October 2011 to September 2012):

⁵¹⁸ Südzucker's answer to the 6th RFI in Phase II.
⁵¹⁹ Confidential information provided by SFIR.
⁵²⁰ Questionnaire to sugar competitors in Italy – Phase II.
⁵²¹ Questionnaire to sugar competitors in Italy – Phase II.
⁵²² Questionnaire to sugar competitors in Italy – Phase II.
⁵²³ Questionnaire to sugar competitors in Italy – Phase II.
⁵²⁴ Questionnaire to sugar competitors in Italy – Phase II.
⁵²⁵ Questionnaire to sugar competitors in Italy – Phase II.

	sales to industrial processors		sales to retailers		sales to industrial processors and retailers	
	Volume	market share	volume	market share	volume	market share
Südzucker ⁵²⁶	[...]*	[30-40]*%	[...]*	[20-30]*%	[...]*	[30-40]*%
EDFM (incl. Brindisi) ⁵²⁷	[...]*	[10-20]*%	[...]*	[10-20]*%	[...]*	[10-20]*%
Südzucker/EDFM combined	[...]*	[50-60]*%	[...]*	[30-40]*%	[...]*	[40-50]*%
COPROB/Italia Zuccheri/Pfeifer & Langen ⁵²⁸	[...]*	[20-30]*%	[...]*	[10-20]*%	[...]*	[20-30]*%
Tereos ⁵²⁹	[...]*	[10-20]*%	[...]*	[0-5]*%	[...]*	[10-20]*%
Eridania/Cristal Union ⁵³⁰	[...]*	[5-10]*%	[...]*	[30-40]*%	[...]*	[10-20]*%
Zuccherificio del Molise ⁵³¹	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Société Vermandoise ⁵³²	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Sunoko ⁵³³	[...]*	[0-5]*%	[...]*	[0-5]*%	[...]*	[0-5]*%
Total volume of competitors	[...]*	[40-50]*%	[...]*	[60-70]*%	[...]*	[50-60]*%
Total market volume	1,278,112	100%	453,827	100%	1,731,939	100%

⁵²⁶ The forecast of overall sugar sales of [...]* tonnes for the campaign year 2011/2012 is based in the internal document submitted as Annex 6 in Südzucker's answer to the 3rd RFI in Phase I. This figure is then attributed between sales to industrial processors and sales to retailers on the basis of the ratios provided in Südzucker's answer to the 6th RFI in Phase II (including the clarification received by email on 13 January 2012).

⁵²⁷ Internal document entitled as "ESI's sales forecast for 2012" and submitted by EDFM on 13 January 2012.

⁵²⁸ Questionnaire to sugar competitors in Italy – Phase II.

⁵²⁹ Questionnaire to sugar competitors in Italy – Phase II.

⁵³⁰ Questionnaire to sugar competitors in Italy – Phase II.

⁵³¹ Questionnaire to sugar competitors in Italy – Phase II.

⁵³² Questionnaire to sugar competitors in Italy – Phase II.

⁵³³ Questionnaire to sugar competitors in Italy – Phase II.

- (576) It follows from the above table that in particular Südzucker, but also EDFM have lower individual and combined market shares in the market for supply of white sugar to retailers than in the market for the supply of white sugar to industrial processors in Italy.
- (577) Their combined market shares remain lower than 40%. In its case practice the Commission has only in some instances found there to be a dominant position with market shares below 40%⁵³⁴.
- (578) In the Italian market for the supply of white sugar to retailers, contrary to the market for the supply to industrial processors, branding and national consumer preferences play an important role and the established Italian market players are stronger competitors.
- (579) In particular the current market leader Eridania would have post-merger a similar strength to the Parties with a market share of [30-40]*%. Eridania has the most significant Italian brand "Zefiro", which benefits from consumers' loyalty. Furthermore, COPROB with [10-20]*% market shares also holds an important market position and has a well-established brand on the Italian market. In reality, the current market leader, Eridania, would face post-merger an equally strong competitor, Südzucker/EDFM. The market investigation confirms the impression that the proposed transaction does not create competitive concerns, since six out of seven retail customers did not claim that the proposed transaction would have negative effects on their business⁵³⁵.
- (580) In addition, an independent study from 2009/2010 showed that in terms of penetration in household, the competitors' brands performed much better than Parties' brands. For instance the Zefiro brand (Eridania) had a penetration of 88,2% on the Italian market while the two other Eridania brands, Eridania and Tropical, reach respectively 64,7% and 41,2% of penetration. Comparatively Notadolce (SFIR) had a penetration of 35,3%. Südzucker was too small to be considered in this study⁵³⁶.
- (581) In view of the above, the proposed transaction does not significantly impede effective competition in the market for the supply of white sugar to retailers in Italy.

(ii) *Greece*

- (582) The proposed transaction does not significantly impede effective competition in Greece under the narrowest possible geographic market definition.
- (583) Indeed, should the proposed transaction be assessed under a national geographic market definition, as is likely to be the case in Greece⁵³⁷ in the Commission's view, the combined market shares of the Parties would remain unaffected, since there

⁵³⁴ See Paragraph 17 of the Horizontal Merger Guidelines.

⁵³⁵ Questionnaire to sugar customers in Italy – Phase II, questions 77 *et seq.*

⁵³⁶ Ricerca esclusiva MARK UP "Grocery: il mercato dello zucchero ricerca un elemento di rivitalizzazione".

⁵³⁷ Questionnaire to sugar customers in Greece – Phase II question 17 to 39 - Questionnaire to sugar competitors in Greece – Phase II, question 25 to 46.

would be no increment added by the proposed transaction and there is no indication that EDFM is likely to enter the Greek sugar market⁵³⁸.

- (584) As already analysed above, EDFM does not currently have sales of white sugar in Greece⁵³⁹. It was also confirmed by competitors and customers that EDFM has no sales of white sugar in Greece. As submitted by the notifying party and confirmed by [a large Greek sugar producer]*⁵⁴⁰, [description of Greek operations between the two sugar producers]*⁵⁴¹.
- (585) As stated in paragraph 60 of the Horizontal Merger Guidelines: "*For a merger with a potential competitor to have significant anti-competitive effects, two basic conditions must be fulfilled. First, the potential competitor must already exert a significant constraining influence or there must be a significant likelihood that it would grow into an effective competitive force. Evidence that a potential competitor has plans to enter a market in a significant way could help the Commission to reach such a conclusion. Second, there must not be a sufficient number of other potential competitors, which could maintain sufficient competitive pressure after the merger*".
- (586) With respect to the likelihood that EDFM could constitute a potential competitor in Greece, there is no evidence at all that EDFM is likely to enter the Greek white sugar market(s) in the near future. It is true that in an internal document dated March 2009, EDFM was indicated to intend to sell [...] tonnes from the Brindisi refinery's production to Greece. However, (i) no further internal documents mention any plans with regard to sales in Greece, (ii) since the beginning of the operation of the Brindisi refinery in December 2010 no white sugar sales have taken place in Greece, and (iii) the internal document in question was drawn up under the hypothetical assumption of a [...] tonnes per year of production. At present therefore, there are no concrete plans indicating that EDFM plans to enter the Greek sugar market. Therefore, it is not likely that EDFM will enter the Greek white sugar markets and if it were to be likely, there is no indication either that it would occur within a reasonable time.
- (587) Furthermore, it is not likely that EDFM will supply sugar in Greece through the purchase of [a large Greek sugar producer]*. The international bid for the sale of [a large Greek sugar producer]* was announced in June 2011 and, at present, [a large Greek sugar producer]* is interviewing the companies that have expressed interest. After the completion of this stage, candidates will submit their economic offer and the whole procedure is expected to be concluded in June 2012. Although EDFM is one of the 10 official candidates, there is no indication at present that EDFM will be the final purchaser of [a larger Greek sugar producer]*.⁵⁴²

⁵³⁸ Horizontal Merger Guidelines, paras 58-60.

⁵³⁹ Südzucker's reply to the 3rd RFI in Phase II, Annex 35-1 Form CO Greece, page 15.

⁵⁴⁰ Südzucker's reply to Questions 6 and 11 of the Questionnaire to Sugar Suppliers/Producers in Greece – Phase II.

⁵⁴¹ Südzucker's reply to the 3rd RFI in Phase II, Annex 35-1 Form CO Greece, page 14.

⁵⁴² E-mail by [...] entitled "ΕΠΙΣΤΟΛΗ ΣΤΟΝ κ. [...] 17-02-12" and received on 17 February 2012 at 13:00.

(588) In view of the above, EDFM does not exert significant constraining influence in Greece and there is no significant likelihood that it will grow into an effective competitive force in Greece.

(589) Therefore, the proposed transaction does not significantly impede effective competition in the Greek sugar market.

6.2. SUPPLY OF PREFERENTIAL RAW CANE SUGAR INTO THE UNION

(590) The supply of raw cane sugar is an upstream market to the production and supply of white sugar in the Union. Both Parties are active in the supply/delivery of raw cane sugar to European refineries (upstream) and in the production and supply of white sugar into the EEA (downstream).

6.2.1. Product market definition

(591) In its ABF/Azucarera⁵⁴³ Decision, the Commission distinguished between sugar beet and sugar cane. Sugar cane can only be grown in tropical climate, while sugar beet favours more temperate climatic conditions like those in the northern Hemisphere. Because of these different growing conditions supply-side substitution is clearly not possible.

(592) At the same time demand-side substitutability seems to be limited as raw cane sugar refiners would have to invest a significant amount of money and time to be able to refine beet as well⁵⁴⁴.

(593) White sugar production from raw cane sugar is mainly done in specialized refineries, that is to say refineries that are optimized for raw cane sugar and in which sugar cannot be produced from processing sugar beet. This is the case for EDFM's refinery in Brindisi as well as Südzucker's refinery in Marseille.

(594) It is possible to refine raw cane sugar in factories that are mainly dedicated to beet processing but this requires some significant modifications. In the Union some beet sugar factories have been equipped in such way. This is the case for example in a factory of the Eridania group in Minerbio (Italy) and Südzucker's refineries in Romania.

(595) However, the production costs of refineries that can process both cane and beet can differ in a significant way mainly due to input costs as stated by Tate & Lyle *"in the current sugar marketing year, cane refiners face over EUR 200 of extra raw material costs relative to beet processors,[...]* [t]he divested business [SRB], like all cane sugar refiners in Europe, will find it very difficult to compete on a lasting basis on the Italian sugar market. This is because it will face unfair terms of competition for its raw material – raw cane sugar for refining – relative to the terms on which beet processors are able to secure raw material"*.

⁵⁴³ Commission Decision of 30 March 2009 in Case No COMP/M.5449 – ABF / AZUCARERA.

⁵⁴⁴ Indeed, as already explained sugar production from beet involves extracting the beet sugar content with water into a raw juice solution which is then filtered, purified and evaporated to remove moisture and impurities and then concentrated until crystallisation occurs. With regard cane sugar, the first stage of processing is carried out in factories close to or in the growing area. The cane is cleaned, crushed and shredded and sprayed with hot water in order to extract the juice.

- (596) In addition, the supply/procurement of sugar beet within the EEA is strictly regulated by the Common Market Organisation in the sugar sector. The quota system currently in place does not allow production of sugar from beet beyond the allocated beet quota. Consequently, producers can only generate sugar from beet if they own the required quota. The procurement of raw cane sugar for refining has a different legal framework.
- (597) Therefore, it is considered that the supply of raw cane sugar represents a separate relevant product market to be distinguished from the one for sugar beet.

6.2.2. *Geographic market definition*

- (598) The analysis of the relevant geographic market for the supply of raw cane sugar has to take into account the current regulatory environment.
- (599) It cannot be excluded that a further distinction should be made between preferential raw cane sugar (including raw cane sugar from ACP/LDC countries, CXL and TRQ quotas and schemes) and other schemes.
- (600) In theory, imports of raw cane sugar originating from non-ACP countries and non-LDCs beyond the limited amount set by the quota are possible. However, that sugar imported from the world market under most favoured nation (MFN) conditions include costly appropriate import duties, namely 339 EUR/tonne for raw sugar for refining, plus additional special safeguard (SSG) duties.
- (601) In comparison, ACP and LDC countries have duty-free-quota-free (“DFQF”) access to the markets in the Union⁵⁴⁵, subject to the transitional safeguard mechanism for sugar of 3.5 million tonnes per annum. CXL sugar quota set by the Commission (around 600,000-700,000 tonnes per year) can currently be imported at a rate of duty of EUR 98/tonne from countries like Brazil, Australia and Cuba. Finally, special rules have been agreed for exceptional tariff rate quotas (TRQs) for sugar, these exceptional quotas being deemed necessary from time to time by the Commission in case of exceptional market conditions.
- (602) On the basis of the market investigation, it is considered that imports of raw cane sugar which benefit from DFQF or low duties (such as TRQs and CXL) are the only sustainable imports for refineries in the Union while raw cane sugar purchased on the world market is only for complementary volumes when the refineries do not manage to source sufficient quantities of preferential raw cane sugar.

[...]*⁵⁴⁶

[...]*

[...]*

- (603) As a result, the relevant geographic market for the market for the procurement of preferential raw cane sugar covers at least the ACP/LDC countries which are allowed

⁵⁴⁵ Under the EPA and EBA schemes

⁵⁴⁶ Presentation to the Commission by Südzucker 02 December 2011.

to have quota-free and duty-free access to the EEA and could also comprise the main countries providing raw cane sugar under CXL and TRQ preferential quotas and duties such as Brazil, Cuba and Australia. However, the question whether the market could be even wider – eventually world-wide – can be left open as in any event the proposed transaction does not raise serious doubts irrespective of the exact scope of the relevant geographic market.

6.2.3. *Effects on competition*

- (604) The changes brought about by the Union sugar market reform have led to an increasing need for imported raw cane sugar from qualified producers.
- (605) In the sugar marketing year 2010/11 the expected use of sugar in the EU was around 17.2 million tonnes. Thereof 13.8 million tonnes were supplied by beet quota sugar production of the marketing year and 1.1 million tonnes by CXL and Balkan import quotas. The 700,000 tonnes under CXL quotas consisted almost exclusively of raw cane sugar for refining while the 400,000 tonnes imported from the Balkans was white sugar for direct consumption
- (606) The remaining 2.3 million tonnes were partially covered by 1.5 million tonnes of imports from ACP/LDC producers, 90% of which being raw cane sugar for refining and 10% white sugar for direct consumption⁵⁴⁷.
- (607) Therefore, for the marketing year 2010/2011, about 2.5 million tonnes of preferential raw cane sugar for refining (including raw sugar from ACP/LDC countries and raw sugar under CXL quotas) were imported into the EEA. This is less than what was necessary to close the gap with European demand. One reason for this gap was that international market prices were briefly and for the first time higher than prices in the Union. Another reason was that the ACP and LDC countries were not able to expand their sugar production as fast as initially expected. It is for that reason that the Commission allowed the release of 0.8 million tonnes of extraordinary tariff reduced imports (TRQ's)⁵⁴⁸.
- (608) Cane sugar refineries are currently operating well below capacity in the EEA, a situation that can be economically difficult for any sugar processor, beet or cane, given the high fixed costs of sugar refining plants.
- (609) Therefore, there is a high demand for preferential raw cane sugar for refining in the Union and there is raw cane sugar excess refining capacity in the EEA.

The Parties do not have the ability to foreclose access to preferential raw cane sugar

- (610) For the marketing year 2010/2011, EDFM has imported around [...] tonnes of preferential raw cane sugar into the EEA⁵⁴⁹ while Südzucker imported around [...] tonnes of raw cane sugar, mainly from [...]⁵⁵⁰.

⁵⁴⁷ See 3rd request for information to EDFM. 10 December 2011.

⁵⁴⁸ See Form CO and 4th request for information to Südzucker 14 October 2011.

⁵⁴⁹ 3rd request for information to Südzucker 9 October 2011 and 2nd request for information to EDFM/ Annex 9A Phase II.

- (611) The Parties' combined market share represents around [30-40]*% of the whole amount of preferential raw cane sugar that entered into the EEA. Their combined shares would be lower if the raw cane sugar imported under exceptional measures (TRQ's) were taken into account. Südzucker did not import raw cane under this scheme in 2011 while EDFM imported around [...]* tonnes (representing less than [10-20]*% of sugar available under TRQ contracts).
- (612) Out of the [...]* tonnes of preferential raw cane sugar imported into the EEA by EDFM, only [...]* tonnes were delivered to third party refineries while the remaining [...]* tonnes were consumed captively by the refineries in which EDFM has a participation in (Brindisi and DAI). [...]*
- (613) Südzucker is also primarily a captive user. It delivers preferential raw cane sugar mainly to its own [...]*.⁵⁵¹ Therefore, Südzucker no longer has specific access to preferential raw cane sugar.
- (614) To summarize, out of the total preferential raw cane sugar brought by the Parties into the EEA, more than [80-90]*% was captive and directly supplied to the refineries where they have participations.
- (615) Another important preferential raw cane sugar importer into the EEA is Tate & Lyle which has raw cane sugar refining capacities of more than 1.3 million tonnes. According to the notifying party, Tate & Lyle imported between 700,000 and 800,000 tonnes of preferential raw cane sugar for its two United Kingdom based refineries. Therefore, it would represent around 30% of the total import of preferential raw cane sugar. The remaining preferential raw cane sugar that entered into the EEA was mainly imported by British Sugar (ABF) for its Spanish refineries (around 80,000 tonnes)⁵⁵², by Litex (Bulgaria), by CristalCo and Tereos (France) or by Pfeifer & Langen (refinery in Romania).

EDFM's role as independent supplier of raw cane sugar has [...] over time*

- (616) The Parties estimate that 10 major long term supply contracts were negotiated with ten ACP/LDC countries, covering an estimated three quarters of available supplies in the 2011/12 marketing year and a similar share of annual quantities until 2015. Those ten ACP/LDC countries are Belize ([...]*), Fiji ([...]*), Guyana ([...]*), Jamaica ([...]*), Malawi ([...]*), Mauritius [...]*), Mozambique ([...]*), Swaziland ([...]*), Zambia ([...]*) and Zimbabwe ([...]*)
- (617) As can be seen, EDFM is the only "trader" having [...]* agreements with raw cane sugar suppliers in ACP/LDC countries ([...]*) and good relationships in "CXL" countries such as Brazil. For that reason, some refiners raised concerns that post-transaction the main independent supplier/trader of raw cane sugar, EDFM, could have the incentive to stop supplying other refineries.

⁵⁵⁰ 1st request for information to Südzucker 26 September 2011. Confirmed in the Response to 6.1(c) decision 17/11/2011.

⁵⁵¹ 4th request for information to Südzucker 14 October 2011 and Annex Q3 A1 [...]*

⁵⁵² But also for a number of other refineries in the Union though its joint venture Mitra that it holds with Illovo which controls a significant amount of raw cane in Malawi, Zambia, Swaziland, Mozambique and Tanzania.

- (618) Even though EDFM has supplied preferential raw cane sugar to third party refineries in the past, the quantities have [...] in the last years, in particular due to [...].
- (619) In September 2008, EDFM acquired a [...] interest in the DAI refinery. Prior to that, it had no interest in - or agreement to provide raw cane sugar to - any refinery in the EEA. Therefore, in FY2007/2008 (i.e. the year ending 31 September 2008), 100% of the [...] tonnes that EDFM brought into the EEA were “independent” volumes to which any EEA refiners could have access⁵⁵³.
- (620) In the FY2008/2009, [...] tonnes were delivered to DAI and were therefore no longer available for the merchant market. Therefore, in FY 2008/2009, EDFM was involved in bringing in [...] tonnes of independent raw cane sugar.
- (621) In the FY2009/2010, EDFM brought [...] tonnes of raw cane sugar into the EEA. Excluding the [...] tonnes delivered to DAI, [...] tonnes of independent raw cane sugar were brought into the EEA by EDFM. Even if EDFM acquired its stake in Brindisi's SRB in December 2008, SRB only started producing in December 2010, therefore not requiring raw cane sugar supplies in FY 2009/2010. However, if one were to take the view that any volumes provided to SFIR (the joint venture party in SRB) were already not independent, then EDFM would have brought only [...] tonnes into the EEA in that period (i.e. less the [...] tonnes delivered to [...]).
- (622) By FY2010/2011, Brindisi was already producing and the amount of non-captively consumed raw cane sugar which EDFM brought into the EEA ([...] was [...] tonnes. The customers for this “independent” raw cane sugar were [...].⁵⁵⁴
- (623) Therefore, the role of EDFM as “independent” raw cane sugar supplier into the EEA has been [...] over the past three years.
- (624) Moreover, the quantities of preferential raw cane sugar delivered by EDFM to third party refineries represent usually less than 10% of those refinery's needs for raw cane sugar. Therefore, even though EDFM has provided preferential raw cane sugar to a number of refineries in the Union which do not all have long term contracts with ACP/LDC countries, most of those refineries only relied on EDFM for a small proportion of their needs, mainly as additional supplies that allowed refineries (temporarily) to operate at full capacity⁵⁵⁵.
- (625) With regard to CXL sugar, which require the payment of some duties, even though EDFM delivered more than [...] of its quantities available to third party refineries, the raw cane sugar imported under this scheme does not request long term contacts and is mainly imported on spot basis. That explains why most of the refiners argue that if EDFM, after the proposed transaction, decided not to supply third party refineries with CXL sugar, they could find alternative volumes with other traders

⁵⁵³ See 3rd request for information to Südzucker 09 October 2011.

⁵⁵⁴ See 3rd request for information to EDFM. 10 December 2011. [...].

⁵⁵⁵ See 3rd request for information to Südzucker 09/10/2011, Annex 6 corrected and 3rd request for information to EDFM - 10/12/2011

such as Cargill, Dreyfus, Bunge, Czarnikow or Sucden⁵⁵⁶. These players can readily replace EDFM:

- Cargill has extensive operations in corn, sugar cane and soya operations around the world and most notably in USA. EDFM estimates that Cargill accounted for around 10 million tonnes of total sugar traded in 2010/2011.
- Louis Dreyfus is a large cereal and sugar trading and producing company, which is privately held. Louis Dreyfus has extended its activities into sugar production in Brazil and is increasing its trading operations. EDFM estimates that Louis Dreyfus accounted for around 2.6 million tonnes of total sugar traded in 2010/2011.
- Bunge is a cereal company that has expanded in recent years to sugar operations, both in terms of trading and production, with investments in Brazil. Bunge acquired the trading desk of Tate & Lyle and has maintained the skills base of the old Tate & Lyle operations. EDFM estimates that Bunge accounted for around 4 million tonnes of total sugar traded in 2010/2011.
- Sucden almost exclusively trades sugar with investments in Russia and Brazil. EDFM estimates that Sucden accounted for around 2 to 5 million tonnes of total sugar traded in 2010/2011.
- Czarnikow is a brokerage trading business with exclusive links to the Australian sugar industry. It was amongst the largest brokers of raw sugar to the Union market until these operations were undermined by regulatory changes in Australia and the demise of brokerage activities in general. EDFM estimates that Czarnikow still accounted for around 5 million tonnes of total sugar traded in 2010/2011.
- Glencore is multinational company in metals, oil, and soft commodities. Although its sugar operations have not expanded significantly over the years, it is estimated that Glencore accounted for around 1.5 million tonnes of total sugar traded in 2010/2011.

(626) A majority of those sugar traders, which are either already present in the supply of preferential raw cane sugar in the Union like Czarnikow and Sucden or preparing an entry and expansion strategy such as Glencore and Louis Dreyfus argued they compete with EDFM for the supply of raw cane sugar, with some of them even arguing they could replace EDFM if it left the market⁵⁵⁷. That mainly applies for CXL countries (Brazil, Australia, Latin America) in which these competing traders have strong ties.

(627) This is also confirmed by [a sugar trade]* which stated "*where the availability of sugar import licenses to the EU is controlled by the sugar refinery (erga omnes, special quotas, ipr) allowing the refinery to freely purchase world market sugar for import into the EU, we would be currently able to replace the quantities [delivered*

⁵⁵⁶ Questionnaire to raw cane sugar suppliers– Phase II, questions 32-44-46-48

⁵⁵⁷ Questionnaire to sugar suppliers– Phase I, questions 26; Questionnaire to raw cane sugar suppliers– Phase II, questions 38

by EDFM]*⁵⁵⁸. In addition, the presence of alternative traders was confirmed by [a sugar trade]* which stated "*Companies such as Cargill, Sucden and Czarnikow are all credible suppliers because of their long-standing relationships*"⁵⁵⁹.

- (628) Given the [...] presence of the Parties on the overall supply of preferential raw cane sugar into the EEA, and in particular the [...] present merchant market position as a result of [...] and given the number of other refiners having directly access to preferential raw cane sugar, it seems unlikely that the Parties could foreclose the access to this raw material.

Lack of incentive to foreclose access to raw cane sugar

- (629) The Parties submit that there is no risk of foreclosure because raw cane sugar producers in the ACP/LDC countries would oppose the Parties engaging in such foreclosure strategies. In fact, any refusal by EDFM to supply Südzucker's competitors would result in the producers of raw cane sugar losing significant profits.
- (630) According to the Parties, it is likely that the raw cane sugar producers will react in either two ways: (i) choosing another trader/broker or (ii) importing the raw cane sugar to the independent sugar refineries themselves.
- (631) The Commission's market investigation has indicated that both scenarios are realistic and would be effective. As confirmed by EDFM's competitors⁵⁶⁰, the trade and brokerage of raw cane sugar into the EEA is currently a very profitable activity. Therefore, EDFM's main activity being trading, there would be no reason that EDFM would halt the import of small quantities of preferential cane sugar to independent refineries that it is currently doing. If EDFM stopped those imports, as already explained above, other traders/ brokers would be a ready substitute to EDFM. Furthermore, the raw cane sugar producers have developed strong ties with the main refineries and already now increasingly arrange all aspects of logistics, employing their own freight-forwarding companies.
- (632) In any event, Südzucker is currently not amongst the most important EEA customers for raw cane sugar. Südzucker currently has four raw cane sugar refineries with an annual output of [...] tonnes in total. [...] ⁵⁶¹ [...].

No effect on competition

- (633) Despite the genuine scarcity of preferential raw cane sugar available for the EEA and despite the fact that EDFM is an important independent player on this market, the proposed transaction is unlikely to have an impact on the other players given (i) the low quantities and percentage of Parties' preferential raw cane sugar currently delivered to third Parties, (ii) the presence of a wide number of already vertically integrated players, (iii) the [...] role of EDFM as an -independent trader over the last years (iv) the presence of alternative well-establish traders, in particular for the supply of CXL sugar that could readily replace EDFM in case it would stop

⁵⁵⁸ Questionnaire to sugar suppliers– Phase I, questions 25

⁵⁵⁹ Questionnaire to raw cane sugar suppliers– Phase II, questions 45

⁵⁶⁰ Questionnaire to raw cane sugar suppliers– Phase II, questions 16-28

⁵⁶¹ Südzucker also has three refineries in Romania, each with an annual capacity of around [...] tonnes.

supplying its current quantities to third party refineries and (v) the potentially low demand from Südzucker in DFQF raw cane sugar for its refineries.

- (634) In the light of the above, it is concluded that the merged entity would have neither the ability nor the incentive to foreclose access to preferential raw cane sugar input to its competitors in the downstream market for the production of white sugar. In addition, given the high percentage of the Parties captive sales and the scarcity of preferential raw cane sugar, the merged entity would have neither the incentive nor the ability to foreclose access to EEA customers of preferential raw cane sugar.

6.3. MOLASSES

6.3.1. Description of molasses

- (635) Molasses is a by-product of the sugar refining process, and is not subject to a regulatory regime. There are two types of molasses, derived from either sugar cane processing (cane molasses) or sugar beet processing (beet molasses). The notifying party estimates that roughly 70% of the Union demand for molasses is beet molasses and 30% cane molasses⁵⁶².
- (636) As molasses is a by-product of sugar refining, sugar producers such as Südzucker are the "natural suppliers" of molasses. In the context of the sugar industry reform, sugar producers had to reduce their output, which led to a decrease in the production of molasses in the Union. As the consumption in the Union of molasses is significantly higher than its production, imports are necessary. According to the Parties, roughly one quarter of the molasses consumed in the EEA are imported cane (for example from Pakistan, Thailand, India, Morocco, Guatemala, El-Salvador, Mauritius, Florida) and beet (from, among others, Egypt, Morocco, Ukraine, Russia, Balkan countries, etc.) molasses⁵⁶³, mainly brought in and sold by traders such as EDFM.
- (637) Südzucker stores molasses in tanks at its respective sugar factories and sells it to the customers usually on terms agreed once a year. Whilst beet molasses are in general marketed locally by Südzucker's entities in the production countries, significant volumes are also shipped cross-border. For example, [...]*⁵⁶⁴.
- (638) EDFM is a trader of molasses, buying beet molasses within the EEA or importing beet and cane molasses on its own account. In the campaign year 2009/2010, EDFM imported into the EEA [...]* tonnes of cane molasses (mainly from [...]*) and [...]* tonnes of beet molasses (mainly from [...]*)⁵⁶⁵.
- (639) There are three sizeable international traders that import molasses (mainly cane molasses) into the EEA, namely EDFM, United Molasses and Peter Cremer Traders also buying beet molasses from sugar producers within the EEA in order to deliver it to customers, which can be located within or outside the Member State of the production. In that respect, a trader will react to occasional imbalances of supply and demand.

⁵⁶² Form CO, p.112.

⁵⁶³ Form CO, p. 90.

⁵⁶⁴ Form CO, p. 133.

⁵⁶⁵ Form CO, Annex 7.5.a.

6.3.2. *Product market definition*

(640) Molasses is mainly used in the fermentation industry or incorporated in animal feed products. The most important sectors of the fermentation industry using molasses are yeast, citric and amino acid, alcohol and increasingly the bioethanol industry. With respect to the animal feed industry, one could distinguish between, on the one hand, direct sales to farmers that buy molasses to mix it with other feedstuff and feed it directly to their own animals and, on the other hand, sales to compound feed producers, who manufacture animal feed from different feedstuffs (including molasses) and resell the resulting animal feed to farmers, their cooperatives, or animal feed wholesalers and distributors. In very small quantities molasses is also used for special purposes in the chemical, pharmaceutical, cement and tobacco industry.

6.3.2.1. Commission's findings in previous cases

(641) In case ABF/Azucarera⁵⁶⁶ the Commission found that within molasses, there is a degree of substitution between beet and cane molasses, and that this degree varies between the customer groups considered: animal feed producers can easily substitute the two types when adding them into their final animal feed products, while customers from the fermentation industry have certain limitations to switch between the two types notably because (i) there are certain limitations for usage of cane molasses depending on the plants' constitution (differences in the composition of beet and cane molasses affect the effluent water quality and therefore additional investments would be required to switch to cane molasses); (ii) additional equipment is necessary for processing cane molasses (separator/centrifuges). In general, due to these constraints, these producers showed reluctance to switching from beet to cane molasses above a certain proportion.

(642) The market investigation in this previous case found that certain molasses customers can substitute molasses altogether. Animal feed producers indicated that they can switch to materials like glycerol or sugar syrups without any investments, and they in fact compare the prices of alternative nutritional inputs and switch swiftly. Yeast producers can also use alternative materials to molasses. In fact, due to a general shortage of molasses in the recent years (caused inter alia by reduction of sugar beet quota in the Union) resulting in increased prices for molasses, yeast producers adapted by partly switching to industrial sugar (produced either off-quota in the Union, or imported from third countries). However, when industrial sugar reaches a certain proportion of the mix with molasses, additives have to be used which increase the cost of the primary material. Therefore, yeast producers prefer to keep the proportion of industrial sugar below a certain percentage⁵⁶⁷.

(643) The Commission however finally decided to leave open the precise scope of the relevant product market in that case⁵⁶⁸.

⁵⁶⁶ Commission Decision of 30 March 2009 in Case No COMP/M.5449 - ABF/Azucarera.

⁵⁶⁷ Questionnaire to molasses competitors, Phase II, question 16-17 and 42.

⁵⁶⁸ In the absence of any competition concerns, it has not been considered necessary to reach a conclusion on the precise scope of the relevant product market, and the questions of whether beet and cane molasses belong to the same market, and whether the market also comprises alternative materials such

6.3.2.2. View of the notifying party

- (644) The notifying party is of the opinion that the relevant product market encompasses the supply of both beet and cane molasses, irrespective of the end-use application. This is because both products represent a source of energy as well as providing a means of binding other ingredients together, where this is necessary. The notifying party, therefore, submitted that beet and cane molasses are completely interchangeable within each client group⁵⁶⁹.
- (645) The notifying party also puts forward that it is not appropriate to consider customer groups for molasses as being distinct markets and points to the considerable degree of demand substitutability of molasses with alternative inputs⁵⁷⁰.

6.3.2.3. Commission findings in the case at hand

- (646) The market investigation conducted in the present case has not revealed any element that would contradict the Commission's previous findings. In fact, it confirms that customers in the fermentation industry, such as yeast and citric acid, can substitute beet and cane molasses only to a limited extent. The degree of substitution between molasses and other products (e.g. grains for the animal feed industry including farmers; industrial sugar for yeast producers) also varies between the different customer groups: the animal feed industry seems to be more able than yeast producers to substitute molasses with other products. For example, one animal feed producer explained that molasses is used *"as an energy ingredient. From the moment the molasses comes to expensive, it will disappear from our feed product.[...]* it will be replaced by cereals (corn, wheat, ...), fats, oils,... all depending on the prices for all these products"*⁵⁷¹.
- (647) Internal documents submitted by the Parties also support the proposition that there are different switching prices for different customer groups, as can be seen from the [...]* :
- [...]*
- (648) Internal documents submitted by the Parties point to some degree of segmentation of the market. Indeed, when EDFM assesses its position as a supplier of molasses it distinguishes between beet and cane molasses, as well as between different customer groups, or even further within a customer group (e.g. EDFM assesses its competitive position also with respect to only "yeast" or "farms" customer groups). Moreover, EDFM explicitly refers in its internal documents to "markets for molasses".
- (649) However, for the purpose of this Decision, the question of whether the market for molasses has to be further delineated can be left open as no competition concerns would arise irrespective of the precise product market definition.

as industrial sugar have been left open. See Case COMP/M.5449 - ABF/Azucarera – decision of 30 March 2009, paragraph 39.

⁵⁶⁹ Form CO, p.54 and 59.

⁵⁷⁰ Form CO, p.61 and 62.

⁵⁷¹ Questionnaire to molasses customers, Phase I, question 38.

6.3.3. Geographic market definition

6.3.3.1. Commission's findings in previous cases

- (650) In case ABF/Azucarera, the Commission left open the precise scope of the relevant geographic market⁵⁷². The Commission stated that the market investigation showed that the purchasing scope of beet molasses seemed to be more limited compared to cane molasses, for which there is no EEA production and all of which is imported from outside Europe. However, whereas the majority of beet molasses was still supplied locally where beet production still existed, imports of beet molasses (via specialized traders) were increasing significantly in regions where beet quota reduction led to less domestic production.
- (651) In 2002, the French competition authority considered, but ultimately left open the question of whether the market is EEA-wide or even worldwide⁵⁷³.

6.3.3.2. View of the notifying party

- (652) The notifying party is of the opinion that the market for molasses is at least EEA-wide, on the grounds that the European market suffers from a structural deficit that requires significant imports and that there is lively trade between different Member States. Even though molasses produced in the Union are typically transported around the production facilities due to the limited intrinsic value of molasses and the subsequent need to optimize transport costs, the notifying party argues that a significant amount crosses national borders, for instance in train wagons⁵⁷⁴.
- (653) In this respect, the Parties refer to F.O.Licht statistics on cross border molasses trade, and particularly to the "World Molasses and Feed Industry Report" published on 14 November 2011 in order to demonstrate that there is a lively trade across borders to and from the neighbouring Member States⁵⁷⁵. Based on the F.O.Licht data for the period October 2009 to September 2010, the Parties have provided a map of the Central Europe region (i.e. the areas of concerns in the first phase market investigation⁵⁷⁶) showing that Member States are connected to each other when it comes to the supply of molasses⁵⁷⁷.

⁵⁷² Commission Decision of 30 March 2009 in Case No COMP/M.5449 - ABF/Azucarera. .

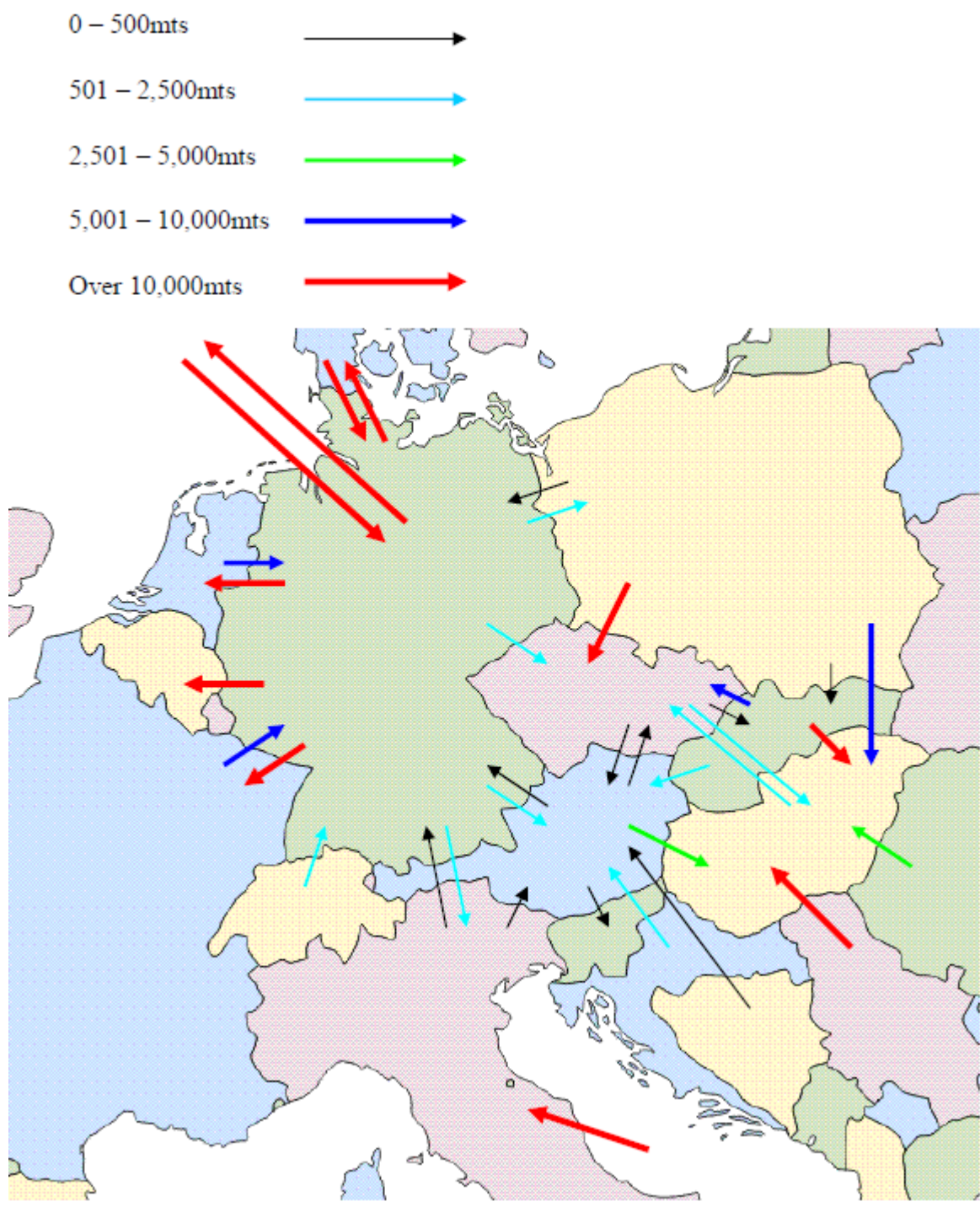
⁵⁷³ Lettre du ministre de l'économie, des finances et de l'industrie du 5 décembre 2002 aux conseils du groupe de l'Union des sucreries et distilleries agricoles et de la société Union des planteurs de betteraves à sucre (Union SDA/Union BS/ Béghin-Say).

⁵⁷⁴ Form CO, p.76 and 77.

⁵⁷⁵ See reply to the 8th RFI to Sudzucker and EDFM, Phase II, p. 10.

⁵⁷⁶ At the end of Phase I, the Commission had as preliminary conclusion that the concentration raised doubts as to its compatibility with the internal market, with respect to the market(s) for molasses in Austria, Czech Republic and Slovakia. It was not excluded that the transaction also raises doubts with respect to the market(s) for molasses in Germany or alternatively southern Germany and Italy. The main reason for these doubts were (i) the high market shares of the parties post-transaction, (ii) the elimination of an competitive pressure on Südzucker/EDFM, (iii) the limited ability of remaining competitors to hinder the merger entity market power, and (iv) the significant barriers to entry and expansion.

⁵⁷⁷ See reply to the 8th RFI to Sudzucker and EDFM, Phase II, p. 11.



6.3.3.3. Commission findings in the case at hand

- (654) The market investigation conducted by the Commission in this case was not conclusive with respect to the geographical scope of the market. Although it provided some indications that the market could – at least for beet molasses - be narrower than the EEA as submitted by the notifying party, it also clearly shows that, from a customer perspective, national borders are not relevant when looking for supplies.
- (655) On the one hand, respondents to the Commission's requests for information explained that transport costs are high in proportion to the value of molasses, since

they may represent, according to some respondents, up to 20% of the final price of molasses. For that reason, customers try to source their molasses from suppliers located in proximity, in particular from nearby beet sugar refineries. That is evidently the case during the sugar processing season (lasting 3 months) when sugar producers need to sell molasses in large volumes as it otherwise blocks the sugar production process⁵⁷⁸.

- (656) As regards the imports of molasses (both cane and beet), accessibility and proximity to the port facilities are important factors determining the extent to which customers can source imported molasses. In areas away from the sea, imports of molasses are therefore rather limited. In the Czech Republic, for example, there are no imports of cane molasses⁵⁷⁹.
- (657) The concentration of demand and supply around ports and sugar refineries does however not imply that the market should be defined as national or even local. The market investigation provided evidence supporting a larger than national definition of the relevant geographic market based on a chain of substitution effect. The natural geographical area of supply of a given molasses production or storage facility can be represented by concentric circles with various lengths of radiuses determined by transport costs. In this light the various supply areas can be seen as a series of overlapping circles with their centres at the sugar plants and molasses storage tanks. Given the number and dispersion at least in northern and central Europe of the individual molasses supply points, price effects seem to be transmitted from one circle to the other. Moreover, some suppliers and customers also seem to supply and buy molasses over much quite long distance beyond the radiuses of the 'natural' supply areas. Finally, large molasses customers such as the fermentation industry have significant coastal storage capacity from which smaller inland terminals are supplied. There appears therefore to be a ripple-through effect of prices which would mean that, as such, the limitations imposed by the limited distance over which molasses can be transported by truck do not exclude the finding of a much broader relevant geographic scope of the market⁵⁸⁰.
- (658) The results of the market investigation were as follows. First, the geographic overview of how supply and demand are organised in Europe, and in particular in Austria, the Czech Republic, Germany, southern Germany and Slovakia (i.e. the areas of concerns in the first phase investigation) shows that even though molasses is typically transported around the production facilities, molasses producers and traders are to varying extents⁵⁸¹ involved in cross-border sales. For example, one competitor (a trader active in several Member States) explained that from its storage location in Bremen, cane molasses is delivered into Germany, Netherlands, Austria, Switzerland

⁵⁷⁸ Questionnaire to molasses customers, Phase II, questions 42-46, 61-66 ; Questionnaire to molasses competitors, Phase II, question 6-17

⁵⁷⁹ Questionnaire to molasses customers, Phase II, questions 42-46, 61-66 ; Questionnaire to molasses competitors, Phase II, question 6-17

⁵⁸⁰ Questionnaire to molasses customers, Phase II, questions 42-46, 61-66 ; Questionnaire to molasses competitors, Phase II, question 6-17

⁵⁸¹ See replies to Questionnaire to molasses competitors, Phase II, question 6. Some of the respondents also explained that they have chosen a different business model, preferring to focus only on national sales.

and Poland⁵⁸². Another competitor, a molasses producer, explained that it also sells molasses from the Member State of production to other Member States⁵⁸³.

- (659) The Parties follow a similar business model with respect to their distribution of molasses. Although most of the molasses sold in a given Member State were produced or sourced locally, molasses are also transported beyond the boundaries of the Member State of production. For example, [...] *⁵⁸⁴. [...] *
- (660) In that respect, the replies to the Request for Information sent during the second phase market investigation also indicate that national boundaries may not be the appropriate way to assess the geographic scope of the market for molasses⁵⁸⁵. Indeed, with one exception, the customers explained that national borders are not important when looking for a molasses supplier⁵⁸⁶.
- (661) Secondly, customers do not seem to highly value the local presence of a supplier. Only a limited number of customers responding to the second phase questionnaires consider purchasing molasses only from a supplier that has production/storage facilities in the Member State where they operate⁵⁸⁷.
- (662) Thirdly, in contrast to the sugar markets, the vast majority of molasses are supplied directly by producers, importers and traders, without the need for an intermediary that supplies the molasses through wholesale operations or national/local distribution centres.
- (663) Fourthly, the market investigation confirmed the notifying party's submission that some customers (e.g. in the fermentation industry) import molasses directly into the EEA, although this practice is limited to a few customers with high volume demands⁵⁸⁸.
- (664) Fifthly, internal documents of Südzucker show that the management of the molasses business attaches great importance to the prices of Molasses 'ex tank' in Bremen. This shows that prices in the north of Germany are of importance for pricing negotiations and pricing strategies in the south of Germany.
- (665) However, while the market investigation shows that the market may be Union wide, for the purpose of this Decision, the question of the precise scope of the geographic market definition for molasses can be left open as no competition concerns would arise irrespective of the geographic market definition retained (i.e. Union-wide markets or national).

⁵⁸² Questionnaire to molasses competitors, Phase II, question 6.

⁵⁸³ Questionnaire to molasses competitors, Phase II, question 6.

⁵⁸⁴ See reply to the 8th RFI to Südzucker and EDFM, Phase II, p. 12.

⁵⁸⁵ Questionnaire to molasses competitors, Phase II, question 15; Questionnaire to molasses customers, Phase II, questions 64 and 67.

⁵⁸⁶ Questionnaire to molasses customers, Phase II, questions 64.

⁵⁸⁷ Questionnaire to molasses customers, Phase II, questions 65.

⁵⁸⁸ Questionnaire to molasses customers, Phase II, question 89.

6.3.4. *Effects on competition*⁵⁸⁹

- (666) The Parties' activities overlap with respect to the supply of molasses to both fermentation customers and farmers / animal feed customers. Depending on the geographic market definition, affected markets would arise at both the EEA and national levels⁵⁹⁰.
- (667) During the first phase investigation, several competitors and customers of the Parties as well as the Confederation of EU Yeast Producers complained with respect to the negative effects arising from the proposed transaction. However, on the basis of the in-depth investigation, it has been considered that these initial concerns are not well-founded as will be further demonstrated.
- (668) In addition to the arguments specifically developed for each affected market, the following considerations on the dynamics of the molasses markets need to be considered when assessing the effects of the proposed transaction.
- (669) First, Südzucker sells most⁵⁹¹ of its molasses directly to customers, without the intervention of traders or other intermediaries (only 5-10% of cross-border sales are directed to traders)⁵⁹². This is a characteristic of the industry. As explained by another major sugar/molasses producer, it also prefers to sell directly to customers. That molasses producer also explained that, in the last years, it increased the proportion of its direct sales while decreasing its sales through traders⁵⁹³.
- (670) Secondly, customers confirmed that they prefer to source directly from molasses producers. The direct supply relationships are more important for customers from the fermentation industry as this enables them to track quality and origin of the molasses which are critical to the fermentation production processes. Such a relationship does not appear important for farmers and animal feed producers⁵⁹⁴. It therefore appears that the role of traders is focussed on molasses imports and spot sales rather than continued supply relations with customers.

6.3.4.1. Assessment on the basis of an EEA-wide market⁵⁹⁵

- (671) Should the market be defined as EEA-wide, the combined entity would hold a market share of [30-40]*%⁵⁹⁶ on the overall molasses market (i.e. comprising beet

⁵⁸⁹ The market shares referred to in this Decision are the Parties' best estimates provided in the Form CO, pp.81-83 and Annex 7.3d.

⁵⁹⁰ Given the limited overlap between the Parties, Slovenia and Italy will not be further considered for the purpose of this Decision (EDFM had sales of only [...] tonnes of beet molasses in Slovenia; Südzucker sold in Italy [...] tonnes of beet molasses). Form CO, Annex 7.3d.

⁵⁹¹ In [...]*, for example, only [...]* of its production has been sold through traders since out of the [...]* tonnes of molasses produced in the campaign year 2009/2010, almost [...]* were delivered directly to customers ([...]* tonnes), and [...]* ([...]*) was used internally.

⁵⁹² See reply to the 2nd RFI to both Parties, Phase II, question 2.

⁵⁹³ Questionnaire to molasses competitors, Phase II, question 17(d) and (e).

⁵⁹⁴ Questionnaire to molasses competitors, Phase II, question 65; Questionnaire to molasses customers, Phase II, question

⁵⁹⁵ Südzucker does not sell molasses in any EEA Member State (Iceland, Liechtenstein, Norway). EDFM as well, does not sell molasses in Norway, Liechtenstein and Iceland (deliver around [...] tonnes of molasses on a CIF basis to Norwegian ports, which volumes are then imported into the EU by the relevant customer). See reply to the 2nd RFI to both Parties, Phase II, question 1.

and cane molasses) for all applications. On the basis of a narrower market definition (i.e. distinguishing between beet and cane molasses), the proposed transaction would lead to a combined market share of [20-30]*% on the potential market for the supply of beet molasses (Südzucker [10-20]*%; EDFM [10-20]*%)⁵⁹⁷.

- (672) Should the market be delineated according to the molasses application, Südzucker would not be an important supplier to farmers ([0-5]*%) and to compound feed producers ([0-5]*%). EDFM is a more important supplier with respectively [20-30]*% and [40-50]*%. The proposed transaction would thus bring no important change to the market structure for the highly volatile demand for molasses in animal feed. Other traders such as United Molasses and Peter Cremer are considered by the market as ready alternatives. It is to be noted that Peter Cremer is part of one of Europe's largest compound feed manufacturer Peter Cremer Holding GmbH & Co. KG.
- (673) In any case, farmers can and do switch between different animal feed products in order substitute molasses. According to the information submitted by the Parties, of all raw materials used for animal feed in the EEA, less than 2% would be represented by molasses⁵⁹⁸. Moreover, farmers account for less than 5% of the European molasses consumption⁵⁹⁹.
- (674) With respect to the supply of molasses to the fermentation industry, comprising yeast, citric acid and alcohol producers, the combined entity would have a combined market share of around [40-50]*% (Südzucker [20-30]*% and EDFM [10-20]*%). Within the fermentation industry, especially the yeast producers are important customers for Südzucker, as the latter sells almost all its molasses directly to the yeast industry, trying to avoid any involvement of traders⁶⁰⁰. Other sugar producers such as Nordzucker ([5-10]*%), but also molasses traders such as United Molasses ([5-10]*%) are suppliers to the fermentation industry.
- (675) Fermentation customers are usually multi-national companies, who follow a multi-sourcing strategy, yet prefer sourcing directly from producers instead of passing through traders. This is mainly because *"a trader has no specific knowledge and no control over product quality compared to a sugar producer who can try to improve the quality of its product if needed"*⁶⁰¹. The second phase market investigation also revealed that fermentation customers have some experience with using other input materials than molasses, such as industrial sugar which can notably be imported from outside the EEA.
- (676) During the market investigation no substantiated concerns were expressed with respect to the impact of the proposed transaction for fermentation customers. On the contrary, the second phase market investigation indicated that, if there is a concern

⁵⁹⁶ Form CO, p.81.

⁵⁹⁷ Südzucker operates also two raw cane refineries in the EEA. Should a distinct market for the supply of cane molasses be considered, Südzucker's market share will be less than [0-5]% (Südzucker does not import cane molasses into the EEA; Form CO, p.114). Therefore, this market is not further addressed in this Decision.

⁵⁹⁸ Form CO, p.106.

⁵⁹⁹ Form CO, p.105.

⁶⁰⁰ Form CO, p.96.

⁶⁰¹ Questionnaire to molasses competitors, Phase II, question 58.

about access to molasses, this is not merger specific, but rather a consequence of the scarcity of molasses due to the sugar reform and the development of the bioethanol industry⁶⁰². In addition, one customer who complained about the effects of the proposed transaction during the first phase investigation confirmed that it could switch from molasses to glucose for which it has its own production facilities (molasses is cheaper than sugar glucose but it requires a more expensive multi-stage process in order to be converted into the fermented product). Moreover, this customer confirmed that it has its own molasses storage facilities and is therefore capable of buying molasses at favourable prices when sugar manufacturers need to sell off this by-product of sugar production⁶⁰³. Whilst third party storage bears an important cost that cannot be compensated through the limited intrinsic value of molasses, large customers have their own dedicated molasses storage capacity.

6.3.4.2. Assessment on the basis of national markets

(677) When considered on the basis of national markets, the market structure in those countries where the proposed transaction leads to affected markets is as follows:

Austria

(678) In Austria, Südzucker is the only sugar manufacturer. Consistent with the limited economic rationale to transport molasses over long distances it also holds a high market share in relation to the supply of molasses. In Austria, 82% of molasses demand is met by beet molasses, with cane molasses accounting for the remainder.

(679) In addition to Südzucker's [70-80]*% market share, EDFM accounts for [10-20]*% of the market of the overall molasses market (i.e. including beet and cane molasses). If considering only the supply of beet molasses, Südzucker accounts for [70-80]*% of the market, while EDFM accounts for no more than [5-10]* of the market. The Parties' activities in Austria overlap only with respect to the supply of molasses to compound feed producers. In line with its overall market position, the new entity's accounts for [90-100]*%, with an increment of [10-20]*% brought about by EDFM. Despite the increment, EDFM has very limited activities in Austria, [...]*⁶⁰⁴ [...]*. As EDFM [...]*, there is no reason why competing traders located in neighbouring countries such as United Molasses or Peter Cremer would not be able to replace EDFM's (for example, during the second phase market investigation one compound feed producer indicated that it could source from another supplier, able to provide better long term access to beet molasses and more reliable than EDFM)⁶⁰⁵. In addition, the market investigation has indicated that EDFM's role is merely one of buying molasses surplus and transporting it to Austrian customers. EDFM has no dedicated molasses storage capacity in Austria and thus would face high storage costs when renting third party storage currently used for more valuable commodities (such as vegetable oils). As such, the role of traders is mainly that of distributing the product which limits their ability to play an important role in the market.

⁶⁰² See non-confidential minutes of a conference call with a third party of 1 December 2011.

⁶⁰³ Questionnaire to sugar and molasses competitors, Phase I - Questionnaire to molasses competitors, Phase II

⁶⁰⁴ See reply to the 8th RFI, Phase II, p. 18 and Annex Q19-2.

⁶⁰⁵ Questionnaire to molasses customers, Phase II, question 66.

- (680) Compound feed manufacturers could readily organise such transport from Germany themselves without the intervention of a trader. In addition, the compound feed producers who replied to the second phase market investigation consider that the proposed transaction would not affect their access to molasses or the price of it⁶⁰⁶.
- (681) As to fermentation customers, the second phase market investigation revealed that they do not perceive EDFM as exerting competitive constraints over Südzucker⁶⁰⁷. If the merged entity were to request a higher price for molasses following the proposed transaction, fermentation customers explain that they would not accept such a change but would rather start buying on spot, source from other molasses producers (for example from Slovakia) or increase the use of alternative input⁶⁰⁸. Given the importance of fermentation customers as a stable and reliable source of demand, it is unlikely that the merged entity would be in a position to behave independently from its customers and competitors.
- (682) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in Austria.

The Czech Republic

- (683) In the Czech Republic, Südzucker operates two sugar factories and consequently accounts for a significant part of the molasses market as well ([30-40]*% of the overall market). At present there is no consumption of cane molasses in the Czech Republic. EDFM's market share is limited ([0-5]*%), which leads to a combined market share of [30-40]*%. The vast majority of EDFM's molasses sales are to farmers for animal feed production.
- (684) EDFM and Südzucker do not closely compete with each other as EDFM primarily sells molasses blends (molasses mixed with vinasses/glycerol) to farmers while Südzucker sells pure molasses. This was indicated by the market investigation⁶⁰⁹. Apart from a limited investment in the form of a mobile blending operation, EDFM has no other storage or logistics infrastructure in the Czech Republic, and as such there is no reason why competing traders would not be able to replace EDFM's activities. In any case, EDFM's lack of dedicated molasses storage capacity in the Czech Republic limits its ability to play an important role in the market other than that of distributing the product.
- (685) No substantiated concerns were expressed during the market investigation.
- (686) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in the Czech Republic.

⁶⁰⁶ Questionnaire to molasses customers, Phase II, question 116 and 117.

⁶⁰⁷ Questionnaire to molasses customers, Phase II, question 68.

⁶⁰⁸ Questionnaire to molasses customers, Phase II, question 79.

⁶⁰⁹ Questionnaire to molasses customers, Phase II, question 114.

Belgium and Luxembourg

- (687) Although Südzucker is the only sugar manufacturer in Belgium, it accounts for only one third of the beet molasses marketed in Belgium (including Luxembourg) and for around [20-30]*% of all molasses (i.e. including beet and cane molasses) in that area. EDFM has a comparably strong position ([20-30]*% of all beet molasses and [20-30]*% of overall molasses) due to storage and import capacity in Belgian ports.
- (688) Südzucker and EDFM supply different customers. Südzucker supplies primarily the fermentation customers that require origin traceability and value supplier relationships. Südzucker hold shares of [30-40]*% in the supplies of molasses to fermentation customers (that have significant production volumes in Belgium). On the same market, EDFM accounts for [10-20]*%. Fermentation customers have alternative suppliers (United Molasses [20-30]*%). In addition, due to their high volume requirements, these customers have acquired know-how to organise alternative supplies from third parties or to source directly from countries of origin outside the EEA. The market investigation indicated⁶¹⁰ that these customers already follow a multi sourcing strategy (for example, one fermentation customer who complained about the effects of the proposed transaction is currently supplying molasses from several other suppliers than the Parties, and indicated as potential suppliers three molasses producers all located in neighbouring Member States).
- (689) When considering a distinct market for the use of molasses in animal feed, EDFM accounts for [30-40]*% of that market whilst Südzucker holds [5-10]*. Other traders, and in particular United Molasses ([30-40]*%) account for the remainder.
- (690) No substantiated concerns were expressed during the market investigation by any customer group.
- (691) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in Belgium and Luxembourg.

France

- (692) EDFM's presence in France is very limited ([0-5]*% of overall molasses sales), which adds to Südzucker's [20-30]*% market share. All of Südzucker's sales are to the fermentation industry, a market for which it holds a share of [40-50]*%. EDFM holds less than [0-5]*%. The combined entity's main competitors are Tereos ([10-20]*%) and United Molasses ([20-30]*%). Südzucker has no sales of molasses for animal feed. EDFM accounts for less than [0-5]*%.
- (693) No substantiated concerns were expressed during the market investigation with respect to the effects of the proposed transaction.
- (694) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in France.

⁶¹⁰ Questionnaire to molasses customers, Phase II.

Germany

- (695) In Germany, the Parties account for [10-20]*% (Südzucker [10-20]*% and EDFM [5-10]*) of the overall molasses (cane and beet molasses) market. They face competition from both sugar producers such as Nordzucker ([5-10]*%) and Pfeifer & Langen ([5-10]*%) as well as from traders such as Peter Cremer ([10-20]*%). Concerning the supply of beet molasses in Germany, the proposed transaction would lead to a combined market shares of [20-30]*% (Südzucker [10-20]*% and EDFM [10-20]*%).
- (696) Südzucker serves primarily the fermentation industry ([20-30]*%), and only accounts for [0-5]*% of the molasses supplied to German customers to be used in the animal feed production (*i.e.* both compound feed producers and farmers)⁶¹¹. EDFM also accounts for only a small percentage of the molasses sold for animal feed production ([5-10]*%). With respect to molasses supplied to the fermentation industry, the Parties are both present (Südzucker [20-30]*% and EDFM [10-20]*%) and face competition of comparable strength, such as Nordzucker ([20-30]*%) and Pfeifer & Langen ([20-30]*%).
- (697) During the market investigation, customers from the fermentation industry complained about the possible effects of the proposed transaction in Germany. On the basis of the investigation conducted during the second phase of the procedure, it is considered that the concerns that were voiced are not merger specific but rather related to the scarcity of molasses flowing from reduced sugar production due to the sugar reform and the increased demand for molasses as a result of the uptake of bioethanol production. The market investigation has therefore focused on the question whether as a result of the evolution in the supply/demand balance of molasses, a reduction in the number of readily available molasses suppliers as brought about by the proposed transaction could negatively impact competition. The results of the market investigation do not support such a conclusion.
- (698) All the fermentation customers who replied to the second phase Request for Information confirmed that they currently multisource their molasses needs⁶¹². Some of them source directly from abroad and one explained it switched from purchasing molasses from EDFM to a producer⁶¹³. In all cases where companies had entered into a supply relationship with EDFM, these supplies were highly fluctuating in importance and were on an occasional basis. This is significantly different from the structural, long-standing and stable relationship that these customers have with sugar producers. Moreover, when asked how they will react in case the merged entity were to request a higher price for molasses, the majority of customers explained that they would not accept such a change and look for alternative suppliers⁶¹⁴.
- (699) With respect to the yeast customers, they largely confirmed that EDFM does not exert a significant competitive constraint on Südzucker due to EDFM's limited role

⁶¹¹ Within the "animal feed" group of customers, the Parties will hold a combined market share above [10-20]*% only with respect to the supply of molasses to farmers ([30-40]*%).

⁶¹² Questionnaire to molasses customers, Phase II, question 29, 56 and 66.

⁶¹³ Questionnaire to molasses customers, Phase II, question 75.

⁶¹⁴ Questionnaire to molasses customers, Phase II, question 79.

as a facilitator in matching occasional demand and supply⁶¹⁵. As to the customers using molasses for the animal feed production, only one raised concerns which relate to the existing market situation of short supply of molasses rather than merger specific elements. Moreover, this customer explained that he would be able to find alternative suppliers.

- (700) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in Germany.

Southern Germany

- (701) During the first phase market investigation, some respondents voiced concerns with respect to the effects of the proposed transaction, and these concerns were concentrated for the southern Germany region, where Südzucker accounts for [60-70]*% of the beet molasses supplied to customers. The second phase market investigation did not confirm these initial concerns.
- (702) In southern Germany, the Parties would hold post-transaction a market share of [70-80]*% on the potential market for the supply of beet molasses), with an increment of [5-10]*% brought by EDFM.⁶¹⁶ Südzucker primarily supplies the fermentation industry ([70-80]*% of market share) and more particularly the yeast customers while EDFM accounts for [10-20]*% of the sales to the fermentation industry, again in particular the yeast customers). Despite what the increment may suggest, EDFM's presence in southern Germany is rather limited, as it only serves [...] customers, [...] yeast producers. The market investigation indicated the limited role of EDFM in southern Germany. One of the competitors, another trader active in Germany and south of Germany, even stated that "*EDFM has no function*" in the southern Germany region⁶¹⁷. Moreover, this competitor does not expect the proposed transaction to change anything in this respect. As for Südzucker, all the molasses supplied to the yeast industry are supplied directly to the customers.
- (703) EDFM's limited role in southern Germany is determined by its lack of dedicated molasses storage capacity in that region. Faced with high storage costs when renting third party storage, EDFM's role is mainly that of distributing surplus capacity molasses.
- (704) During the market investigation, no customers expressed substantiated concerns with respect to the effects of the proposed transaction in southern Germany.
- (705) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in southern Germany.

⁶¹⁵ Questionnaire to molasses customers, Phase II, question 68.

⁶¹⁶ The combined market share will be the same even considering a potential market for beet and cane molasses.

⁶¹⁷ Questionnaire to molasses traders/brokers, Phase II, question 9.

Slovakia

- (706) In Slovakia, the Parties will account for [20-30]*% on the beet molasses market. There is no consumption of cane molasses in Slovakia. The Parties' activities primarily overlap with respect to the supply of molasses to farmers (no overlap arises with respect to the supply to compound feed producers), where EDFM holds a market share of [80-90]*% and Südzucker accounts for the rest [10-20]*% of the supplies. The proposed transaction will therefore bring together the only two suppliers of beet molasses to farmers. However, on the overall market for the supply of beet molasses, the combined entity's market share is limited to [20-30]*%, since Nordzucker accounts for [70-80]*% of the market. Therefore, there is no risk that the merged entity would be able to act independently from its customers and the much stronger Nordzucker, if this segment of the market were to be considered.
- (707) EDFM and Südzucker are not closely competing with each other: EDFM primarily sells molasses blends (molasses mixed with vinasses/glycerol) to farmers, while Südzucker sells pure molasses. The limited competition between suppliers of pure molasses and suppliers of molasses blends was also indicated by the market investigation⁶¹⁸.
- (708) Furthermore, farmers can and do switch away from molasses to other feed components: indeed, of all raw materials used for animal feed in Slovakia, less than [0-5]*% would be represented by molasses.⁶¹⁹ In addition, no substantiated concerns were expressed during the market investigation.
- (709) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in Slovakia.

Input foreclosure

- (710) During the market investigation, one competitor of EDFM raised concerns about a foreclosure of access to molasses (both within the EEA and outside the EEA) for traders.
- (711) On the basis of the market investigation; it is considered that these concerns are not well founded. Indeed, the market investigation shows that Südzucker sells most of its molasses directly to customers without using traders. With respect to the imports of molasses from outside the EEA, these represent only 3% of the world-wide molasses production (if distinguishing between beet and cane molasses, imports into the EEA represent 6% of the beet molasses produced world-wide, while imports of cane molasses represent 3% of the world-wide production). EDFM accounts for [20-30]*% of the imports of molasses into the EEA ([10-20]*% for beet molasses; [20-30]*% for cane molasses). United Molasses for example also accounts for 15-25% of the imports (20-30% for cane molasses)⁶²⁰. Another molasses trader indicated that there are no problems regarding the access to cane molasses at the moment and that the proposed transaction will not change this. On the contrary, according to this

⁶¹⁸ Questionnaire to molasses customers, Phase II, question 106.

⁶¹⁹ Form CO, p. 107.

⁶²⁰ See reply to the 2nd RFI to both Parties, Phase II, question 6.

competitor, the sugar production will increase in Russia and Ukraine and therefore the quantities of available (beet) molasses will also increase⁶²¹. Moreover, the investigation of the internal documents provided by the Parties did not reveal any such plans.

6.3.5. *Conclusion*

(712) In the light of the above elements, it is concluded that the proposed transaction is not likely to lead to competition concerns with respect to the supply of molasses in the EEA or at national level.

6.4. **OTHER PRODUCTS**

(713) The proposed transaction also results in reportable markets; however they do not amount to affected markets⁶²². Those reportable markets are (i) the market for bioethanol, (ii) the market for biofuel and (iii) the market for Feedstuff, DGGS and vinasses/CMS.

6.4.1. *Bioethanol*

(714) Bio-ethanol is ethanol that is produced from the fermentation of sugars derived from plants (as opposed to synthetic ethanol produced from natural gas or naphtha)⁶²³. Ethanol is manufactured by fermenting sugars into alcohol. These sugars can come from a variety of agricultural sources such as sugar cane, grains/cereals, sugar beet, potatoes, other crops, and increasingly even organic waste materials⁶²⁴.

(715) In its case-practice, the Commission has considered whether there could be different product markets according to the use of bioethanol, for example fuel or non-fuel bioethanol, such as alcoholic beverages⁶²⁵, however without concluding on this point whether it is separate from the market for the production and supply of biobutanol, another blending component for bio-fuels⁶²⁶.

(716) While Südzucker produces and markets bioethanol in the EEA, EDFM does not sell bioethanol in the EEA.

(717) With regard to vertical effects stemming from input such as sugar beet and molasses the notifying party puts forward that only 4% of the Union bioethanol production derive from sugar and molasses while the rest from grains and Südzucker's market shares in the EEA was only [10-20]*% ([10-20]*% for fuel bioethanol and [0-5]*% for non-fuel bioethanol) in 2010⁶²⁷.

(718) The proposed transaction does not lead to horizontally and vertically affected markets in the segment of bioethanol. Therefore, no competition concern arises from the proposed transaction as regards bioethanol.

⁶²¹ Questionnaire to molasses competitors, Phase II, question 32 and 40.

⁶²² Horizontal Merger Guidelines, paragraph 18.

⁶²³ Case COMP/M.4798 – BP / Associated British Foods / JV, paragraph 12.

⁶²⁴ Page 64 of the Form CO.

⁶²⁵ Case COMP/M.4798 – BP / Associated British Foods / JV, paragraph 12.

⁶²⁶ Case COMP/M.5550 - BP/DuPont/JV, paragraph 15.

⁶²⁷ Page 64 of the Form CO and Annex 6.3-C of the Form CO.

6.4.2. *Biofuel*

- (719) The oil industry is divided into "upstream" and "downstream activities. "Upstream" activities include crude oil exploration and production, whereas "downstream" activities include crude oil refining and the marketing and distribution of refined products.
- (720) The Commission has considered biodiesel to be part of the fuel market. Indeed, Bioethanol is added to traditional fuels (under current fuel specifications up to 5%) to constitute so-called bio-fuels which are sold through the same channels as "non-bio" gasoline blends. In line with previous Commission practice⁶²⁸, the market for the sale of motor fuels and therefore by assimilation for the sale of bio-fuels, can be further sub-divided in a market for retail sales and a market for non-retail sales. While retail sales of fuels involve sales to motorists through service stations forecourts, the non-retail sales consist principally of sales to three categories of customers, i.e. non-integrated retailers, independent resellers and industrial and commercial consumers⁶²⁹.
- (721) The Commission's approach has consistently been that there is a relevant product market of the retail sale of motor fuels, with no need for a further distinction between different types of fuel⁶³⁰.
- (722) The notifying party submits that the proposed transaction does not lead to horizontally affected market since EDFM supplies negligible quantities of biofuel in the EEA, with approximately [0-5]*% of the market shares on the market for biofuel⁶³¹. On the other hand the market for fuel is wider and Südzucker does not sell biofuel in the EEA but only supplies bioethanol to biofuel producers in the EEA with a market share of [10-20]*% in 2010. Therefore, the vertical effects are also negligible.
- (723) The proposed transaction does not lead to horizontally and vertically affected markets in the segment of biofuel. Therefore, no competition concern arises from the proposed transaction as regards bioethanol.

6.4.3. *Feedstuff, DDGS, CMS*

- (724) The Commission assumed a market for corn gluten animal feedstuffs, which is a by-product of starch and sugar production, while leaving it open whether other animal feedstuffs have to be considered part of this market⁶³² and was considered to be national⁶³³.
- (725) In other cases the Commission tended to assume a uniform market for animal feedstuff additives containing protein, which are not grain based (so called NGFI,

⁶²⁸ Case COMP/M.1383 – *Exxon/Mobil*.

⁶²⁹ Case COMP/M.4798 – *BP / Associated British Foods / JV*, paragraph 24.

⁶³⁰ Case COMP/M.5846 - *Shell/Cosan/JV*, paragraph 16 or Case COMP/M.5781 - *Total Holdings Europe SAS/ERG SPA/JV*, paragraph 16.

⁶³¹ E-mail of Alexander Fritzsche of 24 February 2012, entitled "AW: M.6286 - PHASE II: 8th Request for Information to Südzucker [GL-AM.FID10620522]", at 22:45.

⁶³² COMP/M.2029 – *Tate & Lyle/Amylum*, paragraph 13.

⁶³³ COMP/M.2029 – *Tate & Lyle/Amylum*, paragraph 14.

e.g. by-products of the production of oil, bioethanol (DDGS), starch, fish meal, soy flour and corn gluten) and compound feed, which is to be distinguished from other ingredients such as minerals, vitamins or grain⁶³⁴.

6.4.3.1. Feedstuff

(726) Südzucker markets an animal feedstuff called ProtiGrain ([...]* tonnes sold in 2010) which is a by-product of bioethanol production. ProtiGrain consists of CMS (also called vinasses) and the remainder of the grain used in the fermentation process. EDFM does not sell animal feedstuffs in the EEA which would use molasses as an input other than pure molasses or blends of molasses and vinasses⁶³⁵.

6.4.3.2. DDGS

(727) EDFM does not sell DDGS in the EEA while Südzucker's market share is negligible⁶³⁶.

6.4.3.3. Vinasses/CMS

(728) CMS is a by-product of all fermentation processes where molasses or green syrup is used.

(729) Both Südzucker and EDFM sell CMS or vinasses in small quantities. In 2009/2010 the Südzucker sold [...]* tonnes of vinasses ([...]* tonnes to beet farmers, [...]* tonnes to processors) achieving a turnover of EUR [...]* million. These sales took place in France⁶³⁷.

(730) EDFM sold approx. [...]* tonnes in 2009/2010 in the Union but not in France. Südzucker estimates that vinasses/CMS consumption in the EEA amounts to more than 850,000 tonnes annually⁶³⁸.

(731) The Parties therefore account for well less than 15% of the CMS sales in the EEA.

(732) If the market were to be considered as national, no overlap would occur.

(733) The proposed transaction therefore does not lead to horizontally and vertically affected markets in the segment of feedstuff, DDGS and vinasses/CMS. Therefore, no competition concerns arise from the proposed transaction as regards bioethanol.

⁶³⁴ COMP/M.4042 – *Toepfer/Invivo/Soulès*, paragraphs 14 et seq.

⁶³⁵ Page 71 of the Form CO.

⁶³⁶ Page 71 of the Form CO.

⁶³⁷ Pages 71-72, Form CO and E-mail of Alexander Fritzsche of 24 February 2012, entitled "AW: M.6286 - PHASE II: 8th Request for Information to Südzucker [GL-AM.FID10620522]", at 22:45.

⁶³⁸ Pages 71-72, Form CO and E-mail of Alexander Fritzsche of 24 February 2012, entitled "AW: M.6286 - PHASE II: 8th Request for Information to Südzucker [GL-AM.FID10620522]", at 22:45.

7. ASSESSMENT OF THE REMEDIES

7.1. First remedy package

7.1.1. *The remedies proposed by the Parties on 24 January 2012*

(734) On 24 January 2012 the Parties submitted a first remedy package with commitments to address the competition concerns in the market for the supply of white sugar to industrial processors in Italy ("the First Remedy Package"). The proposed commitments consisted of:

- (a) the divestment of all the shares currently held by EDFM in the Brindisi refinery, SRB, (the "Divestment Shareholding"); and
- (b) the transfer of the three existing contracts for the supply of raw cane sugar to Brindisi⁶³⁹, namely [Supplier A]* Contract, the [Supplier B]* Contract and the [Supplier C]* Contract (together the "Raw Cane Contracts").

(735) The Parties committed that if EDFM were unable to transfer the Raw Cane Contracts as such, EDFM would supply or procure to supply Brindisi with volumes of raw cane sugar [at market prices]*, equivalent to those volumes that are projected to be supplied to Brindisi [...]*.

(736) The Parties also specified certain purchaser requirements, including the capability to source sufficient volumes [at market rates]*.

(737) In order to avoid dependency of SFIR on EDFM via the supply of raw cane sugar to DAI, the Parties also committed that EDFM would use its best efforts to supply, or procure to supply, DAI with volumes of raw cane sugar, [at market rates]*, equivalent to those volumes that EDFM supplied to DAI during the relevant reference period.

7.1.2. *Market test of the First Remedy Package*

(738) The Commission launched a market test on 25 January 2012⁶⁴⁰ to gather the opinion of competitors, customers, raw cane sugar suppliers and SFIR on the proposed remedies.

7.1.2.1. *The response of competitors, customers and raw cane sugar suppliers*

(739) The majority of the respondents found⁶⁴¹ that the proposed commitments with regard to the Divestment Shareholding could, in principle, be appropriate to address the competition concerns in the market for the supply of white sugar to industrial processors in Italy.

⁶³⁹ [Supplier A]* contract ([...]* tonnes/year), [Supplier B]* contract ([...]* tonnes/year) and [Supplier C]* contract ([...]* tonnes/year).

⁶⁴⁰ M.6286 – Südzucker / ED & F Man - questionnaires to customers and competitors market test remedies of 25 January 2012.

⁶⁴¹ M.6286 – Südzucker / ED & F Man - questionnaires to customers and competitors market test remedies of 25 January 2012.

- (740) While respondents could not be provided with the precise terms and conditions of the Raw Cane Contracts, which are confidential, nevertheless some respondents stressed that the price, quantities and duration are key elements of such supply contracts and that, in order to maintain the viability of the divested business, these key features should not be deteriorated as a result of the transfer.
- (741) For example, a raw cane sugar supplier, [...]*, indicated that *"the key element [for the viability of the divested business]* is the transfer of raw sugar supply contracts"*. This statement was confirmed by [sugar trader]*. Raw cane sugar supplier [...]* also pointed out that *"[t]he value of these contracts, and the new enterprise's ability to be competitive/viable will depend on the transfer value/tonnage/timing of these contracts"*. According to [large sugar producer]*, *"[t]he key challenge that the divested business will face in competing effectively will be in securing enough raw material at a competitive price to operate the plant sustainably and thus be able to compete effectively on the Italian white sugar market"*⁶⁴².
- (742) Some respondents also stated that the remedy package must address the issue of SFIR's dependency on EDFM via the supply of raw cane sugar to the DAI refinery in Portugal.

7.1.2.2. The response of SFIR

- (743) During the market test, SFIR expressed the following concerns on the proposed commitments: [Description of SFIR's concerns]*
- (744) [Description of SFIR's concerns]*.

7.1.3. Assessment of the First Remedy Package in the Statement of Objections

- (745) On 14 February 2012, a Statement of Objections was adopted, where the preliminary view was expressed that the proposed transaction would significantly impede effective competition in the market for the supply of white sugar to industrial processors in Italy.
- (746) The Commission considered that the First Remedy Package could not address these competition concerns, because it could not ensure with sufficient certainty that the Brindisi refinery would remain a viable and competitive force in the Italian market for the supply of white sugar to industrial processors.

7.1.3.1. The Raw Cane Contracts are a key element for the continued viability and competitiveness of the Brindisi refinery

- (747) It is true that the Divestment Shareholding was capable of contributing to address the competition concerns by ensuring in a durable way that the Parties would not be able to influence the operation of the Brindisi refinery and its sales policy in Italy post-merger.

⁶⁴² M.6286 – Südzucker / ED & F Man – questionnaire to competitors market test remedies of 25 January 2012.

(748) However, the effective transfer of the Raw Cane Contracts was also a key element for the continued viability and competitiveness of the Brindisi refinery. Given (i) the significant scarcity of preferential raw cane sugar as an essential input in the Union, [...]*, the First Remedy Package failed to ensure that the Brindisi refinery would continue to constitute a viable and competitive force on its competitors in Italy, and in particular on Südzucker.

(749) The price formula of the Raw Cane Contracts is [Description of the Raw Cane Contracts]*. [Description of the Raw Cane Contracts]* prices for preferential raw cane sugar. Indeed, prices under the Raw Cane Contracts and current market prices differ significantly. By way of example, in campaign year 2011/2012 the Brindisi refinery paid EUR [...]* per tonne of raw cane sugar from the [Supplier A]* Contract⁶⁴³, while for smaller quantities of preferential raw cane sugar going beyond the Raw Cane Contracts (around [...]* tonnes) SRB had to pay current market prices of approximately EUR [...]* per tonne⁶⁴⁴.

7.1.3.2. The First Remedy Package could not ensure the transfer of the economic benefit of the Raw Cane Contracts

(750) [Description of the Raw Cane Contracts]*, the First Remedy Package did not secure at a sufficient level the transfer of the economic benefit of the Raw Cane Contracts.

(751) Since market prices for preferential raw cane sugar are currently much higher than the prices obtained under the Raw Cane Contracts, [Description of the Raw Cane Contracts]*.

(752) The [Supplier B]* and [Supplier C]* Contracts contain [Description of the Raw Cane Contracts]*.

(753) [Description of the Raw Cane Contracts]*.

7.1.3.3. The proposed alternative commitment did not ensure the competitiveness and viability of the Brindisi refinery

(754) As an alternative commitment, the Parties proposed that, should the transfer of the Raw Cane Contracts fail, EDFM would supply the Brindisi refinery with volumes of raw cane sugar equivalent to those projected to be supplied from the [Supplier A]* Contract as well as the [Supplier B]* and [Supplier C]* Contracts, [at market prices]*.

(755) This alternative commitment would secure only the *volume* of preferential raw cane sugar provided under the Raw Cane Contracts. However, it did not provide any guarantee as to the [Raw Cane Contracts prices]*.

(756) [Description of the Raw Cane Contracts]*.

⁶⁴³ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

⁶⁴⁴ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

(757) Therefore, the alternative commitment to supply raw cane sugar to the Brindisi refinery [at market prices]* would not create a viable competitor once implemented.

7.1.3.4. Additional concerns from the existing structural and commercial links between EDFM and SFIR

(758) In the Statement of Objections the following concerns were also noted: (i) the uncertainties of the implementation of the divestiture could increase by virtue of rights that SFIR might exercise under the JV Agreement, such as [Description of SRB]*⁶⁴⁵; (ii) the ability of the Brindisi refinery to act as an independent competitive force in Italy should not be hampered by the dependency of SFIR upon EDFM via the DAI refinery; and (iii) during the divestiture period EDFM should not pose practical impediments to the operation of the Brindisi refinery.

7.2. Second Remedy Package

(759) In order to address the competition concerns expressed in the Statement of Objections, the Parties submitted significantly improved commitments on 16 March 2012 (the "Second Remedy Package"). The proposed commitments now consist in:

- (a) the divestment of all the shares currently held by EDFM in the Brindisi refinery, SRB, (the "Divestment Shareholding");
- (b) the transfer to an eventual purchaser of the *economic benefit* of the three existing contracts for the supply of raw cane sugar to Brindisi⁶⁴⁶, namely the [Supplier A]* Contract, the [Supplier B]* Contract and the [Supplier C]* Contract (together "the Raw Cane Contracts");
- (c) the alternative commitment that, if EDFM is unable to transfer the economic benefit of the [Supplier A]* Contract, EDFM will supply or procure to supply Brindisi with volumes of preferential raw cane sugar [on the basis of certain guarantees that EDFM undertakes regarding the Supplier A Contract]*; and
- (d) with respect to the [Supplier B]* Contract and the [Supplier C]* Contract, to the extent that EDFM is unable to transfer the economic benefit of these two contracts, EDFM will supply or procure to supply Brindisi with the respective volumes of preferential raw cane sugar [on the basis of certain guarantees that EDFM undertakes regarding the Supplier B and Supplier C Contracts]*. [...]*

(760) The Parties have also specified certain purchaser requirements, including the proven expertise and incentive to maintain and develop Brindisi as a viable and active competitive force in competition with the Parties and other competitors, and in particular the capabilities to source sufficient volumes of preferential raw cane sugar to enable Brindisi to operate at full capacity.

(761) In order to avoid dependency of SFIR on EDFM via the supply of raw cane sugar to DAI, the Parties have also committed that EDFM would use its best efforts to supply,

⁶⁴⁵ [...]*.

⁶⁴⁶ [Supplier A]* contract ([...]*tonnes/year), [Supplier B]* contract ([...]*tonnes/year) and [Supplier C]* contract ([...]*tonnes/year).

or procure to supply, DAI with volumes of preferential raw cane sugar [at market prices]*, equivalent to those volumes that EDFM supplied to DAI during the relevant reference period.

- (762) A final set of the proposed commitments with certain clarifications and the addition of a fast-track arbitration clause was submitted on 30 March 2012.

7.3. SFIR's response on the currently proposed commitments

- (763) The improvements of the Second Remedy Package as compared to the First Remedy Package concerned the conditions, mechanisms and guarantees for the transfer of the economic benefit of the Raw Cane Contracts. They include elements pointing towards the detailed operation and cost of input of the Brindisi refinery. Such business secrets were already confidential towards all market players that were not partners in the Brindisi Joint Venture during the market test of the First Remedy Package. Therefore, the improvements of these elements in the Second Remedy Package could not be subject to a meaningful market test with suppliers other than SFIR. Consequently, only SFIR's opinion was sought on the improvements of the Second Remedy Package through a questionnaire sent on 20 March 2012.

- (764) SFIR expressed the following concerns with respect to the Second Remedy Package: [Description of SFIR's concerns]*

7.4. Assessment of the currently proposed commitments

7.4.1. Introduction

- (765) According to the Commission Notice on Remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the "Notice on Remedies")⁶⁴⁷, the Commission only has the power to accept commitments that are deemed capable of rendering the concentration compatible with the internal market so that they will prevent significant impediment of effective competition⁶⁴⁸. According to the Merger Regulation and established case law of the Court of Justice of the European Union, commitments have to eliminate competition concerns entirely⁶⁴⁹ and have to be comprehensive and effective from all points of view⁶⁵⁰. Indeed, the Court of Justice's judgment in *Cementbouw* stated that "*in order to be accepted by the Commission [...] the parties' commitments must not only be proportionate to the competition problem identified by the Commission in its decision but must eliminate it entirely*"⁶⁵¹.
- (766) In assessing whether or not the remedy will restore effective competition, the Commission considers the type, scale and scope of the remedies by reference to the structure and the particular characteristics of the market in which these serious doubts arise. The most effective way to maintain effective competition is to create the conditions for the emergence of a new competitive entity or for the strengthening

⁶⁴⁷ OJ C267, 22 October 2008, p.1.

⁶⁴⁸ Notice on Remedies, paragraph 9.

⁶⁴⁹ Recital 30 of the Merger Regulation.

⁶⁵⁰ See, for example, the case-law cited in the Notice on Remedies, notably paragraphs 10 to 12.

⁶⁵¹ Judgment of the Court of Justice in case C-202/06P, *Cementbouw Handel & Industrie BV v Commission of the European Communities*, paragraph 307.

of existing competitors via divestiture by the merging Parties. The divested activities must consist of a viable business, which if operated by a suitable purchaser, can compete effectively with the merged entity on a lasting basis and that is divested as a going concern⁶⁵².

- (767) The divested business has to be viable as such. Therefore, the resources of a possible purchaser or even a presumed future purchaser are not taken into account by the Commission at the stage of assessing the remedy⁶⁵³.
- (768) In certain cases *"the implementation of the parties preferred divestiture option (of a viable business solving the competition concerns) might be uncertain, in view for example of third parties' pre-emption rights or uncertainty as to the transferability of key contracts or [...] the uncertainty of finding a suitable purchaser"*⁶⁵⁴. In such circumstances the Commission cannot take the risk that, in the end, effective competition will not be maintained⁶⁵⁵.
- (769) The Commission will only accept such divestiture commitments if two conditions are fulfilled: (a) absent the uncertainty, the first divestiture proposed in the commitments would consist of a viable business, and (b) the merging parties will have to propose an alternative divestiture which the merging parties will be obliged to implement if they are not able to implement the first commitment within the given time frame for the first divestiture⁶⁵⁶. Therefore, the merging parties have to propose an alternative divestiture which they will be obliged to implement if they cannot implement the first commitment. According to the Commission's remedy policy such an alternative remedy (i) must create a viable competitor once implemented, (ii) should not involve any uncertainties as to its implementation, and (iii) should be capable of being implemented quickly⁶⁵⁷.
- (770) The Notice on Remedies makes also clear⁶⁵⁸ that, in case there is uncertainty as to the implementation of the divestiture due to third party rights or as to finding a suitable purchaser, both (i) an alternative commitment⁶⁵⁹ or (ii) an upfront buyer solution⁶⁶⁰ are in principle capable of addressing the concern in question and that therefore the merging parties may choose between both structures.
- (771) In this case, in order to address the uncertainty regarding the transfer of the economic benefit of the Raw Cane Contracts, the Parties have chosen an alternative commitment⁶⁶¹ solution, namely (i) the [certain guarantees provided by EDFM regarding the Supplier A Contract]* for the supply of preferential raw cane sugar to

⁶⁵² Notice on Remedies, paragraph 23.

⁶⁵³ Notice on Remedies, paragraph 30.

⁶⁵⁴ Notice on Remedies, paragraph 44.

⁶⁵⁵ Notice on Remedies paragraph 45.

⁶⁵⁶ Notice on Remedies, paragraph 45.

⁶⁵⁷ Notice on Remedies, paragraph 45.

⁶⁵⁸ Notice on Remedies paragraph 46.

⁶⁵⁹ Notice on Remedies, paragraph 45. Such an alternative commitment normally should be at least as good as the first proposed divestiture in terms of creating a viable competitor once implemented, it should not involve any uncertainties as to its implementation and it should be capable of being implemented quickly in order to avoid that the overall implementation period exceeds what would normally be regarded as acceptable in the conditions of the market in question.

⁶⁶⁰ See on upfront buyer solutions paragraph 53 to 55 of the Notice on Remedies.

⁶⁶¹ Notice on Remedies, paragraph 45.

the Brindisi refinery, and (ii) the [certain guarantees provided by EDFM regarding the Supplier B and Supplier C Contracts]* for the supply of preferential raw cane sugar to the Brindisi refinery.

7.4.2. *Aim and scope of the remedy package*

- (772) In the present case, the aim of the remedy package is to ensure, post-merger, the presence of a viable competitor to Südzucker/EDFM on the market for the supply of white sugar to industrial processors in Italy. In particular, in order to entirely eliminate competition concerns in compliance with paragraph 23 of the Notice on Remedies, the remedy package must ensure that the Brindisi refinery continues to be on a lasting basis a strong competitive constraint on the suppliers of white sugar in Italy, especially on Südzucker which imports in Italy beet sugar from its factories in Germany, France and Belgium.
- (773) The first element of the divestiture, i.e. the divestment of all the [...] shares in Brindisi currently held by EDFM and corresponding to [...] of the outstanding shares of Brindisi (the Divestment Shareholding), is capable of contributing to address the competition concerns. The divestiture of the shareholding ensures in durable way that the Parties will not be able to influence the operation of the Brindisi refinery and its sales policy in Italy post-merger.
- (774) The second element of the divestiture, i.e. the effective transfer of the economic benefit of the Raw Cane Contracts, is also a key element for the continued viability and competitiveness of the Brindisi refinery. The Parties undertake the primary obligation to transfer the *economic benefit* of the Raw Cane Contracts to the new purchaser [Descriptions regarding the transfer of the Raw Cane Contracts]*.
- (775) However, uncertainties as to the effective implementation of the Parties' primary obligation cannot be completely excluded, since it involves third parties, namely the suppliers of preferential raw cane sugar under the Raw Cane Contracts.
- (776) Given (i) the significant scarcity of preferential raw cane sugar as an essential input in the Union, and (ii) [Descriptions regarding the transfer of the Raw Cane Contracts]*, the proposed commitments include the alternative commitment of the [certain guarantees provided by EDFM regarding the Supplier A, Supplier B and Supplier C Contracts]* for the supply of preferential raw cane sugar to the Brindisi refinery. This alternative commitment does not involve any uncertainties as to its implementation, creates a viable competitor once implemented and can be implemented quickly.
- (777) Under the proposed commitments, [certain guarantees provided by EDFM regarding the Supplier A Contract]* ([...] of Brindisi's contracted input) and [certain guarantees provided by EDFM regarding the Supplier B and Supplier C Contracts]* ([...] of Brindisi's contracted input) are triggered if the transfer of the economic benefit fails, and not solely as a result of the divestiture of EDFM's shareholding. The scope of the "trigger-clause" of the [certain guarantees provided by EDFM regarding the Supplier A Contract, Supplier B and Supplier C]* effectively covers all merger-related possible failures to transfer the economic benefit of the Raw Cane Contracts.

7.4.3. *Brindisi's viability and competitiveness under the primary commitment to transfer the economic benefit of the Raw Cane Contracts*

- (778) Following the exit of Tate & Lyle from Italy all remaining competitors of the Brindisi refinery in Italy are essentially beet sugar producers. Only the newly upgraded facility in Minerbio is capable of refining quantities of raw cane sugar that are comparatively small. This is also confirmed by internal documents of EDFM stating that "[m]ain competition inside the EU can only come from beet sugar producers, as there are no other refiners in or near the Italian market"⁶⁶².
- (779) Based on Südzucker's actual total production costs⁶⁶³ in the campaign year 2010/2011⁶⁶⁴, a beet sugar producer is able to supply white sugar to industrial processors in Italy starting from a total production cost of EUR [...] per tonne. On the basis of Südzucker's forecasted total production costs in the campaign year 2011/2012, a beet sugar producer is able to supply white sugar to industrial processors in Italy starting from a total production cost of EUR [...] per tonne⁶⁶⁵.
- (780) At present, the Brindisi refinery is an efficient cane refinery with production costs that are almost as efficient as those of sugar beet factories. With a refining cost of approximately EUR [...] per tonne⁶⁶⁶, the input price of raw cane sugar for the Brindisi refinery accounts for the greatest part of its production costs. In the campaign year 2011/2012, SRB's average input price was EUR [...] per tonne [Description of the Raw Cane Contracts]*⁶⁶⁷.
- (781) [Description of the Raw Cane Contracts]*⁶⁶⁸ [Description of the Raw Cane Contracts]*.
- (782) According to SFIR⁶⁶⁹, on the basis of these pricing formulas in campaign year 2010/2011 the Brindisi refinery paid EUR [...] per tonne of raw cane sugar from the [Supplier A]* Contract. EDFM has put forward similar figures⁶⁷⁰: in campaign year 2010/2011 the Brindisi refinery paid EUR [...] per tonne of raw cane sugar from the [Supplier A]* Contract. In campaign year 2011/2012, according to SFIR⁶⁷¹, the Brindisi refinery paid EUR [...] per tonne of raw cane sugar from the [Supplier A]*

⁶⁶² Annex 5.b of EDFM's reply to the 2nd RFI in Phase I.

⁶⁶³ Total production costs refer to all input, production and transport costs.

⁶⁶⁴ Annex 23-1 of Südzucker's answer to the 3rd RFI in Phase II.

⁶⁶⁵ Annex Q1-b of Südzucker's reply to the RFI in Phase II, sent by email entitled "AW: M.6286 - PHASE II: Request for Information to Südzucker [GL-AM.FID10620522]" received on 2 March 2012 at 15:24.

⁶⁶⁶ Südzucker's reply to the 4th RFI in Phase I indicated refining costs of EUR [...] per tonne, whereas in its reply to the Statement of Objections (at footnote 146) Südzucker stated that EDFM's most recent estimates for 2011/2012 indicate refining costs of EUR [...] per tonne. The Brindisi refinery also has unit fixed costs of EUR [...] per tonne (Südzucker's reply to the Statement of Objections, para. 312) allocated over a yearly quantity of [...] tonnes, and thus expected to be reduced when the produced quantity increases.

⁶⁶⁷ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

⁶⁶⁸ OJ L 58, 28.2.2006, p. 1.

⁶⁶⁹ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

⁶⁷⁰ Reply by EDFM dated 9 February 2012 and entitled "M.6286 - PHASE II - URGENT REQUEST" received at 11:27.

⁶⁷¹ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

Contract, while EDFM puts forward that in campaign year 2011/2012 the Brindisi refinery paid EUR [...] per tonne of raw cane sugar from the [Supplier A] Contract⁶⁷².

- (783) By contrast, in campaign year 2011/2012, for smaller quantities of preferential raw cane sugar for the Brindisi refinery going beyond the Raw Cane Contracts (around [...] tonnes), SFIR puts forward that SRB had to pay current market prices of approximately EUR [...] per tonne⁶⁷³. In its reply to the Statement of Objections, Südzucker also estimated an average spot price of EUR [...] per tonne for the purchase of raw cane sugar⁶⁷⁴.
- (784) [Description of the Raw Cane Contracts and SRB]⁶⁷⁵.
- (785) Therefore, although in practice currently the Brindisi refinery [Description of the Raw Cane Contracts and SRB], it constitutes a viable and competitive force on the Italian market for the supply of white sugar to industrial processors. Thus, the Commission considers that the viability and competitiveness of the Brindisi refinery would remain ensured, if it were to benefit from the economic benefit of the [Supplier A] Contract and of the [Supplier B] and [Supplier C] Contracts.
- (786) Consequently, [...], the Parties' primary obligation to transfer the economic benefit of the Raw Cane Contracts ensures the viability and competitiveness of the Brindisi refinery.
- 7.4.4. *Brindisi's viability and competitiveness under the alternative commitment to [provide certain guarantees regarding the Supplier A, Supplier B and Supplier C Contracts]**
- 7.4.4.1. The alternative commitment to [provide certain guarantees regarding the Supplier A, Supplier B and Supplier C Contracts] strikes the right balance between eliminating the competition concerns entirely and the principle of proportionality
- (787) Under the alternative commitment, the Brindisi refinery will benefit with certainty from [certain guarantees provided by EDFM regarding the Supplier A Contract]. The [Supplier A] Contract provides for approximately [...] tonnes of preferential raw cane sugar per year, i.e. [...] of the total volume under the three Raw Cane Contracts. In campaign year 2011/2012 the Brindisi refinery paid EUR [...] per tonne of raw cane sugar from the [Supplier A] Contract⁶⁷⁶.
- (788) In addition, the Brindisi refinery will also benefit with certainty from the [certain guarantees provided by EDFM regarding the Supplier B and Supplier C Contracts], i.e. approximately [...] tonnes of preferential raw cane sugar per year. [...]⁶⁷⁷.

⁶⁷² Reply by EDFM dated 9 February 2012 and entitled "M.6286 - PHASE II - URGENT REQUEST" received at 11:27.

⁶⁷³ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

⁶⁷⁴ Südzucker's reply to the Statement of Objections, para. 310.

⁶⁷⁵ EDFM's submission of 2 February 2012.

⁶⁷⁶ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

⁶⁷⁷ Reply by SFIR dated 8 February 2012 and entitled "M.6286 - Phase II - URGENT REQUEST #2" received at 17:56.

- (789) [Description of the Raw Cane Contracts]*⁶⁷⁸, [Description of the Raw Cane Contracts and SRB]*.
- (790) Therefore, the alternative commitment to [provide certain guarantees regarding the Supplier A, Supplier B and Supplier C Contracts]* ensures with certainty the viability and competitiveness of the Brindisi refinery, should the transfer of the economic benefit of the Raw Cane Contracts not be possible. It follows that a hypothetical requirement that the Parties also [provide certain guarantees regarding the Supplier B and Supplier C Contracts]* would be disproportionate, [...]*.
- 7.4.4.2. A hypothetical alternative commitment to [provide certain guarantees regarding the Supplier A, Supplier B and Supplier C Contracts]* cannot be imposed upon the Parties
- (i) Since no competition concern has been identified in the white sugar markets of Portugal and Spain, the Notice on Remedies does not require that the proposed commitments ensure a viable and competitive DAI refinery
- (791) The proposed commitments are subject to a different test with respect to, on the one hand, their effects on the Brindisi refinery and, on the other, their effects on the DAI refinery.
- (792) With respect to the Brindisi refinery, in the Italian market for the supply of white sugar to industrial processors where competition concerns have been identified, the proposed commitments have to eliminate these competition concerns entirely⁶⁷⁹ and have to be comprehensive and effective from all points of view⁶⁸⁰. Therefore, the proposed commitments must ensure that the Brindisi refinery will be a viable business, which if operated by a suitable purchaser, can compete effectively with the merged entity on a lasting basis⁶⁸¹.
- (793) However, in Portugal, no competition concerns have been identified as a result of the proposed transaction. While Südzucker is present in Portugal, EDFM has no activity at all in Portugal and negligible ([0-5]*%) sales in Spain. While it is true that, EDFM has a [...]* share in the DAI refinery in Portugal, this minority shareholding does not provide EDFM with control over the sales of DAI. Furthermore, there is only one customer of the DAI refinery in relation to sugar to be sold in the EEA: Azucarera Ebro. Since 2006 Azucarera Ebro and DAI have entered into an agreement under which Azucarera Ebro would commercialise 100% of DAI's sugar production to be sold in the EEA with absolute discretion to establish the sale price⁶⁸².
- (794) Therefore, given that competition concerns have been identified only with regard to Italy but not to Portugal, the proposed commitments must at most ensure that no dependency of SFIR upon EDFM via the DAI refinery will jeopardise the competitiveness of the Brindisi refinery.

⁶⁷⁸ Reply by EDFM dated 13 January 2012 entitled "M.6286 - PHASE II: request for document" received at 17:20.

⁶⁷⁹ Recital 30 of the Merger Regulation.

⁶⁸⁰ See, for example, the case-law cited in the Notice on Remedies, notably paragraphs 10 to 12.

⁶⁸¹ Notice on Remedies, paragraph 23.

⁶⁸² Reply by EDFM to the 4th RFI in Phase I.

(795) Therefore, since no competition problem has been identified in Portugal or Spain, it cannot be imposed upon the Parties that the proposed commitments ensure as well the competitiveness of the DAI refinery through [...]*

(ii) The proposed commitments guarantee the *status quo* in Brindisi and even a more competitive situation

(796) [Description of the Raw Cane Contracts and SRB]*. The proposed commitments guarantee the *status quo* in Brindisi and even a more competitive situation, since post-merger the Brindisi refinery will also benefit from (and use) [the certain guarantees provided by EDFM regarding the Supplier B and Supplier C Contracts]*.

(797) SFIR claims that the [Supplier B]* and [Supplier C]* Contracts were originally entered into under the clear intent that the raw cane sugar could and would be supplied to Brindisi as a matter of priority⁶⁸³.

(798) [Description of the Raw Cane Contracts]*.

(799) [Description of the Raw Cane Contracts]*⁶⁸⁴, [Description of the Raw Cane Contracts]*.

(800) [Description of the Raw Cane Contracts]*⁶⁸⁵. [Description of the Raw Cane Contracts]*⁶⁸⁶, [Description of the Raw Cane Contracts]*.

(801) Therefore, the Brindisi refinery [Description of the Raw Cane Contracts and SRB]* the [Supplier B]* and [Supplier C]* Contracts, and thus the proposed commitments guarantee at least the *status quo* in terms of Brindisi's current competitiveness. By contrast, with respect to the DAI refinery, it cannot be required that the proposed commitments maintain its present competitiveness.

(iii) [Description of the Raw Cane Contracts]*

(802) [The]* request that EDFM should [Description of the Raw Cane Contracts]* of the [Supplier B]* and [Supplier C]* Contracts would go beyond the contractual protection of SFIR under the relevant contracts.

(803) Under clause [...] of the [Supplier C]* Contract and clause [...] of the [Supplier B]* Contract, [Description of the Raw Cane Contracts]*.

(804) It follows that it is not the proposed commitments but EDFM's decision to partner with Südzucker in combination with SFIR's insufficient contractual protection that [Description of the Raw Cane Contracts]*.

⁶⁸³ SFIR's reply to Question 4 of the Remedies Questionnaire, received on 23 March 2012.

⁶⁸⁴ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

⁶⁸⁵ This is evidenced by the information provided by SFIR in document with ID 3591, which shows that [...] tonnes were sourced for [...] from [Supplier C] [...] tonnes of these were supplied under the [Supplier C] Contract: [...]. See also the Response of EDFM of 9 February 2012 to the Phase II RFI of 7 February 2012.

⁶⁸⁶ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

(805) The purpose of the proposed commitments is to safeguard competition in the Italian market for the supply of white sugar to industrial processors. Although not being the purpose of the proposed commitments, these proposed commitments do offer to SFIR a more advantageous contractual situation with respect to the Raw Cane Contracts, since [Description of the Raw Cane Contracts]*.

(iv) The Notice on Remedies requires that the proposed commitments ensure that the viability and competitiveness of the Brindisi refinery will not be jeopardised because of SFIR's dependence upon EDFM via the DAI refinery

(806) According to the Notice on Remedies, the proposed divestiture must result in a viable and competitive business and "*a viable business is a business that can operate on a stand-alone-basis, which means independently of the merging parties as regards the supply of input materials or other forms of cooperation other than during a transitory period*"⁶⁸⁷.

(807) In the case at hand, the proposed remedies must safeguard the independence of the Brindisi refinery *inter alia* in relation to the supply of raw cane sugar by EDFM to the DAI refinery, where SFIR has a shareholding of [...]*. In order to avoid any dependency of SFIR upon EDFM via the DAI refinery, the Parties have proposed to commit that EDFM will supply, or procure to supply, DAI until [...]* with volumes of preferential raw cane sugar, [at market prices]*, equivalent to those volumes that EDFM supplied to DAI during the period from [...]* to [...]*. [Description of the Raw Cane Contracts]*.

(808) Therefore, EDFM cannot actively disrupt the operation of the DAI refinery, and thus the independence of the Brindisi refinery *vis-à-vis* the Parties is ensured. By contrast since no competition problem has been identified in Portugal or Spain, it cannot be imposed that the proposed commitments ensure as well the competitiveness of the DAI refinery.

(v) EDFM has incentives to deliver raw cane sugar to the DAI refinery at the lowest possible price

(809) EDFM participates in the profits and losses of the DAI refinery with a significant shareholding of [...]*. [...]*, and (ii) a strong incentive to provide itself [...]* raw cane sugar to the DAI refinery at the best possible terms.

(810) Furthermore, EDFM has an incentive to continue supplying DAI at the best available rates not only because of its [...]*% shareholding in DAI but also because it benefits from certain additional payments for the logistics services it provides in this respect to DAI. SFIR itself has also stated that "*EDFM has no interest in jeopardising its own business*"⁶⁸⁸.

(811) Therefore, EDFM has strong incentives to ensure and provide sufficient volumes of raw cane sugar to the DAI refinery at the lowest possible price, in order to maintain it profitable and operational.

⁶⁸⁷ Notice on Remedies, paragraph 32.

⁶⁸⁸ SFIR's reply to Question 11 of the Remedies Questionnaire, received on 23 March 2012.

(vi) In any event, the risk that the proposed commitments allegedly pose for the profitability of the DAI refinery is overstated [...]*

- (812) [Description regarding the DAI refinery]*⁶⁸⁹.
- (813) [...]* the DAI refinery has for a long time, since it started refining raw cane in 2006 until 2009, operated with raw cane supplied to it at market rates. Indeed, this is how the DAI refinery was conceived: at the moment its refining capacity was created, the [Supplier C]* and [Supplier B]* Contracts had not yet been concluded. The fact that the DAI refinery now benefits from these contracts [Description regarding the DAI refinery]*.
- (814) Furthermore, as stated by shareholder EDFM⁶⁹⁰, [Description regarding the DAI refinery]*.
- (815) [Description regarding the DAI refinery]*⁶⁹¹.
- (816) [Description regarding the DAI refinery]*.
- (817) [Description regarding the DAI refinery]*⁶⁹². [Description regarding the DAI refinery]*⁶⁹³.
- (818) [Description regarding the DAI refinery]*⁶⁹⁴ [Description regarding the DAI refinery]*.
- (819) [Description regarding the DAI refinery]*⁶⁹⁵ [Description regarding the DAI refinery and SRB]*.
- (820) [Description regarding the DAI refinery and SRB]*.

(vii) No quantities from the [Supplier A]* Contract can be diverted to the [...]* refinery

- (821) SFIR has claimed that [...]*, it might need to direct volumes of the [Supplier A]* Contract from the Brindisi refinery to [...]*.
- (822) Nevertheless, such a scenario would be highly unlikely in practice, [...]*.
- (823) Under an at this stage hypothetical scenario according to which SFIR can prove that it fulfils the purchaser requirements, especially the capability to source sufficient volumes of preferential raw cane sugar to enable Brindisi to operate at full capacity, and is accepted as the purchaser of the Divestment Shareholding, this acceptance would also need to be based on the requirement of clause 15(b) of the proposed commitments to "*maintain and develop Brindisi as a viable and active competitive force in competition with the Parties and other competitors*". This requirement would

⁶⁸⁹ SFIR's reply to Question 4 of the Remedies Questionnaire, received on 23 March 2012.

⁶⁹⁰ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

⁶⁹¹ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

⁶⁹² SFIR's reply to Question 4 of the Remedies Questionnaire, received on 23 March 2012.

⁶⁹³ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

⁶⁹⁴ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

⁶⁹⁵ SFIR's reply to Question 4 of the Remedies Questionnaire, received on 23 March 2012.

not be satisfied if SFIR directed quantities of the [Supplier A]* Contract from the Brindisi refinery to [...]*.

(824) [Description of the Raw Cane Contracts]*⁶⁹⁶.

(825) Therefore, it can be excluded that under the proposed commitments SFIR would be able to direct quantities of the [Supplier A]* Contract from the Brindisi refinery to [...]*.

7.4.4.3. The proposed commitments ensure that EDFM cannot pose practical impediments to the Brindisi refinery during the divestiture period

(826) SFIR has claimed that the divestiture period could cause serious disruptions to the operation of the Brindisi refinery. For instance:

(a) EDFM could delay or deny financing facilities that it currently provides to SRB for the raw cane sugar delivered; or

(b) EDFM could disrupt the supply of raw cane sugar or vegetable oil (fuel) to the Brindisi refinery.

(827) In order to address such concerns common to all cases involving divestiture periods, the Commission's model texts on remedies provide for (i) the Parties' obligation to preserve the viability, marketability and competitiveness of the divested business, (ii) hold-separate obligations of the Parties, and (iii) ring-fencing measures. All the abovementioned safeguards have been incorporated in paragraphs 5 to 9 of the proposed commitments.

(828) In the case at hand, given that the risk of disruptions to the divested business during the divestiture period is slightly higher⁶⁹⁷ than in other cases involving divestiture periods, the abovementioned safeguards are sufficient to ensure against the risk of such disruptions. This is even more so, given that there is no element of EDFM's past behaviour towards SFIR or other companies to base such an increased risk of disruption. SFIR, on its part, has also admitted that it has no interest in disrupting the divestiture process⁶⁹⁸.

(829) Therefore, the abovementioned Parties' obligation to preserve the viability, marketability and competitiveness of the divested business, the Parties' hold-separate obligations and the ring-fencing measures effectively ensure that the divestiture period will not cause disruptions to the operation of the Brindisi refinery, e.g. in case EDFM would delay or deny financing facilities that it currently provides to SRB for the raw cane sugar delivered or in case EDFM would disrupt the supply of raw cane sugar or vegetable oil (fuel) to the Brindisi refinery.

⁶⁹⁶ EDFM's comments to SFIR's reply to the Remedies Questionnaire, received on 29 March 2012.

⁶⁹⁷ [...]*.

⁶⁹⁸ SFIR's reply to Question 10 of the Remedies Questionnaire, received on 23 March 2012.

7.4.4.4. A requirement for an upfront buyer solution is not necessary and would be disproportionate

(830) The Notice on Remedies makes clear⁶⁹⁹ that, in case there is uncertainty as to the implementation of the divestiture due to third party rights or as to finding a suitable purchaser, both (i) an alternative commitment⁷⁰⁰ or (ii) an upfront buyer solution⁷⁰¹ are in principle capable of addressing the concern in question and that therefore the merging parties may choose between the two possibilities.

(831) In this case, in order to address the uncertainty regarding the transfer of the economic benefit of the Raw Cane Contracts, the Parties have chosen a satisfactory alternative commitment⁷⁰² solution, namely (i) [certain guarantees provided by EDFM regarding the Supplier A Contract]* for the supply of preferential raw cane sugar to the Brindisi refinery, and (ii) [certain guarantees provided by EDFM regarding the Supplier A Contract]* for the supply of preferential raw cane sugar to the Brindisi refinery.

(832) Indeed, according to paragraph 9 of the Notice on Remedies, "*[u]nder the Merger Regulation, the Commission only has power to accept commitments that are deemed capable of rendering the concentration compatible with the common market so that they will prevent a significant impediment of effective competition. The commitments have to eliminate the competition concerns entirely and have to be comprehensive and effective from all points of view. Furthermore, commitments must be capable of being implemented effectively within a short period of time as the conditions of competition on the market will not be maintained until the commitments have been fulfilled*". In addition, paragraph 53 of the Notice on Remedies states that an upfront buyer solution is only envisageable when no other solution "*will allow the Commission to conclude with the requisite degree of certainty that the business will be effectively divested to a suitable purchaser*".

(833) In the case at hand, the proposed commitments eliminate the competition concerns identified by the Commission, therefore an upfront buyer is not the only effective solution envisageable.

7.4.5. Conclusion

(834) In view of the above, the commitments proposed by the Parties on 30 March 2012 sufficiently address the competition concerns in the market for the supply of white sugar to industrial processors in Italy.

8. CONCLUSION

(835) For the reasons outlined above the proposed transaction, as modified by the commitments proposed by the Parties on 30 March 2012, should be declared compatible with the internal market and with the EEA Agreement pursuant to Article

⁶⁹⁹ Notice on Remedies paragraph 46.

⁷⁰⁰ Notice on Remedies, paragraph 45.

⁷⁰¹ See on upfront buyer solutions paragraphs 53 to 55 of the Notice on Remedies.

⁷⁰² Notice on Remedies, paragraph 45.

8(2) of the Merger Regulation, subject to compliance with the Commitments in the Annex to this Decision.

HAS ADOPTED THIS DECISION:

Article 1

The proposed transaction whereby Südzucker acquires sole control of EDFM within the meaning of Article 3(1)(b) of the Merger Regulation is hereby declared compatible with the internal market and the EEA Agreement.

Article 2

Article 1 is subject to compliance with the conditions set out in Section B including Annexes 1, 2 and 3 (Schedule 1) to the commitments.

Article 3

Südzucker shall comply with the obligations set out in the sections of the commitments not referred to in Article 2 of this Decision.

Article 4

This Decision is addressed to:

Südzucker AG Mannheim/Ochsenfurt
Maximilianstraße 10, D-68165 Mannheim
Germany

Done at Brussels, 16.5.2012

(signed)

For the Commission
Joaquín ALMUNIA
Vice-President

By hand and by fax: 00 32 2 296 4301
European Commission – Merger Task Force
DG Competition
Rue Joseph II 70 Jozef-II straat
B-1000 BRUSSELS

Case M.6286 – Südzucker / ED&F Man

COMMITMENTS TO THE EUROPEAN COMMISSION

Pursuant to Articles 8(2) and 10(2) of Council Regulation (EC) No 139/2004 (the “**Merger Regulation**”), Südzucker AG Mannheim/Ochsenfurt (“**Südzucker**”) and ED&F Man Holding Limited (“**EDFM**”) (together, the “**Parties**”) hereby provide the following Commitments (the “**Commitments**”) in order to enable the European Commission (the “**Commission**”) to declare the acquisition of control within the meaning of Article 3(1)(b) of the EU Merger Regulation of EDFM by Südzucker (the “**Transaction**”) compatible with the common market and the EEA Agreement by its decision pursuant Article 8(2) of the Merger Regulation (the “**Decision**”).

The Commitments shall take effect upon the date of adoption of the Decision.

This text shall be interpreted in the light of the Decision to the extent that the Commitments are attached as conditions and obligations, in the general framework of EU law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004.

Section A. Definitions

For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled by one of the Parties and/or by the ultimate parents of the one of the Parties, whereby the notion of control shall be interpreted pursuant to Article 3 Merger Regulation and in the light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004.

Brindisi: SFIR Raffineria di Brindisi S.p.A., a [CONFIDENTIAL]* joint venture between EDFM and SFIR, with its registered office at Via Benedetto Croce 7, 47521, Cesena, Italy and registered with the Register of Companies of Forli-Cesena under number 03673640409.

Closing: the date on which the Divestment Shareholding is divested by EDFM.

[CONFIDENTIAL]*

Divestiture Trustee: one or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by the Parties and who has received from EDFM the exclusive Trustee Mandate to sell the Divestment Shareholding to a Purchaser at no minimum price.

Divestment Business: the Divestment Shareholding and accompanying supply arrangements as defined in Section B that the Parties commit to divest.

Divestment Shareholding: [CONFIDENTIAL]* shares in Brindisi currently held by EDFM corresponding to [CONFIDENTIAL]* of the outstanding shares of Brindisi.

EDFM: ED&F Man Holding Limited, with its registered office at Cottons Centre, Hays Lane, London SE1 2QE, UK.

Effective Date: the date of adoption of the Decision.

First Divestiture Period: the period of [CONFIDENTIAL]* months from the Effective Date.

[CONFIDENTIAL]*

Hold Separate Manager: the person appointed by the Parties to exercise EDFM's rights in relation to the operation of Brindisi following the Effective Date.

Monitoring Trustee: one or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by the Parties, and who has the duty to monitor the Parties' compliance with the conditions and obligations attached to the Decision.

Parties: refers jointly to EDFM and Südzucker.

Personnel: all personnel currently employed by Brindisi and shared personnel.

Purchaser: the entity approved by the Commission as acquirer of the Divestment Shareholding in accordance with the criteria set out in Section D.

Raw Cane Contracts: [CONFIDENTIAL]*

SFIR: Società Fondiara Industriale Romagnola, SpA.

Südzucker: Südzucker AG Mannheim/Ochsenfurt, with registered office at Theodor-Heuss-Anlage 12 D-68165 Mannheim, Germany.

[CONFIDENTIAL]*

Trustee(s): the Monitoring Trustee and the Divestiture Trustee.

Trustee Divestiture Period: the period of [CONFIDENTIAL]* months from the end of the First Divestiture Period.

[CONFIDENTIAL]*

Section B. The Divestment

Commitment to divest

1. In order to maintain effective competition, the Parties commit that EDFM will divest or procure the divestment of, the Divestment Business by the end of the Trustee Divestiture Period to a Purchaser and on terms of sale approved by the Commission in accordance with the procedure described in paragraph 16. To carry out the divestiture, the Parties commit that EDFM will find a Purchaser and enter into a final binding sale and purchase agreement for the sale of the Divestment Business within the First Divestiture Period. If EDFM has not entered into such an agreement at the end of the First Divestiture Period, EDFM shall grant the Divestiture Trustee an exclusive mandate to sell the Divestment Business in accordance with the procedure described in paragraph 25 in the Trustee Divestiture Period.
2. The Parties shall be deemed to have complied with this commitment if, by the end of the Trustee Divestiture Period, EDFM has entered into a final binding sale and purchase agreement, if the Commission approves the Purchaser and the terms in accordance with the procedure described in

paragraph 16 and if the closing of the sale of the Divestment Business takes place within a period not exceeding 3 months after the approval of the Purchaser and the terms of sale by the Commission.

3. In order to maintain the structural effect of the Commitments, the Parties shall, for a period of [CONFIDENTIAL]* years after the Effective Date, not acquire direct or indirect influence over the whole or part of Brindisi, unless the Commission has previously found that the structure of the market has changed to such an extent that the absence of influence over Brindisi is no longer necessary to render the proposed concentration compatible with the common market.

Structure and definition of the divestment

4. The object of the divestment is the Divestment Shareholding and the transfer of the Raw Cane Contracts. [CONFIDENTIAL]*

Section C. Related Commitments

Preservation of Viability, Marketability and Competitiveness

5. From the Effective Date until Closing, the Parties shall preserve the economic viability, marketability and competitiveness of the Divestment Business, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Business. In particular the Parties undertake:
 - (a) not to carry out any act upon their own authority that might have a significant adverse impact on the value, management or competitiveness of the Divestment Business or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of Brindisi; and
 - (b) to continue to make available resources for the development of Brindisi, alongside SFIR, on the basis and continuation of the existing business and projections.

Hold-separate obligations of Parties

6. The Parties commit, from the Effective Date until Closing, to keep the Divestment Business and EDFM's participation in Brindisi separate from the remainder of their businesses and to ensure that personnel involved in the operation of Brindisi, as well as the Hold Separate Manager, have no involvement in any business retained and vice versa. The Parties shall also ensure that the Personnel do not report to any individual of the Parties.
7. Until Closing, the Parties shall assist the Monitoring Trustee in ensuring that Brindisi is managed separately from the businesses retained by the Parties. The Parties shall appoint a Hold Separate Manager who shall be responsible for EDFM's participation in the management of Brindisi, under the supervision of the Monitoring Trustee. The Hold Separate Manager shall act independently and in the best interest of Brindisi with a view to ensuring its continued economic viability and competitiveness and its independence from the businesses retained by the Parties.
8. To ensure that the Divestment Business is held and managed separately, the Hold Separate Manager shall exercise EDFM's rights as shareholder in Brindisi (except for its rights for dividends that may be due before Closing), with the aim of acting in the best interest of the business, determined on a stand-alone basis, as an independent financial investor, and with a view to fulfilling the Parties' obligations under the Commitments. Furthermore, the Hold Separate Manager shall have the power to exercise all rights relating to Brindisi, including those relating to the appointment and replacement of members of the board who have been appointed on behalf of EDFM.

Ring-fencing

9. The Parties shall implement all necessary measures to ensure that they do not after the Effective Date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to Brindisi, [CONFIDENTIAL]*. In particular, the participation of Brindisi in a central information technology network accessible by the Parties shall be severed to the extent possible, without compromising the viability of Brindisi. EDFM may obtain information relating to Brindisi which is reasonably necessary for the divestiture of the Divestment Business or whose disclosure to the Parties is required by law. In this regard, the Parties shall implement, under the supervision of the Monitoring Trustee, all necessary measures to ensure that information relating to Brindisi which is reasonably necessary for the divestiture of the Divestment Business or whose disclosure to the Parties is required by law is disclosed to only EDFM (and not to Südzucker), and that Südzucker personnel would not have access to such information.

Non-solicitation clause

10. The Parties undertake, subject to customary limitations, not to solicit, and to procure that Affiliated Undertakings do not solicit, the Personnel of Brindisi for a period of two years after Closing.

Due Diligence

11. In order to enable potential purchasers to carry out a reasonable due diligence of the Divestment Business and Brindisi, EDFM shall, subject to customary confidentiality assurances and dependent on the stage of the divestiture process, provide to potential purchasers sufficient information as regards the Divestment Business.

Reporting

12. The Parties shall submit written reports in English on potential purchasers of the Divestment Business and developments in the negotiations with such potential purchasers to the Commission and the Monitoring Trustee no later than 10 days after the end of every month following the Effective Date (or otherwise at the Commission's request).
13. The Parties shall inform the Commission and the Monitoring Trustee on the preparation of the data room documentation and the due diligence procedure and shall submit a copy of an information memorandum to the Commission and the Monitoring Trustee before sending the memorandum out to potential purchasers.

[CONFIDENTIAL]*

14. [CONFIDENTIAL]*

Section D. The Purchaser

15. In order to ensure the maintenance of effective competition, the Purchaser, in order to be approved by the Commission, must:
 - (a) be independent of and unconnected to the Parties (the mere fact that a party has, or has had, a supply arrangement with EDFM would not as such preclude it from being potentially considered as independent of and unconnected to the Parties);

- (b) have the financial capabilities, proven expertise and incentive to maintain and develop Brindisi as a viable and active competitive force in competition with the Parties and other competitors and in particular have the capabilities to source sufficient volumes of preferential raw cane sugar for refining at Brindisi to enable Brindisi to operate at full capacity; and
- (c) neither be likely to create, in the light of the information available to the Commission, *prima facie* competition concerns nor give rise to a risk that the implementation of the Commitments will be delayed, and must, in particular, reasonably be expected to obtain all necessary approvals from the relevant regulatory authorities for the acquisition of the Divestment Business (the before-mentioned criteria for the purchaser hereafter the “*Purchaser Requirements*”).

16. The final binding sale and purchase agreement shall be conditional on the Commission’s approval. When the Parties have reached an agreement with a purchaser, they shall submit a fully documented and reasoned proposal, including a copy of the final agreement(s), to the Commission and the Monitoring Trustee. The Parties must be able to demonstrate to the Commission that the purchaser meets the Purchaser Requirements and that the Divestment Shareholding is being sold in a manner consistent with the Commitments. For the approval, the Commission shall verify that the purchaser fulfils the Purchaser Requirements and that the Divestment Business is being sold in a manner consistent with the Commitments. The Commission may approve the sale of part of the Divestment Business or [CONFIDENTIAL]* or not all the Personnel if this does not affect the viability and competitiveness of Brindisi after the sale, taking into account the proposed purchaser.

Section E. Trustee

I. Appointment Procedure

17. The Parties shall appoint a Monitoring Trustee to carry out the functions specified in the Commitments for a Monitoring Trustee. If the Parties have not entered into a binding sales and purchase agreement one month before the end of the First Divestiture Period or if the Commission has rejected a Purchaser proposed by the Parties at that time or thereafter, the Parties shall appoint a Divestiture Trustee to carry out the functions specified in the Commitments for a Divestiture Trustee. The appointment of the Divestiture Trustee shall take effect upon the commencement of the Trustee Divestiture Period.
18. The Trustee shall be independent of the Parties, possess the necessary qualifications to carry out its mandate, for example as an investment bank or consultant or auditor, and shall neither have nor become exposed to a conflict of interest. The Trustee shall be remunerated by the Parties in a way that does not impede the independent and effective fulfilment of its mandate. In particular, where the remuneration package of a Divestiture Trustee includes a success premium linked to the final sale value of the Divestment Shareholding, the fee shall also be linked to a divestiture within the Trustee Divestiture Period.

Proposal by the Parties

19. No later than one week after the Effective Date, the Parties shall submit a list of one or more persons whom they propose to appoint as the Monitoring Trustee to the Commission for approval. No later than one month before the end of the First Divestiture Period, the Parties shall submit a list of one or more persons whom they propose to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the proposed Trustee fulfils the requirements set out in paragraphs 18 and shall include:
- (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;

- (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks;
- (c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether different trustees are proposed for the two functions.

Approval or rejection by the Commission

20. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations, such approval not being unreasonably withheld. If only one name is approved, the Parties shall appoint or cause to be appointed, the individual or institution concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Parties shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Parties

21. If all the proposed Trustees are rejected, the Parties shall submit the names of at least two more individuals or institutions within one week of being informed of the rejection, in accordance with the requirements and the procedure set out in paragraphs 17 and 20.

Trustee nominated by the Commission

22. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom the Parties shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

23. The Trustee shall assume its specified duties in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or the Parties, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee

24. The Monitoring Trustee shall:
- (i) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision.
 - (ii) oversee the on-going management of EDFM's participation in Brindisi the Divestment Business with a view to ensuring its continued economic viability, marketability and competitiveness, and monitor compliance by the Parties with the conditions and obligations attached to the Decision. To that end the Monitoring Trustee shall:
 - (a) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Business, and the keeping separate of the Divestment Business from the business retained by the Parties, in accordance with paragraphs 5 and 6 of the Commitments;

- (b) supervise the Hold Separate Manager's participation in the management of Brindisi in accordance with paragraph 7 of the Commitments.
- (c) (i) in consultation with the Parties, determine all necessary measures to ensure that the Parties do not after the Effective Date obtain any business secrets, knowhow, commercial information, or any other information of a confidential or proprietary nature relating to Brindisi, in particular strive for the severing of Brindisi's participation in a central information technology network to the extent relevant and possible, and (ii) review the information to be disclosed to the Parties as the disclosure is reasonably necessary to allow the Parties to carry out the divestiture or as the disclosure is required by law;
- (iii) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision;
- (iv) propose to the Parties such measures as the Monitoring Trustee considers necessary to ensure the Parties' compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability and competitiveness of the Divestment Business, the holding separate of the Divestment Business and the non-disclosure of competitively sensitive information;
- (v) review and assess potential purchasers as well as the progress of the divestiture process and verify that, dependent on the stage of the divestiture process, (a) potential purchasers receive sufficient information relating to the Divestment Business and the Personnel in particular by reviewing, if available, the data room documentation, the information memorandum and the due diligence process, and (b) potential purchasers are granted reasonable access to Personnel;
- (vi) provide to the Commission, sending the Parties a non-confidential copy at the same time, a written report within 15 days after the end of every month. The report shall cover the operation and management of the Divestment Business so that the Commission can assess whether the shareholding is held in a manner consistent with the Commitments and the progress of the divestiture process as well as potential purchasers. In addition to these reports, the Monitoring Trustee shall promptly report in writing to the Commission, sending the Parties a non-confidential copy at the same time, if it concludes on reasonable grounds that the Parties are failing to comply with these Commitments;
- (vii) within one week after receipt of the documented proposal referred to in paragraph 16, submit to the Commission a reasoned opinion as to the suitability and independence of the proposed purchaser and the viability of Brindisi after the sale and as to whether the Divestment Business is sold in a manner consistent with the conditions and obligations attached to the Decision, in particular, if relevant, whether the sale of part of the Divestment Business or [CONFIDENTIAL]** or not all the Personnel affects the viability of the Divestment Business after the sale, taking account of the proposed purchaser.

Duties and obligations of the Divestiture Trustee

25. Within the Trustee Divestiture Period, the Divestiture Trustee shall sell at no minimum price the Divestment Business to a purchaser, provided that the Commission has approved both the purchaser and the final binding sale and purchase agreement in accordance with the procedure laid down in paragraph 16. The Divestiture Trustee shall include in the sale and purchase agreement such terms and conditions as it considers appropriate for an expedient sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the sale and purchase agreement such customary representations and warranties and indemnities as are reasonably required to effect the sale. The Divestiture Trustee shall protect the legitimate financial interests of

the Parties, subject to the Parties' unconditional obligation to divest at no minimum price in the Trustee Divestiture Period.

26. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the end of every month with a simultaneous copy to the Monitoring Trustee and a non-confidential copy to the Parties.

III. Duties and obligations of the Parties

27. The Parties shall provide and shall cause their advisors to provide the Trustee with all such cooperation, assistance and information as the Trustee may reasonably require to perform its tasks. The Trustee shall have full and complete access to any of the Parties' books, records, documents, management or other personnel, facilities, sites and technical information in relation to Brindisi as is in the Parties' hands as may be necessary for fulfilling its duties under the Commitments and the Parties shall provide the Trustee upon request with copies of any document. The Parties shall make available to the Trustee one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of its tasks.
28. The Parties shall provide the Monitoring Trustee with the support that it may reasonably request in respect of the Divestment Business. This shall include all administrative support functions relating to the Divestment Business which are currently carried out at headquarters level. The Parties shall provide and shall cause their advisors to provide the Monitoring Trustee, on request, with the information submitted to potential purchasers, in particular give the Monitoring Trustee access to the data room documentation and other information granted to potential purchasers in the due diligence procedure. The Parties shall inform the Monitoring Trustee on possible purchasers, submit a list of potential purchasers, and keep the Monitoring Trustee informed of developments in the divestiture process.
29. The Parties shall grant or procure Affiliated Undertakings to grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee to effect the sale, the Closing and all actions and declarations which the Divestiture Trustee considers necessary or appropriate to achieve the sale and the Closing, including the appointment of advisors to assist with the sale process. Upon request of the Divestiture Trustee, the Parties shall cause the documents required for effecting the sale and the Closing to be duly executed.
30. The Parties shall indemnify the Trustee and its employees and agents (each an "***Indemnified Party***") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to the Parties for any liabilities arising out of the performance of the Trustee's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee, its employees, agents or advisors.
31. At the expense of the Parties, the Divestiture Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to the Parties' approval (this approval not to be unreasonably withheld or delayed) if the Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate, provided that any fees and other expenses incurred by the Trustee are reasonable. Should the Parties refuse to approve the advisors proposed by the Trustee the Commission may approve the appointment of such advisors instead, after having heard the Parties. Only the Trustee shall be entitled to issue instructions to the advisors. Paragraph 30 shall apply mutates mutandis. In the Trustee Divestiture Period, the Divestiture Trustee may use advisors who served the Parties during

the Divestiture Period if the Divestiture Trustee considers this in the best interest of an expedient sale.

IV. Replacement, discharge and reappointment of the Trustee

32. If the Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a conflict of interest:
 - (a) the Commission may, after hearing the Trustee, require the Parties to replace the Trustee; or
 - (b) the Parties, with the prior approval of the Commission, may replace the Trustee.
33. If the Trustee is removed according to paragraph 32, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in paragraphs 17-22.
34. Beside the removal according to paragraph 32, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section F. The Review Clause

35. The Commission may, where appropriate, in response to a request from the Parties showing good cause and accompanied by a report from the Monitoring Trustee:
 - (i) grant an extension of the time periods foreseen in the Commitments, or
 - (ii) waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments.
36. Where the Parties seek an extension of a time period, they shall submit a request to the Commission no later than one month before the expiry of that period, showing good cause. Only in exceptional circumstances shall the Parties be entitled to request an extension within the last month of any period.

Section G. Fast Track Dispute Resolution

37. In the event that either the Purchaser or SFIR claims that the Parties or an Affiliated Undertaking is failing to comply with the commitments set out in paragraphs 4 [CONFIDENTIAL]* and/or 14, the fast track dispute resolution procedure as described herein shall apply.
38. If the Purchaser or SFIR wishes to avail itself of the fast track dispute resolution procedure (a "**Requesting Party**"), it shall send a written request to the Parties (the "**Request**") (with a copy to the Monitoring Trustee) setting out in detail the reasons leading the Requesting Party to believe that the Parties are failing to comply with the requirements of paragraphs 4 [CONFIDENTIAL]* and/or 14. The Requesting Party and the Parties will use their best efforts to resolve all differences of opinion and to settle all disputes that may arise through co-operation and consultation within a reasonable period of time not exceeding fifteen 15 working days after receipt of the Request.
39. The Monitoring Trustee shall present its own proposal (the "**Trustee Proposal**") for resolving the dispute within eight 8 working days after receipt of the Request, specifying in writing the action, if

any, to be taken by the Parties or an Affiliated Undertaking in order to ensure compliance with the commitments vis-à-vis the Requesting Party, and be prepared, if requested, to facilitate the settlement of the dispute.

40. Should the Requesting Party and the Parties (together the “*Parties to the Arbitration*”) fail to resolve their differences of opinion in the consultation phase, the Requesting Party shall serve a notice (the “*Notice*”), in the sense of a request for arbitration, to the International Chamber of Commerce (the “*ICC*”), (hereinafter the “*Arbitral Institution*”), with a copy of such Notice and request for arbitration to the Parties.
41. The Notice shall set out in detail the dispute, difference or claim (the “*Dispute*”) and shall contain, *inter alia*, all issues of both fact and law, including any suggestions as to the procedure, and all documents relied upon shall be attached, e.g. documents, agreements, expert reports, and witness statements. The Notice shall also contain a detailed description of the action to be undertaken by the Parties (including, if appropriate, a draft contract comprising all relevant terms and conditions) and the Trustee Proposal, including a comment as to its appropriateness.
42. The Parties shall, within 10 working days from receipt of the Notice, submit their answer (the “*Answer*”), which shall provide detailed reasons for their conduct and set out, *inter alia*, all issues of both fact and law, including any suggestions as to the procedure, and all documents relied upon, e.g. documents, agreements, expert reports, and witness statements. The Answer shall, if appropriate, contain a detailed description of the action which the Parties proposes to undertake vis-à-vis the Requesting Party (including, if appropriate, a draft contract comprising all relevant terms and conditions) and the Trustee Proposal (if not already submitted), including a comment as to its appropriateness.

Appointment of the Arbitrators

43. The Arbitral Tribunal shall consist of three persons. The Requesting Party shall nominate its arbitrator in the Notice; the Parties shall nominate their arbitrator in the Answer. The arbitrator nominated by the Requesting Party and by the Parties shall, within five working days of the nomination of the latter, nominate the chairman, making such nomination known to the Parties to the Arbitration and the Arbitral Institution which shall forthwith confirm the appointment of all three arbitrators.
44. Should the Relevant Party or Parties fail to nominate an arbitrator, or if the two arbitrators fail to agree on the chairman, the default appointment(s) shall be made by the Arbitral Institution.
45. The three-person arbitral tribunal are herein referred to as the “*Arbitral Tribunal*”.

Arbitration Procedure

46. The Dispute shall be finally resolved by arbitration under the rules of the Arbitral Institution, with such modifications or adaptations as foreseen herein or necessary under the circumstances (the “*Rules*”). The arbitration shall be conducted in Paris, France, in the English language.
47. The procedure shall be a fast-track procedure. For this purpose, the Arbitral Tribunal shall shorten all applicable procedural time-limits under the Rules as far as admissible and appropriate in the circumstances. The Parties to the Arbitration shall consent to the use of e-mail for the exchange of documents.
48. The Arbitral Tribunal shall, as soon as practical after the confirmation of the Arbitral Tribunal, hold an organisational conference to discuss any procedural issues with the Parties to the Arbitration. Terms of Reference shall be drawn up and signed by the Parties to the Arbitration and the Arbitration Tribunal at the organisational meeting or thereafter and a procedural time-table

shall be established by the Arbitral Tribunal. An oral hearing shall, as a rule, be established within two months of the confirmation of the Arbitral Tribunal.

49. In order to enable the Arbitral Tribunal to reach a decision, it shall be entitled to request any relevant information from the Parties to the Arbitration, to appoint experts and to examine them at the hearing, and to establish the facts by all appropriate means. The Arbitral Tribunal is also entitled to ask for assistance by the Monitoring Trustee in all stages of the procedure if the Parties to the Arbitration agree.
50. The Arbitral Tribunal shall not disclose confidential information and apply the standards attributable to confidential information under the Merger Regulation. The Arbitral Tribunal may take the measures necessary for protecting confidential information in particular by restricting access to confidential information to the Arbitral Tribunal, the Monitoring Trustee, and outside counsel and experts of the opposing party.
51. The burden of proof in any dispute under these Rules shall be borne as follows: (i) the Requesting Party must produce evidence of a prima facie case and (ii) if the Requesting Party produces evidence of a prima facie case, the Arbitral Tribunal must find in favour of the Requesting Party unless the Parties can produce evidence to the contrary.

Involvement of the Commission

52. The Commission shall be allowed and enabled to participate in all stages of the procedure by:
 - (a) Receiving all written submissions (including documents and reports, etc.) made by the Parties to the Arbitration;
 - (b) Receiving all orders, interim and final awards and other documents exchanged by the Arbitral Tribunal with the Parties to the Arbitration (including Terms of Reference and procedural time-table);
 - (c) Giving the Commission the opportunity to file amicus curiae briefs; and
 - (d) Being present at the hearing(s) and being allowed to ask questions to parties, witnesses and experts.
53. The Arbitral Tribunal shall forward, or shall order the Parties to the Arbitration to forward, the documents mentioned to the Commission without delay.
54. In the event of disagreement between the Parties to the Arbitration regarding the interpretation of the Commitments, the Arbitral Tribunal may seek the Commission's interpretation of the Commitments before finding in favour of any Party to the Arbitration and shall be bound by the interpretation.

Decisions of the Arbitral Tribunal

55. The Arbitral Tribunal shall decide the dispute on the basis of the Commitments and the Decision. Issues not covered by the Commitments and the Decision shall be decided (in the order as stated) by reference to the Merger Regulation, EU law and the laws applicable to the Raw Cane Contracts without reference to the respective rules of conflicts of laws. The Arbitral Tribunal shall take all decisions by majority vote.
56. Upon request of the Requesting Party, the Arbitral Tribunal may make a preliminary ruling on the Dispute. The preliminary ruling shall be rendered within one month after the confirmation of the Arbitral Tribunal, shall be applicable immediately and, as a rule, remain in force until a final decision is rendered.

- 57. The Arbitral Tribunal shall, in the preliminary ruling as well as in the final award, specify the action, if any, to be taken by the Parties or an Affiliated Undertaking in order to comply with the commitments vis-à-vis the Requesting Party (e.g. specify a contract including all relevant terms and conditions). The final award shall be final and binding on the Parties to the Arbitration and shall resolve the Dispute and determine any and all claims, motions or requests submitted to the Arbitral Tribunal. The arbitral award shall also determine the reimbursement of the costs of the successful party and the allocation of the arbitration costs. In case of granting a preliminary ruling or if otherwise appropriate, the Arbitral Tribunal shall specify that terms and conditions determined in the final award apply retroactively.
- 58. The final award shall, as a rule, be rendered within six months after the confirmation of the Arbitral Tribunal. The time-frame shall, in any case, be extended by the time the Commission takes to submit an interpretation of the Commitments if asked by the Arbitral Tribunal.
- 59. The Parties to the Arbitration shall prepare a non-confidential version of the final award, without business secrets. The Commission may publish the non-confidential version of the award.
- 60. Nothing in the arbitration procedure shall affect the power to the Commission to take decisions in relation to the Commitments in accordance with its powers under the Merger Regulation.

.....
duly authorised for and on behalf of
ED&F Man Holding Limited

.....
duly authorised for and on behalf of
Südzucker AG Mannheim/Ochsenfurt

Schedule 1

[CONFIDENTIAL]*

***Case No COMP/M.6944 - THERMO FISHER SCIENTIFIC/
LIFE TECHNOLOGIES***

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) in conjunction with Art 6(2)
Date: 26/11/2013

***In electronic form on the EUR-Lex website under document
number 32013M6944***



EUROPEAN COMMISSION

Brussels, 26.11.2013
C(2013) 8535 final

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE

To the notifying party

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Dear Sir/Madam,

**Subject: Case No COMP/M.6944 – THERMO FISHER SCIENTIFIC/ LIFE TECHNOLOGIES
Commission decision pursuant to Article 6(1)(b) in conjunction with Article 6(2) of Council Regulation No 139/2004¹**

1. On 7 October 2013, the European Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004¹ (the "Merger Regulation") by which the undertaking Thermo Fisher Scientific Inc. ("Thermo Fisher" or "the Notifying Party", USA) intends to acquire within the meaning of Article 3(1)(b) of the Merger Regulation sole control over Life Technologies Corporation ("Life Technologies", USA) by way of purchase of shares ("the Transaction").² Thermo Fisher and Life Technologies are designated hereinafter as the "Parties" or the "Merged Entity".

I. THE PARTIES

2. **Thermo Fisher** is active in the production and supply of analytical instruments and laboratory consumables (e.g. reagents) across almost the entire experimental sciences spectrum including life sciences, chemistry and physics. It also operates a strong multi-brand distribution business for science products, Customer Channel Group ("CCG"). Thermo Fisher was formed in 2006 through the merger of Thermo Electron and Fisher Scientific. It is headquartered in Massachusetts (USA).
3. **Life Technologies** is a global biotechnology company. It is specialised in producing analytical instruments and laboratory consumables for life sciences. It was formed in 2008 through the merger of Invitrogen Corporation and Applied Biosystems, Inc. It is headquartered in California (USA).

II. THE TRANSACTION

4. The Transaction entails the acquisition of sole control by Thermo Fisher over Life Technologies by way of purchase of 100% shares of Life Technologies. The Transaction therefore constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. EU DIMENSION

5. The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5,000 million (Thermo Fisher: EUR 9,731 million; Life Technologies: EUR 2,955 million). The two of them have an EU-wide turnover in excess of EUR 250 million (Thermo Fisher: EUR [...]; Life Technologies: EUR [...]), but they do not

¹ OJ L 24, 29.1.2004, p. 1. With effect from 1 December 2009, the Treaty on the Functioning of the European Union ("TFEU") has introduced certain changes, such as the replacement of "Community" by "Union" and "common market" by "internal market". The terminology of the TFEU will be used throughout this decision.

² Publication in the Official Journal of the European Union No C 296, 12.10.2013, p. 3.

achieve more than two-thirds of their aggregate EU-wide turnover within one and the same Member State.³

6. Therefore, the Transaction has an EU dimension pursuant to Article 1(2) of the Merger Regulation.

IV. RELEVANT MARKETS AND COMPETITIVE ASSESSMENT

IV.A. INTRODUCTION TO THE LIFE SCIENCES INDUSTRY

7. The Transaction concerns the supply of laboratory equipment and consumables for life sciences.⁴
8. The laboratory equipment (or "instruments") bring samples and reagents together and measure the result, e.g. thermal cyclers, qPCR instruments, gel boxes, magnetic bead-based purification instruments, etc.
9. Consumables are the wide range of different products necessary for and consumed in the operation of analytical instruments. They include for example reagents (e.g. enzymes, dyes, antibodies, etc.), chemicals, cell culture sera and media, or plastic products (e.g. pipette, tubes, etc.).
10. The Parties' products, in the areas of cell culture, molecular biology, particles, protein biology, are mainly supplied to (i) research and scientific laboratories in universities, research institutions, government agencies and the private sector such as in pharmaceutical and biotech companies, (ii) bioproduction customers in the pharmaceutical and biotech sectors who use the products as input for their bioproduction processes of e.g. pharmaceutical products, (iii) other original equipment manufacturers ("OEMs"), (iv) customers in the applied science space, e.g. hospitals and clinical diagnostic laboratories for diagnostics products, government agencies for forensic DNA detection products or food safety analytical tools for the food industry.
11. The present decision analyses in detail the competitive effects of the Transaction with respect to (i) media and sera for cell culture, (ii) small interfering RNA ("siRNA") and microRNA ("miRNA") within the gene silencing area, (iii) delivery systems (transfection), (iv) high fidelity polymerase, hot start polymerase, other specialty reagents and reverse transcriptase ("RT") enzymes within the nucleic acid ("NA") amplification area, (v) magnetic beads based instruments and molecular weight standards within the NA purification area, (vi) polymer-based magnetic beads to original OEMs within the particles area, (vii) sequence specific primers ("SSP") within

³ Given that the agreement between the Parties was concluded prior to Croatia's accession to the European Union on 1 July 2013, Croatia is neither considered for the purposes of the assessment of Union Dimension nor for the purposes of the competitive assessment of this Transaction.

⁴ With respect to all product areas, the present Decision refers to market shares of 2012. The market investigation has not pointed to significant fluctuations of the Parties' market shares during previous years. This is without prejudice to analysis in specific sections of the present Decision.

the area of human leukocyte antigen ("HLA") typing, (viii) filter fluorometers and (ix) distribution of laboratory and life science products.⁵

12. With respect to several other product areas, namely (i) short hairpin RNA ("shRNA"), (ii) NA amplification instruments, (iii) Taq polymerase reagents, (iv) NA amplification reagents sold in ready-to-use kits, (v) electrophoresis gel boxes for DNA, (vi) cloning, (vii) sodium dodecyl sulphate polyacrylamide gel electrophoresis ("SDS-PAGE"), (viii) Western blotting, (ix) protein modification and (x) dyes, on the basis of the market investigation, the Commission has concluded that the Transaction does not raise serious doubts as to its compatibility with the internal market. In particular, the Commission has taken into account a number of factors, such as the combined shares of the Parties,⁶ the limited increment post-Transaction under any of the alternative market definitions considered,⁷ the large number of multinational competitors⁸ and the absence of capacity constraints on competitors to expand their output quickly.⁹ In addition, in general, such product areas are fast-moving industries characterised by a high level of innovation. During the last decades, a number of techniques and products have become redundant and new technologies have been developed.¹⁰ Furthermore, on these product areas, no third parties have put forward substantiated claims according to which competition would be significantly impeded, and the Commission's analysis supports this view. With respect to these product areas, therefore, reference is made to the present paragraph regarding the considerations that led the Commission to conclude that the Transaction does not raise serious doubts.¹¹
13. As mentioned above, the large number of multinational competitors in products for life sciences would include companies such as Sigma-Aldrich (active in products for molecular biology, protein biology, cell culture, and market leader in the area of shRNA), BioRad (active in products for molecular biology, protein biology, transplant

⁵ See sections 17, IV.C.2, IV.D.1, IV.D.2, IV.D.3, IV.D.4, IV.E, IV.F, IV.H and IV.I of the present Decision.

⁶ For example, the Parties' combined market shares are generally below 35% under any of the alternative market definitions considered.

⁷ For example, the increment is generally below 1% under any of the alternative market definitions considered.

⁸ For example, in Taq polymerase, the Commission market reconstruction confirmed that at least 13 other players independent from the Parties are active.

⁹ For example, in the areas of SDS Page and dyes all competitors stated that they would be able to increase their output as a result of an increase in demand. See replies to question 48 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013.

¹⁰ For instance, dPCR is a new technology which has been recently introduced and allows for absolute quantification of the PCR product. According to the Notifying Party, this technology is expected to replace existing PCR techniques within the next years. Similar considerations have been taken into account also in past cases where the Commission reviewed transactions in the life sciences sector as elements supporting a clearance decision. See for example Case COMP M.5264 *Invitrogen / Applied Biosystems*, paragraphs 70-73.

¹¹ See also in that regard, Case COMP M.5253 *Sanofi-Aventis / Zentiva*.

diagnostic, and market leader in the area of SDS page and electrophoresis gel boxes), Qiagen (active in products for molecular biology, particles, and market leader in the area of RT-PCR kits), Merck Millipore (active in products for cell culture, particles, etc.), Promega (active in products for molecular biology, protein biology, particles, and market leader in the area of Taq polymerase), GE Healthcare (active in products for protein biology, cell culture, molecular biology, etc.), etc.

IV.B. MARKET INVESTIGATION

14. The Commission has sent a large number of requests for information pursuant to Article 11 of the Merger Regulation addressed to market participants and the Parties, and has received additional submissions from third parties. The Commission has also carried out a market reconstruction exercise for a number of affected markets and has used the reconstructed market shares for the purposes of its assessment in these markets. Finally, the Commission has requested transaction data from the Parties and made use of such data for the purposes of its assessment.
15. In addition, given the worldwide scope of the Parties' activities, the Commission cooperated closely with the competition authorities of several jurisdictions outside the EEA during the pre-notification and phase I stages of this case. This international cooperation involved *inter alia* a mutual exchange of evidence, consisting mainly of internal documents of the Parties, with the Federal Trade Commission ("FTC") in the United States and with the Australian Competition and Consumer Commission ("ACCC").

IV.C. CELL CULTURE

16. Cell culture is the process by which cells are grown under controlled conditions, generally outside of their natural environment. Cell culture is one of the major tools used in cellular and molecular biology, since it provides excellent model systems for studying the normal physiology and biochemistry of cells and the effects of drugs and toxic compounds on the cells. It is also used in the development of biological compounds (e.g. vaccines, therapeutic proteins).
17. Cell culture media and cell culture sera are a range of products which supply nutrients to human, animal, insect and plant cells growing in vitro (i.e. outside the living organisms). Media are water-based liquids and sera are blood-based liquids. Generally, customers blend sera with media to facilitate cell culture.

IV.C.1 Cell culture media

18. In cell culture, media are used to facilitate the growth of cells. Media are water-based liquids that can be provided in liquid or in dry powder format. Dry powder media has to be hydrated with water or with process liquids. Process liquids are water-based buffers and saline solutions which facilitate the cell culture process and ensure that the cell culture environment remains at a constant pH.
19. Thermo Fisher and Life Technologies are both active in the supply of media for cell culture, under the brand names HyClone and Gibco, respectively.

IV.C.1.a Product market definition

20. The Notifying Party submits that media can be divided into two distinct product markets on the basis of whether they are sold to bioproduction customers or customers in the research sector. The Notifying Party also considers that process liquids form a distinct product market from media for cell culture.¹²
21. In previous cases, the Commission has not defined media product markets. Although some decisions referred to media, the Commission did not reach conclusions relating to this sector.¹³
22. In the present case, on the basis of the market investigation, media for cell culture can be divided into different potential product markets in accordance with the following four criteria.
23. First, on the basis of the customer groups to which the product is supplied, media can be divided into (i) a potential product market encompassing media sold to *bioproduction* customers, and (ii) a potential product market encompassing media sold to the *research* sector. There appear to be significant differences between the two customer groups in terms of purchasing patterns, pricing and expected quality.¹⁴
24. Second, media can be divided into (i) a potential product market encompassing media sold in *liquid* form, and (ii) a potential product market encompassing media sold in *dry* form. There appear to be significant differences between those two forms of media in terms of pricing, performance, suitability, purchasing patterns and equipment required for their production.¹⁵ Moreover, the majority of customers would not switch from dry media to liquid media or vice versa in case of price increase or of shortages in availability.¹⁶
25. Third, media can be divided into (i) a potential product market encompassing *standard basal* media, (ii) a potential product market encompassing *custom* media, and (iii) a potential product market encompassing *proprietary* media. In general, customers can buy a standard basal medium (based on publicly available formulations), a custom medium (internally developed medium which is later outsourced for manufacturing) or

¹² Form CO, paragraphs C.6.127 - C.6.157.

¹³ See case COMP/M.5264 *Invitrogen / Applied Biosystems*, paragraph 3.

¹⁴ See replies to question 12 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

¹⁵ See replies to questions 25 and 26 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to question 26 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to question 26 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

¹⁶ See replies to questions 27 and 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 27 and 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

a proprietary medium from a supplier. There appear to be significant differences between those three forms of media in terms of purchasing patterns. Furthermore, especially for the production of several types of custom and proprietary media a high level of know-how, investment and time is required.¹⁷

26. Fourth, media can be divided into (i) a potential product market encompassing *chemically defined* media, and (ii) a potential product market encompassing *non-chemically defined* media. Chemically-defined media are serum free media that do not contain any proteins and are fully defined chemical entities. There appear to be significant differences between those two forms of media, since chemically defined media can eliminate the animal-derived component risk, and thus perform better, are priced higher and are provided by fewer suppliers than non-chemically defined media.¹⁸
27. Finally, according to the market investigation process liquids appear to form a product market distinct from media for cell culture, because the former are mostly commodity products with publicly available formulas and they are used in a wide variety of scientific fields beyond cell culture.¹⁹
28. In view of the above, the Commission considers that media for cell culture is most likely divided into further potential product markets. However, the precise product market definition regarding media for cell culture can be left open, since the commitments proposed by the Parties eliminate serious doubts under any plausible market definition.

IV.C.1.b Geographic market definition

29. The Notifying Party submits that the geographic scope of all media product markets is global or at least EEA-wide mainly due to low transport costs, the absence of regulatory barriers and the global presence of manufacturers.²⁰

¹⁷ See replies to questions 29-32 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 31 and 33 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 31 and 33 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

¹⁸ See replies to question 34 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to question 37 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to question 37 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

¹⁹ See replies to questions 39 and 40 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 40 and 41 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 40 and 41 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

²⁰ Form CO, paragraphs C.6.158 – C.6.166.

30. There are no previous Commission decisions as to the scope of the geographic markets for media products.
31. It appears in the present case, according to the market investigation, that manufacturers process the relevant products at centralised sites, which are subsequently shipped from those sites to regional distribution hubs around the world. Moreover, EEA and non-EEA customers have the same preferences and technical/commercial needs. On the other hand, several respondents claimed that there are significant transport costs, regulatory barriers and taxes for suppliers who do not confine their activity to the EEA.²¹
32. However, the precise definition of the relevant geographic market regarding media for cell culture can be left open, as the commitments proposed by the Parties eliminate the serious doubts identified by the Commission as regards the compatibility of the Transaction with the internal market.

IV.C.1.c Assessment

33. Media is a rapidly growing area of cell culture. The potential for viral contamination associated with animal serum is one of the factors that have led manufacturers to formulate media that minimise or entirely dispense with the need for material sourced from animals. Drugs and vaccines are increasingly serum free. Thermo Fisher estimates that the value of the total media market in the EEA was approximately EUR [...] in 2012, comprising approximately EUR [...] in bioproduction sales and EUR [...] in research sales. Demand for media is growing more rapidly than demand for sera.²²
34. Life Technologies is the strongest player across most of the cell culture media products while Thermo Fisher is a significant competitor across a wide number of them. The Commission's market reconstruction has provided the following market shares in the different plausible markets.
35. The market reconstruction indicates the following market shares for the different potential product markets:

²¹ See replies to questions 42-45 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 44-46 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 44-46 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

²² Form CO, paragraph C.6.3.

A) Bioproduction customers

Table 1– Parties' and competitors' market shares in the supply of media to bioproduction customers in the EEA in 2012

Market shares	EEA							
	TF	LT	TF+LT	Sigma Aldrich	BD	Lonza	Others	MKT - Size € m
Media (all)	[5-10]%	[30-40]%	[40-50]%	[30-40]%	[10-20]%	[5-10]%	[0-5]%	[...]
Media in liquid form	[5-10]%	[40-50]%	[40-50]%	[20-30]%	[0-5]%	[10-20]%	[10-20]%	[...]
Media in dry form	[5-10]%	[30-40]%	[40-50]%	[30-40]%	[20-30]%	[5-10]%	[0-5]%	[...]
Custom Media	[0-5]%	[30-40]%	[30-40]%	[50-60]%	[0-5]%	[0-5]%	[5-10]%	[...]
Proprietary Media	[10-20]%	[40-50]%	[50-60]%	[10-20]%	[30-40]%	[0-5]%	[0-5]%	[...]
Standard Basal Media	[0-5]%	[30-40]%	[30-40]%	[5-10]%	[0-5]%	[50-60]%	[0-5]%	[...]
Chemically defined Media	[10-20]%	[50-60]%	[70-80]%	[0-5]%	[0-5]%	[20-30]%	[0-5]%	[...]
Non-chemically defined media	[0-5]%	[30-40]%	[30-40]%	[30-40]%	[10-20]%	[0-5]%	[0-5]%	[...]
Process liquids	[10-20]%	[10-20]%	[20-30]%	[30-40]%	[0-5]%	[10-20]%	[20-30]%	[...]

Source: Commission's market reconstruction

Table 2 – Parties' and competitors' market shares in the supply of media to bioproduction customers at global level in 2012

Market shares	Global							
Product	TF	LT	TF+LT	Sigma Aldrich	BD	Lonza	Others	MKT - Size € m
Media (all)	[10-20]%	[30-40]%	[50-60]%	[20-30]%	[10-20]%	[0-5]%	[0-5]%	[...]
Media in liquid form	[20-30]%	[40-50]%	[60-70]%	[20-30]%	[0-5]%	[5-10]%	[10-20]%	[...]
Media in dry form	[10-20]%	[30-40]%	[40-50]%	[20-30]%	[10-20]%	[0-5]%	[0-5]%	[...]
Custom Media	[10-20]%	[30-40]%	[40-50]%	[40-50]%	[0-5]%	[0-5]%	[5-10]%	[...]
Proprietary Media	[10-20]%	[40-50]%	[60-70]%	[10-20]%	[20-30]%	[0-5]%	[0-5]%	[...]
Standard Basal Media	[0-5]%	[40-50]%	[40-50]%	[10-20]%	[0-5]%	[30-40]%	[0-5]%	[...]
Chemically defined Media	[20-30]%	[60-70]%	[80-90]%	[0-5]%	[0-5]%	[10-20]%	[0-5]%	[...]
Non-chemically defined media	[10-20]%	[30-40]%	[40-50]%	[30-40]%	[10-20]%	[0-5]%	[0-5]%	[...]
Process liquids	[30-40]%	[10-20]%	[40-50]%	[20-30]%	[0-5]%	[20-30]%	[10-20]%	[...]

Source: Commission's market reconstruction

B) Research customers

Table 3 – Parties' and competitors' market shares in the supply of media to research customers in the EEA in 2012

Market shares	EEA							
	Thermo	Life	Combined	Sigma Aldrich	Merk Millipore	Lonza	Others	MKT - Size € m
Media (all)	[0-5]%	[50-60]%	[50-60]%	[5-10]%	[5-10]%	[20-30]%	[10-20]%	[...]
Media in liquid form	[0-5]%	[50-60]%	[50-60]%	[5-10]%	[5-10]%	[20-30]%	[5-10]%	[...]
Media in dry form	[0-5]%	[20-30]%	[20-30]%	[10-20]%	[0-5]%	[0-5]%	[60-70]%	[...]
Custom Media	[0-5]%	[5-10]%	[5-10]%	[30-40]%	[5-10]%	[40-50]%	[10-20]%	[...]
Proprietary Media	[0-5]%	[30-40]%	[30-40]%	[10-20]%	[0-5]%	[40-50]%	[5-10]%	[...]
Standard Basal Media	[0-5]%	[50-60]%	[50-60]%	[0-5]%	[5-10]%	[30-40]%	[0-5]%	[...]
Chemically defined Media	[0-5]%	[10-20]%	[10-20]%	[0-5]%	[0-5]%	[80-90]%	[0-5]%	[...]
Non-chemically defined media	[0-5]%	[50-60]%	[50-60]%	[10-20]%	[5-10]%	[20-30]%	[5-10]%	[...]
Process liquids	[0-5]%	[50-60]%	[50-60]%	[40-50]%	[0-5]%	[0-5]%	[0-5]%	[...]

Source: Commission's market reconstruction

Table 4– Parties' and competitors' market shares in the supply of media to research customers at global level in 2012

Market shares	Global							
Product	TF	LT	TF+LT	Sigma Aldrich	Merk Millipore	Lonza	Others	MKT - Size € m
Media (all)	[0-5]%	[60-70]%	[60-70]%	[5-10]%	[0-5]%	[10-20]%	[5-10]%	[...]
Media in liquid form	[0-5]%	[60-70]%	[60-70]%	[5-10]%	[0-5]%	[20-30]%	[5-10]%	[...]
Media in dry form	[0-5]%	[40-50]%	[40-50]%	[10-20]%	[0-5]%	[0-5]%	[40-50]%	[...]
Custom Media	[0-5]%	[10-20]%	[10-20]%	[20-30]%	[5-10]%	[10-20]%	[30-40]%	[...]
Proprietary Media	[0-5]%	[40-50]%	[40-50]%	[10-20]%	[0-5]%	[30-40]%	[10-20]%	[...]
Standard Basal Media	[0-5]%	[60-70]%	[60-70]%	[0-5]%	[0-5]%	[20-30]%	[5-10]%	[...]
Chemically defined Media	[0-5]%	[10-20]%	[10-20]%	[0-5]%	[10-20]%	[70-80]%	[0-5]%	[...]
Non-chemically defined media	[0-5]%	[60-70]%	[60-70]%	[5-10]%	[0-5]%	[10-20]%	[10-20]%	[...]
Process liquids	[0-5]%	[50-60]%	[60-70]%	[30-40]%	[0-5]%	[0-5]%	[5-10]%	[...]

Source: Commission's market reconstruction

36. The above reconstruction indicates that, although the Parties have strong positions in almost all potential media markets, the Merged Entity appears to be particularly strong in sales of liquid media, proprietary media and chemically defined media to bioproduction customers in the EEA and worldwide.
37. During the market investigation almost all competitors and several customers expressed concerns regarding the position of the Merged Entity in media cell culture.²³ In their

²³ See replies to questions 86-88 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 77-79 of the

responses to the questionnaires, competitors and customers generally point out that the Merged Entity would be the clear market leader in the supply of media for cell culture.²⁴ The Parties appear to be particularly close competitors to each other, together with Sigma Aldrich and (to a lesser extent) Lonza, in terms of their product portfolio quality, range, customer relationships and price positioning.²⁵

38. In its internal documents, Thermo Fisher describes itself as a [...] and presents Life Technologies as [...].²⁶
39. Competitors and customers do not foresee any new entry in the next three years. There seem to be important barriers to entry since a supplier needs significant time and investment in order to establish the necessary track record and reliability. Reliability appears to be the main consideration for bioproduction customers, while some research customers can be more price-sensitive. The importance of track record and reliability in media cell culture is also illustrated by GE Healthcare's recent decision to massively suspend shipments and to withdraw already shipped media due to traceability concerns.²⁷
40. Moreover, even large bioproduction customers appear unable to produce media themselves due to the required specialised equipment and know-how, as well as the absence of economies of scale.²⁸ Customers are also unable to sponsor the entry of new competitors.²⁹

Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 80-82 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

²⁴ See replies to questions 62 and 63 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 55-56 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 55-56 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

²⁵ See replies to questions 72-74 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 70-72 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 73-75 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

²⁶ See slide [...] in Thermo Fisher's internal presentations provided by the Parties to the FTC; see also slide entitled [...] in Thermo Fisher's internal presentations provided by the Parties to the FTC.

²⁷ See letter by GE Healthcare to its customers dated 31 May 2013 provided by the Parties to the FTC.

²⁸ However, some customers claim that they have the possibility to produce process liquids themselves.

²⁹ See replies to questions 61.2, 70 and 80-83 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013; See replies to questions 61 and 75-76 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013; See replies to questions 61 and

41. In view of the above, the Commission concludes that the Transaction raises serious doubts as to its compatibility with the internal market regarding media for cell culture. However, the commitments proposed by the Parties would effectively eliminate the serious doubts raised under any plausible market definition, as analysed in section V.A.1 of the present Decision.

IV.C.2 Cell culture sera

42. In cell culture, sera are blended with media to facilitate the growth of cells. Sera are blood-based animal by-products which provide nutrients, proteins, growth factors and other components to promote cell growth.
43. A variety of sera can be used for cell culture: foetal bovine serum (FBS)³⁰, calf serum³¹, adult bovine serum³², sera from other species³³ and engineered sera products.³⁴ According to the Notifying Party, FBS is the most widely used sera representing 73% of all sera used for bioproduction customers and 92% of all sera used for research customers in the EEA.
44. Thermo Fisher and Life Technologies are both active in the supply of sera for cell culture, under the brand names HyClone and Gibco, respectively.

IV.C.2.a Product market definition

45. The Notifying Party submits that sera can be divided into two distinct product markets depending on whether they are sold to bioproduction customers or customers in the research sector. Moreover, the Notifying Party submits that each type of sera (i.e. FBS, calf sera, adult bovine, etc.) forms a distinct product market. With particular regards to FBS, the Notifying Party also considers that its geographic origin is of great importance from a demand-side point of view, in particular for bioproduction customers. On that basis, the Notifying Party claims that FBS can be segmented according to its origin, namely (i) Australia and New Zealand origin; (ii) US and Canadian origin; and (iii) South American (EU approved) origin.³⁵

78-79 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

- ³⁰ FBS is obtained from the blood of foetuses of healthy, pre-partum bovine dams that have been fit for human consumption through *ante* and/or *post-mortem* veterinary inspection.
- ³¹ Calf serum is defined as the liquid fraction of clotted blood derived from healthy, slaughtered bovine calves or donor calves, aged from 20 days up to 12 months, deemed fit for human consumption through *ante* and/or *post-mortem* veterinary inspection.
- ³² Adult bovine serum is defined as the liquid fraction of clotted blood derived from healthy, slaughtered cattle or donor herds 12 months of age or older deemed fit for human consumption through *ante* and/or *post-mortem* veterinary inspection.
- ³³ Sera from other species include porcine, equine, goat, chicken, sheep and other animal sera.
- ³⁴ Engineered sera products are considered as low quality serum that has been augmented with a combination of nutrients to improve performance.
- ³⁵ Form CO, paragraphs C.6.26 - C.6.58.

46. In previous cases, the Commission has not defined sera product markets. Although some decisions referred to sera, the Commission did not reach conclusions relating to this area.³⁶
47. In the present case, according to the market investigation, it appears that sera can be divided into different potential product markets on the basis of the following three criteria.
48. First, on the basis of the customer groups to which the product is supplied, sera can be divided into (i) a potential product market encompassing sera sold to *bioproduction* customers, and (ii) a potential product market encompassing sera sold to the *research* sector. The results of the market investigation confirmed in line with the Notifying Party's view that there are significant differences between these two customer groups in terms of purchasing patterns, pricing and expected quality.³⁷
49. Second, sera can be divided on the basis of their animal type, i.e. FBS (the most widely used), calf sera, bovine adult sera and other species. The market investigation in the present case confirmed that sera from different types of animals are distinct products as they fulfil different needs. Moreover, customers indicated that they would not switch from FBS to other types of sera in case of price increase or of shortages in availability.³⁸
50. Third, sera can be divided on the basis of their geographic origin into (i) a potential product market encompassing sera from *Australia*, (ii) a potential product market encompassing sera from *New Zealand*, (iii) a potential product market encompassing sera from *Australia and New Zealand*, (iv) a potential product market encompassing sera from *the US*, (v) a potential product market encompassing sera from *Canada*, (vi) a potential product market encompassing sera from *the US and Canada*, and (vii) a potential product market encompassing sera from *South American countries (EU approved)*. The market investigation in the present case showed that there are significant differences between the geographic origin of sera in terms of quality and that customers have distinct preferences as to specific origins of sera due to differences in the risk of cattle disease, price and availability.³⁹ Moreover, the market investigation

³⁶ See case COMP/M.5264 *Invitrogen / Applied Biosystems*, paragraph 3; see case M.285 *Pasteur Mérieux / Merck*, paragraph 4.

³⁷ See replies to question 12 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

³⁸ See replies to questions 13-16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013. See replies to questions 13-16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 13-16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

³⁹ See replies to questions 13-16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013. See replies to questions 13-16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 13-16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

showed that although the majority of customers considered that Australian origin sera and New Zealand origin sera might be substitutable in terms of quality and performance, most of them also stated that prices of New Zealand sera are higher and they have not switched from one country to another. The same arguments applied for US origin sera and Canadian origin sera.⁴⁰

51. On the basis of the above considerations, it is likely that there are separate product markets for (i) bioproduction customers and research customers; (ii) types of sera from different animals (FBS, calf, bovine, etc.); and (iii) geographic origins. However, the precise product market definition regarding sera for cell culture can be left open, since the commitments proposed by the Parties would eliminate any serious doubts under any plausible market definition.

IV.C.2.b Geographic market definition

52. The Notifying Party submits that the relevant geographic market for sera products is at least EEA-wide in scope mainly due to low transport costs, the absence of regulatory barriers and the global presence of manufacturers.⁴¹
53. There are no previous Commission decisions as to the scope of the geographic markets for sera products.
54. The market investigation in the present case showed that manufacturers process the relevant products at centralised sites, which are subsequently shipped from those sites to regional distribution hubs around the world. Moreover, EEA and non-EEA customers have the same preferences and technical/commercial needs. On the other hand, several respondents claimed that there are significant transport costs, regulatory barriers and taxes for suppliers who do not confine their activity to the EEA.⁴²
55. However, the precise definition of the relevant geographic market regarding sera for cell culture can be left open, as the commitments proposed by the Parties eliminate the serious doubts identified by the Commission as regards the compatibility of the Transaction with the internal market.

⁴⁰ See replies to questions 20 and 21 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 20 and 21 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

⁴¹ Form CO, paragraphs C.6.61 – C.6.70.

⁴² See replies to questions 42-45 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013. See replies to questions 44-46 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 44-46 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

IV.C.2.c Assessment

56. The Notifying Party estimates that the value of the total sera market in the EEA was approximately EUR [...] in 2012, comprising approximately EUR [...] in bioproduction sales and EUR [...] in research sales.⁴³
57. Life Technologies is the strongest player across most of the cell culture sera products with its brand Gibco, while Thermo Fisher is a significant competitor in most of them with its brand HyClone. The Parties' brands are well recognised in the markets for sera as high quality products.
58. The main area of overlap between the Parties' activities is the supply of FBS to the bioproduction sector and to the research sector.⁴⁴ The Transaction would bring together the number one (Life) and number three (Thermo) player in this segment.
59. According to the Notifying Party, the market shares in the different plausible markets for FBS in 2012 are the following.

A) Bioproduction customers

Table 5– Parties' and competitors' market shares in the supply of sera to bioproduction customers in the EEA level in 2012

Market shares	EEA							
	Thermo	Life	Combined	Sigma Aldrich	GE	Merck Millipore	Others	Market Size (EUR m)
Australian and New Zealand FBS	[10-20]%	[30-40]%	[40-50]%	[20-30]%	[5-10]%	[0-5]%	[20-30]%	[...]
Australian FBS	[5-10]%	[20-30]%	[20-30]%	[20-30]%	[10-20]%	[5-10]%	[20-30]%	[...]
New Zealand FBS	[10-20]%	[30-40]%	[50-60]%	[20-30]%	[5-10]%	[0-5]%	[10-20]%	[...]
US and Canadian FBS	[20-30]%	[5-10]%	[30-40]%	[30-40]%	[5-10]%	[5-10]%	[20-30]%	[...]
US FBS	[20-30]%	[5-10]%	[30-40]%	[20-30]%	[10-20]%	[5-10]%	[20-30]%	[...]

Source: Parties' estimates.

⁴³ Form CO, paragraph C.6.2.

⁴⁴ The Parties also overlap in the supply of sera from different type of animals such as adult bovine sera, calf sera, equine sera and porcine sera. As FBS represent the most widely type of sera used (see paragraph 49) and the proposed commitments submitted by the Notifying Party removes the serious doubts in relation to any of possible markets, these types of sera products are not further considered on this Decision.

Table 6– Parties' and competitors' market shares in the supply of sera to bioproduction customers at global level in 2012

Market shares	Global							
Product	Thermo	Life	Combined	Sigma Aldrich	GE	Merck Millipore	Others	Market Size (EUR m)
Australian and New Zealand FBS	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[5-10]%	[0-5]%	[20-30]%	[...]
Australian FBS	[5-10]%	[10-20]%	[20-30]%	[20-30]%	[5-10]%	[5-10]%	[30-40]%	[...]
New Zealand FBS	[10-20]%	[30-40]%	[40-50]%	[20-30]%	[5-10]%	[0-5]%	[20-30]%	[...]
US and Canadian FBS	[10-20]%	[0-5]%	[20-30]%	[20-30]%	[5-10]%	[5-10]%	[40-50]%	[...]
US FBS	[20-30]%	[0-5]%	[20-30]%	[20-30]%	[5-10]%	[5-10]%	[40-50]%	[...]
Canadian FBS	[0-5]%	[0-5]%	[0-5]%	[5-10]%	-	[0-5]%	[90-100]%	[...]
South American (EU approved) FBS	[10-20]%	[0-5]%	[10-20]%	[20-30]%	[5-10]%	[5-10]%	[40-50]%	[...]

Source: Parties' estimates.

B) Research customers⁴⁵

Table 7– Parties' and competitors' market shares in the supply of sera to research customers in the EEA level in 2012

Market shares	EEA							
Product	Thermo	Life	Combined	Sigma Aldrich	GE	Merck Millipore	Others	Market Size (EUR m)
US and Canadian FBS*	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[10-20]%	[5-10]%	[20-30]%	[...]
US FBS	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[10-20]%	[5-10]%	[20-30]%	[...]
South American (EU approved) FBS	[0-5]%	[20-30]%	[20-30]%	[20-30]%	[10-20]%	[5-10]%	[30-40]%	[...]

Source: Parties' estimates. *Regarding sales to research customers, the Parties' activities do overlap in the supply of FBS Canadian in the EEA.

⁴⁵ Regarding sales to research customers, the Parties' activities do overlap neither in the supply of FBS Australian origin nor in the supply of FBS New Zealand origin.

Table 8– Parties' market shares in the supply of sera to research customers at global level in 2012

Market shares	Global			
Product	Thermo	Life	Combined	Market Size
US and Canadian FBS	[10-20]%	[20-30]%	[30-40]%	[...]
US FBS	[10-20]%	[20-30]%	[30-40]%	[...]
Canadian FBS	[10-20]%	[10-20]%	[30-40]%	[...]
South American (EU approved) FBS	[10-20]%	[10-20]%	[20-30]%	[...]

Source: Parties' estimates.

60. The Notifying Party claims that the Transaction would not lead to a significant impediment to effective competition in the supply of FBS. First, there are many alternative suppliers of sera⁴⁶ and the Parties will continue to face competition constraints from at least five of them: Sigma Aldrich, Merck Millipore, GE Healthcare (PAA), Moregate and Atlanta Biologicals. Second, the Parties will not have a strong position in the procurement of raw sera, the crucial input for FBS⁴⁷. Third, entry and expansion into the sale of sera is relatively easy, especially for abattoirs and/or intermediaries of raw sera. Finally, bioproduction customers are strong buyers who use their volume of business and ability to sponsor entry and directly source from abattoirs to constrain sera suppliers.
61. During the market investigation, almost all competitors and several customers raised concerns as regards the impact of the Transaction in sera for cell culture.⁴⁸
62. First, respondents to the market investigation indicated that the Parties would achieve a strong position in the supply of sera, with a dominant position in particular in FBS of New Zealand and Australian origin. In their responses to the questionnaires, the vast majority of competitors and customers have indicated that Life Technologies is at

⁴⁶ In the supply of FBS from New Zealand and Australia, other suppliers mentioned by the Notifying Party are Serana, South Pacific, JR Scientific, etc. In the supply of FBS from US and Canada, other suppliers mentioned by the Notifying Party are Corning, SeraLab, Seradigm, etc.

⁴⁷ Raw sera are the liquid portion left after blood is allowed to clot. It is separated from raw blood through spinning and then frozen for further filtering and processing.

⁴⁸ See replies to questions 86-89 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013. See replies to questions 77-81 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 80-84 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

present the clear market leader in the supply of sera and the Parties appear to be close competitors.⁴⁹

63. The Parties' internal documents confirmed the findings of the market investigation. They showed that the Parties' combined market shares would be in the range of [60-70]% in the supply of FBS of Australian and New Zealand origin with only two competitors considered significant, namely Sigma Aldrich and Moregate.⁵⁰

[...]

64. The Parties' internal documents also showed that Life Technologies is the market leader and Thermo Fisher is its closest competitor.⁵¹
65. Second, the Parties' internal document also showed that the Parties currently have a strong position in the procurement of sera from different origins and that the availability of raw serum, mainly from Australia and New Zealand, is scarce.⁵²
66. Third, competitors and customers do not foresee any new entry in the next three years. There seem to be important barriers to entry since a supplier needs several years and significant investments in order to become established as a recognized supplier of sera. Reliability appears to be the main consideration for bioproduction customers, while some research customers can be more price-sensitive.⁵³
67. Furthermore, it appears that abattoirs are also extremely unlikely to possess the facilities and technical expertise necessary to engage in the sterile filtration of raw sera and the dispensing of the final product, in order to sell processed FBS. Moreover, it appears that customers are unable to be in contact with abattoirs and/or intermediaries for FBS, mainly because of budget constraints, knowledge and technical barriers, staffing requirements, logistical barriers and quality control requirements across batches.⁵⁴

⁴⁹ See replies to questions 63 and 74-76 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013. See replies to questions 56, 71 and 72 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 56, 74 and 75 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

⁵⁰ See slide [...] in Life Technologies' internal presentations provided by the Parties to the FTC; see also slide [...] in Thermo Fisher's internal presentations provided by the Parties to the FTC.

⁵¹ See slide [...] in Life Technologies' internal presentations dated 9/2/2013 provided by the Parties to the FTC; see also slide [...] in Thermo Fisher's internal presentations provided by the Parties to the FTC.

⁵² See Thermo Fisher's presentation [...] dated on April 8, 2013.

⁵³ See replies to questions 83 and 84 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013. See replies to questions 76 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013. See replies to questions 79 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 October 2013.

⁵⁴ Information provided by the Australian Competition and Consumer Commission.

68. Finally, even large bioproduction customers appear unable to sponsor the entry of new competitors.⁵⁵
69. In view of the above, the Commission concludes that the Transaction raises serious doubts as to its compatibility with the internal market regarding sera for cell culture. However, the commitments proposed by the Parties would effectively eliminate the serious doubts raised under any plausible market definition, as analysed in section V.A.1 of the present Decision.

IV.D. MOLECULAR BIOLOGY

70. Molecular biology is the study of the molecular components present in the cells of living organisms, primarily RNA and DNA. The study of molecular biology and, in particular, the function of genes within cells is an important activity for academic and bio-industrial researchers.
71. This section analyses the following product areas within molecular biology: gene silencing, transfection, NA amplification, NA purification and cloning.

IV.D.1 Gene silencing

IV.D.1.a Product market definition

72. Gene silencing (also known as “gene modulation”) is the process by which the expression of a particular gene is inhibited (i.e. the gene is “switched off”). The most common downstream application for gene silencing products is gene function studies (e.g. to study what happens when a gene is switched off).
73. Gene silencing is achieved through a process known as RNAi. RNAi normally requires (i) an effector reagent to silence the gene and (ii) a delivery system to cause the effector to enter the particular cell.⁵⁶
74. Traditionally, there have been two main types of effectors: small interfering RNA (siRNA) and short hairpin RNA (shRNA). In addition, in the last years a third type of effector has been developed: microRNA (miRNA), which can be in turn divided into mimics⁵⁷ and inhibitors.⁵⁸ Effectors can be sold as standalone reagents or as bundle of reagents (libraries).

⁵⁵ See replies to questions 60 of the Commission’s request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 October 2013.

⁵⁶ Product market definition for delivery systems (transfection) is discussed in section IV.D.2 below.

⁵⁷ miRNA mimics are small, double-stranded RNAs that mimic endogenous miRNAs, which may or may not be chemically modified. These enable miRNA functional analysis by upregulation of miRNA activity, which results in the suppression of gene translation.

⁵⁸ miRNA inhibitors are small, chemically modified single-stranded RNA molecules designed to specifically bind to and inhibit endogenous miRNA molecules and enable miRNA functional analysis by down-regulation of miRNA activity. This has the net effect of increasing gene translation.

75. The Commission addressed gene silencing in Case COMP/M.5264 *Invitrogen/Applied Biosystems*. However, the product market definition was left open as the transaction under review did not give rise to any affected market regardless of the definition retained (i.e. whether effectors and delivery systems were to be considered together or separately, or whether a further segmentation within each of effectors and delivery systems was made).
76. The Notifying Party submits that within the effectors area, a distinction can be drawn between siRNA, shRNA and miRNA. The Notifying Party does not consider it necessary or appropriate to further segment these categories between libraries and standalone reagents.
77. The results of the market investigation confirmed the segmentation between siRNA, shRNA and miRNA.
78. From a demand-side viewpoint, customers referred to significant differences in prices and usage between these effectors. As one customer stated: “*siRNA are small RNA molecule you deliver into the cytosol in order to get an inhibition of the gene expression. shRNA are plasmid DNA you have to deliver into the nucleus in order to get an inhibition of the gene expression. Depending on the application and the cell types we work with siRNA or shRNA can be completely inefficient.*”⁵⁹ As another customer explained, siRNA and miRNA should be distinguished from each other as “*although they belong to same pathway their role is completely different. siRNA degrade mRNA while miRNA inhibits translation without degrading mRNA.*” As a result of these differences, the majority of customers indicated that they would not switch from one of these effectors to another as a result of a non-transitory 5-10% price increase.⁶⁰
79. From a supply-side perspective, the majority of competitors indicated that it is not possible to manufacture siRNA, shRNA and miRNA with the same equipment and technology.⁶¹ As a result, competitors in general stated that it would not be possible for a supplier active in the manufacturing of one effector to start swiftly and without any significant costs to produce a different effector.⁶²
80. Within each category of effector, a further segmentation between standalone reagents and libraries does not seem appropriate. Even if from a demand-side there has been a traditional distinction between standalone reagents and libraries, such distinction appears is softening as the relative importance of libraries vis-à-vis standalone reagents in terms of sales volume is decreasing over time.⁶³ Moreover, from a supply-side

⁵⁹ See replies to question 13 of the Commission’s request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁶⁰ See replies to questions 10-12 of the Commission’s request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁶¹ See replies to question 12 of the Commission’s request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁶² See replies to question 13, 14 and 15 of the Commission’s request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁶³ See See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

perspective, the manufacturers of libraries and standalone reagents are essentially the same and many competitors confirmed that switching between standalone reagents and libraries could occur swiftly and without incurring a significant cost.⁶⁴

81. In view of the above, the Commission concludes that there are separate markets for siRNA, shRNA and miRNA.

IV.D.1.b Geographic market definition

82. The Commission concluded in *Invitrogen/Applied Biosystems* that the markets for gene silencing were at least EEA-wide.
83. The Notifying Party submits, relying on Commission precedents, that the relevant geographic market is at least EEA-wide, and possibly global, in scope.
84. The market investigation in the present case has confirmed that the relevant geographic markets are likely to be global in scope. In particular, while some customers stated that there are differences in the price of effectors between the EEA and the rest of the world,⁶⁵ the majority of customers stated that there are no significant barriers to sourcing effectors from outside the EEA.⁶⁶ With specific regard to transport costs, most customers confirmed that such costs remain below 10%.⁶⁷
85. In view of the above, the Commission concludes that the relevant geographic markets in gene silencing reagents are global in scope.

IV.D.1.c Assessment

86. The Commission's market reconstruction exercise has shown that the combined shares of the Parties are generally [...] than those estimated by the Parties in the Form CO.⁶⁸
87. The tables below shows the market shares of the Parties and their competitors in the markets for siRNA, shRNA and miRNA reagents, according to the Commission's market reconstruction.
88. The Decision will analyse in detail siRNA and miRNA. With respect to shRNA, in the light of the elements mentioned in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market.

⁶⁴ See replies to questions 21-30 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁶⁵ See replies to question 31 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁶⁶ See replies to question 30 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁶⁷ See replies to question 33 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁶⁸ See Form CO.

Table 9 – Parties and competitors market shares in the supply of gene silencing reagents worldwide in 2012

Product		Worldwide market shares and market size							MKT Size - € m
		TF	LT	TF+ LT	Qiagen	Sigma Aldrich	IDT	Others	
Gene silencing	siRNA	[40-50]%	[20-30]%	[70-80]%	[10-20]%	[5-10]%	[0-5]%	[5-10]%	[...]
	shRNA	[20-30]%	[0-5]%	[30-40]%	[0-5]%	[50-60]%	[0-5]%	[5-10]%	[...]
	miRNA	[20-30]%	[50-60]%	[70-80]%	[10-20]%	[0-5]%	[0-5]%	[5-10]%	[...]

Source: Commission's market reconstruction

A) siRNA

89. While mainly used at present for research purposes, siRNA is expected in the future to be extended to pharmacological and agricultural applications. Consequently, its market value is potentially to increase significantly in the coming years.⁶⁹
90. Thermo Fisher and Life Technologies are respectively the first and the second manufacturers of siRNA reagents worldwide.
91. According to the Parties' internal documents, the Parties are the closest competitors on the siRNA market. They appear to have the widest siRNA reagents portfolio, and seem to compete fiercely as main drivers for innovation in the sector. In particular, Thermo Fisher is seen by Life Technologies as [...] ⁷⁰ and notably as [...] ⁷¹. As for Thermo Fisher's views on Life Technologies, the slide below shows that Life Technologies is [...] ⁷².

[...]

92. Moreover, Life Technology's internal documents also show that [...] ⁷³.
93. On the basis of the Parties' internal documents, the only remaining significant competitors producing siRNA reagents, Qiagen and Sigma Aldrich, would have [...] for instance is considering as [...]. As for [...], it is considered as having [...] compared to Life Technologies and Thermo Fisher. ⁷⁴ Both competitors appear to [...] ⁷⁵.

⁶⁹ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁷⁰ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁷¹ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁷² See Thermo Fisher's presentation [...] provided by the Parties to the FTC.

⁷³ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁷⁴ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

94. In addition, competition in the market for siRNA appears to be influenced to an appreciable extent by IP rights. The most significant intellectual property related to siRNA reagents are the so called "Tuschl patents", for which the Massachusetts Institute of Technology (MIT) is the licensing agent. In particular, the Tuschl I patent protects siRNA duplex designs of a certain length (from 19-mer to 23-mer).
95. Thermo Fisher and Life Technologies are two out of the only four licensees of the Tuschl patents, along with Qiagen and Sigma Aldrich. Whilst some competitors have found possible ways to manufacture and commercialise siRNA without being licensees of the Tuschl patents (e.g. IDT), the position enjoyed by the four licensees clearly shows that such patents provide an important competitive advantage against other manufacturers.
96. This competitive advantage has been confirmed by competing firms, which stressed that "*[a]ll other suppliers are excluded from selling siRNA into the research market*" and that "*[i]t is almost impossible to use RNA interference (siRNAs) without infringing one of the Tuschl patents*".⁷⁶
97. A potential impact on competition resulting from the Transaction in siRNA have also been confirmed by the numerous and generally substantiated concerns raised by almost all competitors and by a number of customers which replied to the Commission's requests for information.⁷⁷
98. In view of the above, the Transaction raises serious doubts regarding siRNA reagents. However, the proposed commitments would effectively remove the serious doubts raised, as analysed in section V.B.2 of the present Decision.

B) miRNA

99. The market for miRNA represents a relatively small part of the gene silencing industry. However, miRNA is becoming increasingly popular among scientists and that the overall market size is expected to experience double digit growth in the coming years.⁷⁸
100. Life Technologies is clearly the leading producer and supplier of miRNA reagents, [...] ⁷⁹ and a worldwide market share exceeding 50%. [...] ⁸⁰ [...].⁸¹

⁷⁵ See Thermo Fisher's presentation [...] provided by the Parties to the FTC.

⁷⁶ See replies to question 42 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁷⁷ See replies to questions 58 and following of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁷⁸ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁷⁹ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁸⁰ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

101. In turn, Thermo Fisher is the clear number two in the market. Life Technologies sees Thermo Fisher as [...].⁸² [...].⁸³

[...]

102. The Commission's market investigation has also shown that the companies that the Notifying Party has identified as significant competitors (i) have very limited activities, or (ii) are not active at all at production level [...]. In practice, therefore, the Transaction would almost amount to a merger to monopoly with respect to miRNA reagents.

103. Additional barriers to entry appear to be constituted by the fact that miRNA is a relatively young technology, where Life Technologies and Thermo Fisher enjoy a significant first-mover advantage. Each of Thermo Fisher and Life Technologies hold or have applied for IP rights in the area of miRNA.⁸⁴

104. Finally, the majority of competitors and some customers have also pointed out that the Transaction may result in a reduction of competition as regards miRNA.⁸⁵

105. In view of the above, the Transaction raises serious doubts regarding miRNA reagents. However, the proposed commitments would effectively remove the serious doubts raised, as analysed in section V.B.2 of the present Decision.

IV.D.2 Delivery systems (Transfection)

IV.D.2.a Product market definition

106. Delivery systems are used to introduce external material (including siRNA effectors and other materials such as proteins) into a cell. Delivery can be either physical (electric or ballistic) or chemical (transfection).

107. The Parties' activities overlap only with respect to transfection reagents.

108. Transfection is a widely used chemical technology in a broad range of applications across cell types, such as transient gene expression studies, protein and antibody production and generation of stable cell lines. While certain transfection reagents are marketed for specific uses (e.g. in RNAi), each is capable of being used across multiple applications.

⁸¹ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁸² See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 [...].

⁸³ See Annex 1.01 attached to Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013 – [...].

⁸⁴ See Thermo Fisher's response to the Commission's Article 11 request of 21 October 2013.

⁸⁵ See replies to questions 58 and following of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

109. The primary method for chemical transfection (also referred to as lipofection) involves using lipids. The lipids form complexes called liposomes, which are made up of material similar to the cell membrane and which are therefore capable of readily fusing with the cell membrane to introduce materials such as effectors.
110. The Notifying Party consider that transfection should be distinguished from other means of delivery such as electric delivery and ballistic delivery. The Notifying Party does not consider any further segmentation of the transfection reagents category to be appropriate, for example by reference to reagents used in the transfection of siRNA. According to the Notifying Party, while transfection reagents may be marketed as being particularly effective for certain applications, all transfection reagents are designed to, and do, achieve the same outcome, i.e. making cells permeable to allow for the introduction of external material into the cell.
111. The majority of customers confirmed that there are significant differences between the various types of delivery systems in terms of price, performance and suitability to particular processes.⁸⁶ With regard to a possible distinction within transfection, the Commission has not found any element suggesting that the market definition proposed by the Parties (i.e. a single market for all transfection reagents) would not be appropriate.
112. In view of the above, the Commission concludes that there is one separate market for transfection reagents.

IV.D.2.b Geographic market definition

113. The Commission concluded in *Invitrogen/Applied Biosystems* that the market for transfection is at least EEA-wide in scope.
114. The Notifying Party submits, relying on Commission precedents, that the relevant geographic market is at least EEA-wide, and possibly global, in scope.
115. The market investigation has also confirmed that the relevant geographic markets are likely to be global in scope. In particular, while some customers are of the view that there are differences in the price of transfection reagents between the EEA and the rest of the world,⁸⁷ the majority of customers considered that there are no significant barriers to sourcing transfection reagents from outside the EEA.⁸⁸ With specific regard to transport costs, most customers confirmed that such costs remain below 5%.⁸⁹

⁸⁶ See replies to question 63 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁸⁷ See replies to question 69 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁸⁸ See replies to question 68 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁸⁹ See replies to question 71 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

116. In view of the above, the Commission concludes that the relevant geographic market for transfection reagents is global in scope.

IV.D.2.c Assessment

117. The table below shows the market shares of the Parties and their competitors in the market for transfection according to the results of the Commission's market reconstruction exercise.

Table 10 – Parties and competitors market shares in the supply of transfection worldwide in 2012

Worldwide market shares and market size								
Product	TF	LT	TF+ LT	Qiagen	Promega	Roche	Others	MKT Size - € m
Transfection	[0-5]%	[60-70]%	[60-70]%	[5-10]%	[10-20]%	[5-10]%	[10-20]%	[...]

Source: Commission's market reconstruction

118. While most competitors replying to the Commission's requests for information expressed a negative view on the impact of the Transaction in transfection, only one of customer stated that the Transaction could result in an increase of prices.

119. Moreover, while Life Technologies' position in the transfection area is significant thanks to its leading product line Lipofectamine, Thermo Fisher is only a small player in this field through its TurboFect and DharmaFect products. As a result, the increment brought about to Life Technologies' market share would be *de minimis* (below 5%).

120. Further, when questioned about potential Life Technologies' competitors, many customers referred to Qiagen, Roche and Promega, and not to Thermo Fisher, as established players which will remain active on the market.⁹⁰

121. The Commission has not found any element in its market investigation showing that Thermo Fisher currently represents an important competitive constraint for Life Technologies. In this respect, a majority of customers stated that Thermo Fisher does not enjoy any particular advantage with regard to the main competition drivers in the market.⁹¹

122. In view of the above considerations, the Commission therefore concludes that the Transaction does not raise serious doubts with respect to transfection.

IV.D.3 Nucleic Acid ("NA") Amplification

123. NA amplification comprises technologies for amplifying (or copying) a segment of a nucleic acid (DNA or RNA) to enable further analysis of the sample. This is most

⁹⁰ See replies to question 74.1 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁹¹ See replies to question 74.1 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

commonly achieved through the use of Polymerase Chain Reaction ("PCR") techniques. The PCR sector comprises instruments and reagents used in PCR processes.

IV.D.3.a Product market definition

Instruments

124. The Notifying Party relies on the Commission's conclusion in *Invitrogen/Applied Biosystems*⁹² where the Commission concluded that separate markets exist for instruments and reagents.
125. With regard to instruments, the Notifying Party submits that it is appropriate to differentiate between (i) thermal cyclers, and (ii) qPCR instruments. The market investigation has brought no elements pointing to a different conclusion on these product markets.

Reagents

126. As for reagents, this area includes standard reagents (i.e. buffers, dNTPs and other ancillary reagents) and differentiated reagents. The Notifying Party submits that standard reagents constitute a separate market. In *Invitrogen/Applied Biosystems*, the Commission concluded that a distinction should be made between standard and differentiated reagents. The market investigation has brought no elements pointing to a different conclusion on these product markets. The market for standard reagents is not affected and is hence not discussed further in this decision. The Commission's assessment therefore concerns differentiated reagents only.
127. Differentiated reagents are sold (i) on a standalone basis, and (ii) in ready-to-use kits.
 - (i) Reagents sold on a standalone basis
128. In *Invitrogen/Applied Biosystems*, the Commission considered further segmentations within differentiated reagents as follows: between (i) Taq DNA polymerase and (ii) non-Taq DNA polymerase; (iii) for Reverse Transcriptase ("RT") enzymes; and between (iv) dye-based and (v) probe-based detection chemistries.
129. In line with the Commission decision in *Invitrogen/Applied Biosystems*, the Notifying Party submits that Taq polymerase constitutes a separate market. The market investigation has confirmed that Taq polymerase is a separate product market from non-Taq polymerase.
130. However, the Notifying Party departs from *Invitrogen/Applied Biosystems* when submitting that the non-Taq thermostable category comprises various enzymes that have been modified for different use and comprise distinct product markets, namely (i) high fidelity polymerase enzymes; (ii) hot start polymerase enzymes; (iii) speciality enzymes, although it also submits that there is a relatively high-degree of supply-side substitutability between the different non-Taq thermostable polymerases.

⁹² Case COMP M.5264, paragraph 51.

131. For the non-Taq polymerase area, the market investigation pointed at the absence of demand-side substitutability⁹³, and limited supply-side substitutability⁹⁴ between the different non-Taq polymerases (high fidelity, hot start, other specialty). IP rights cover specific categories of non-Taq polymerases (e.g. there are specific IP rights for high fidelity polymerase)⁹⁵, and know-how represents a significant barrier to entry for specific categories of non-Taq polymerase. In light of the above, the Commission concludes that high fidelity, hot start and other specialty polymerase reagents constitute separate relevant product markets.
132. In line with *Invitrogen/Applied Biosystems*, the Notifying Party submits that RT enzymes constitute a separate market, which has been confirmed by the market investigation.
133. Finally, also in line with *Invitrogen/Applied Biosystems*, the Notifying Party submits that dye-based detection chemistries and probe-based detection chemistries are more properly viewed as distinct product markets⁹⁶. The market investigation has brought no elements pointing to different conclusions on this matter.

(ii) Reagents sold in ready-to-use kits

134. In *Invitrogen/Applied Biosystems*, the Commission considered justifiable a differentiation between reagents that are sold as part of kits and those that are sold on a standalone basis. The Notifying Party has also identified separate markets regarding differentiated reagents in ready-to-use kits. The market investigation has confirmed that reagents sold as part of kits and those sold on a standalone basis are part of separate product markets.
135. In the context of kits, in *Invitrogen/Applied Biosystems* the Commission considered appropriate to distinguish between each of the four main PCR processes (i.e. PCR, qPCR, RT-PCR and RT-qPCR). The Notifying Party has also identified the following markets regarding differentiated reagents in ready-to-use kits: (i) PCR kits; (ii) dye-based qPCR kits; (iii) probe-based qPCR kits; (iv) cDNA synthesis kits, (v) RT-PCR kits; (vi) dye-based RT-qPCR kits; and (vii) probe-based RT-qPCR kits. The market investigation has brought no elements pointing to different conclusions on these product markets.

⁹³ See replies to question 14 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

⁹⁴ See replies to question 223 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁹⁵ See replies to questions 224 and 225 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁹⁶ The differentiation between dye-based and probe-base detection chemistries is relevant in the context of ready-to-use kits.

Conclusion

136. In view of the above, the Commission concludes that:
- (i) there are separate markets for instruments, with distinctions between thermal cyclers and qPCR instruments;
 - (ii) there are separate markets for reagents, with distinctions between standard reagents and differentiated reagents;
 - (iii) the relevant markets in differentiated reagents are further segmented in differentiated reagents sold on a standalone basis, and differentiated reagents sold in ready-to-use kits;
 - (iv) the differentiated reagents on a standalone basis are further broken down in Taq polymerase reagents, high fidelity polymerases, hot start polymerases, other specialty polymerases and RT enzymes;
 - (v) the differentiated reagents in ready-to-use kits are further broken down in PCR kits; dye-based qPCR kits; probe-based qPCR kits; cDNA synthesis kits, RT-PCR kits; dye-based RT-qPCR kits; and probe-based RT-qPCR kits.

IV.D.3.b Geographic market definition

137. In *Invitrogen/Applied Biosystems*, the Commission concluded that the various markets within the area of NA amplification were at least EEA-wide.
138. The Notifying Party agreed with the above conclusion.
139. In the market investigation, all competitors indicated that customers share the same technical and commercial needs regardless of the customer's location⁹⁷. The majority of competitors submitted that transport costs are not significant⁹⁸ and that prices in the US are slightly lower on average than in the EEA⁹⁹.
140. In view of the above, the Commission concludes that the relevant markets within the area of NA amplification are at least EEA-wide.

IV.D.3.c Assessment

A) Instruments

141. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the markets for instruments for NA amplification.

⁹⁷ See replies to question 251 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁹⁸ See replies to question 252 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

⁹⁹ See replies to question 253 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 October 2013.

B) Reagents

(i) Reagents sold on a standalone basis

I. Taq polymerase reagents

142. For Taq polymerase reagents, after considering the elements referred to in paragraph 12 above, the Commission considers that the Transaction does not give rise to serious doubts as to its compatibility with the internal market.

II. Non-Taq polymerase reagents

143. The Transaction would bring together two of the leading suppliers of non-Taq polymerase reagents, both active in high fidelity, hot start and other specialty polymerases.

144. The table below shows the market shares of the Parties and their competitors for stand-alone non-Taq polymerase reagents for PCR techniques. These figures are based on a market reconstruction carried out by the Commission.

Table 11 – Parties and competitors market shares in the supply of non-Taq polymerase reagents in the EEA in 2012

Non-Taq polymerase reagents	EEA market shares and market size								
	TF	LT	TF+ LT	Qiagen	Agilent	Promega	Roche	Others	MKT Size - € m
High fidelity polymerase	[20-30]%	[20-30]%	[40-50]%	[0-5]%	[5-10]%	[0-5]%	[10-20]%	[20-30]%	[...]
Hot start polymerase	[0-5]%	[40-50]%	[40-50]%	[20-30]%	[0-5]%	[0-5]%	[10-20]%	[10-20]%	[...]
Other specialty polymerase	[30-40]%	[10-20]%	[40-50]%	[0-5]%	[0-5]%	[0-5]%	[20-30]%	[20-30]%	[...]
Total Non-Taq polymerase	[10-20]%	[30-40]%	[40-50]%	[10-20]%	[0-5]%	[0-5]%	[10-20]%	[20-30]%	[...]

Source: Commission's market reconstruction

High fidelity polymerase

145. The Parties are the first and the second largest manufacturers of high fidelity polymerase in the EEA and the market share of the Merged Entity would be in the range of 40%, according to the Commission's market reconstruction. The remaining significant competitors post-Transaction producing high fidelity reagents would be Agilent, New England Biolabs ("NEB"), Qiagen, Roche, and Takara Clontech.

146. The market for high fidelity polymerase reagents is characterized by IP rights but almost every player active in the market has its own IP rights.

147. The Notifying Party submits that in the high fidelity polymerase area there are no significant barriers to switching between suppliers and that all suppliers active in the market have the expertise, capacity and ability to increase production¹⁰⁰.
148. The market investigation confirmed that the market for high fidelity enzymes is not characterized by capacity constraints and that barriers to expansion in this area are limited¹⁰¹.
149. In the market investigation, the majority of customers stated that the Transaction would result neither in a reduction of competition nor in an increase of prices in relation to high fidelity polymerase reagents¹⁰².
150. In addition, the parties' own internal documents confirm that they are not close competitors in the market for high fidelity enzymes. As can be seen from Thermo Fisher's internal documents¹⁰³, Thermo Fisher sees [...] as being the closest competitor to Thermo Fisher's Phusion enzyme. Thermo Fisher's high fidelity enzyme was benchmarked against [...] and other competitors' enzymes. It was not benchmarked against any of Life Technologies' high fidelity enzymes.
151. Life Technologies' internal documents confirm this lack of close competition with Thermo Fisher. Life Technologies observes in them that [...]¹⁰⁴.
152. In view of the above, the Commission concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the supply of high fidelity polymerase enzymes.

Hot start polymerase

153. The Transaction would bring together the leading supplier of hot start polymerase (Life Technologies) with the [...] manufacturer of hot start polymerase in the EEA. The market share of the Merged Entity would be in the range of [40-50]%. The remaining significant competitors post-Transaction producing high fidelity reagents would be Qiagen, Roche, Sigma Aldrich and Takara Clontech.
154. The increment brought by Thermo Fisher is *de minimis* (below 5% in the EEA); Thermo Fisher's sales are around EUR 1 million in the EEA compared to EUR 12 million of Life Technologies.

¹⁰⁰ The Notifying Party estimates that the cost of entering a different non-Taq polymerase reagent, for example the high fidelity one, would be about [less than EUR 200,000 over a period of less than half a year].

¹⁰¹ See minutes of the conference calls with Qiagen (competitor) on 25 October 2013 and with Illumina on 23 October 2013 and see replies to question 54 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹⁰² See replies to questions 66 and 67 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹⁰³ [...].

¹⁰⁴ [...].

155. The market for hot start polymerase reagents is characterized by IP rights but almost every player active in the market has its own IP rights.
156. The Commission's investigation confirmed the Notifying Party's claims that there are no significant barriers to switch between suppliers and that all suppliers active in the market have the expertise, capacity and ability to increase production¹⁰⁵. The market investigation equally confirmed that the market for hot start enzymes is not characterized by capacity constraints and that barriers to expansion in this area are limited¹⁰⁶.
157. In the market investigation, the majority of customers stated that the Transaction will not result in a reduction of competition and will not result in an increase of prices in relation to high fidelity polymerase reagents¹⁰⁷.
158. According to Life Technologies' internal documents, [...] ¹⁰⁸. [...] ¹⁰⁹.
159. In view of the above, the Commission concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the supply of hot start polymerase enzymes.

Other specialty polymerase

160. The Parties are the first (Life Technologies) and the [...] largest manufacturers of other specialty polymerase in the EEA and the market share of the Merged Entity would be in the range of [40-50]%, according to the Commission's market reconstruction. The remaining significant competitors post-Transaction producing other specialty polymerase reagents would be Agilent, GE Healthcare and Roche.
161. The Notifying Party submits that in the other specialty polymerase area there are no significant barriers to switch between suppliers and that all suppliers active in the market have the expertise, capacity and ability to increase production¹¹⁰.
162. The market investigation confirmed that the market for other specialty enzymes is not characterized by capacity constraints and that barriers to expansion in this area are limited¹¹¹.

¹⁰⁵ The Notifying Party estimates that the cost of entering a different non-Taq polymerase reagent, for example the high fidelity one, would be about [less than EUR 200,000 over a period of less than a year].

¹⁰⁶ See replies to question 54 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹⁰⁷ See replies to questions 66 and 67 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹⁰⁸ See Life Technologies' [...], October 2013.

¹⁰⁹ See Life Technologies' [...], March 2012.

¹¹⁰ The Notifying Party estimates that the cost of entering a different non-Taq polymerase reagent, for example the high fidelity one, would be about [...].

163. In the market investigation, the strong majority of customers stated that the Transaction will not result in a reduction of competition and will not result in an increase of prices in relation to other specialty polymerase reagents¹¹².
164. In addition, the Parties' portfolio of other specialty polymerases is predominantly complementary rather than overlapping. A large part of Thermo Fisher's portfolio is directed at the generation of long PCR products while Life Technologies mainly offers specialised enzymes which are not included in Thermo Fisher's portfolio, namely Tth and Tsp (which is optimised for genotyping applications) polymerases.
165. In view of the above, the Commission concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the supply of other specialty polymerase enzymes.

III. RT enzymes

166. The Transaction would bring together the leading supplier of RT enzymes (Life Technologies) with the [...] manufacturer of RT enzymes in the EEA. The market share of the Merged Entity would be in the range of [80-90]%, according to the Commission's market reconstruction. The remaining significant competitors post-Transaction producing RT enzymes on a standalone basis would be Agilent, NEB, Promega, Roche and Takara Clontech.
167. The table below shows the market shares of the Parties and their competitors in RT enzymes on a standalone basis, according to the market reconstruction carried out by the Commission.

Table 12 – Parties and competitors market shares in the supply of RT enzymes in the EEA in 2012

RT enzymes	EEA market shares and market size							
	TF	LT	TF+ LT	Agilent	Promega	Roche	Others	MKT Size - € m
RT enzymes	[0-5]%	[70-80]%	[80-90]%	[0-5]%	[5-10]%	[0-5]%	[5-10]%	[...]

Source: Commission's market reconstruction

168. The Commission's investigation confirmed that despite this relatively high combined market share, the Transaction does not raise serious doubts in the area of RT enzymes for the following reasons.
169. First, the increment brought by Thermo Fisher is *de minimis* (below 5% in the EEA); Thermo Fisher's sales in the EEA are less than EUR [...], compared to EUR [...] of Life Technologies.

¹¹¹ See replies to question 54 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹¹² See replies to questions 66 and 67 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

170. Second, Thermo Fisher's R&D and marketing costs in RT enzymes is and was limited (for R&D EUR [...] in 2011, EUR [...] in 2012 and EUR [...] to date in 2013; for marketing EUR [...] in 2012 and EUR [...] to date in 2013).
171. Third, the 2012 market shares do not fully reflect important developments that occurred in that year. Life Technologies owned a relevant patent for the US (Superscript II) which expired in May 2012. The expiry of this patent presented a major opportunity for new entrants to develop their offerings based on the Superscript II technology. [...]. Following the expiry of the Superscript II patent, some players developed H Minus RT enzymes (the H Minus attributes were originally the main subject of Superscript II), including NEB, Promega and Thermo Fisher.
172. It is true that Life Technologies still owns a patent (Superscript III) for the high-end segment of the RT enzymes market. The Commission's investigation however confirmed that almost every player active in the market has its own IP rights.
173. Fourth, the investigation in fact revealed that all suppliers active in the market have the expertise, capacity and ability to increase production and that there are no significant barriers to switch between suppliers.¹¹³ The market investigation furthermore confirmed that the market for RT enzymes is not characterized by capacity constraints and that barriers to expansion in this area are limited¹¹⁴. It is therefore likely that the remaining competitors left post-merger could expand their production so as to replace Thermo Fisher's supply, even in its entirety. The significant growth opportunities following the expiry of Life Technologies' Superscript II patent are corroborated by other facts. In the first half of 2013 Life Technologies' EEA sales in RT enzymes [...] compared to the first half of 2012 and Thermo Fisher's sales in the EEA in the same period [...]. Hence, following the expiry of this patent, Life Technologies [...]. The market investigation also confirmed that there have been new entries (NEB, Agilent, Bioline Reagents and Takara Clontech) in the standalone RT enzymes field.¹¹⁵
174. Finally, and in accordance with these findings, the majority of customers stated, in the market investigation, that the Transaction would result neither in a reduction of competition nor in an increase of prices in relation to RT enzymes¹¹⁶.
175. In view of the above, the Commission concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the supply of RT enzymes.

¹¹³ The Notifying Party estimates that the cost of entering the RT enzymes market would be about [less than EUR 300,000 over a period of less than a year].

¹¹⁴ See minutes of the conference calls with Roche (competitor) on 18 October 2013 and with Illumina on 23 October 2013 and see replies to question 54 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹¹⁵ See minutes of the conference call with Illumina on 23 October 2013.

¹¹⁶ See replies to questions 66 and 67 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

(ii) Reagents sold in ready-to-use kits

176. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the markets for reagents sold in ready-to-use kits.

IV.D.4 NA Purification

177. Purification techniques are used to isolate a target element, which may be a nucleic acid molecule (RNA, DNA), protein or cell.

IV.D.4.a Product market definition

Instruments

178. The Notifying Party submits that purification instruments take four forms, which are (i) liquid-based instruments; (ii) column-based instruments; (iii) magnetic bead-based instruments; and (iv) electrophoresis gel boxes (horizontal gel boxes in the case of NA purification).

179. The market investigation confirmed that there are separate markets for (i) liquid-based instruments; (ii) column-based instruments; (iii) magnetic bead-based instruments; and (iv) electrophoresis gel boxes (horizontal gel boxes in the case of NA purification).¹¹⁷ Affilogic stated in this respect that "*magnetic beads separation systems are very different from other systems making use of non-magnetic beads.*"¹¹⁸

180. In the NA purification instruments area, the Transaction leads to horizontally affected markets only in magnetic bead-based instruments and electrophoresis gel boxes (horizontal gel boxes in the case of NA purification).

Electrophoresis consumables - Molecular weight standards

181. The Commission has previously examined the market for molecular weight standards (i.e. DNA ladders) in *Invitrogen/Applied Biosystems*,¹¹⁹ although the Commission ultimately left the product market definition open.

182. The Notifying Party submits that molecular weight standards constitute a separate product market. The market investigation has brought no elements pointing to different conclusion on this product market¹²⁰.

183. The Transaction leads to horizontally affected markets in molecular weight standards.

¹¹⁷ See replies to questions 33, 34, 35, 36 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹¹⁸ See Affilogic's reply to question 4 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013

¹¹⁹ See Case No COMP/M.5264, paragraph 65.

¹²⁰ See replies to question 39 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

IV.D.4.b Geographic market definition

184. In *Invitrogen/Applied Biosystems* the Commission concluded that all relevant markets in NA purification were at least EEA-wide.
185. The Notifying Party submits that the geographic market is least EEA-wide, due to the following characteristics: (i) customers are sophisticated and products are identical wherever customers are located; (ii) low transport costs; and (iii) there is a degree of global harmonisation of pricing.
186. The market investigation has brought no elements pointing to different conclusions on these geographic markets.

IV.D.4.c Assessment

A) Instruments

187. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets for electrophoresis gel boxes. The Commission will therefore assess below the impact of the Transaction in the market for magnetic bead-based instruments for nucleic acid purification ("MBB instruments").
188. The table below shows the market shares of the Parties and their competitors for MBB instruments, according to the market reconstruction carried out by the Commission.

Table 13 – 2012 market shares in the supply of magnetic bead-based instruments for nucleic acid purification

	TF	LT	TF+LT	Qiagen	Roche	Abbott	Promega	Others	Market Size - EURm
World	[10-20]%	[20-30]%	[40-50]%	[20-30]%	[10-20]%	[5-10]%	[5-10]%	[5-10]%	[...]
EEA	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[10-20]%	[0-5]%	[5-10]%	[10-20]%	[...]

Source: Commission's market reconstruction

189. Despite the significant market shares outlined in the table above, the Commission considers that the Transaction does not raise serious doubts as regards the markets for MBB instruments.
190. First, the Merged Entity would still face a number of significant competitors, including Qiagen, Roche, Perkin Elmer, Abbott and Promega. The market investigation has not revealed any capacity constraint or other barrier to expansion on the part of these competitors.¹²¹

¹²¹ See replies to the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

191. Second, whilst the Transaction would create a clear market leader in terms of sales, it appears that the competitive significance of the Merged Entity going forward may be overstated by these market shares. Indeed, Life Technologies has already announced the discontinuing of several of its product ranges accounting for approx. [...] % of its 2012 sales at global level and [...] % at EEA level.¹²²
192. Third, the market investigation has shown that a majority of customers see sufficient alternatives to the Parties for MBB instruments, including the competitors listed above, and that there are no barriers to switching for research customers.¹²³ In addition, competitors such as Eppendorf and Promega have entered the market or significantly expanded their position in the last three years. [Customer] stated in this respect "*there are other big companies who supply magnetic bead-based instruments, for example Promega, Qiagen, Eppendorf*"¹²⁴
193. Fourth, customers and competitors have confirmed the Parties' claim that their product offerings are not competing for the same applications, based on the different technical characteristics of their product offerings. Stratec stated in this respect that "*We do not see [the Parties] as Close competitors as they both are offering Systems for different markets or throughput Needs.*"¹²⁵
194. Moreover, according to the Parties, Life Technologies achieved [...] % of its 2012 global sales (and [...] % of its EEA sales) with a product line which is exclusively targeted at customers performing next-generation sequencing, and is furthermore closely linked to Life Technologies' own next generation sequencing product range. The remainder of Life Technologies' sales (apart from the discontinued products mentioned above) are achieved through instruments that are already toll-manufactured by Thermo Fisher pre-merger. The Commission therefore considers that Thermo Fisher and Life Technologies are distant competitors in this field with complementary offerings.
195. Finally, most customers and competitors stated that the Transaction was unlikely to have a negative impact on competition in this area,¹²⁶ and the Commission considers

¹²² See annex 7.1 to the submission of the Parties of 7 November 2013.

¹²³ The Commission notes in this respect that the Parties' product offering is not focused on applied segments. As stated by Qiagen, "*In the MDx market we do not consider Life Technologies or Thermo Fisher as close competitors based on their current magnetic bead based instruments product offering. Their current products do not provide sufficient process safety features and sample to result automation, which is requested by MDx customers. Both instruments do not have CE-IVD status.*" See Qiagen's reply to question 153 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹²⁴ See replies to question 55 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹²⁵ See replies to question 153 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹²⁶ See replies to question 80 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

that the few customer complaints in this area were either unsubstantiated¹²⁷ or linked to the potential increased market power of the Merged Entity in the upstream market for the supply of magnetic beads.¹²⁸ In this last respect, the proposed commitments would effectively remove the serious doubts raised, as analysed in section V.B.3 below.

196. In light of the above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in the area of MBB instruments.

B) Electrophoresis consumables - Molecular weight standards

197. The market share of the Merged Entity would be [30-40]% in the EEA, according to the Parties' estimates ([10-20]% increment brought by Life Technologies). The remaining significant competitors post-Transaction producing molecular weight standards would be Bio-Rad, GE Healthcare, NEB and Promega.
198. The Notifying Party submits that there are no significant barriers to entry in relation to molecular weight standards¹²⁹, there are no blocking IP rights, the relevant know-how is readily available and the production molecular weight standards requires only basic and laboratory facilities. According to the Notifying Party, examples of recent entrants include NEB, SERVA and SBS Genetech.
199. The market investigation confirmed that, first, IP rights are of relative importance in this market,¹³⁰ second, that it is possible for customers to easily switch between suppliers within a short time period¹³¹ and, finally, that many relevant players would remain post-Transaction (e.g. Bio-Rad, GE Healthcare, NEB, Promega, Sigma-Aldrich and Takara Clontech).
200. Furthermore, in the market investigation, almost all customers stated that the Transaction would result neither in a reduction of competition nor in an increase of prices in relation to molecular weight standards¹³².

¹²⁷ One customer claimed that the Merged Entity would have market power through leveraging both Parties' strong positions in reagent kits for these instruments, however the combined market share of the Parties for reagent kits for MBBs is below 15% under all possible market definitions. Another customer's comments that "*in our eyes mergers of this size always have a negative impact on competition.*" are representative of most remaining complaints.

¹²⁸ See replies to question 80 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹²⁹ The Notifying Party submits that it would take only a few weeks at minimal cost to develop molecular weight standards products.

¹³⁰ See replies to question 70 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹³¹ See replies to question 75 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

¹³² See replies to questions 82 and 85 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 October 2013.

201. In view of the above, the Commission concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the supply of molecular weight standards.

IV.D.5 Cloning

202. Cloning involves the replication of a single DNA molecule starting from a single living cell to generate a large population of cells containing identical DNA molecules. In the cloning area, the Parties' activities overlap in the supply of cloning enzymes (restriction and modifying enzymes) and in the supply of cloning kits.

IV.D.5.a Product market definition

203. For cloning enzymes, the Notifying Party submits that the relevant product market is the market for all cloning enzymes, whether restriction or modifying in nature. The market investigation has confirmed a relatively high degree of supply side substitutability between restriction and modifying enzymes but has also indicated a limited demand side substitutability.

204. The Commission considers that it can be left open whether restriction enzymes and modifying enzymes would constitute separate relevant product markets, as the Transaction would not give rise to serious doubts in these potential segments.

205. With respect to cloning kits, the Notifying Party submits that the relevant product market is a separate market for cloning kits. The market investigation has brought no elements pointing to a different conclusion on this product market.

IV.D.5.b Geographic market definition

206. The Notifying Party submits that the markets for the cloning category (both cloning enzymes and cloning kits) are at least EEA-wide in scope. The market investigation has brought no elements pointing to different conclusions on these geographic markets.

IV.D.5.c Assessment

207. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets comprised within this area.

IV.E. PARTICLES

208. Particles (also known as beads or microspheres) are spherical beads from 20 nanometres to 2,000 microns (2mm) in diameter, which are either hollow or solid, made from a range of materials, including polymer (such as polystyrene latex), glass, ceramics, silica, metal and wax, and can be produced on an off-the-shelf or custom made basis.

209. Different types of particles (magnetic, plain, fluorescent, dyed, standard, etc.) are used in a variety of different applications, in particular in the life sciences and medical diagnostics industries.

IV.E.1 Product market definition

IV.E.1.a Magnetic beads vs other particles

210. Magnetic beads are super-paramagnetic particles and therefore respond to a magnetic field while not retaining any magnetism outside a magnetic field. This feature enables easier – and possibly automated – handling with a magnetic rod or equivalent. According to the Parties, the key end-user applications for magnetic beads are nucleic acid, protein and cell sample preparation and immunoassays. The Parties supply magnetic beads (i) to Original Equipment Manufacturers ("OEMs") for inclusion in their own kits and instruments, and (ii) directly to end-customers, generally as part of the Parties' own kits.
211. The Notifying Party submits that different types of particles constitute separate product markets. This conclusion would be justified on the basis of very limited demand-side and supply-side substitutability between the different types of particles. The market investigation has confirmed that the production and supply of magnetic beads should be distinguished from other types of particles for the purposes of market definition.¹³³

IV.E.1.b Distinction between polymer-based magnetic beads and other types of magnetic beads

212. Magnetic beads can be classified according to the non-magnetic material covering and/or encapsulating the magnetic core(s) or layer(s) giving the particle its super-paramagnetic nature. The most common types of beads are polymer-based and silica-based, but other types of beads exist, such as cellulose-based beads.
213. The Notifying Party submits that all magnetic beads belong to the same product market, without distinction according to the type of bead, because of high substitutability between polymer-based and silica-based magnetic beads and of similarity in price levels.
214. The market investigation has however shed light on the absence of supply-side substitutability between polymer-based magnetic beads and other types of magnetic beads. This finding is based on the following factors: (i) polymer-based magnetic beads are supplied by different market players compared to other types of magnetic beads,¹³⁴ (ii) polymer-based magnetic beads cannot be produced on the same production line as other types of magnetic beads,¹³⁵ (iii) producers of other types of magnetic beads cannot

¹³³ See replies to questions 10 to 14 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013, and replies to questions 9 to 12 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹³⁴ The Commission notes that the Parties only manufacture polymer-based magnetic beads, as opposed to other types of magnetic beads. Many competitors of the Parties such as Agilent, Ademtech and JSR also do not produce other types of magnetic beads. On the other hand, competitors such as Promega only manufacture other types of magnetic beads.

¹³⁵ See replies to question 15 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013. Promega stated in this respect that "Different magnetic beads require different manufacturing processes."

start swiftly and without significant cost the production and sales of polymer-based magnetic beads,¹³⁶ (iv) specific patents are in place protecting both the composition of polymer-based magnetic beads and their manufacturing processes¹³⁷ and (v) specific know-how is required to operate polymer-based magnetic bead manufacturing processes.¹³⁸

215. The market investigation has also shown that demand-side substitutability between different types of magnetic beads is minimal across all applications. No willingness to switch from polymer-based magnetic beads to other types of magnetic beads in case of a small but significant increase in prices was indicated by any customers, whether active in sample preparation, immunodiagnosics or other applications.¹³⁹ Most customers of magnetic beads – whether OEM customers or end-user customers – also indicated that they consider polymer-based magnetic beads as a distinct product fulfilling different needs compared to silica-based magnetic beads.¹⁴⁰ [OEM customer] indicated for instance that "*the properties of silica-based are significant[ly] different to prevent straight substitution [from polymer-based beads]*".¹⁴¹
216. With regard to the use of magnetic beads for sample preparation, Qiagen stated that "[p]olymer-based magnetic beads are used for automated processes to extract nucleic acids from biological fluids. They come in small quantities and are highly priced. Other types of particles (mainly silica) are either used for manual processes to extract nucleic acids from biological fluids. They come in small quantities and are moderately priced. The other use is in industrial processes for purification of fluids (filtering, treatment of toxic waste)."¹⁴²
217. OEM customers using magnetic beads for other applications than sample preparation also indicated no sign of demand-side substitutability. [OEM customer] stated in this respect that "*[p]olymer-based magnetic beads are generally more suitable for certain downstream applications, such as diagnostics, since the magnetic content of the particles is more stable.*"¹⁴³ [OEM customer] also indicated that "*Due to their physical*

¹³⁶ See replies to question 16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹³⁷ Both Life Technologies and Thermo Fisher have patents protecting their polymer-based magnetic beads, see section IV.E.3.b below.

¹³⁸ See replies to questions 15 and 16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013. Bangs Polysciences stated in this respect that "*Polymer beads are made through a different process. The material can be sold through the same channels, but the production process would be more difficult to quickly acquire.*"

¹³⁹ See replies to question 14 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁴⁰ See replies to question 15 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁴¹ See [OEM customer]'s reply to question 15 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁴² See minutes of conference call with [OEM customer].

¹⁴³ See minutes of conference call with [OEM customer].

properties, silica based beads are easier to centrifuge (higher density) and show lower adhesion. Polymer based beads have a density closer to 1g/cm³, which prevents them from fast sedimentation, which is important for our application". The market investigation has in particular indicated that OEM customers using magnetic beads as a raw material for immunoassays would incur large barriers to switching, both at individual assay level and for their overall diagnostic platforms.¹⁴⁴

218. In the light of the above, the Commission concludes that the production and supply of polymer-based magnetic beads should be distinguished from other types of magnetic beads for the purposes of market definition.

IV.E.1.c Distinction between supply to OEM customers and to end-user customers

219. The Notifying Party submits that no distinction is warranted between the production and supply of magnetic beads to OEM customers and to end-user customers, on the grounds that (i) most suppliers supply to both OEM and end-user customers, (ii) there are very few differences between the technologies or manufacturing capabilities required to supply these two potential segments, (iii) magnetic bead manufacturers provide the same product to both customer groups.
220. The market investigation has however highlighted a number of limitations to the supply-side substitutability between the OEM and the end-user customer segments. First, contrary to the Parties' claims, the number of suppliers of magnetic beads for OEM customers is *de facto* significantly smaller than for end-user customers.¹⁴⁵ The market investigation has also identified as prerequisites for a presence in the OEM segment the ability to custom, investments in quality control and quality assurance, reliability of the manufacturing process, and the long-term scalability of production.¹⁴⁶ Competitor Miltenyi, for instance, manufactures its magnetic beads for research use and for clinical use in different facilities.¹⁴⁷
221. Contrary to the Notifying Party's view, the market investigation has also shed light on significant differences between products supplied to OEM customers and to end-user customers. The Commission's market investigation has shown that end-user customers

¹⁴⁴ According to [OEM customer], "[switching] implies significant investments with unforeseeable consequences for assay performance." See reply to question 14 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013. See also section IV.E.3.c below.

¹⁴⁵ See replies to question 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013. Bangs Polysciences stated in this respect that "*The OEM market is generally supplied [by] very few companies. This is due to the qualification and resistance to change. The end-user market is supplied by many more companies.*" The Commission also notes that Thermo Fisher, while being a significant player in the supply of polymer-based magnetic beads to OEM customers, achieves a comparatively much smaller presence on the market for end-user customers.

¹⁴⁶ See replies to questions 28 and 35 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁴⁷ See Miltenyi's reply to question 29 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

rarely purchase surface-activated magnetic beads, while OEM customers purchase both surface-activated and ligand-coupled magnetic beads depending on their needs.¹⁴⁸ In this respect, the Commission notes that most OEM customers have the capacity to couple ligands to surface-activated beads in-house and often do so using proprietary molecules such as particular antibodies.¹⁴⁹ On the contrary, OEMs generally purchase beads already coupled when the ligand is generic, such as streptavidin. [OEM customer] stated in this respect "*OEMs generally prefer surface-activated beads when they do not want to be restricted to one specific ligand and/or one specific application.*"¹⁵⁰

222. OEM customers also exhibit preferences for specific criteria such as the automated use of magnetic beads, as well as sterility or biocompatibility, or, more generally, technical characteristics imposed by regulatory requirements on downstream products.¹⁵¹
223. Moreover, most suppliers indicated that there are differences in prices of the same products when sold to OEM customers and to end-users, and that the two segments typically have different margins.¹⁵² Similarly, most suppliers indicated that there are differences in the lengths of the contracts, in the importance of distribution channels, and in the sales and tender processes between the two customer segments.
224. The market investigation has also highlighted that OEM customers purchase high volumes, preferably via long-term contracts, with an emphasis on quality, scalability and reliability, while end-user customers are more sensitive to brand and innovation. The market investigation has shown that the requirements of OEM customers are also very different from the requirements of end-user customers as regards manufacturing processes, and that this requires higher investments from magnetic beads manufacturers.¹⁵³ [OEM customer] stated in this respect that "*the reliability of the supplier is an important factor. For instance, [...]*."¹⁵⁴
225. An internal document of Thermo Fisher also shows that OEM demand for particles is identified as a particular customer segment, and [...].¹⁵⁵

¹⁴⁸ According to the Commission's market reconstruction, sales of surface-activated polymer-based magnetic beads (as opposed to ligand-coupled polymer-based magnetic beads) account for less than half of sales to OEM customers, while they account for more than two thirds of corresponding sales to OEM customers.

¹⁴⁹ [OEM customer] stated in this respect that "*[OEM customer] couples the magnetic beads to specific ligands in-house, instead of buying ligand-coupled magnetic beads. [OEM customer] believes that it would be more expensive to purchase the magnetic beads already coupled. In addition, [OEM customer] might need specific ligands that are not available on the market.*" See minutes of conference call with [OEM customer].

¹⁵⁰ See minutes of conference call with [OEM customer].

¹⁵¹ See replies to question 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁵² See replies to question 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013. [...].

¹⁵³ Id.

¹⁵⁴ See minutes of conference call with [OEM customer].

¹⁵⁵ See [...]. The customer segments are [...].

226. In the light of the above, the Commission concludes that the production and supply of polymer-based magnetic beads to OEM customers constitutes a separate product market.¹⁵⁶

IV.E.1.d Conclusion

227. In the light of the above, the Commission will analyse the effects of the Transaction as regards the market for the production and supply of polymer-based magnetic beads to OEM customers.

228. As regards other types of particles, the precise product market definition can be left open, as the Transaction would not give rise to serious doubts under any plausible market definition.

IV.E.2 Geographic market definition

229. The Notifying Party submits that the geographic market definition for particles is global or at least EEA-wide because (i) manufacturers produce particles at centralised sites, and ship from those sites to regional distribution hubs around the world, and (ii) manufacturers are typically present worldwide either through subsidiaries making direct sales or through distributors.

230. As regards the supply of polymer-based magnetic beads to OEM customers, the market investigation has confirmed the Parties' claims insofar as manufacturers such as the Parties and their main competitors produce polymer-based magnetic beads for OEM customers at centralised sites,¹⁵⁷ and most suppliers pursue sales of polymer-based magnetic beads to OEMs on a global scale. No particular barrier to expansion between geographic regions at worldwide level was identified by competitors in the area of magnetic beads.¹⁵⁸

231. In addition, the market investigation has confirmed that there are no significant differences in demand worldwide.

232. First, all competitors and customers confirmed that the technical and commercial requirements of OEM customers are the same inside and outside the EEA.¹⁵⁹ Second, most customers indicated that there are no significant barriers to sourcing magnetic beads from outside the EEA,¹⁶⁰ and that there are no differences between the EEA and

¹⁵⁶ The Parties are not active in the production and supply of other types of magnetic beads.

¹⁵⁷ See replies to question 29 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁵⁸ See replies to question 31 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁵⁹ See replies to question 30 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013, and to question 23 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁶⁰ See replies to question 25 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013. [OEM customer] stated in this respect that

other geographic areas in terms of prices of magnetic beads. [OEM customer] stated in this respect that "[p]rices depend on bead performance and company pricing strategy more than on geographic origin".¹⁶¹

233. Finally, the market investigation has also confirmed that the majority of OEM customers negotiate their supply agreements for magnetic beads on a global level.¹⁶² Competitor Agilent stated in this respect that "[m]any OEM customers are global and have unified pricing."¹⁶³ [OEM customer] stated in this respect that "*The geographic scope of the distribution agreement with Thermo Fisher is global.*"¹⁶⁴
234. In the light of the above, the Commission concludes that the geographic market definition for the supply of polymer-based magnetic beads to OEM customers is global in scope.
235. As regards all other possible product markets in the area of particles, the market investigation has confirmed that the geographic scope of markets is, as claimed by the Parties, global or at least EEA-wide. The geographic scope of these possible product markets can however be left open as no geographic market definition would give rise to affected markets.

IV.E.3 Assessment

236. The Parties' activities only give rise to affected markets for the supply of polymer-based magnetic beads to OEM customers. The Commission will therefore only assess below the global market for the production of polymer-based magnetic beads to OEM customers.

IV.E.3.a Competitive landscape and market shares

237. The Commission's market reconstruction exercise has shown that the Parties' combined shares are [...].¹⁶⁵
238. The tables below shows the market shares of the Parties and their competitors in the markets for polymer-based magnetic beads to OEM customers, according to the Commission's market reconstruction.

"These [magnetic beads] are typically small packages and transport cost is minimal. There are no significant tariffs or regulatory barriers."

¹⁶¹ See replies to question 26 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁶² See replies to question 27 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁶³ See Agilent's reply to question 32 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁶⁴ See minutes of conference call with [OEM customer].

¹⁶⁵ See Form CO, table E.6.8.

Table 14 –market shares in the supply of polymer-based magnetic beads to OEM customers in 2012

	Worldwide market shares and market size						
	TF	LT	TF+LT	Agilent	Merck Millipore	Others	MKT Size - € m
Polymer-based magnetic beads to OEM customers	[10-20]%	[50-60]%	[60-70]%	[10-20]%	[10-20]%	[5-10]%	[...]

Source: Commission's market reconstruction¹⁶⁶

239. The competitive landscape outlined in the table above is corroborated by an internal document of Thermo Fisher¹⁶⁷ presenting Life Technologies as a clear market leader for magnetic particles. [...].¹⁶⁸
240. Similarly, an internal document of Life Technologies¹⁶⁹ depicts Life Technologies as the clear market leader in terms of sales of magnetic beads to the immunodiagnostic OEM customers, with Merck Millipore, Thermo Fisher and Agilent as its only significant competitors, enjoying comparable market positions.
241. The competitive landscape outlined above has also been corroborated by the results of the market investigation. A majority of competitors and customers have indicated that Life Technologies is already currently the clear market leader for the supply of magnetic beads.¹⁷⁰ Competitor Promega stated that "*Life Technologies is the clear market leader for the supply of polymer-based magnetic beads, while Promega and Qiagen are stronger for RNA/DNA purification.*"¹⁷¹ [OEM customer] stated that "*Dynal (Life) has been a leader in this space for many years.*"¹⁷²
242. In addition, the market investigation has shown that most customers and competitors regard the competitive landscape as relatively stable in terms of the number of suppliers

¹⁶⁶ [...].

¹⁶⁷ [...].

¹⁶⁸ See Annex E.87 to the Form CO.

¹⁶⁹ See SR1 – Immunodiagnostics (IDx) deep dive, submitted as Annex F.27 to the Form CO, slide 9.

¹⁷⁰ See replies to question 31 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013, and to question 37 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁷¹ See minutes of conference call with Promega. The Commission notes in this respect that neither Promega nor Qiagen are active in manufacturing polymer-based magnetic beads.

¹⁷² See [OEM customer]'s reply to question 37 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

of magnetic beads and the products they offer.¹⁷³ [OEM customer] stated in this respect that "*There is a small number of suppliers decreasing by mergers and acquisitions. Smaller suppliers mostly provide only small scale amounts for R&D applications.*"¹⁷⁴ The Commission thus considers that the relative stability of the supplier landscape renders the combined market shares outlined above particularly meaningful as a first indication of market power regarding the market for the supply of polymer-based magnetic beads to OEM customers.

IV.E.3.b Barriers to entry

243. The market investigation has also highlighted significant levels of barriers to entry in the relevant market.
244. Overall, the market investigation has shown that most competitors and customers consider that new entry in the relevant market would require significant investment and time, and that any new entrant would face significant obstacles.¹⁷⁵ [OEM customer] thus stated that a potential new entrant would face a "*large barrier [to] market entry due to R&D costs, IP (patents, know-how) and established supplier relationships.*" All competitors and most customers have indicated that the time required to enter the relevant market would be more than 3 years.¹⁷⁶ The Commission considers that barriers to entry in the relevant market are based on a number of factors, which are outlined below.
245. First, both Life Technologies and Thermo Fisher, as well as several competitors, have currently enforceable patents protecting their magnetic particles and manufacturing processes for magnetic beads. Life Technologies has a number of patents expiring in 2020 or after, relating to both the composition of magnetic particles and to processes for their manufacturing, and in particular on processes for the production of monodisperse polymer-based magnetic beads. Thermo Fisher also has currently valid patents on the Sera-Mag process, and additional patents on the composition of its Speedbeads magnetic particles expire in 2026/2027.
246. Second, [...]. The Commission considers that pending patent litigations is an additional element pointing to the importance of intellectual property rights as a barrier to entry, as well as corroborating Life Technologies' role as market leader.
247. Third, the market investigation has confirmed that most customers and competitors regard intellectual property rights as playing a significant role in the markets for the

¹⁷³ See replies to question 40 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013

¹⁷⁴ See replies to question 34 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁷⁵ See replies to questions 41 and 42 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁷⁶ See replies to question 51 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013 and replies to question 41 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

supply of magnetic beads.¹⁷⁷ Potential competitor Promega, which is not active in the supply of polymer-based magnetic beads but of silica and cellulose-based magnetic beads, stated in this respect that *"New competitors have high barriers to innovate and smaller companies do not have the ability to innovate due to lack of access to the IP."* [OEM customer] stated that *"IP rights are an important factor in this field. According to [OEM customer], a new company starting to manufacture magnetic beads would not be free to operate since known processes are already covered by existing companies' patent portfolios."*¹⁷⁸

248. Fourth, the market investigation has indicated that the know-how required for producing polymer-based magnetic beads constitutes a significant barrier to entry, even for large companies with significant resources such as the Parties' OEM customers. [OEM customer] thus stated that *"even more important than the patent rights is the production know-how of the bead producing companies. This includes know-how on production equipment, raw materials and production processes."*¹⁷⁹ Potential competitor Promega also stated that *"Starting production would take significant efforts, would be expensive, often would require IP, requires specific technical know-how and expertise - all of which would be difficult for most companies."*¹⁸⁰
249. Fifth, the market investigation has shown that the relevant market is characterized by established commercial relationships between the few existing suppliers and downstream OEM customers. [OEM customer] stated for example that *"[OEM customer] has a long-term supply agreement (...) for magnetic beads with a subsidiary of Thermo Fisher, [...]."*¹⁸¹ [OEM customer] stated that *"[OEM customer] has an [...]."*¹⁸²
250. The Commission considers that such practices create additional disincentives for new entrants, in particular in the growing immunoassay segment where downstream products remain on the market longest. Indeed, new entrants may find it harder to recoup investments if only competing for new downstream business, while established competitors enjoy existing revenue streams and economies of scale. In addition, the presence of long-term contracts and the importance of established customer relationships signal that customer preferences do not favour switching. Competitor Agilent stated in this respect that *"established commercial relationship is important for OEM customers. Contracts with the magnetic beads suppliers (in terms of price and volume) are negotiated on a regular basis. In general, OEM customers can get discounts based on larger volumes."*

¹⁷⁷ See replies to question 41 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁷⁸ See minutes of conference call with [OEM customer].

¹⁷⁹ See [OEM customer]'s reply to question 35 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁸⁰ See Promega's reply to question 51 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁸¹ See minutes of call with [OEM customer].

¹⁸² See minutes of call with [OEM customer].

251. Against this backdrop, most competitors and all customers responding to the market investigation have indicated that they consider that there has not been significant new entry in the market in the last three years.¹⁸³ In addition, most competitors and customers have indicated that they do not expect any new entry in the close future in the markets for the production and supply of magnetic beads.¹⁸⁴
252. In the light of the significant barriers mentioned above, the Commission concludes that future entry by new players is unlikely.

IV.E.3.c Barriers to switching

253. The Commission considers that OEM customers of polymer-based magnetic beads have substantial barriers to switching between suppliers for polymer-based magnetic beads.
254. First, the market investigation has shown that all competitors and OEM customers consider that it is not possible for OEM customers to switch easily to other magnetic beads suppliers within a short time period.¹⁸⁵ Indeed, OEM customers generally have their downstream products on the market for very long periods (10 or more years). [OEM customer] stated that "*[OEM customer] considers it most likely that, when taking into account all the validation costs and delays, a price increase of less than 30% would not lead to switching.*" Overall, the market investigation has shown that quality and process reliability are two of the most important drivers of competition for suppliers of polymer-based magnetic beads to OEM customers, and all OEM customers have ranked product quality and process reliability as more important factors than price in this respect.¹⁸⁶
255. Second, the market investigation has shown that there are few reliable suppliers for OEM customers and the Transaction would eliminate one of the remaining alternatives with sufficient quality and reliability for OEM customers. [OEM customer] thus stated that "*The number of competing bead suppliers is decreasing. Larger entities supplying different products could fend off new market entries with their established supply connections. Price negotiations will likely become more difficult.*"¹⁸⁷ [OEM customer]

¹⁸³ See replies to question 43 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013, and replies to question 52 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁸⁴ See replies to question 44 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013, and replies to question 53 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁸⁵ See replies to question 54 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013 and to question 57 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁸⁶ See replies to question 29 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁸⁷ See [OEM customer]'s reply to question 67.1 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

also expressed similar concerns: "*A price increase of 5-10 % in magnetic beads would be a concern for [OEM customer], since they would have to significantly investigate in order to find an alternative supplier.*"¹⁸⁸

256. Third, as outlined in section IV.E.3.b above, established commercial relationships and long-term contracts are an important feature of the relevant market. The Commission considers that such practices constitute an additional barrier to switching away from the Merged Entity for OEM customers. Against this backdrop, the Commission considers that the addition of Thermo Fisher's volumes to Life's existing position would also strengthen the Merged Entity's market power after the merger through reducing the ability of OEM customers to switch away from the Merged Entity.

IV.E.3.d Closeness of competition

257. As noted in section IV.E.3.a above, the Commission considers that the Transaction would essentially amount to a 4 to 3 concentration in the market for the supply of polymer-based magnetic beads to OEM customers, with the only significant competitors of the Parties in this market being Merck Millipore and Agilent.
258. A majority of customers and competitors also see Life Technologies and Thermo Fisher as each other's closest competitors,¹⁸⁹ in particular due to the size of the beads, their consistent size (also referred to as "monodispersity", i.e. narrow size distribution of particles in a batch), their roundness (sphericity) and their downstream applications, as well as to the reliability of their products and global reach. [OEM customer] stated in this respect that "*Life Technologies would be their [OEM customer's] first alternative supplier for Thermo Fisher (and vice versa). Unlike these two companies, other producers are small and focus on niche products. In addition, established suppliers such as Thermo or Life are necessary to ensure reliability of [OEM customer's] supply chain.*"¹⁹⁰
259. As regards the monodispersity of magnetic beads, the Commission first notes that monodispersity appears to be an increasingly important factor for OEM customer choice, in particular for immunodiagnostic applications. [OEM Customer] thus stated that "*A key factor for some uses of magnetic particles, such as diagnostics, is that all magnetic beads should be of the same size (monodispersity).*"¹⁹¹
260. Second, the market investigation has highlighted that market participants view the Parties' beads as good performers as regards this criterion. Competitor Agilent stated for instance that "*Thermo Fisher and Life Technologies' magnetic beads are of a consistent*

¹⁸⁸ See minutes of call with [OEM customer].

¹⁸⁹ See replies to questions 39 and 40 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013, and replies to questions 46 to 48 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

¹⁹⁰ See minutes of conference call with [OEM customer].

¹⁹¹ See minutes of conference call with [OEM customer].

size within lots, and these two companies sell one-micron sized magnetic beads."¹⁹² On the contrary, competitor Merck Millipore uses a different production process compared to both Thermo Fisher and Life Technologies, which results in lower monodispersity.¹⁹³ [OEM customer] stated in this respect that "*Both Parties have a unique manufacturing know how regarding polymer-based magnetic beads. Only they can provide a highly uniform product with regards to size distribution and purity and also ensure constant supply. Competitors do either lack the global reach and size to ensure reliable supply or don't have the quality (mainly size distribution and/or uniformity).*"¹⁹⁴

261. As regards the size of magnetic beads, [OEM customer] stated that "*The ideal size for automated instruments is between 1 and 3 microns, as smaller particles tend to leak through the instrument's valves, while bigger particles have a lower specific surface.*"¹⁹⁵ The Commission notes in this respect that Life Technologies achieves most of its magnetic beads sales to OEM customers in that size range, while Thermo Fisher achieves its entire sales within that size range.
262. The Commission also notes that beads of a 1 micron size constitute a growing segment of OEM demand,¹⁹⁶ where Thermo Fisher achieves its entire sales, and on account of which Life Technologies has developed its new MyOne product range, which achieves significant growth.¹⁹⁷ The Commission also notes that competitor Agilent does not currently provide 1 micron size magnetic beads, and has estimated that "*it would take up to 6 years to develop and bring to market the new type of one-micron sized magnetic bead. Agilent estimates that it is probably in the second year of this six-year process.*"¹⁹⁸
263. Overall, the market investigation has shown that, apart from Merck Millipore and Agilent, OEM customers do not view other competitors as having the product quality,

¹⁹² See minutes of conference call with Agilent. Competitor Ademtech also declared that "*While Dynal and Seradyn's magnetic beads exhibit good monodispersity, the key difference between Ademtech's magnetic beads on the one hand and Dynal's and Seradyn's on the other hand is the size of the beads, as the latter's diameters are between 1 and 3 microns, while Ademtech's products are sub-micronic.*"

¹⁹³ See minutes of conference call with Ademtech: "*Other competitors are Merck Millipore, Spherotech and Microsphere. However, the key difference with Ademtech's products is that these companies do not produce monodisperse magnetic beads.*"

¹⁹⁴ See [OEM customer]'s reply to question 67.1 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013.

¹⁹⁵ See minutes of conference call with [OEM customer].

¹⁹⁶ OEM customer [OEM customer] stated that "*Generally, Original Equipment Manufacturers (OEMs) consider the size of magnetic beads as an important factor (ideally up to 1 micron range). Most suppliers provide either very small particles or particles above the 1 micron range.*" See minutes of conference call with [OEM customer].

¹⁹⁷ The Commission notes that Life Technologies' sales of MyOne beads to OEM customers have increased by [...] % in 2012, compared to an overall growth of sales of polymer-based magnetic beads to OEM customers of [...] %.

¹⁹⁸ Agilent also confirmed the growing importance of this particular bead size during a conference call: "*customer preferences are trending towards 1 micron magnetic beads due to the better precision offered by the smaller beads.*" See minutes of conference call with Agilent.

reliability and scalability of the Parties. Moreover, Thermo Fisher and Life Technologies appear to be closer competitors than the other two significant players in the relevant market. This relative competitive positioning is consistent with the above-mentioned internal document of Thermo Fisher, [...].¹⁹⁹ This competitive interaction is also corroborated by an internal document of Life Technologies, [...].²⁰⁰

264. The Commission concludes that the Parties are likely each other's closest competitors as regards the supply of polymer-based magnetic beads to OEM customers.

IV.E.3.e Thermo Fisher appears to be a significant competitive constraint on Life Technologies' existing strong position

265. The Parties have claimed that Thermo Fisher is a small player in the market and will not compete aggressively going forward.

266. The Commission notes in this respect that [...].²⁰¹ [...].

267. Moreover, the historical sales figures of Thermo Fisher show that sales to OEM customers have increased by approx. [...] from 2010 to 2012, at [...] pace than Life Technologies'.²⁰² Going forward, [...]. The Commission notes that these forecasts are consistent with Thermo Fisher being a significant competitive constraint both today and in years to come in the relevant market. [...].

268. The Commission also notes that Thermo Fisher is present in the same segments of demand as Life Technologies (sample preparation and immunodiagnosics). Competitor Agilent stated in this respect that "*Life Technologies, through the acquisition of Dynal, has approximately 50 % of sales as regards magnetic beads for immunodiagnosics. Life Technologies is present also in the other market segments of OEM demand. Thermo Fisher, through the acquisition of Seradyn, has a sizable presence in the supply to OEM customers across segments.*"²⁰³

269. Against this backdrop, a number of OEM customers have expressed concerns as regards the market power of the Merged Entity. For instance, [OEM customer] stated that "*[t]aking into account the market as a whole, Thermo Fisher and Life Technologies would dominate the market for magnetic beads and this could have an impact on prices.*"²⁰⁴ Most competitors of the Parties have expressed similar concerns, Chemicell

¹⁹⁹ See [...].

²⁰⁰ See [...].

²⁰¹ See [...].

²⁰² The Commission notes that Thermo Fisher's sales growth for polymer-based magnetic beads to OEM customers [...].

²⁰³ See minutes of call with Agilent.

²⁰⁴ See minutes of call with [OEM customer]. See also minutes of call with customer [OEM customer]: "*Such a transaction between market leaders will probably mean less pressure to innovate and lead to harder-to-negotiate supply agreements.*" See also paragraph 54255 above.

stating for instance that "*after the transaction the new entity would have a near monopoly on this market.*"²⁰⁵

270. In the light of the above, the Commission concludes that Thermo Fisher appears to be a significant competitive constraint on Life Technologies' existing strong position.

IV.E.3.f Other countervailing arguments of the Parties

271. The Parties have submitted that large OEM customers are able to self-supply and could therefore defeat any price increase of the Parties in the relevant market. The Parties have also submitted that large OEM customers have sufficient buyer power to defeat any price increase by magnetic bead suppliers.
272. Contrary to the Parties' claim, the in-house capacity of OEM customers does not appear to constitute a significant competitive constraint on polymer-based magnetic beads suppliers.
273. First, the market investigation has shown that, as outlined in paragraph 248 above, even large OEM customers of the Parties are unable to manufacture polymer-based magnetic beads of the same quality and reliability as the Parties. [OEM customer] stated in this respect that "*We do everything in-house with silica-based magnetic beads but not polymer-based magnetic beads because we neither have knowhow nor the production facilities to do polymerization reactions.*"
274. Second, neither competitors nor customers of polymer-based magnetic beads view in-house capacity as a credible alternative to third-party suppliers. Third, the market investigation has not revealed any example of switching by OEM customers of polymer-based magnetic beads from a third-party supplier to magnetic beads manufactured in-house.²⁰⁶
275. As regards the Parties' claims of buyer power, the Commission first notes that the Parties have also claimed that Life Technologies already today commands a [...] price premium over its competitors' products.²⁰⁷ It would therefore appear that OEM customers, in spite of high volume orders, are not able to defeat potential price increases, possibly due to Life Technologies' established position as market leader.

²⁰⁵ See minutes of call with Chemicell.

²⁰⁶ See replies to questions 55 to 57 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 7 October 2013 and questions 58 and 59 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

²⁰⁷ See for instance submission of the Parties of 31 October 2013. The Parties presented a comparison of end-use prices for streptavidin-coated magnetic beads in order to assess the closeness of competition of various suppliers in terms of prices. However, the Commission considers that comparing end-use prices is not informative on the price positioning with relation to OEM customers, who typically order customized products in bulk from a much smaller set of potential suppliers (see section IV.E.1.c above).

276. Second, the Commission notes that the inelastic demand conditions outlined in section IV.E.3.c above and in particular the inability of OEM customers to switch to alternative suppliers in a short time frame are not supportive of buyer power constituting a significant factor in the relevant market.
277. Third, the Commission notes that in order to effectively prevent price increases, buyer power (if any) must also persist and remain effective following the merger, as a merger between two suppliers may reduce buyer power if it thereby removes a credible alternative.²⁰⁸ In the Commission's view, a significant supply alternative will be removed after the merger, and it is therefore unlikely that buyer power would be sufficient to defeat anticompetitive outcomes.

IV.E.3.g Conclusion

278. In the light of the above, the Commission considers that the Transaction would eliminate a substantial competitive constraint to Life Technologies' strong existing position. The Transaction therefore raises serious doubts regarding the production and supply of polymer-based magnetic beads to OEM customers. However, the proposed commitments would effectively remove the serious doubts raised, as analysed in paragraph 429 below.

IV.F. HLA TYPING

279. Human Leukocyte Antigen ("HLA")²⁰⁹ typing is the first stage in transplant diagnostics, which is used to determine the compatibility of the donor's organ with recipient in order to reduce the risk of transplant rejection.
280. HLA typing is used for both solid organ transplant ("SOT") and bone marrow transplants ("BMT") and can be conducted by using four types of tests: (i) serology; (ii) Sequence Specific Primers ("SSP"); (iii) Sequence Specific Oligonucleotides ("SSO"); and (iv) Sequence Based Typing ("SBT").
281. The Parties' activities only overlap in the supply of SSP typing kits.

IV.F.1 Product market definition

282. The Notifying Party submits that each type of HLA typing tests (serology, SSP, SSO and SBT) constitutes a distinct product market and that a further segmentation in terms of resolution (low vs high)²¹⁰ should not be considered.
283. There are no Commission precedents dealing specifically with HLA typing.

²⁰⁸ See Commission Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31, 5.2.2004, p. 5, paragraph 67.

²⁰⁹ Human Leukocyte Antigen is a key component of the immune system.

²¹⁰ High resolution SSP kits allow identifying HLA alleles to at least four-digit level while low resolution SSP kits identify alleles at two-digit level.

284. In line with the Notifying Party's claims, respondents to the Commission's requests for information confirmed that there are significant differences between the various types of HLA typing tests (serology, SSP, SSO and SBT) in terms of characteristics, performance, price and technologies used.²¹¹
285. From a supply-side perspective, the market investigation confirmed that each of HLA typing tests requires different technologies and expertise. Thus a supplier of SSP typing kits would not be able to start production and sales of other types of HLA typing kits swiftly and without significant costs.²¹² By contrast, the market investigation showed that although there are differences between high and low resolution SSP typing kits, a supplier of low resolution SSP typing kits could easily and without significant costs enter the supply of high resolution SSP typing kits.²¹³
286. From a demand-side perspective, most of the replies to the Commission's requests for information confirmed that SSP typing kits and other types of HLA typing kits are distinct products fulfilling different needs. Moreover, a number of customers indicated that SSP typing kits can also be used to resolve ambiguities found when using other testing (e.g. SBT or SSO) in some specific cases. For example, SSP high resolution is generally used to resolve SBT ambiguities.²¹⁴
287. In the light of the above, the Commission considers that SSP typing kits constitute a separate product market from other types of HLA typing kits (serology, SSO and SBT). For the purpose of this decision, the Commission considers that a further segmentation between high and low resolution may be left open as this would not change the outcome of the competitive assessment in this case.

IV.F.2 Geographic market definition

288. The Notifying Party considers that the relevant geographic market for HLA typing, including SSP typing kits, is EEA-wide due to the following reasons: (i) the suppliers of SSP typing kits are active globally; (ii) the transportation and storage costs are minimal; (iii) there is a common regulatory framework across the EEA and the products are technically the same; and (iv) the prices between Member States are similar.
289. The responses to the Commission's requests for information indicated that suppliers have one or few production facilities that supply HLA typing kits all across the EEA and the rest of the world. Moreover, EEA customers have the same technical and commercial needs and there are not significant barriers in terms of costs or regulatory

²¹¹ See replies to question 13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013. See replies to question 12 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 9 October 2013

²¹² See replies to question 17 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013

²¹³ See replies to questions 23 and 24 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013

²¹⁴ See replies to questions 14 and 16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 9 October 2013

barriers to source HLA typing kits from one geographic area to another within EEA. Nevertheless, some respondents claimed that prices differs from one country to other and some customers prefer purchasing HLA typing kits from suppliers located near them.²¹⁵

290. For the purpose of this decision, the Commission considers that the precise geographic market definition can be left open as this would not change the outcome of the competitive assessment in this case.

IV.F.3 Assessment

291. The Parties' activities overlap only in the supply of SSP typing kits. At EEA level, the Parties' combined market share in the supply of SSP typing kits is [10-20]%. At national level, the Parties' highest market shares would be [50-60]% in Austria and [30-40]% in the United Kingdom.²¹⁶
292. On a narrower market distinguishing between SSP *high* and SSP *low* resolution, the Parties' combined market shares at EEA level would be [10-20]% and [5-10]%, respectively. At national level, the Parties' highest market shares for SSP high resolution would be [30-40]% in Cyprus and [30-40]% in the United Kingdom.²¹⁷ On a possible market for SSP low resolution at national level, the Parties' highest market shares will be [90-100]% in Austria, [50-60]% in Cyprus and [40-50]% in the United Kingdom.²¹⁸
293. Post-Transaction, the remaining strong competitors will be Allenex/Olerup, Immucor/Genprobe, BioRad, BAG Healthcare and Abbot.
294. The Notifying Party submits that the Transaction would not give rise to a significant impediment to effective competition since the Parties' products for HLA typing are complementary, the Parties will achieve a modest combined share in the only overlap segment for HLA typing, i.e. SSP typing kits, and the Parties will face several strong competitors post-Transaction.
295. The vast majority of the respondents to the Commission's requests for information indicated that they do not expect that the Transaction will have a negative impact on competition and/or prices.²¹⁹

²¹⁵ See replies to questions 27- 30 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013. See replies to questions 27- 32 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 9 October 2013.

²¹⁶ In the remaining national markets, the Parties' combined position is limited or the increment brought about by the Transaction is insignificant.

²¹⁷ In the remaining national markets, the Transaction would lead only to affected markets in Italy and Greece with a combined market share of [20-30]% with and an insignificant increment, respectively.

²¹⁸ In the remaining national markets, the Transaction would lead only to an affected markets in Sweden with a combined market share of [20-30]%.

²¹⁹ See replies to questions 53 and 54 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013. See replies to questions 54 and 55 of

296. The market investigation showed that competitors are active across all Member States and a supplier would be able to start supplying easily and without significant costs to other Members States.²²⁰ Moreover, most of the customers indicated that there are sufficient alternative and credible competitors.²²¹
297. In addition, the market investigation confirmed that there have been new entries during the last three years, the market is not characterised by capacity constraints and the Parties are not viewed as the closest competitors.²²²
298. Finally, it should be noted that even under the narrowest hypothetical geographic scope for HLA typing and sub-segments (low and high resolution),²²³ the Transaction would not have a negative impact on competition. In the United Kingdom, the increment brought about the Transaction is *de minimis* (less than 5%). In Austria and Cyprus, the Parties would have small combined sales, namely [...] for total Thermo Fisher's sales in Austria and [...] for total Life Technologies' sales in Cyprus. In addition, as mentioned above, the Parties would face competition constraints from strong competitors who are active across the EEA and able to increase the production of SSP typing kits easily and without significant costs.
299. In the light of the above, the Commission concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the supply of HLA typing kits.

IV.G. PROTEIN BIOLOGY

300. Protein biology is the study of the structure and function of proteins, an essential constituent of cells. The study of proteins is central to understanding cellular functioning and, in particular, to better understanding the link between proteins, genes and diseases. Researchers and biopharmaceutical companies study defective proteins that are implicated in particular diseases in order to develop new drugs that either alter the shape of a defective protein or mimic a missing one.
301. The Transaction would lead to affected markets in the supply of products for the following techniques used in the study of proteins.

the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 9 October 2013.

²²⁰ See replies to questions 27, 34 and 35 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 9 October 2013

²²¹ See replies to question 38 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 9 October 2013

²²² See replies to questions 48-50 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013

²²³ This would be at national level, where the Parties would have a strong position in Austria, Cyprus and the United Kingdom.

IV.G.1 SDS-PAGE

302. SDS-PAGE (sodium dodecyl sulphate polyacrylamide gel electrophoresis) is a technique used to separate single or multiple proteins from a complex mixture by exploiting differences in the electrophoretic mobility of different protein molecules.
303. The Parties' activities overlap in the supply of vertical gel boxes, power suppliers, pre-cast gels, standards and gel stains ("the SDS-PAGE products").

IV.G.1.a Product market definition

304. The Notifying Party submits that each of the SDS-PAGE products constitutes a distinct product market and that no further segmentation should be considered. The market investigation has brought no elements pointing to a different conclusion on these product markets.

IV.G.1.b Geographic market definition

305. The Notifying Party submits that the markets for SDS-PAGE products are at least EEA-wide in scope. The market investigation has brought no elements pointing to different conclusions on these geographic markets.

IV.G.1.c Assessment

306. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets comprised within this area.

IV.G.2 Western Blotting

307. Western blotting is a technique used to identify specific proteins after they have been isolated by electrophoresis. With respect to products used in Western blotting, the Parties' activities overlap in the supply of transfer boxes, membranes and chemiluminescent substrates.

IV.G.2.a Product market definition

308. The Notifying Party submits that each of the abovementioned three Western blotting products constitutes a separate product market. Within membranes, the Notifying Party submits that the two types of Western blotting membranes (nitrocellulose or polyvinylidene difluoride (PVDF)) are interchangeable.
309. The market investigation confirmed that transfer boxes, membranes and chemiluminescent substrates are separate products, because each of them fulfils entirely different needs. However, respondents to the Commission's requests for information considered that the two types of Western blotting membranes are different in terms of performance, characteristics and prices.
310. The Commission considers that it can be left open whether nitrocellulose membranes and PVDF membranes would constitute separate product markets, as this would not change the outcome of the competitive assessment in this case.

IV.G.2.b Geographic market definition

311. The Notifying Party submits that the markets for Western Blotting products are at least EEA-wide in scope. The market investigation has brought no elements pointing to different conclusions on these geographic markets.

IV.G.2.c Assessment

312. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets comprised within this area.

IV.G.3 Protein Modification

313. Protein modification refers to the artificial modification of the properties of the original protein in order to study their shape and how they interact with other molecules.
314. There are three main methods which use different reagents to modify proteins: (i) chemical modification; (ii) cross-linking and (iii) adding proteases. The Parties' activities overlap in the supply of these three types of protein modification reagents.

IV.G.3.a Product market definition

315. The Notifying Party submits that the three types of protein modification reagents perform different functions. The market investigation seems to confirm that the three reagents constitute different markets since they do not appear substitutable due to the differences in terms of characteristics, performance and prices.

IV.G.3.b Geographic market definition

316. The Notifying Party submits that the markets for protein modification reagents are at least EEA-wide in scope. The market investigation has brought no elements pointing to different conclusions on these geographic markets.

IV.G.3.c Assessment

317. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets comprised within this area.

IV.G.4 Dyes

318. Dyes are products used across a range of techniques mentioned above to create colour, chemiluminescence or fluorescence for detecting, identifying and quantifying a target molecule. The Parties' activities overlap in the supply of reactive dyes.

IV.G.4.a Product market definition

319. The Notifying Party submits that reactive dyes are used in applications that require a significantly higher level of specificity and sensitivity of analysis than other types of dyes can provide, and thus there is limited substitutability from a demand-side perspective. The market investigation has brought no elements pointing to a different conclusion on this product market.

IV.G.4.b Geographic market definition

320. The Notifying Party submits that the markets for protein modification reagents are at least EEA-wide in scope. The market investigation has brought no elements pointing to different conclusions on these geographic markets.

IV.G.4.c Assessment

321. In the light of the elements referred to in paragraph 12 above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets comprised within this area.

IV.H. FLUOROMETERS

322. Fluorometers are devices used in fluorescent spectroscopy which involves the examination of the intensity and wavelength of emissions of light from electrons in molecules.

323. There are four types of fluorometers: (i) filter fluorometers, (ii) spectrofluorometers, (iii) luminometers and (iv) lifetime fluorometers. The Parties' activities only overlap in the supply of filter fluorometers.

IV.H.1 Product market definition

324. The Notifying Party submits that it is appropriate to adopt a product market encompassing all four types of fluorometers since there is a degree of demand-side substitutability, because all fluorometers utilise a similar process and are capable of quantifying nucleic acid or protein samples. In addition, the Notifying Party submits that the manufacturers tend to supply different types of fluorometers rather than focusing on one particular type.

325. The responses to the Commission's requests for information showed that there are significant differences between the different types of fluorometers for example in terms of price, performance, suitability to particular processes and the number of suppliers.²²⁴

326. From a supply-side perspective, the market investigation showed that the suppliers of fluorometers are not able to start production and sales of other types of fluorometers (where they are not already active) swiftly and without significant costs, mainly due to time and investment associated with the development of a new instrument.²²⁵

327. From a demand-side perspective, most of the replies to the Commission's requests for information confirmed that the different types of fluorometers are distinct products

²²⁴ See replies to question 29 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013. See replies to question 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

²²⁵ See replies to question 28 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013.

fulfilling distinct needs. Many customers indicated that the type of the fluorometer is application-specific.²²⁶

328. However, for the purpose of this decision, the Commission considers that the precise product market definition can be left open as this would not change the outcome of the competitive assessment in this case.

IV.H.2 Geographic market definition

329. The Notifying Party submits that the market for fluorometers is at least EEA-wide in scope.

330. The responses to the Commission's requests for information indicated that there are no barriers as such to sourcing fluorometers from outside the EEA, although transport costs and delivery time are mentioned in many replies as possible barriers.²²⁷

331. For the purpose of this decision, the Commission considers that the precise geographic market definition can be left open as this would not change the outcome of the competitive assessment in this case.

IV.H.3 Assessment

332. In a potential market encompassing all four types of fluorometers, the Parties' combined market share would be [5-10]% at EEA level. At worldwide level, the Parties' combined market share would be [5-10]%.

333. On a narrower potential market encompassing only filter fluorometers, the Parties' combined market share in the EEA would be [40-50]% with an increment of [5-10]% by Thermo Fisher. At worldwide level, the Parties' combined market share for filter fluorometers would be [50-60]% with an increment of [10-20]% by Thermo Fisher.

334. Post-Transaction, there will be enough competitors in the market such as Promega, Jasco Jenway, Agilent Technologies, Bio-Rad and Expedeon.

335. The Notifying Party submits that the Transaction would not give rise to anti-competitive effects in the fluorescent spectroscopy space. The Notifying Party submits that the Parties' presence [...].

336. Most of the respondents to the Commission's requests for information indicated that they do not expect that the Transaction will have a negative impact on the market for fluorometers. The majority of customers indicated that there will still be many alternative suppliers in the market.²²⁸

²²⁶ See replies to question 29 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

²²⁷ See replies to question 34 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

²²⁸ See replies to question 49 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

337. Furthermore, the market investigation showed that customers tend to source fluorometers from more than one supplier²²⁹ and the majority of respondents did not identify a clear market leader for fluorometers.²³⁰ In addition, the majority of respondents indicated that they can easily switch between various suppliers.²³¹
338. In the light of the above, the Transaction does not give rise to serious doubts as to its compatibility with the internal market in any of the potential markets comprised within this area.

IV.I. DISTRIBUTION

339. Thermo Fisher is active as a distributor of both its own and third party products on a worldwide basis, and in particular in the EEA, through its distribution business Fisher Scientific (referred to hereafter as the "Customer Channels Group" or "CCG"). CCG distributes a broad range of laboratory and life science products, including laboratory equipment (such as microscopes, weighing balances, freezers and centrifuges) and consumables (such as plastic ware, glassware, chemicals, reagents and laboratory supplies). Life Technologies is only active as a manufacturer²³² and uses [...] direct sales as a route to market in the EEA. However, Life Technologies also sells a proportion of its products through third-party distributors, including CCG.
340. The Transaction therefore gives rise to vertically affected markets in the distribution of laboratory and life science products.

IV.I.1 Product market definition

341. The Notifying Party submits, in line with Commission precedents,²³³ that distributors are able to offer life science customers a wide range of products from different manufacturers, allowing customers to purchase many products from a single catalogue, and simplifying customers' procurement processes, and that the components of this service do not differ according to the nature of the product being distributed. The Notifying Party therefore submits that the relevant product market for distribution comprises the distribution of all laboratory and life science products.

²²⁹ See replies to question 27 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

²³⁰ See replies to question 41 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 9 October 2013. See replies to question 36 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

²³¹ See replies to question 38 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 10 October 2013.

²³² Life Technologies also has a *de minimis* activity in the reselling of third party products, of less than [...] in 2012.

²³³ See case COMP M. 4242 *Thermo Electron/Fisher Scientific*.

342. The market investigation has confirmed that most distributors offer a range of products encompassing both life science products and other laboratory equipment and consumables. Moreover, customers source through distributors for reasons including convenience, one-stop-shopping and ease of access to a wide range of products.²³⁴
343. The market investigation has also confirmed that the distribution of clinical diagnostics, including for instance HLA typing tests (see section IV.F above), constitutes a separate product market due to specific regulatory and technical requirements, the importance of long term contracts and exclusivity agreements, as well as different levels of sales support, after-sales service and technical input from salespersons.²³⁵
344. The Commission therefore concludes that the relevant product market is likely to be the distribution of laboratory and life science products.

IV.I.2 Geographic market definition

345. In *Thermo Electron/Fisher Scientific*, the Commission has taken the view that the appropriate geographic market definition for distribution of laboratory products is national in scope.
346. The market investigation has confirmed that most distributors operate in a single Member State,²³⁶ and that most of the cross-border distributors such as CCG, VWR, Sigma-Aldrich, Dominique Dutscher and 2B Scientific organize their sales forces at national level and offer different catalogues in different Member States.²³⁷
347. Moreover, most distributors consider that customer prices for life science products and conditions for sales (such as the importance of tenders, the scope of such tenders, the presence of centralized purchasing, etc.) differ significantly between different EEA countries.²³⁸
348. Finally, most distributors have indicated that commercial negotiations with their customers for their procurement of life science products take place at national level.²³⁹

²³⁴ See replies to question 7 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²³⁵ See replies to questions 9 and 10 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013. The Commission notes that CCG is not active in the distribution of clinical diagnostics.

²³⁶ See replies to question 6 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²³⁷ See replies to questions 11 and 12 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²³⁸ See replies to questions 13 and 14 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²³⁹ See replies to question 15 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

349. In light of the above, the Commission concludes that the relevant geographic market for the distribution of laboratory and life science products is national in scope.

IV.I.3 Assessment

350. The market investigation has confirmed the basic characteristics of the markets for the distribution of laboratory and life science products, as outlined by the Commission in *Thermo Electron/Fisher Scientific*.

IV.I.3.a Competitive dynamics in distribution markets

351. National markets for the distribution of laboratory and life science products are characterised by a high number of players. Whereas the vast majority of distributors are only active in one Member State, some operate in more than one, such as Dominique Dutscher (UK and France), Euroclone (Italy, Spain, Greece, Germany), Omnilab (Germany and Netherlands) or Analis (France and Belgium). Only VWR and CCG and, to a limited extent, Sigma-Aldrich, have a truly pan-European presence across the EEA. In certain Member States, direct sales by manufacturer might play an important role, in particular for the more technically sophisticated products.

352. As mentioned in section IV.I.1 above, distributors of laboratory and life science products usually offer a range of products which they source from different manufacturers. The basket of goods provided by distributors comprises the offering of a very wide range of products (in the order of hundreds or thousands) to customers as well as some ancillary services, such as logistics, inventory management, marketing, product advisory and if necessary, after-sales services. The market investigation has also confirmed that the majority of distributors offer competing brands in their product portfolio.²⁴⁰

IV.I.3.b Impact of the Transaction

353. During the market investigation some respondents indicated that the Merged Entity might be in a position to foreclose its competitors from the market. The Commission has carefully analysed the vertical effects of the merger and concluded that the Merged Entity would lack the ability and incentive to restrict access to input for distributors or to foreclose access of competing manufacturers to customers for the reasons outlined below.

IV.I.3.b.a Input foreclosure

354. According to the concerns voiced by some market players, the Merged Entity may decide to streamline its route to market by ending Thermo Fisher's and Life Technologies' supply relationships with independent distributors and focusing their route to market on CCG, thereby foreclosing other distributors from access to the Merged Entity's portfolio. Overall, a number of the market players indicating the risk of input foreclosure were some of the Parties' independent distributors whose main concerns were related to the possible termination of their supply contracts

²⁴⁰ See replies to question 21 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

post Transaction.²⁴¹ Final customers did not voice concerns with regard to the vertical effects of the Transaction.

355. The market investigation has confirmed that there are no "must-have" brands for distributors of laboratory and life sciences products.²⁴² Streamlining the sale of Thermo Fisher and/or Life Technologies products via the new Merged Entity would therefore not change the current competitive environment from the point of view of distributors, except in the specific product areas where the Merged Entity may acquire market power through the Transaction. These product areas are analysed in sections IV.C to IV.H above, and the proposed commitments would effectively remove the serious doubts raised, as analysed in section V.B below.
356. The Commission further notes that as regards other product areas where Life Technologies enjoyed a strong position before the merger, the Transaction will not change the competitive environment from the point of view of other distributors, given that more than [...]% of Life Technologies' 2012 EEA sales were realised through direct sales and that CCG was already [...] EEA distributor before the merger as regards Life Technologies' remaining sales.²⁴³
357. Moreover, as indicated by the Parties and confirmed by the market investigation, final costumers' primary aspect of choice relates to products they wish to acquire and not to a certain distributor(s).²⁴⁴ Final customers typically apply either a multi-sourcing strategy or conclude agreements based on tender procedures with a certain distributor for a certain period of time. According to the market investigation, switching to another distributor does not appear to be problematic for customers. Given the purchasing patterns in the industry, even if the Merged Entity would decide to sell only via its own distribution system, final customers would have the possibility to switch and to be supplied by other distributors with alternative products.
358. Finally, as less than [...]% of Life Technologies' sales in the EEA are realised through CCG, that CCG achieves market shares below 15% in all national downstream distribution markets,²⁴⁵ [...],²⁴⁶ the Merged Entity would be unlikely to recoup at distribution level or through margins on direct sales the losses incurred at manufacturing level by the exclusion of efficient distributors commanding access to a particular customer base. It does not therefore seem to be profitable for the Merged Entity to exclude other efficient distributors from its sales.

²⁴¹ See replies to question 48 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²⁴² See replies to question 38 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013

²⁴³ See Form CO, paragraph 6.34.

²⁴⁴ As regards the areas where the Merged Entity would likely acquire market power through the Transaction, the proposed commitments would effectively remove the serious doubts raised, as analysed in section V.B below.

²⁴⁵ See Parties' estimates in General Annex 18 of the Form CO.

²⁴⁶ See transaction data submitted by the Parties.

359. The Commission therefore concludes that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to possible input foreclosure towards other distributors of laboratory and life science products in the EEA.

IV.I.3.b.b Customer foreclosure

360. During the market investigation, a number of manufacturers of life science products expressed concerns that the Merged Entity might decide not to distribute any more competing manufacturers' products or to substantially worsen the terms of such distribution, thereby excluding competitors' access to CCG's distribution network and ultimately to final customers. Competitor Promega stated in this respect that "[f]requently, many institutions have contracts with VWR or Fisher slating them as the preferred vendor, making it difficult for the end user to purchase directly from any other company."²⁴⁷

361. The Notifying Party submits that CCG will continue to operate on a competitively neutral, arm's length basis from Thermo Fisher's other businesses and will continue to distribute products supplied by a wide range of third party manufacturers.

362. In assessing the likelihood of a customer foreclosure scenario, the Commission has first examined whether the Merged Entity would have the ability to foreclose access to downstream markets by reducing its purchases from its upstream rivals.²⁴⁸ In this respect, for customer foreclosure to be a concern, it must be the case that the vertical merger involves a company which is an important customer with a significant degree of market power in the downstream market.²⁴⁹

363. First, the Commission notes that across the EEA as a whole, VWR is the clear market leader in terms of sales and achieves significantly higher market shares than CCG in the markets for the distribution of laboratory and life science products.²⁵⁰ This finding also holds true in Member States where CCG achieves significant presence. With its size and product coverage, VWR will remain the strongest distributor in the market, especially for customers that tend to consolidate purchases. In this respect, the market investigation has confirmed that other manufacturers see VWR as a stronger distributor than CCG in Europe. Lonza stated for instance that "*VWR is the main global distributor besides Fisher and has very few own brands (private label only). Lonza also distributes the same products through VWR because many pharma companies have VWR as a*

²⁴⁷ See Promega's reply to question 158 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 7 October 2013.

²⁴⁸ Paragraph 59, Non-horizontal Mergers Guidelines

²⁴⁹ Paragraph 61, Non-horizontal Mergers Guidelines

²⁵⁰ The Notifying Party estimates that VWR achieved sales of third party products of EUR 1.2 billion across the EEA in 2012, compared with CCG's sales of third party products of EUR [...]. See also General Annex 18 to the Form CO for market shares at national level.

preferred supplier. While VWR is stronger in Europe, globally Fisher is the number one and is performing better."²⁵¹

364. Second, the Commission considers that direct sales by competing manufacturers represent a real alternative for life science manufacturers to reach final customers. The Commission notes in this respect that direct sales represent the main route to market for the Parties overall. In the case of Life Technologies, direct sales represent more than [...] % of its revenues from life science products in the EEA overall.²⁵² For Thermo Fisher, the proportion of direct sales is also high (with the exception of fluorescent spectroscopy where sales are mainly done through third party-distributors), reaching [...] % in the segment of cell culture for bioproduction. In addition, Thermo Fisher transaction data shows that a proportion of customers purchase similar products through direct sales and through CCG. According to the market investigation, other important suppliers such as Roche, Merck Millipore, Sigma-Aldrich, Bio-Rad, New England Biolabs and Promega have direct distribution capabilities and hence would not be vulnerable to a hypothetical customer foreclosure strategy.
365. Third, the Commission notes that the only suppliers that could be potentially foreclosed as a result of the Transaction would be those that, at present, choose third party distributors to sell part of or their entire product ranges. In this respect, the Parties have provided market shares in the market for distribution of third party products (i.e. excluding sales of own products). Overall in the EEA, the Parties' combined market share²⁵³ is in the range of [5-10]%.²⁵⁴ At national level, this percentage is higher only in the Czech Republic ([10-20]%), France ([5-10]%), Ireland ([10-20]%), the Netherlands ([10-20]%), Spain ([5-10]%) and the UK ([10-20]%). The Commission therefore concludes that CCG's shares in the distribution of third party products are below [10-20] % in all Member States, and do not support claims of market power at distribution level.²⁵⁵
366. Fourth, the market investigation has also shown that most market participants do not see any significant obstacles for a manufacturer of life science products to find distribution partners in the EEA.²⁵⁶ In addition, most respondents to the market investigation indicated that final customers multi-source among distributors of laboratory and life

251 See minutes of conference call with Lonza. Eppendorf also declared that "*Fisher Scientific is an important contractual partner everywhere in Europe (...), second to VWR. There are also local distributors and manufacturers' direct sales force.*"

252 See transaction data submitted by the Parties.

253 See footnote 232 above.

254 Parties' estimates.

255 The Commission further notes that significant competitors to CCG exist in all above-mentioned Member States, including VWR and Sigma-Aldrich. In addition, according to Parties' estimates, Dominique Dutscher enjoys a market position of [5-10] % in France, while SLS enjoys a [5-10] % market share in the UK. The Commission notes that Westburg is also a significant competitor in the Netherlands, while Cultek and Teknovas have a substantial presence in Spain.

256 See replies to question 41 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

science products.²⁵⁷ Furthermore, most distributors have indicated that they are able and willing to distribute another brand in a variety of areas.²⁵⁸ The Commission therefore considers that there is no barrier for competing manufacturers to distribute their products through third-party distributors.

367. Fifth, the Commission notes that some of CCG's contracts with third party suppliers include [...],²⁵⁹ [...].²⁶⁰
368. As regards concerns raised by a few market participants concerning foreclosure strategies limited to large pharma and biotech companies that tend to consolidate their supplies, [...].²⁶¹ This indicates that this customer segment may possess a degree of buyer power vis-à-vis suppliers and distributors for their overall purchases of laboratory and life science products.²⁶² Moreover, even for this customer segment, CCG would continue to face competition from VWR, Sigma-Aldrich and other large competitors present across the board in the supply of life science products.²⁶³
369. The Commission concludes that even if the Merged Entity were to decide to entirely cease current distribution agreements with competing manufacturers, these competitors will not be foreclosed from distributing their products in the EEA, either through direct sales or through other distributors. Alternative available distributors include the leading independent distributor VWR which has a larger market share than CCG in all European markets and a large number of cross-border and national distributors.
370. The Commission concludes that the Merged Entity will be likely unable to foreclose customers from other life science manufacturers through the CCG distribution platform after the merger.
371. Finally, the Transaction does not appear, in any event, to significantly increase the economic incentives for Thermo Fisher to exclude other manufacturers as CCG suppliers. In 2012, CCG derived [...] of its EEA revenues from distributing Thermo

²⁵⁷ See replies to question 37 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²⁵⁸ See replies to question 40 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²⁵⁹ CCG's contract with [...] foresees for instance that CCG will not "[...]", see submission of the Parties of 13 September 2013.

²⁶⁰ See minutes of conference call with [distribution supplier].

²⁶¹ See transaction data submitted by the Parties.

²⁶² As regards the specific areas where the Merged Entity would likely acquire market power through the Transaction, the proposed commitments would effectively remove the serious doubts raised, as analysed in section V.B below.

²⁶³ While concerned about the impact of the Transaction, Lonza stated in this respect that "*Many larger customers do not even buy from smaller suppliers as they prefer to buy through larger resellers out of convenience. Such preferred suppliers are often Fisher, VWR, Life Technologies, Sigma-Aldrich or GE.*" See minutes of conference call with Lonza.

Fisher products and [...] through the sale of Life Technologies products.²⁶⁴ Foreclosure would imply the loss of a proportion of CCG sales, which is likely to be all the more important since a majority of distributors highlighted that customers can switch easily between distributors, see demand as pulled rather than pushed,²⁶⁵ and do not regard any product or brand as a "must-have" at distribution level.²⁶⁶ [...],²⁶⁷ [...].

IV.1.3.c Conclusion

372. In the light of the above considerations, the Transaction does not give rise to serious doubts as to its compatibility with the internal market as regards any of the vertically affected markets in the distribution of laboratory and life science products in the EEA.

V. REMEDIES

373. In order to render the concentration compatible with the internal market, the Parties have modified the notified concentration by entering into commitments on 5 November in relation to: (i) cell culture; (ii) gene silencing; and (iii) magnetic beads. Following the market test of these proposed commitments, the final and improved version of the commitments (the "Proposed Commitments") described below was submitted on 20 November 2013. The commitments are annexed to this Decision and form an integral part thereof.

V.A. PROPOSED COMMITMENTS

V.A.1 Cell culture

374. In order to address the serious doubts identified by the Commission in relation to cell culture, the Parties entered into the commitments annexed to this Decision as Annex I.

375. Specifically, Thermo Fisher commits to divest its entire HyClone cell culture business ("the Cell Culture Business") excluding single use technologies ("SUT"),²⁶⁸ where the Parties' activities do not overlap.

376. The Cell Culture Business, described in more detail in Annex I, includes:

- a) Thermo Fisher's sera and media processing facilities in the US, Australia, New Zealand, Singapore, and its distribution facilities in the US and Europe.

²⁶⁴ See Form CO, figure 6.1.

²⁶⁵ See for instance minutes of call with Illumina, which stated that "*A customer may tie his account to one distributor to get easier access to general-purpose reagents, but this does not necessarily make it easier for that distributor to also take over the sales of more specialized reagents.*"

²⁶⁶ See replies to questions 30 and 38 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to distributors of 10 October 2013.

²⁶⁷ See submission of the Parties of 13 September 2013.

²⁶⁸ SUT products consist of disposable plastic containers, bags, ports, tubing and fittings that may incorporate ancillary components like filters and valves. SUT products are relatively cheap and widely available from several suppliers. SUT products do not solely serve sera and media products but a wider range of life science applications. See Form CO, paragraph C.6.41.

- b) The rights to all intellectual property, technology and know-how associated with Thermo Fisher's sera and media operations, including its proprietary and media formulations.
- c) The respective licences, permits and authorisations.
- d) The respective contracts, agreements, leases, commitments and understandings.
- e) The respective customer, credit and other records.
- f) All dedicated sera and media manufacturing employees covering all areas of operation and key personnel.

V.A.2 Gene silencing

377. In order to address the serious doubts identified by the Commission in relation to gene silencing, the Parties entered into the commitments annexed to this Decision in Annex I.

378. Thermo Fisher commits to divest its gene modulation business in Lafayette, Colorado, USA (the "Gene Modulation Business").

379. The Gene Modulation Business, described in more detail in Annex I, includes:

- a) The Lafayette facility where Thermo Fisher develops and manufactures gene modulation products, including all siRNA reagents and libraries (including siGENOME, on-TARGET plus, Accell, and IncRNA); all shRNA reagents, viral particles, and libraries (including GIPZ, TRIPZ, Decode, TRC); and all miRNA reagents and libraries (including miRIDIAN; shMIMIC; RNAi controls; DharmaFECT transfection reagents; cDNA and ORF clones and gene collections; and custom RNA, DNA and other molecules).
- b) The following main intangible assets: one of a total of four licenses to the Tuschl patents granted by MIT; other intellectual property rights, technology and know-how related to the development, design and manufacture of Thermo Fisher's siRNA, shRNA and miRNA product lines (including siGENOME design, on-TARGET plus design, Accell molecule design, SMART vector design, miRIDIAN designs, shMIMIC design, SMARTchoice design, gene sequences²⁶⁹, and ACE chemistry processes²⁷⁰); the code relating to the legacy Dharmacon and Open Biosystems websites and the underlying content which support the aforementioned product lines; the rights to the Dharmacon and Open Biosystems brands, as well as the names to various product lines, such as siRNA, shRNA and miRNA product names and DharmaFECT.
- c) The relevant contracts, agreements, leases, commitments and understandings, including relevant customer records.
- d) All relevant employees and key personnel in the Lafayette facility.

²⁶⁹ Through an exclusive license.

²⁷⁰ The transfer of ACE chemistry processes is subject to a licence back for applications outwith gene silencing.

V.A.3 Magnetic beads

380. In order to address the serious doubts identified by the Commission in relation to magnetic beads (see section IV.E above), the Parties entered into the commitments annexed to this Decision in Annex I.
381. Pursuant to the Proposed Commitments, Thermo Fisher would commit to divest its magnetic beads business, excluding its facilities used for the production and supply of magnetic beads in Fremont, California.
382. The Magnetic Bead Business, described in more detail in Annex I, includes:
- a) Thermo Fisher's equipment used in the manufacture of magnetic beads, or, at the option of the purchaser, equivalent new equipment (to be acquired by Thermo Fisher).
 - b) The following main intangible assets: the Sera-Mag and Sera-Mag SpeedBeads brand names and associated trademarks; patents relating to the manufacture of magnetic beads with negligible residual magnetism and the reduction of response time of the beads to a magnet; and access to Thermo Fisher's transfer plan relating to the execution of its recent move of Thermo Fisher's magnetic bead production facilities from Indianapolis, Indiana, to Fremont, California.
 - c) The respective main licences, permits and authorisations.
 - d) The respective main contracts, agreements, leases, commitments and understandings.
 - e) The respective customer, credit and other records.
 - f) All employees whose function predominantly relates to the manufacture and supply of magnetic beads and key personnel.

V.B. ASSESSMENT OF THE PROPOSED COMMITMENTS

383. Where a concentration raises serious doubts as to its compatibility with the internal market, the Parties may undertake to modify the operation so as to remove the grounds for the serious doubts identified by the Commission with a view to having the transaction approved in phase I of the merger review procedure.
384. As set out in the Commission Notice on remedies²⁷¹ the commitments have to eliminate the competition concerns entirely and have to be comprehensive and effective from all points of view and must be capable of being implemented effectively within a short period of time as the conditions of competition on the market will not be maintained until the commitments have been fulfilled.²⁷²
385. In assessing whether or not the remedies will restore effective competition, the Commission considers the type, scale and scope of the remedies by reference to the

²⁷¹ Commission Notice on remedies.

²⁷² Commission Notice on remedies, paragraph 9.

structure and the particular characteristics of the market in which the competition concerns arise.²⁷³

386. Divestiture commitments are the best way to eliminate competition concerns resulting from horizontal overlaps.²⁷⁴ Other commitments (such as licensing) may be suitable to resolve competitive concerns if those remedies are equivalent to divestitures in their effects. The divested activities must consist of a viable business that, if operated by a suitable purchaser, can compete effectively with the Merged Entity on a lasting basis and that is divested as a going concern.²⁷⁵
387. The business must include all the assets which contribute to its current operation or which are necessary to ensure its viability and competitiveness and all personnel which are currently employed or which are necessary to ensure the business' viability and competitiveness. Personnel and assets which are currently shared between the business to be divested and other businesses of the parties, but which contribute to the operation of the business or which are necessary to ensure its viability and competitiveness, must also be included. Otherwise, the viability and competitiveness of the business to be divested would be endangered. Therefore, the divested business must contain the personnel providing essential functions for the business such as, for instance, group R&D staff — at least in a sufficient proportion to meet the on-going needs of the divested business.²⁷⁶
388. Furthermore, the intended effect of the divestiture will only be achieved if and once the business is transferred to a suitable purchaser with proven relevant expertise and ability to maintain and develop the divested business as a viable and active competitive undertaking.

V.B.1 Cell culture

389. In response to the Commission's concerns regarding sera and media for cell culture, Thermo Fisher has committed to divest its HyClone cell culture business including both the sera and the media businesses.
390. In the present case, the Commission launched a market test regarding the proposed commitments in order to check whether they were sufficient to clearly rule out the serious doubts identified by the Commission. In general, the market test of the proposed commitments has confirmed that the commitments are comprehensive, effective and capable of being implemented effectively and therefore suitable to eliminate the serious doubts identified in media and sera for cell culture.

²⁷³ Commission Notice on remedies, paragraph 12.

²⁷⁴ Commission Notice on remedies, paragraph 17.

²⁷⁵ Commission Notice on remedies, paragraph 23.

²⁷⁶ Commission Notice on remedies, paragraphs 25 and 26.

391. The vast majority of competitors and customers expressed the view that the divestment of HyClone would remove the serious doubts raised by the Transaction.²⁷⁷ HyClone is a viable business that can compete effectively in cell culture. Moreover, the intellectual property rights and know-how included in the divestment business are sufficient for its viability and competitiveness. The arrangements for the transfer of intellectual property rights as well as customer and distribution contracts were also deemed feasible and sufficient,²⁷⁸
392. During the market test, the majority of competitors and customers stressed that a six-month licence to the purchaser in order to use during this transitional period the Thermo Fisher Scientific brand for selling the existing media and sera inventory would be too short. The purchaser would need much longer to sell this inventory. Rebranding of these sensitive products would be prohibitively expensive.²⁷⁹ However, Thermo Fisher addressed this concern in the final commitments by committing to provide a two-year licence for the purchaser to use during this transitional period the Thermo Fisher Scientific brand for selling the existing media and sera inventory.
393. Furthermore, as regards purchaser requirements, several competitors and customers had stated that the purchaser should be already active in the life science industry.²⁸⁰ However, Thermo Fisher addressed this concern in the final commitments by explicitly committing to divest the Cell Culture Business to a purchaser with a proven manufacturing expertise in the life sciences sector. This should ensure that the Cell Culture Business is divested to a purchaser that can develop it as a viable and effective force in the supply of sera and media for cell culture.

²⁷⁷ See replies to questions 1 and 2 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013; See replies to questions 1 and 2 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 November 2013; See replies to questions 1 and 2 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 November 2013.

²⁷⁸ See replies to questions 3-6 and 8-13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013; See replies to questions 3-6 and 8-13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 November 2013; See replies to questions 3-6 and 8-13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 November 2013.

²⁷⁹ See replies to question 7 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013; See replies to question 7 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 November 2013; See replies to question 7 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 November 2013.

²⁸⁰ See replies to question 16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013; See replies to question 16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 November 2013; See replies to question 16 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 November 2013.

394. Finally, almost all competitors and customers consider that the Cell Culture Business is sufficiently interesting to attract suitable purchasers. A considerable number of credible market players have already expressed an interest in acquiring it.²⁸¹
395. In view of the above, the Commission concludes that the Proposed Commitments are suitable and sufficient to eliminate the serious doubts raised by the Transaction in the areas of sera and media for cell culture.

V.B.2 Gene silencing

396. The majority of competitors and customers confirmed that, subject to certain caveats, the divestment of the Gene Modulation Business would remove the serious doubts raised by the Commission, both for siRNA reagents and miRNA reagents.²⁸² The same majority indicated that, subject to certain caveats, the Gene Modulation Business is a viable business that can compete effectively and on a lasting basis in the gene silencing area.²⁸³
397. The vast majority of respondents confirmed that, as such, the production assets and other tangible assets are sufficient to ensure that the purchaser of the Gene Modulation Business can compete effectively and on a lasting basis in the gene silencing area. The majority of respondents reached the same conclusion for the brands, patents, know-how and other intangible assets that are to be part of the Gene Modulation Business. Respondents highlighted in particular that Dharmacon is a strong brand, and that the purchaser of the Gene Modulation Business would have an important IPR advantage by obtaining a Tuschl patent licence under competitive conditions.²⁸⁴
398. The majority of respondents confirmed that the personnel to be included in the Gene Modulation Business was sufficient, but highlighted that the purchaser would have to

²⁸¹ See replies to questions 17-18 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013; See replies to question 17 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 November 2013; See replies to question 17 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 November 2013.

²⁸² See replies to questions 1 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013, and of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 November 2013

²⁸³ See replies to questions 2 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013, and of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 November 2013

²⁸⁴ See, for instance, replies of Agilent and Qiagen to question 12 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013.

compensate for the relatively small number of sales personnel included in the business, and its lack of global distribution capabilities.²⁸⁵

399. The arrangements for the transfer of the various assets, including the intellectual property rights and the customer contracts were deemed feasible and sufficient,²⁸⁶
400. The important caveat that competitors and customers expressed was that the Gene Modulation Business can only be viable and competitive in the hands of certain purchasers. The overwhelming majority of competitors and customers confirm that the purchaser would have to have experience in life sciences.²⁸⁷ These respondents indicated that only a purchaser with such experience and track record can overcome possible obstacles in gaining acceptance by customers, and can offer the manufacturing expertise, quality control and assurance, and the global sales and distribution assets that are required to be an effective competitive force.²⁸⁸ Respondents explain that only such players can integrate the business within their existing business efficiently, and can ensure that it remains innovative and successful in introducing new products in this quickly emerging field of molecular biology.²⁸⁹
401. In addition, a significant number of respondents stated that the duration of the sub-licence of the Thermo Fisher brand to sell existing inventory (6 months) is too short.²⁹⁰ These concerns mirror the ones that were voiced for the Cell Culture Business. Importantly, the respondents who express this concern include Parties that are potentially interested in purchasing the Gene Modulation Business.
402. Subject to these two caveats, the vast majority of respondents confirmed that the Gene Modulation Business is attractive enough to attract a significant number of suitable

²⁸⁵ See, for instance, replies of Agilent, Integrated DNA Technologies, Merck Millipore, Qiagen and Sigma-Aldrich to question 8 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013.

²⁸⁶ See replies to questions 3-6 and 8-13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013; See replies to questions 3-6 and 8-13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to bioproduction customers of 8 November 2013; See replies to questions 3-6 and 8-13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to research customers of 8 November 2013.

²⁸⁷ See replies to questions 11 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013, and of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 November 2013.

²⁸⁸ See, for instance, the replies of Agilent, Merck Millipore, Promega and Qiagen to question 11 of the the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013.

²⁸⁹ See, for instance, the replies of Agilent, Integrated DNA Technologies and Merck Millipore to question 12 of the the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013

²⁹⁰ See replies to question 10 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers and competitors of 8 November 2013.

purchasers.²⁹¹ A considerable number of credible market players expressed an interest in acquiring it.²⁹²

403. Following this market test and further observations made by the Commission, Thermo Fisher has improved the commitments it had offered.
404. First, Thermo Fisher explicitly commits to divest the Gene Modulation Business to a purchaser with a proven manufacturing expertise in the life sciences sector. This should ensure that the Gene Modulation Business is divested to a purchaser that can develop it as a viable and effective force in gene silencing.
405. Second, Thermo Fisher has increased the duration of the sub-licence for the Thermo Fisher brand that it offers to the purchaser to one year. This should allow the purchaser to sell the existing inventory of the Gene Modulation Business in an effective manner.
406. Finally, and following the Commission's observations to this effect, Thermo Fisher has increased the duration of the non-solicitation clause, according to which it commits not to solicit the Key Personnel transferred with the Gene Modulation Business to [...] after the closing of the sale of the Gene Modulation Business.
407. The Commission has subsequently assessed the suitability and sufficiency of these final commitments to eliminate its serious doubts in the area of gene silencing reagents.
408. If sold to a suitable purchaser with the required manufacturing experience, the Gene Modulation Business comprises all the assets and resources that are necessary for that purchaser to be a viable and long-term effective competitive force in the supply of gene silencing reagents.
409. The purchaser will have at its disposal the strong Dharmacon brand, the Tush1 patent licence and all other relevant IP. The purchaser can couple these assets with the quality equipment and skilled personnel of Thermo Fisher, and the full breadth of its current product portfolio, know-how and general technology advantages. The purchaser can use these assets as a solid basis to further develop the Gene Modulation Business. The Commission considers that the Gene Modulation Business comprises all the assets to allow the purchaser to fully replicate the competitive constraint that Thermo Fisher has exerted in this area.
410. In view of the above, the Commission concludes that the Proposed Commitments are suitable and sufficient to eliminate the serious doubts raised by the Transaction in the area of gene silencing reagents.

²⁹¹ See replies to questions 13 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013, and of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 November 2013.

²⁹² See replies to questions 14 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to competitors of 8 November 2013 and of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers of 8 November 2013.

V.B.3 Magnetic Beads

411. The market test confirmed that, subject to certain important caveats, the Magnetic Beads business to be transferred is a viable business that can compete effectively and on a lasting basis with Life Technologies and other suppliers of magnetic beads.
412. First, the vast majority of respondents who expressed an opinion indicated that the business can only be viable and competitive in the hands of a purchaser that already has manufacturing capabilities in the life science sector.²⁹³ As Turbobeads underlines, this is particularly the case as in the current situation, Thermo Fisher's Magnetic Beads business relies on other internal business resources within Thermo.²⁹⁴
413. Second, the respondents highlighted issues concerning the implementation of Thermo Fisher's commitment to divest, at the option of the purchaser, either its current production equipment or new equipment to be purchased by Thermo Fisher. These respondents underlined that it may be complex to transfer the equipment effectively and within a reasonably short timeframe. These respondents indicate that this process can be complex given the validation and audits required by current magnetic beads customers, the potential complexity of the bead types to be divested and the need to integrate, with the assistance of experienced personnel, the equipment into existing production facilities. Qiagen highlighted that the uncertainty that the ultimate investment cost can be recouped could decrease the number of purchasers that would ultimately be interested in the Magnetic Beads Business.²⁹⁵
414. It is therefore deducible from the market test that the commitments should include further arrangements to ensure that the transition of the equipment to the purchaser is as smooth as possible and that the necessary investment cost is reduced to the extent reasonably possible.
415. Third, the majority of respondents indicated that the number of sales personnel that Thermo Fisher proposed to divest was not sufficient.²⁹⁶ These respondents reiterate that customer relationships are important in the market for magnetic beads. It follows from this that it should be ensured that the Divestment Business contains sufficient sales personnel, taking account of the existing capabilities that Thermo Fisher has in this area.
416. Finally, a significant number of respondents stated that the duration of the sub-licence of the Thermo Fisher brand to sell existing inventory (6 months) is too short.²⁹⁷ These

²⁹³ See replies to question 2 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers and competitors of 8 November 2013.

²⁹⁴ See Turbobead's reply to question 2 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers and competitors of 8 November 2013.

²⁹⁵ Qiagen's reply to question 8 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers and competitors of 8 November 2013.

²⁹⁶ See replies to question 11 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers and competitors of 8 November 2013.

²⁹⁷ See replies to question 10 of the Commission's request for information pursuant to Article 11 of the Merger Regulation addressed to customers and competitors of 8 November 2013.

concerns mirror the ones that were voiced for the Gene Modulation and Cell Culture Businesses. Importantly, the respondents who express this concern include Parties that are potentially interested in purchasing the Divestment Business.

417. Following this market test and further observations made by the Commission, Thermo Fisher has improved the commitments it had offered.
418. First, Thermo Fisher explicitly commits to divest the Magnetic Beads Business to a purchaser with a proven manufacturing expertise in the life sciences sector. This should ensure that the Magnetic Beads Business is divested to a purchaser that can develop it as a viable and effective force in the supply of polymer-based magnetic beads.
419. Second, Thermo Fisher has strengthened the arrangements for the transfer of the production equipment to the purchaser. Thermo Fisher now explicitly commits to transport and install the production equipment at a manufacturing site chosen by the purchaser. It also commits to provide further support to enable the purchaser to utilise the equipment to manufacture magnetic beads of the same type and quality as currently manufactured by Thermo Fisher. The Commission considers that this eliminates any further risk in the implementation of the commitments, ensuring that it can produce the magnetic beads with the same consistency in size and the same quality of the beads that Thermo Fisher currently produces and significantly reducing the necessary investment cost for the purchaser.
420. Third, Thermo Fisher has increased the duration of the sub-licence to Thermo Fisher brand from six months to one year. This should allow the purchaser to sell the existing inventory of polymer-based magnetic beads in an effective manner.
421. Fourth, Thermo Fisher has [increased] the number of sales personnel to be transferred with the Magnetic Beads Business. It has also ensured that the sales personnel that is to be transferred, covers all existing top customers of Thermo Fisher for the supply of polymer-based magnetic beads. This ensures that the purchaser will immediately have at its disposal the necessary sales personnel to maintain the established commercial relationships with the customers of the Magnetic Beads Business. The Commission considers that this also addresses the comments that respondents in the market test made regarding the sufficiency of the sales personnel to be transferred.
422. Finally, and following the Commission's observations to this effect, Thermo Fisher has increased the duration of the non-solicitation clause, according to which it commits not to solicit the Key Personnel transferred with the Magnetic Beads Business to [...] after the closing of the sale of that Business. This longer period will allow the purchaser to preserve the viability and competitiveness of the Magnetic Beads Business pending the transfer of equipment and other assets of that business.
423. The Commission has subsequently assessed the suitability and sufficiency of these final commitments to eliminate its serious doubts in the area of polymer-based magnetic beads.
424. The Commission considers that on the basis of the results of the market test, its own assessment of the Proposed Commitments and the improvements that Thermo Fisher has made, its serious doubts in the area of magnetic beads are eliminated.

425. If sold to a suitable purchaser, the Magnetic Beads Business comprises all the assets and resources that are necessary for that purchaser to be a viable and long-term effective competitive force in the supply of polymer-based magnetic beads. Moreover, the divestiture of the Magnetic Beads Business would remove the entire overlap in the market for the production and supply of polymer-based magnetic beads to OEM customers, where serious doubts were raised.
426. The purchaser will have at its disposal the Sera-Mag brand, associated patents and other relevant IP, coupled with the equipment, know-how and skilled personnel currently employed by Thermo Fisher. The final arrangements regarding the transfer of the production equipment explicitly ensure that the purchaser can produce magnetic beads that have the same consistency in size and the same quality that Thermo Fisher currently offers. The purchaser can use these assets to develop the Magnetic Beads further. The Commission hence considers that the Magnetic Beads business comprises all the assets that allow the purchaser to fully replicate the competitive constraint that Thermo Fisher has exerted in this area.
427. The purchaser criteria ensure that the Magnetic Beads Business is sold to a purchaser with a wide manufacturing experience in the bio science sector. These criteria ensure that the purchaser can compete on the basis of a wide presence in the life sciences field, as Thermo Fisher has done. Importantly, these criteria also ensure that the purchaser has the necessary resources and skills to integrate the equipment into an existing manufacturing site. Thermo Fisher's commitment to transport and set-up the equipment at that site, [...] and the longer non-solicitation period for the Key Personnel of the Magnetic Beads Business, eliminates the remaining implementation risk in the integration process that was identified during the market test.
428. On this basis, the Commission considers that the commitments are effective and capable of being effectively implemented.
429. In view of the above, the Commission concludes that the Proposed Commitments are suitable and sufficient to eliminate the serious doubts raised by the Transaction in the area of polymer-based magnetic beads.

VI. CONDITION AND OBLIGATION

430. Under the first sentence of the second subparagraph of Article 6(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the internal market.
431. The achievement of the measure that gives rise to the structural change of the market is a condition, whereas the implementing steps which are necessary to achieve this result are generally obligations on the Parties. Where a condition is not fulfilled, the Commission's decision declaring the concentration compatible with the internal market and the EEA Agreement no longer stands. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(6)(b) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2) and 15(1) of the Merger Regulation.

432. In accordance with the basic distinction between conditions and obligations, the decision in this case is conditional on full compliance with the requirements set out in Section B of the final commitments, which constitute conditions. The remaining requirements set out in the other Sections of the said commitments are considered to constitute obligations.
433. The full text of the final commitments is annexed to this decision as Annex I and forms an integral part thereof.

VII. CONCLUSION

434. For the above reasons, the Commission has decided not to oppose the notified operation as modified by the commitments and to declare it compatible with the internal market and with the functioning of the EEA Agreement, subject to full compliance with the conditions contained in Section B of the commitments annexed to the present decision, and with the obligations contained in the other Sections of the said commitments.
435. This decision is adopted in application of Article 6(1)(b) in conjunction with Article 6(2) of the Merger Regulation.

*For the Commission
(signed)
Joaquín ALMUNIA
Vice-President*

Case M.6944 Thermo Fisher Scientific / Life Technologies

COMMITMENTS TO THE EUROPEAN COMMISSION

Pursuant to Article 6(2) of Council Regulation (EC) No. 139/2004 as amended (the "**Merger Regulation**"), Thermo Fisher Scientific Inc. (the "**Company**") hereby provides the following Commitments (the "**Commitments**") in order to enable the European Commission (the "**Commission**") to declare the proposed acquisition by the Company of Life Technologies Corporation ("**Life Technologies**") compatible with the internal market and the EEA Agreement by its decision pursuant to Article 6(1)(b) of the Merger Regulation (the "**Decision**").

The Commitments shall take effect upon the date of adoption of the Decision.

This text shall be interpreted in the light of the Decision to the extent that the Commitments are attached as conditions and obligations, in the general framework of EU law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EC) No. 139/2004 and under Commission Regulation (EC) No. 802/2004.

SECTION A. DEFINITIONS

For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled by the Parties and/or by the ultimate parents of the Parties, whereby the notion of control shall be interpreted pursuant to Article 3 of the Merger Regulation and in the light of the Commission Notice on the concept of concentration under Council Regulation (EC) No. 139/2004.

Cell Culture Business: the business as defined in Section B and Exhibit A.

Closing: the transfer of the legal title of the Divestment Businesses to the Purchaser.

Divestment Businesses: the Cell Culture Business, the Gene Modulation Business and the Magnetic Bead Business.

Divestiture Trustee: one or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by the Company and who has received from the Company the exclusive Trustee Mandate to sell the Divestment Businesses to a Purchaser at no minimum price.

Effective Date: the date of adoption of the Decision.

First Divestiture Period: the period of [...] from the Effective Date.

Gene Modulation Business: the business as defined in Section B and Exhibit B.

Hold Separate Manager: the person or persons appointed by the Company for the Divestment Businesses to manage the day-to-day business of the Divestment Businesses under the supervision of the Monitoring Trustee.

Key Personnel: all personnel necessary to maintain the viability and competitiveness of the Divestment Businesses, listed in Exhibits A, B and C.

Life Technologies: Life Technologies Corporation, a US company incorporated under the laws of Delaware, with its head office at 5791 Van Allen Way, Carlsbad, California, United States of America.

Magnetic Bead Business: the business as defined in Section B and Exhibit C.

Monitoring Trustee: one or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by the Company, and who has the duty to monitor the Company's compliance with the conditions and obligations attached to the Decision.

Parties: Thermo Fisher Scientific Inc. and Life Technologies.

Personnel: all personnel currently employed by the Divestment Businesses, including Key Personnel, staff seconded to the Divestment Businesses, shared personnel and the additional personnel listed in Exhibits A, B and C.

Purchaser: the entity or entities approved by the Commission as acquirer or acquirers of the Divestment Businesses in accordance with the criteria set out in Section D.

Thermo Fisher Scientific Inc: a US company incorporated under the laws of Delaware, with its head office at 81 Wyman Street, Waltham, Massachusetts, United States of America.

Transaction: the Company's proposed acquisition of Life Technologies.

Trustee(s): the Monitoring Trustee and the Divestiture Trustee.

Trustee Divestiture Period: the period of [...] from the end of the First Divestiture Period.

SECTION B. THE DIVESTMENT BUSINESSES

Commitment to Divest

1. In order to restore effective competition, the Company commits to divest, or procure the divestiture of, the Divestment Businesses by the end of the Trustee Divestiture Period as a going concern to a Purchaser and on terms of sale approved by the Commission in accordance with the procedure described in paragraph 14. To carry out the divestiture, the Company commits to find a Purchaser and to enter into a final binding sale and purchase agreement for the sale of each of the Divestment Businesses within the First Divestiture Period. If the Company has not entered into a final binding sale and purchase agreement for the sale of the Divestment Businesses at the end of the First Divestiture Period, the Company shall grant the Divestiture Trustee an exclusive mandate to sell the Divestment Businesses in accordance with the procedure described in paragraph 23 in the Divestiture Period.
2. The Company shall be deemed to have complied with this commitment if, by the end of the Trustee Divestiture Period, the Company has entered into a final binding sale and purchase agreement, if the Commission approves the purchaser and the terms of sale in accordance

with the procedure described in paragraph 14 and if the closing of the sale of the Divestment Businesses takes place within a period not exceeding [...] after the approval of the purchaser and the terms of sale by the Commission.

3. In order to maintain the structural effect of the Commitments, the Parties shall, for a period of 10 years after the Effective Date, not acquire direct or indirect influence over the whole or part of the Divestment Businesses, unless the Commission has previously found that the structure of the market has changed to such an extent that the absence of influence over the Divestment Businesses is no longer necessary to render the proposed concentration compatible with the internal market.

Structure and Definition of the Divestment Businesses

4. The Divestment Businesses consist of:

- (1) The Cell Culture Business, as described in more detail in Exhibit A, which includes the following assets (referred to collectively as “**Assets**”):

- (a) all tangible and intangible assets (including intellectual property rights) which contribute to the current operation or are necessary to ensure the viability and competitiveness of the Cell Culture Business;
- (b) all raw materials, stocks, work in progress and semi-finished and finished goods relating to the Cell Culture Business;
- (c) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Cell Culture Business;
- (d) all contracts, leases, commitments and customer orders of the Cell Culture Business; all customer, credit and other records of the Cell Culture Business (to the extent assignable);
- (e) the Key Personnel employed in the Cell Culture Business and any other Personnel necessary to ensure its continued economic viability, marketability and competitiveness; and
- (f) the benefit, for a transitional period of 12 months on terms and conditions equivalent to those at present afforded to the Cell Culture Business, of all current arrangements under which the Company or Affiliated Undertakings supply products or services to the Cell Culture Business, as detailed in Exhibit A, unless otherwise agreed with the Purchaser.

- (2) The Gene Modulation Business, as described in more detail in Exhibit B, which includes the following assets (referred to collectively as “**Assets**”):

- (a) all tangible and intangible assets (including intellectual property rights), which contribute to the current operation or are necessary to ensure the viability and competitiveness of the Gene Modulation Business;

- (b) all raw materials, stocks, work in progress and semi-finished and finished goods relating to the Gene Modulation Business;
 - (c) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Gene Modulation Business;
 - (d) all contracts, leases, commitments and customer orders of the Gene Modulation Business; all customer, credit and other records of the Gene Modulation Business (to the extent assignable);
 - (e) the Key Personnel and any other Personnel currently employed in the Gene Modulation Business necessary to ensure its continued economic viability, marketability and competitiveness; and
 - (f) the benefit, for a transitional period of 12 months on terms and conditions equivalent to those at present afforded to the Gene Modulation Business, of all current arrangements under which the Company or Affiliated Undertakings supply products or services to the Gene Modulation Business, as detailed in Exhibit B, unless otherwise agreed with the Purchaser.
- (3) The Magnetic Bead Business, as described in more detail in Exhibit C which includes the following assets (referred to collectively as “**Assets**”):
- (a) all tangible and intangible assets (including intellectual property rights) which contribute to the current operation or are necessary to ensure the viability and competitiveness of the Magnetic Bead Business;
 - (b) all raw materials, stocks, work in progress and semi-finished and finished goods relating to the Magnetic Bead Business;
 - (c) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Magnetic Bead Business;
 - (d) all contracts, leases, commitments and customer orders of the Magnetic Bead Business; all customer, credit and other records of the Magnetic Bead Business (to the extent assignable);
 - (e) the Key Personnel employed in the Magnetic Bead Business and any other Personnel necessary to ensure its continued economic viability, marketability and competitiveness; and
 - (f) the benefit, for a transitional period of 2 years on terms and conditions equivalent to those at present afforded to the Magnetic Bead Business, of all current arrangements under which the Company or Affiliated Undertakings supply products or services to the Magnetic Bead Business, as detailed in Exhibit C, unless otherwise agreed with the Purchaser.

SECTION C. RELATED COMMITMENTS

Preservation of Viability, Marketability and Competitiveness

5. From the Effective Date until Closing, the Company shall preserve the economic viability, marketability and competitiveness of the Divestment Businesses, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Businesses. In particular the Company undertakes:
 - (a) not to carry out any act upon its own authority that might have a significant adverse impact on the value, management or competitiveness of the Divestment Businesses or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of the Divestment Businesses;
 - (b) to make available sufficient resources for the development of the Divestment Businesses, on the basis and continuation of the existing business plans; and
 - (c) to take all reasonable steps, including appropriate incentive schemes (based on industry practice), to encourage all Key Personnel to remain with the Divestment Businesses.

Hold-Separate Obligations

6. The Company commits, from the Effective Date until Closing, to keep the Divestment Businesses separate from the businesses it is retaining and to ensure that Key Personnel of the Divestment Businesses – including the Hold Separate Manager – have no involvement in any business retained and *vice versa*. The Company shall also ensure that the Personnel do not report to any individual outside the Divestment Businesses.
7. Until Closing, the Company shall assist the Monitoring Trustee in ensuring that the Divestment Businesses are managed as distinct and saleable entities separate from the businesses retained by the Parties. The Company shall appoint a Hold Separate Manager for each Divestment Business who shall be responsible for the management of that Divestment Business, under the supervision of the Monitoring Trustee. The Hold Separate Manager shall manage the Divestment Business independently and in the best interest of the business with a view to ensuring its continued economic viability, marketability and competitiveness and its independence from the businesses retained by the Parties.

Ring-fencing

8. The Company shall implement all necessary measures to ensure that it does not after the Effective Date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to the Divestment Businesses. In particular, the participation of the Divestment Businesses in a central information technology network shall be severed to the extent possible, without compromising the viability of the Divestment Businesses. The Company may obtain information relating to the Divestment Businesses which is reasonably necessary for the divestiture of the Divestment Businesses, which is reasonably required to maintain the viability of the Divestment Businesses, or whose disclosure to the Company is required by law.

Non-solicitation Clause

9. The Company undertakes, subject to customary limitations, not to solicit, and to procure that Affiliated Undertakings do not solicit, the Key Personnel transferred with the Divestment Businesses for a period of:
 - (a) [...] after Closing in the case of the Cell Culture Business and the Gene Modulation Business; and
 - (b) [...] after Closing in the case of the Magnetic Bead Business.

Due Diligence

10. In order to enable potential purchasers to carry out a reasonable due diligence of the Divestment Businesses, the Company shall, subject to customary confidentiality assurances and dependent on the stage of the divestiture process:
 - (a) provide to potential purchasers sufficient information as regards the Divestment Businesses; and
 - (b) provide to potential purchasers sufficient information relating to the Personnel and allow them reasonable access to the Key Personnel.

Reporting

11. The Company shall submit written reports in English on potential purchasers of the Divestment Businesses and developments in the negotiations with such potential purchasers to the Commission and the Monitoring Trustee no later than 10 days after the end of every month following the Effective Date (or otherwise at the Commission's request).
12. The Parties shall from the Effective Date inform the Commission and the Monitoring Trustee on the preparation of the data room documentation and the due diligence procedure and shall submit a copy of an information memorandum in respect of each of the Divestment Businesses to the Commission and the Monitoring Trustee before sending the memorandum out to potential purchasers.

SECTION D. THE PURCHASER

13. In order to ensure the immediate restoration of effective competition, the Purchaser, in order to be approved by the Commission, must satisfy the following criteria (the "**Purchaser Requirements**"):
 - (a) be independent of and unconnected to the Parties;
 - (b) have the financial resources, proven manufacturing expertise in the life sciences sector and incentive to maintain and develop the relevant Divestment Business as a viable and active competitive force in competition with the Parties and other competitors; and
 - (c) neither be likely to create, in the light of the information available to the Commission, *prima facie* competition concerns nor give rise to a risk that the implementation of the

Commitments will be delayed, and must, in particular, reasonably be expected to obtain all necessary approvals from the relevant regulatory authorities for the acquisition of the relevant Divestment Business.

14. The final binding sale and purchase agreement shall be conditional on the Commission's approval. When the Company has reached an agreement with a purchaser, it shall submit a fully documented and reasoned proposal, including a copy of the final agreement(s), to the Commission and the Monitoring Trustee. The Company must be able to demonstrate to the Commission that the proposed purchaser meets the Purchaser Requirements and that the relevant Divestment Business is being sold in a manner consistent with the Commitments. For the approval, the Commission shall verify that the proposed purchaser fulfils the Purchaser Requirements and that the relevant Divestment Business is being sold in a manner consistent with the Commitments. The Commission may approve the sale of each Divestment Business without one or more Assets or parts of the Personnel, if this does not affect the viability and competitiveness of that Divestment Business after the sale, taking account of the proposed purchaser.

SECTION E. TRUSTEE

I. Appointment Procedure

15. The Company shall appoint a Monitoring Trustee to carry out the functions specified in the Commitments for a Monitoring Trustee. If the Company has not entered into a binding sale and purchase agreement one month before the end of the First Divestiture Period or if the Commission has rejected a purchaser proposed by the Company at that time or thereafter, the Company shall appoint a Divestiture Trustee to carry out the functions specified in the Commitments for a Divestiture Trustee. The appointment of the Divestiture Trustee shall take effect upon the commencement of the Trustee Divestiture Period.
16. The Trustee shall be independent of the Parties, possess the necessary qualifications to carry out its mandate, for example as an investment bank or consultant or auditor, and shall not have or be reasonably likely to have a conflict of interest. The Trustee shall be remunerated by the Parties in a way that does not impede the independent and effective fulfilment of its mandate. In particular, where the remuneration package of a Divestiture Trustee includes a success premium linked to the final sale value of the Divestment Businesses, the fee shall also be linked to a divestiture within the Trustee Divestiture Period.

Proposal by the Company

17. No later than one week after the Effective Date, the Company shall submit a list of one or more persons whom the Company proposes to appoint as the Trustee to the Commission for approval. No later than one month before the end of the First Divestiture Period, the Company shall submit a list of one or more persons whom the Company proposes to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the proposed Trustee fulfils the requirements set out in paragraph 16 and shall include:
 - (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;

- (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks; and
- (c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether a different trustee may be proposed (if subsequently required) as the Divestiture Trustees for the two functions.

Approval or Rejection by the Commission

18. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, the Company shall appoint or cause to be appointed, the individual or institution concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Company shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New Proposal by the Company

19. If all the proposed Trustees are rejected, the Company shall submit the names of at least two more individuals or institutions within one week of being informed of the rejection, in accordance with the requirements and the procedure set out in paragraphs 15 to 18.

Trustee Nominated by the Commission

20. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom the Company shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

21. The Trustee shall assume its specified duties in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or the Company, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and Obligations of the Monitoring Trustee

22. The Monitoring Trustee shall:
- (i) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision.
 - (ii) oversee the on-going management of the Divestment Businesses with a view to ensuring its continued economic viability, marketability and competitiveness and monitor compliance by the Company with the conditions and obligations attached to the Decision. To that end the Monitoring Trustee shall:

- (a) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Businesses, and the keeping separate of the Divestment Businesses from the business retained by the Parties, in accordance with paragraphs 5 and 6 of the Commitments;
 - (b) supervise the management of the Divestment Businesses as a distinct and saleable entity, in accordance with paragraph 7 of the Commitments;
 - (c) (i) in consultation with the Company, determine all necessary measures to ensure that the Company does not after the Effective Date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to the Divestment Businesses, in particular strive for the severing of the Divestment Businesses' participation in a central information technology network to the extent possible, without compromising the viability of the Divestment Businesses, and (ii) decide whether such information may be disclosed to the Company as the disclosure is reasonably necessary to allow the Company to carry out the divestiture or as the disclosure is required by law;
 - (d) monitor the splitting of assets and the allocation of Personnel between the Divestment Businesses and the Company or Affiliated Undertakings;
- (iii) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision;
 - (iv) propose to the Company such measures as the Monitoring Trustee considers necessary to ensure the Company's compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability or competitiveness of the Divestment Businesses, the holding separate of the Divestment Businesses and the non-disclosure of competitively sensitive information;
 - (v) review and assess potential purchasers as well as the progress of the divestiture process and verify that, dependent on the stage of the divestiture process, (a) potential purchasers receive sufficient information relating to the Divestment Businesses and the Personnel in particular by reviewing, if available, the data room documentation, the information memorandum and the due diligence process, and (b) potential purchasers are granted reasonable access to the Key Personnel;
 - (vi) provide to the Commission, sending the Company a non-confidential copy at the same time, a written report within 15 days after the end of every month. The report shall cover the operation and management of the Divestment Businesses so that the Commission can assess whether the business is held in a manner consistent with the Commitments and the progress of the divestiture process as well as potential purchasers. In addition to these reports, the Monitoring Trustee shall promptly report in writing to the Commission, sending the Company a non-confidential copy at the same time, if it concludes on reasonable grounds that the Company is failing to comply with these Commitments;

- (vii) within one week after receipt of the documented proposal referred to in paragraph 14, submit to the Commission a reasoned opinion as to:
 - (a) the suitability and independence of the proposed purchaser and the viability of the relevant Divestment Business after the sale; and
 - (b) whether the relevant Divestment Business is sold in a manner consistent with the conditions and obligations attached to the Decision, in particular (if relevant) whether the sale of the relevant Divestment Business without one or more Assets or all of the Personnel affects the viability of that Divestment Business after the sale, taking account of the proposed purchaser.

Duties and Obligations of the Divestiture Trustee

- 23. Within the Trustee Divestiture Period, the Divestiture Trustee shall sell at no minimum price the relevant Divestment Business to a purchaser, provided that the Commission has approved both the relevant purchaser and the relevant final binding sale and purchase agreement in accordance with the procedure laid down in paragraph 14. The Divestiture Trustee shall include in the sale and purchase agreement such terms and conditions as it considers appropriate for an expedient sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the sale and purchase agreement such customary representations and warranties and indemnities as are reasonably required to effect the sale. The Divestiture Trustee shall protect the legitimate financial interests of the Company, subject to the Company's unconditional obligation to divest at no minimum price in the Trustee Divestiture Period.
- 24. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the end of every month with a simultaneous copy to the Monitoring Trustee and a non-confidential copy to the Company.

III. Duties and Obligations of the Company

- 25. The Company shall provide and shall cause its advisors to provide the Trustee with all such cooperation, assistance and information as the Trustee may reasonably require to perform its tasks. The Trustee shall have full and complete access to any of the Company's or the Divestment Businesses' books, records, documents, management or other personnel, facilities, sites and technical information necessary for fulfilling its duties under the Commitments and the Company and the Divestment Businesses shall provide the Trustee upon request with copies of any document. The Company and the Divestment Businesses shall make available to the Trustee one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of its tasks.
- 26. The Trustee shall provide the Monitoring Trustee with all managerial and administrative support that it may reasonably request on behalf of the management of the Divestment Businesses. This shall include all administrative support functions relating to the Divestment Businesses which are currently carried out at headquarters level. The Company shall provide and shall cause its advisors to provide the Monitoring Trustee, on request, with the information

submitted to potential purchasers, in particular give the Monitoring Trustee access to the data room documentation and all other information granted to potential purchasers in the due diligence procedure. The Company shall inform the Monitoring Trustee on possible purchasers, submit a list of potential purchasers, and keep the Monitoring Trustee informed of all developments in the divestiture process.

27. The Company shall grant or procure that Affiliated Undertakings grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee to effect the sale, the Closing and all actions and declarations which the Divestiture Trustee considers necessary or appropriate to achieve the sale and the Closing, including the appointment of advisors to assist with the sale process. Upon request of the Divestiture Trustee, the Company shall cause the documents required for effecting the sale and the Closing to be duly executed.
28. The Company shall indemnify the Trustee and its employees and agents (each an "**Indemnified Party**") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to the Company for any liabilities arising out of the performance of the Trustee's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee, its employees, agents or advisors.
29. At the expense of the Company, the Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to the Company's approval (this approval not to be unreasonably withheld or delayed) if the Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate, provided that any fees and other expenses incurred by the Trustee are reasonable. Should the Company refuse to approve the advisors proposed by the Trustee the Commission may approve the appointment of such advisors instead, after having heard the Company. Only the Trustee shall be entitled to issue instructions to the advisors. Paragraph 28 shall apply *mutatis mutandis*. In the Trustee Divestiture Period, the Divestiture Trustee may use advisors who served the Company during the Divestiture Period if the Divestiture Trustee considers this in the best interest of an expedient sale.

IV. Replacement, Discharge and Reappointment of the Trustee

30. If the Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a conflict of interest:
 - (a) the Commission may, after hearing the Trustee, require the Company to replace the Trustee; or
 - (b) the Company, with the prior approval of the Commission, may replace the Trustee.
31. If the Trustee is removed according to paragraph 30, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in paragraphs 15 to 20.
32. Beside the removal according to paragraph 30, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at

any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

SECTION F. THE REVIEW CLAUSE

33. The Commission may, where appropriate, in response to a request from the Company showing good cause and accompanied by a report from the Monitoring Trustee:
- (i) grant an extension of the time periods foreseen in the Commitments; or
 - (ii) waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments.
34. Where the Company seeks an extension of a time period, it shall submit a request to the Commission no later than one month before the expiry of that period, showing good cause. Only in exceptional circumstances shall the Company be entitled to request an extension within the last month of any period.

Brussels, 19 November 2013

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duly authorised for and on behalf of
Thermo Fisher Scientific Inc.

EXHIBIT A: The Cell Culture Business

Thermo Fisher proposes to divest its entire HyClone cell culture business (excluding single use technologies (“SUT”)), which includes the following assets:

HyClone sera and media facilities. Thermo Fisher processes and manufactures HyClone sera and media at the sites listed below, all of which would be divested as part of this offer. These facilities represent an autonomous cell culture business, including procurement, manufacture, operations and supply chain, customer service, finance, sales and marketing organisations. As discussed below, Thermo Fisher also hydrates a small amount of media at facilities in Cramlington, UK, and Beijing, China, but those facilities will not be part of the divestiture because the Cramlington facility is by and large an SUT facility and the Beijing facility is primarily used for Thermo Fisher’s microbiological division.

- *Omokora facility, Tauranga, New Zealand:* This cGMP site is used to process and manufacture New Zealand Fetal Bovine Serum (“FBS”), New Zealand Calf sera and New Zealand Adult Bovine sera. It is composed of 17,000 square feet across multiple buildings that include manufacturing lines (filtration, freezers, incubators, pooling tank, filling equipment and packaging equipment) as well as supply chain and operations infrastructure (shipping and logistics, quality assurance and inventory control). The facility has an annual production capacity of [150-200],000 litres. Its utilisation rate in 2012 was [30-40]%, and its output was [10-20],000 litres of FBS, [10-20],000 litres of calf sera and [10-20],000 litres of adult bovine sera.
- *Mordialloc facility, Melbourne, Australia:* This cGMP facility is used to process and manufacture Australian FBS. It is a 5,500 square feet building that includes manufacturing lines (single-use filtration, freezers, incubators, single-use pooling tank, single-use filling equipment and packaging equipment) as well as supply chain and operations infrastructure (shipping and logistics, quality assurance and inventory control). The facility has an annual production capacity of [90-100],000 litres. Its utilisation rate in 2012 was [10-20]%.
- *Omaha, Nebraska facility:* This 2,200 square feet facility is exclusively dedicated to the processing of US calf blood into raw newborn calf sera. The facility contains centrifuges and a freezer. The facility has an annual production capacity of [300-500],000 litres. Its utilisation rate in 2012 was [10-20]%.
- *Green Bay, Wisconsin facility:* This 14,000 square feet facility is exclusively dedicated to the processing of US calf blood into raw calf sera. The facility contains centrifuges and a freezer. The facility has an annual production capacity of [700-1000],000 litres. Its utilisation rate in 2012 was [20-30]%.
- *Logan, Utah facilities:* Thermo Fisher currently manufactures and distributes media and sera at its Logan, Utah facilities as follows:
 - Sera and liquid media facility: This cGMP facility is about 55,000 square feet, and includes both sera and media operations.
 - *Sera:* The facility is used to process and manufacture US FBS, Calf sera and Equine sera. It includes manufacturing lines and inventory storage (filtration, freezers, incubators, pooling tank, filling equipment and packaging equipment).

The facility has an annual production capacity of about [600-800],000 litres. Its utilisation rate in 2012 was [50-60]%.

- *Media*: This facility is used to manufacture liquid media and includes coolers, powder milling equipment, powder blending equipment, liquid hydration equipment (stainless steel tanks and single-use bags), filtration equipment, filling lines, packaging equipment. It has an annual production capacity of [20-30] million litres. Its utilisation rate in 2012 was [70-80]%.
- Powder media and component facility: This cGMP facility is dedicated to the manufacture of dry powder media, media component storage and raw sera warehousing. It is about 55,000 square feet. The facility is equipped with coolers, powder milling equipment, powder blending equipment, liquid hydration equipment (stainless steel and single-use), filtration equipment, filling lines, and packaging equipment. It has an annual production capacity of about [500-1000] tons. Its utilisation rate in 2012 was [50-60]%.
- USDA FBS & porcine sera facility: This cGMP facility is used to process and manufacture USDA FBS (Central American origin) and porcine sera. It is a 3,000 square feet building that includes manufacturing equipment (single-use filtration, freezer for finished sera, incubators, single-use pooling tank, single use filling equipment, bottling line and boxing station). The facility has an annual production capacity of [100-200],000 litres. Its utilisation rate in 2012 was [20-30]%, and its output was [10-20],000 litres of USDA FBS and [0-10],000 litres of porcine sera.
- Distribution warehouse facility: This cGMP facility spans approximately 50,000 square feet and contain sera and media finished product storage freezers with a capacity of [750-950],000 litre for finished sera products and [900-1600],000 litre for finished media products. While this warehouse is primarily used for storage of finished sera and media, it also currently houses a small SUT inventory, which will be relocated within [...] of completion of the divestiture.
- General administration building: This approximately 18,000 square feet facility houses the administrative staff and operations (finance, customer service, management, marketing, human resources, accounting and finance), and is also offered as part of the divestiture offer. All SUT personnel located in this building will be moved to another location within [...] of completion of the divestiture; the migration of IT systems will take up to [...].
- *Singapore*: This new 30,000 square feet facility manufactures dry powder media. It is equipped with coolers, powder milling equipment, powder blending equipment and packaging equipment. [...]. It is in start-up mode and in the process of being validated.
- *Aalst, Belgium*: This facility has 16,000 square feet of storage and distribution space for finished product sera and media. It is equipped with 12,000 square feet of ambient storage, 2000 square feet of refrigerated storage and 2000 square feet of freezer storage. While this warehouse is primarily used for storage of finished sera and media, it also currently houses a small inventory of non-cell culture products, which will be relocated within [...] of completion of the divestiture.

Product lines. The proposed divestiture includes Thermo Fisher's entire HyClone sera and media product lines, including, but not limited to, ANZ FBS, US FBS, and USDA FBS, and all HyClone liquid and dry powder media (including process liquids) product lines.

Brand names and intellectual property. As part of the proposed divestiture, Thermo Fisher offers to transfer the rights to all intellectual property, technology and know-how associated with its sera and media operations, including its proprietary media formulations. The intellectual property to be transferred to the purchaser includes:

- Hyclone™ and HyQ™: these brands and trade marks will be assigned to the purchaser. Immediately following the assignment, the purchaser will be required to grant Thermo Fisher an exclusive licence to use these trade marks/brand names in relation to Thermo Fisher's single use technology products and in any pre-existing company or legal entity name for two years. In that licence agreement, the purchaser will also agree not to use either brand name for SUT products or any products other than media and sera, in perpetuity;
- The Alpha Calf™ brand and trade mark;
- The FetalClone I™ brand and trade mark;
- The FetalClone II™ brand and trade mark;
- The FetalClone III™ brand and trade mark;
- The Cosmic Calf™ brand and trade mark; and
- Proprietary information kept as trade secrets relating to details on production processes, including in relation to standard operating procedures, for both sera and media.

Thermo Scientific name. Thermo Fisher will grant a licence to the purchaser to use the Thermo Scientific name for a period of two years in order to facilitate the sale of existing inventory held by the Cell Culture Business and to allow the purchaser to transition to packaging featuring its own corporate name and branding. For the avoidance of doubt:

- This licence will apply only in respect of inventory existing at the date of the sale of the Cell Culture Business and which has already been labelled with the Thermo Scientific name; and
- This licence will no longer apply in respect of any particular Stock Keeping Unit (SKU) labelled with the Thermo Scientific name once the purchaser has made sales of that SKU labelled without the Thermo Scientific name.

Personnel. The divestiture business will include all dedicated sera and media manufacturing employees covering all areas of operation, including processing, filling, packaging, operations and supply chain (approximately [...] full time employees).¹ Notably, Thermo Fisher also offers to transfer all key sera and media product management, quality, R&D, product management, and technical support personnel, as well as all personnel responsible for sera procurement (who have the relationships with abattoirs and blood collections). In addition, the divestiture will include an appropriate allocation of the personnel that split their time between sera and media, on the one hand, and SUT products, on the other hand (including sales, marketing, quality control, distribution, customer service and other support functions) (approximately [...] full time employees).

¹ Thermo Fisher will provide necessary leaders for appropriate support of the business. [...]

Key Personnel. The Key Personnel and their functions are as follows:

- [...] – Vice President / General Manager;
- [...] – Director Finance/IT;
- [...] – Director Sales and Marketing;
- [...] – Director Quality / Regulatory Affairs;
- [...] – Director Human Resources;
- [...] – Director Operations;
- [...] – Director Sera Procurement; and
- [...] – Director R&D and Field Application.

Supply chain. Thermo Fisher will provide its existing distribution capabilities and infrastructure at the above-listed facilities and relevant supply chain personnel.

Thermo Fisher distributes the bulk of its cell culture products in North America and Europe from its dedicated cell culture distribution facilities in Logan and Aalst which are included in the divestiture.² Thermo Fisher's Asia Pacific customers are served either directly or by Thermo Fisher's shared service centres in Japan and China. These shared service centres will not be part of the divestiture because they are used for distribution of many different products (beyond cell culture), but that should not have any meaningful impact on the divestiture buyer's cell culture business because (1) the most likely divestiture buyers will already have their own distribution facilities; (2) the divestiture buyer can use third party warehousing providers similar to what Thermo Fisher does in many countries; or (3) the divestiture buyer can easily build its own cell culture warehouse (it is essentially no more than leased space with a freezer). Nonetheless, Thermo Fisher commits to continue to distribute sera and media products on behalf of the divestiture buyer under a transitional services agreement, for up to [...].

Inventory. The divested business will include transfer of Thermo Fisher's entire HyClone sera and media inventory, which currently amounts to approximately [600-700],000 litres of sera (including [20-30],000 litres of ANZ FBS and [100-200],000 litres of US FBS), [10-20] million litres of liquid media and [100-200] tons of powder media. Thermo Fisher estimates that this inventory would last [...], on average.

Customer contracts. The divested business will include transfer of all existing sera and media supply contracts between Thermo Fisher and its bioproduction and research customers to the extent those contracts can be assigned. Thermo Fisher will provide its cell culture customer database and invoicing information.

Distributors / Dealers. Thermo Fisher will facilitate the assignment of its existing distributor / dealer arrangements, to the extent possible.

² Thermo Fisher distributes a small portion of its media and sera for research customers through CCG.

SUT is not part of the divestiture. Thermo Fisher will not divest its SUT business because (1) SUT is not an overlap product, and (2) SUT is not needed to compete successfully in the sera and media markets, as LIFE and other suppliers have demonstrated. All but one of Thermo Fisher's SUT facilities are standalone buildings dedicated to SUT operations that will not raise any separation issues for the sera and media business. The only (minor) exception is Thermo Fisher's SUT facility in Cramlington, which also houses a small media hydration operation.

- Thermo Fisher primarily uses its Cramlington facility for SUT manufacturing and, therefore, has not included this facility in its divestiture proposal. A small part of this facility is dedicated to media hydration for European customers.
- Tolling agreement for media sold in SUT bags. Some of Thermo Fisher's customers purchase its media in SUT bags. To minimise disruption for those customers, Thermo Fisher is prepared to enter into a tolling agreement to supply the divestiture buyer with SUT bags, so that the divestiture buyer can continue to supply the media in the same SUT bags, just like Thermo Fisher does today.

Media hydration equipment. As mentioned above, the Cramlington and Beijing facilities will not form part of the divestiture. However, the media hydration equipment contained in these two facilities will be offered to the purchaser to be used at a different site or sites. That equipment includes liquid hydration equipment, filtration equipment, filling lines and packaging equipment. The Cramlington facility has a production (practical) capacity of about [0-10] million litres with a utilisation rate of [20-30]% in 2012. The Beijing facility has a production capacity of about [500-700],000 litres with a utilisation rate of [60-70]% in 2012.

Transitional supply to Thermo Fisher. Thermo Fisher's cell culture division currently supplies minimal amounts of both sera and media products to other parts of Thermo Fisher for use in research and other applications. The value of such sales was less than [...] in 2012. Thermo Fisher would require the purchaser to continue supplying Thermo Fisher with the same products for a maximum of 3 years (at current transfer prices, which are above cost).

EXHIBIT B: The Gene Modulation Business

To resolve the Commission's concerns about the parties' overlap in siRNA and miRNA, Thermo Fisher, therefore, commits to divest the assets described below, comprising its gene modulation business in Lafayette, Colorado (subject to the limitations below, such as the retention of certain executives and personnel at the Lafayette facility ([...]) who will remain with Thermo Fisher because they have responsibilities in its molecular biology business beyond gene modulation).

Lafayette, Colorado facility: This is the only location where Thermo Fisher develops and manufactures gene modulation products (including siRNA, shRNA, and miRNA reagents and libraries), as well as Thermo Fisher's distribution hub for gene modulation products (all of Thermo Fisher's customers of gene modulation products are supplied from the Lafayette facility). Thermo Fisher acquired the facility through its purchase of Dharmacon, Inc. in 2004, and has since expanded it. It is now a leased 78,721 square feet facility, spread across two buildings (65,971 and 12,750). The manufacturing processes at the Lafayette facility include RNA and DNA synthesis; siRNA plating, storage and retrieval; RNA viral construct production and plating; viral particle production; and gene content clone distribution. The Lafayette facility is a standalone, autonomous site, including R&D, manufacturing operations and supply chain, customer service, finance, and sales and marketing organisations, as well as management for the referenced product lines.

Product lines. The gene modulation product lines manufactured in Lafayette include:

- All siRNA reagents and libraries including:
 - siGENOME
 - On-TARGETplus
 - Accell
 - lncRNA
- All shRNA reagents, viral particles, and libraries including:
 - GIPZ
 - TRIPZ
 - Decode
 - TRC
- All miRNA reagents and libraries including:
 - miRIDIAN
 - shMIMIC
- RNAi controls

- DharmaFECT transfection reagents³
- cDNA and ORF clones and gene collections
- Custom RNA, DNA, and other molecules

Personnel. If divested in its entirety, the gene modulation business in Lafayette would include:

- Approximately [...] employees (including several original Dharmacon employees).
- Manufacturing, materials sourcing, distribution, marketing, sales and management (including all key gene modulation product management).
- A complete R&D and bio-informatics team, a Call Centre (including customer service and technical support), and administrative support functions such as Finance and IT.

Most personnel currently at the Lafayette facility would be part of the divested business, except a few executives and some other personnel that manage aspects of Thermo Fisher's molecular biology business beyond gene modulation ([...] employees). Those employees will be transferred to another Thermo Fisher location if the Lafayette facility is divested.⁴ The divested business would also include several sales representatives in the US and in other countries that represent and sell the gene modulation products.

Key Personnel. The Key Personnel and their functions are as follows:

- [...] – Vice President / General Manager;
- [...] – Director of Operations;
- [...] – Finance Director;
- [...] – R&D Director;
- [...] – Marketing Director;
- [...] – North America Sales Director;
- [...] – EU Sales Director; and
- [...] – APAC & Distributor Sales Director.

³ But note that the divestiture will not include Thermo Fisher's *TurboFect* transfection reagents because those are manufactured in its facility in Vilnius, Lithuania and the Commission has not expressed concern about the parties' overlap in transfection reagents.

⁴ In the event of a divestiture of the Lafayette facility, the transfer of Thermo Fisher's limited non-gene modulation operations out of the Lafayette facility (some personnel and IT-systems) may take up to six (6) months to complete.

Supply chain and infrastructure. Thermo Fisher will provide existing direct distribution capabilities at the Lafayette facility and relevant personnel, together with access on a transitional basis to the shared services centres in Germany, Japan and China.

Distributors / Dealers. Thermo Fisher will facilitate the assignment of distribution agreements with third party distributor partners to the extent that they are assignable.

Information technology. Thermo Fisher will provide the code relating to the legacy Dharmacon and Open Biosystems websites and the underlying content which support the aforementioned product lines.

Tuschl licence. Thermo Fisher's gene modulation business includes one of a total of four licences to the Tuschl patents granted by MIT. Thermo Fisher's Tuschl patents licence will be transferred to the purchaser of the gene modulation business (or otherwise terminated by Thermo Fisher).

Other intellectual property. Thermo Fisher's gene modulation business includes intellectual property, technology and know-how related to the development, design and manufacture of its siRNA, shRNA and miRNA product lines, including:

- siGENOME design;
- On-TARGETplus design;
- Accell molecule design;
- SMARTvector design;
- miRIDIAN designs;
- shMIMIC design;
- SMARTchoice design;
- Gene sequences; and
- ACE chemistry processes.

Thermo Fisher uses or expects to use some of intellectual property covering the development, design and manufacture of the above product lines (notably intellectual property covering gene sequences but also the ACE chemistry processes) for broader purposes than the gene modulation business. Therefore the transfer to the divestiture buyer of the ACE chemistry processes will be subject to a licence back for applications outwith gene silencing; and the intellectual property relating to gene sequences will be the subject of an exclusive licence to the divestiture buyer for gene modulation applications.

Brand names. Thermo Fisher's gene modulation business includes the rights to the Dharmacon and Open Biosystems brands, as well as the names to various product lines, such as:

- siRNA product names (e.g., siGENOME, ON-TARGETplus, Accell);

- shRNA product names (e.g., GIPZ, TRIPZ, Decode);
- miRNA product names (e.g., shMIMIC, miRIDIAN); and
- DharmaFECT.

Thermo Scientific name. Thermo Fisher will grant a licence to the purchaser to use the Thermo Scientific name for a period of one year in order to facilitate the sale of existing inventory held by the Gene Modulation Business and to allow the purchaser to transition to packaging featuring its own corporate name and branding.

Customer contracts. Customers typically purchase gene modulation products on an *ad hoc* basis. Thermo Fisher will provide relevant customer records to the purchaser.

Inventory transfer. Virtually all of Thermo Fisher's inventory of gene modulation products is warehoused at the Lafayette facility. This inventory, which includes all existing siRNA, shRNA and miRNA reagents and libraries, as well as the extensive cDNA and ORF collections, would be transferred to the divestiture buyer as part of a full divestiture of the gene modulation business.

EXHIBIT C: The Magnetic Bead Business

Thermo Fisher proposes to divest its existing magnetic bead business (excluding its facilities used for the production and supply of magnetic beads). This business will be carved out from Thermo Fisher's existing clinical diagnostics business. The objective of the divestment is to allow the purchaser to manufacture magnetic beads of the same type and quality and under the same brand names as currently manufactured by Thermo Fisher.

The Magnetic Bead Business will include the following assets:

Brand name. As part of the divestiture, Thermo Fisher commits to assign the Sera-Mag™ and Sera-Mag SpeedBeads™ brand names and associated trade marks to the purchaser.

Thermo Scientific name. Thermo Fisher will grant a licence to the purchaser to use the Thermo Scientific name for a period of one year in order to facilitate the sale of existing inventory held by the Magnetic Bead Business and to allow the purchaser to transition to packaging featuring its own corporate name and branding.

Other intellectual property. In addition to the above brand names and trade marks, Thermo Fisher will offer to assign all intellectual property rights which contribute to the current operation or are necessary for the manufacture and supply of Thermo Fisher's magnetic bead products. This includes a transfer of the following:

- (i) **Patents:** relating to (a) the manufacture of magnetic beads with negligible residual magnetism and (b) the reduction of response time of the beads to a magnet;
- (ii) **Know-how:** Thermo Fisher also commits to provide a purchaser with access to Thermo Fisher's transfer plan relating to the execution of its recent move of its magnetic bead production facilities from Indianapolis, Indiana, to Fremont, California, on the basis that the confidential information contained in such plan remains confidential and personal to the purchaser. Together with the transfer of personnel with R&D and operations capabilities (described below), this will assist the purchaser in managing the validation of its new facilities.

Equipment. Thermo Fisher will offer to the purchaser its equipment used in the manufacture of magnetic beads, or, at the option of the purchaser, equivalent new equipment (to be acquired by Thermo Fisher). Thermo Fisher will transport and install this equipment at a manufacturing location chosen by the purchaser. Thermo Fisher will provide such support as is reasonably required to enable the purchaser to utilise the equipment to manufacture magnetic beads of the same type and quality as currently manufactured by Thermo Fisher.

Transitional supply agreement. Thermo Fisher expects that it could take up to two years for the above-mentioned equipment to be installed at the purchaser's premises and validated by customers. Thermo Fisher will therefore offer the purchaser the benefit of entering into a transitional supply agreement ("**Transitional Supply Agreement**") under which Thermo Fisher will supply the purchaser with magnetic beads for resale⁵ (to meet the reasonable needs of the purchaser) until such time as the magnetic beads equipment is removed from Thermo Fisher's facilities or, if the purchaser elects to

⁵ This will ensure the purchaser can operate the Magnetic Bead Business as a viable entity until the purchaser has completed customer and site revalidation at its production facilities.

acquire new equipment from Thermo Fisher, up to a maximum of two years (following the purchase of the Magnetic Bead Business). Under the Transitional Supply Agreement, Thermo Fisher will supply the purchaser with magnetic beads at standard costs of sales terms.

As Thermo Fisher uses magnetic beads in the production of downstream products, including products that are marketed under the Pierce brand, the Transitional Supply Agreement will also provide for Thermo Fisher to continue self-supply of magnetic beads until the magnetic beads equipment is removed from Thermo Fisher's facilities or until six months after a decision by the Commission to approve the proposed transaction under Phase 1 of the EUMR (whichever is sooner). At the end of the Transitional Supply Agreement, Thermo Fisher will cease to manufacture magnetic beads at its facilities in Fremont, California.

Customer contracts. The divestiture business will include transfer of all existing magnetic bead supply contracts between the Thermo Fisher magnetic bead business and its customers to the extent those contracts can be assigned. Thermo Fisher will provide its magnetic bead customer database and invoicing information.

Personnel. The divestiture business will include all employees whose function predominantly relates to the manufacture and/or supply of magnetic beads, which equates to six full-time employees across the following functions:

- 2 full-time employees in sales *OR* 1 full-time employee in sales and 1 full-time employee in marketing;
- 1 full-time employee in R&D;
- 2 full-time employees in operations (manufacturing); and
- 1 full-time employee in operations (quality assurance/quality control).

Key Personnel. Thermo Fisher is prepared to consider each of the six above-mentioned employees as Key Personnel.

Supply chain. The purchaser will be able to enter into a Transitional Supply Agreement with Thermo Fisher for supply chain and distribution services, until such time as it is able to supply magnetic beads from its own facilities (up to a maximum of two years), on equivalent terms as currently supplied to Thermo Fisher's magnetic bead business.

Inventory. Upon the expiry of the Transitional Supply Agreement, the divestiture business will include the transfer of Thermo Fisher's entire remaining magnetic bead inventory as well as any remaining inventory of raw materials specific to the production of magnetic beads at the Fremont facility.

Facilities are not part of the divestiture. Thermo Fisher's magnetic bead business is conducted on several sites in Fremont, California. These facilities are primarily used for the production and supply of products other than magnetic beads. Separating these facilities would be difficult and impose disproportionate costs on Thermo Fisher, given the very limited size of Thermo Fisher's presence in magnetic beads. For a purchaser with suitable production facilities, the divestiture business contains all the assets necessary to ensure its viability and competitiveness.

Distributors / Dealers. The divestiture business will not include Thermo Fisher's distribution facilities; however, Thermo Fisher will continue to distribute magnetic beads on behalf of the purchaser, for the duration of the Transitional Supply Agreement.



EUROPEAN COMMISSION
DG Competition

***CASE M.7292 - DEMB/ MONDELEZ/
CHARGER OPCO***

(Only the English text is authentic)

**MERGER PROCEDURE
REGULATION (EC) 139/2004**

Article 8(2) Regulation (EC) 139/2004

Date: 5/5/2015

This text is made available for information purposes only. A summary of this decision is published in all EU languages in the Official Journal of the European Union.

Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets and marked with an asterisk.

EUROPEAN
COMMISSION

Brussels, 5.5.2015
C(2015) 3000 final

Public version

COMMISSION DECISION

of 5.5.2015

**declaring a concentration to be compatible with the internal market and the EEA
agreement (Case M.7292 - DEMB / MONDELEZ / CHARGER OPCO)**

(Only the English text is authentic)

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COMMISSION DECISION

of 5.5.2015

declaring a concentration to be compatible with the internal market and the EEA agreement (Case M.7292 - DEMB / MONDELEZ / CHARGER OPCO)

(Only the English text is authentic)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to the Agreement on the European Economic Area¹, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings², and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 15 December 2014 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations³,

Having regard to the final report of the Hearing Officer in this case⁴,

Whereas:

1. THE NOTIFICATION

(1) On 27 October 2014 the European Commission received a notification of a proposed concentration pursuant to Article 4 of Regulation (EC) No 139/2004 by which the undertakings Acorn Holdings BV ("Acorn"), the holding company of D.E. Master Blenders 1753 B.V. ("DEMB", Netherlands) and [...]× ("Mondelēz", USA) acquire joint control of Charger OpCo B.V. ("Charger" or "the JV"), a newly created company constituting a joint venture, by way of purchase of shares (the "Transaction"). DEMB and Mondelēz are jointly referred to as the "Parties" or "Notifying Parties".

2. THE PARTIES

(2) DEMB is an international coffee and tea company, established in the Netherlands, which offers a range of coffee and tea products for in-home consumption as well as hot beverage solutions for the out-of-home markets. In the EEA DEMB also operates, including through the use of franchising arrangements, coffee houses in the

¹ OJ L 1, 3.1.1994, p. 3 ("the EEA Agreement").

² OJ L 24, 29.1.2004, p. 1. With effect from 1 December 2009, the Treaty on the Functioning of the European Union ("TFEU") has introduced certain changes, such as the replacement of "Community" by "Union" and "common market" by "internal market". The terminology of the TFEU will be used throughout this decision.

³ OJ C200. , p....

⁴ OJ C200. , p....

× Should read: Mondelēz International, Inc.

Netherlands. DEMB is indirectly owned by Acorn, which in turn is majority owned by JAB Holding Company s.à r.l. ("JAB").

- (3) Mondelēz is a company established in the United States, created following a spin-off of Kraft Foods Group in October 2012. It is a global snack company with a product offering spanning biscuits, chocolate, candy, cheese, powdered beverages, chewing gum and coffee. Mondelēz has an in-house coffee procurement and trading business.

3. THE CONCENTRATION

- (4) Charger, incorporated in the Netherlands, will combine all material assets of DEMB's and Mondelēz's coffee businesses.⁵ Acorn will hold [...] % of Charger's shares, while Mondelēz is to hold up to [...] % of those shares and to receive a cash payment of approximately EUR [...] billion for the contributed assets. As the majority shareholder, Acorn will also control a majority of the JV's Board and have the right to appoint its Chairman. Both Acorn and Mondelēz will have veto rights over the [...] of Charger, which is meant to identify [...] ; as well as [...]. According to the Parties the investments covered by the [...] are not merely akin to minority shareholder protection rights but are directly related to the commercial policy of the JV. Furthermore, the [...] will also include [...] ; which are in fact key elements of the JV's budget. As a result, the veto rights over the [...] confer joint control over the JV to Acorn and Mondelēz.
- (5) Charger will have sufficient resources to operate independently on the market (including management, staff, financing and assets transferred by DEMB and Mondelēz). It will be an independent market-facing business, which will procure, manufacture and sell coffee and tea products. The JV will source coffee beans independently from third parties and not from its parents. It will also sell products to independent downstream customers and not to its parents. The shareholders' agreement, concluded between Acorn's subsidiary ("Oak") and Mondelēz, contains deadlock provisions⁶ on the basis of which Oak can [...]. However [...] ⁷. Therefore those provisions do not call into question the intention to operate the JV on a lasting basis.⁸ For those reasons Charger can be considered as a full-function joint venture.
- (6) The Transaction therefore constitutes a concentration within the meaning of Articles 3(1)(b) and 3(4) of the Regulation (EC) No 139/2004.

4. UNION DIMENSION

- (7) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million⁹ (JAB: EUR [...] million, Mondelēz: EUR 26 579 million). Each of them has a Union-wide turnover in excess of EUR 250 million (JAB EUR [...], Mondelēz EUR [...] million), but they do not achieve more than two-thirds of their aggregate Union-wide turnover within one and the same Member State. The Transaction therefore has a Union dimension.

⁵ As regards coffee business of Mondelēz in France, Mondelēz is obliged to consult with representatives of its French workforce prior to contributing these assets. The consultation process is currently ongoing.

⁶ To this effect that [...].

⁷ Shareholders' Agreement clauses 7 and 16.7.6.

⁸ Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings, paragraph 103.

⁹ Turnover calculated in accordance with Article 5 of the Merger Regulation and the Commission Consolidated Jurisdictional Notice (OJ C95, 16.4.2008, p. 1).

5. THE PROCEDURE

- (8) In the course of first phase proceedings the Commission contacted competitors and customers (general retailers) of the Parties by means of questionnaires and conference calls. The Parties submitted commitments to the Commission on 26 November 2014. However based on a market investigation, including a market test of the proposed commitments, the Commission preliminarily considered that the Transaction raised serious doubts as to its compatibility with the internal market and adopted a decision to initiate proceedings pursuant to Article 6(1)(c) of Regulation (EC) No 139/2004 on 15 December 2014 (the "Article 6(1)(c) Decision").¹⁰
- (9) The Parties submitted written comments to the Article 6(1)(c) Decision on 9 January 2015.
- (10) The market investigation in the second phase consisted, among others, in analysing responses of market participants to the Commission's questionnaires and conference calls with some of the participants. They included: competitors (that is to say other suppliers of the various coffee products), customers (that is to say general retailers); electronic goods retailers as well as manufacturers of coffee machines.
- (11) During the second phase investigation the Commission sent, on the basis of Article 11(2) of Regulation (EC) No 139/2004, a number of simple requests for information to the Parties. The Parties responded to the Commission's request for information of 19 December 2014 on 19 January 2015, to the request for information of 21 January 2015 on 31 January 2015, to the request for information of 30 January 2015 on 5 February 2015 and to the request for information of 13 February 2015 on 17 February 2015.
- (12) On 21 January 2015 the Commission, having received the agreement of the Parties, extended the procedure by a total of five working days, in accordance with Article 10(3) second subparagraph, third sentence of Regulation (EC) No 139/2004.
- (13) On 20 February 2015 the Commission, having received the agreement of the Parties, extended the procedure by a total of ten working days, in accordance with Article 10(3) second subparagraph, third sentence of Regulation (EC) No 139/2004.
- (14) On 13 February 2015, the Commission held a state-of-play meeting with the Parties and orally set out its provisional competition concerns following the in-depth investigation.
- (15) On 23 February 2015, the Parties submitted commitments to the Commission. The Commission launched a market test on those commitments on 25 February 2015. Following the results of the market test, the Parties provided a revised version of commitments to take account of comments received during the market test. On 20 March 2015, the Parties submitted final commitments that render the Transaction compatible with the internal market.

6. DESCRIPTION OF PRODUCTS

- (16) The Parties are active in the manufacture and sale of coffee products both for the multi-serve (that is to say machines producing multiple portions of coffee at a time) and single-serve (that is to say machines producing one portion of coffee at a time) segments. Parties offer coffee products in various formats for use in the different coffee brewing methods: instant coffee, roasted coffee beans (whole and ground) for use in multi-serve machines as well as consumables for single-serve machines: filter

¹⁰ O.J. C 461, 20.12.2014, p. 11.

pads, capsules compatible with the Nespresso machines and Mondelēz produces T-discs for its Tassimo.¹¹

6.1. Roast and ground coffee ("R&G")

- (17) R&G consists of coffee beans which have been pre-roasted and pre-ground for use in coffee-specific appliances. Whole beans are simply roasted beans sold to consumers who prefer to grind them freshly at home or use them in fully automated bean-to-cup machines. R&G comprises a wide variety of coffee flavours, aromas and intensities depending on the specific blend of the coffee varieties and origins, and the length of the roasting process. R&G coffee can be used in a range of appliances which often produce multiple cups of coffee at a time.

6.2. Instant coffee

- (18) Instant coffee (also called coffee powder or soluble coffee) is prepared by freeze-drying or spray-drying brewed coffee. Consumers can then re-hydrate the coffee by mixing it with hot water. Instant coffee can be prepared at short notice with ready-available appliances (such as a kettle or a stove). Due to its preparation method, instant coffee has a very long shelf life.

6.3. Filter pads

- (19) Filter pads are pre-packaged individual portions of R&G coffee for use in compatible machines to produce a single or double serving of coffee. Filter pad coffee is brewed through a process of infusion (whereby hot water is made to flow through ground coffee with minimal or no pressure). Filter pads are circular, flat and naturally permeable (like a traditional tea bag). Filter pads are used in specific single-serve machines. Classic filter pads produce a long coffee with a smooth taste and larger serving size than "espresso-style" coffees; however filter pads with other flavours (caramel, chocolate etc.) are also available.

6.4. Nespresso-compatible capsules ("N-capsules")

- (20) Nespresso is a type of single-serve machine which produces individual servings of espresso coffee. The consumables for Nespresso are coffee capsules with a solid shell (in contrast with the soft permeable packaging of a filter pad). N-capsules are compatible only with Nespresso machines. Coffee is prepared by placing the N-capsule in the machine which incorporates a mechanism whereby pressurised water comes into contact with the coffee inside the N-capsule. Some N-capsules are pre-opened or pre-perforated; others are opened or perforated in the machine. Nestlé sells Nespresso coffee machines as well as the original N-capsules (in specialised boutiques and online), while the Parties and other suppliers offer compatible N-capsules on retailers' shelves.

¹¹ In addition DEMB operates coffeehouses in the Netherlands, while Mondelēz does not have such activities anywhere in the world and is only a recent entrant into the in-home coffee markets in the Netherlands. According to DEMB its share in the potential market for outlets serving coffee (whether considering all establishments offering coffee or more specialist coffee shops or coffee houses) is less than [0-5]*% in the Netherlands as a whole or in any given city or town within Netherlands. Due to the limited presence of DEMB in the putative market for coffeehouses the potential vertical link between Mondelēz's activities in in-home coffee and DEMB's activities in coffeehouses in the Netherlands will not be analysed further. Furthermore DEMB manufactures and sells tea. Mondelēz does not have any tea activities save for sales of Twinning's tea T-discs sold under licence.

6.5. Other consumables for single-serve machines

- (21) Consumables are individually packed (in capsules, pods, pads) portions of coffee to be inserted into a single-serve machine and produce a cup of coffee. In addition to filter pads and N-capsules, there are other types of single-serve consumables on sale to consumers. These consumables will generally all be based on proprietary technology with the aim of producing a single cup of coffee. Each consumable is made to function in a specific type of machine.

6.6. Single-serve systems – Senseo and Tassimo

- (22) DEMB owns the Senseo trademark and, together with Philips develops and markets the Senseo system. The consumables for Senseo machine are filter pads. Mondelēz owns the Tassimo trademark and, together with Bosch, develops and markets the Tassimo system. The consumables for Tassimo machines are T-discs. As set out in section 9.4.2, the Parties, although they do not sell single-serve machines¹², are involved in the promotion and advertising of those machines and have influence on their prices. For the purpose of this Decision the term "single-serve system" means single-serve machine and the consumables compatible with those machines.

7. RELEVANT PRODUCT MARKETS

- (23) Both Parties are active in the manufacture and sale of various coffee products through different channels, covering many different "routes to the cup". They include sales to businesses ("out-of-home") and to consumers ("in-home"). While multi-serve coffee machines (such as drip filter machine, French press or *cafetière*) produce more than one portion of coffee at a time, single-serve machines produce in principle one cup of coffee at a time. The main coffee formats used in multi-serve machines are R&G coffee and whole beans. The consumables used for single-serve machines include: filter pads for DEMB's Senseo system, N-capsules for Nestlé's Nespresso system and, additionally, Mondelēz' capsules ("T-discs") for its closed¹³ single-serve system Tassimo. Another coffee format is instant coffee, for which no machine is needed.

Parties' arguments

- (24) While the Parties consider that it is not necessary for the Commission to reach a conclusion on the precise market definition in this case, they nevertheless analyse the overlaps of their activities in the coffee sector on the narrowest – in their view – plausible segmentations.

Market segmentations assessed in this Decision

- (25) The Commission analysed several possible segmentations of the overall coffee sector. First of all it will be analysed whether in-home coffee and out-of home coffee belong to the same product market. Secondly it will be assessed whether private label brands compete with branded coffee products in the same market. Thirdly it will be considered whether conventional and non-conventional coffee should be considered as one relevant market. Fourthly the single-serve machines and their consumables (such as filter pads and N-capsules) will be analysed. Fifthly coffee format compatible with multi-serve machines, that is R&G coffee and its potential

¹² Tassimo machines are sold by Bosch while Senseo machines are sold by Philips.

¹³ As Mondelēz has intellectual property rights ("IP") to produce capsules for its Tassimo single-serve system, no other company can lawfully produce compatible T-discs.

segmentations (whole beans, Greek coffee, Robusta and Arabica) will be assessed. Finally the instant coffee segment will be considered.

(26) An overview of the segments referred to Recital (25) is provided in Figure 1.

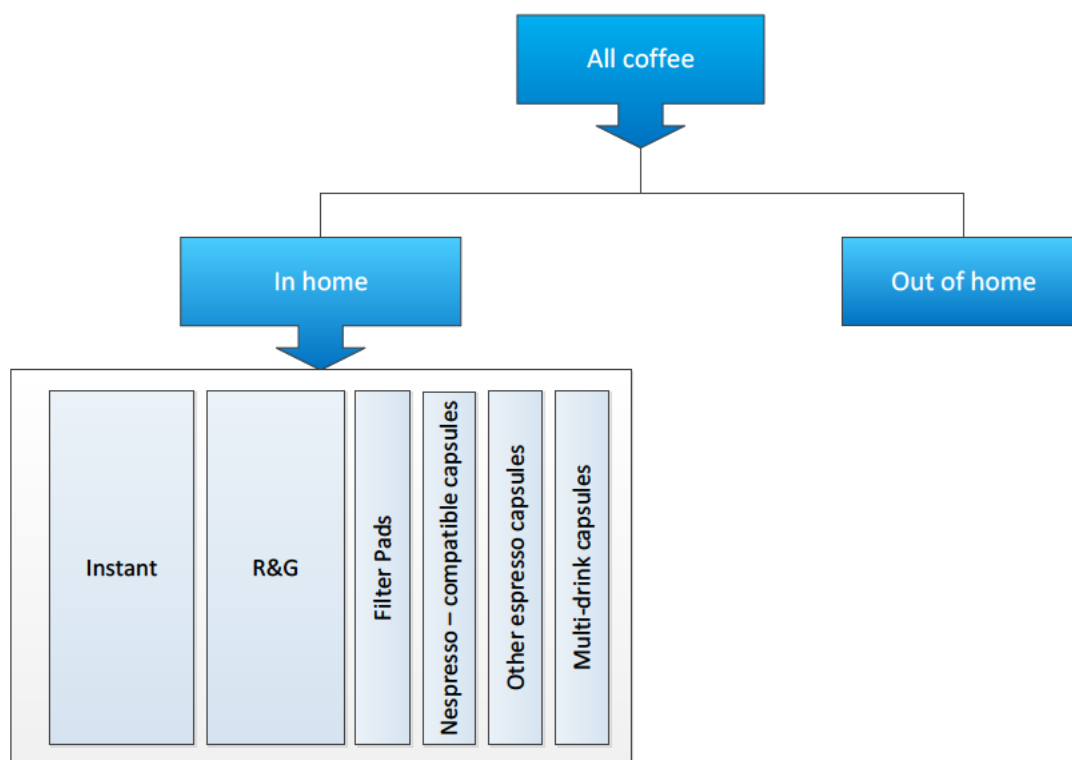


Figure 1 Coffee Sector¹⁴

7.1. In-Home vs. Out-Of-Home

(27) The Parties are both active in the manufacture and sale of coffee products through two key channels:

- (1) "in-home", that encompasses the sale of coffee to consumers via retailers or directly to consumers through, for example, mail order systems; and
- (2) "out-of-home", that encompasses the sale of coffee to hotels, restaurants, cafes (referred to as "HoReCa") but also to offices, hospitals, educational establishments and other work places.

(28) According to the Parties, the in-home channel covers around 70% of the worldwide coffee sales, while the out-of-home channel represents the remaining 30%.

7.1.1. Out-of-home

(29) The out-of-home channel targets a variety of customers, to which the coffee manufacturers offer a portfolio of products and related services based on the individual customers' needs (that is to say types of beverages, crockery and maintenance of machines).

(30) The out-of-home channel could potentially be further segmented, that is per portfolio of drinks sourced, per customer categories, or per type of contract (whether it includes also any maintenance or just the supply of coffee products).

¹⁴ Source: Form CO.

Parties' arguments

- (31) The Parties submit that the solutions offered to customers usually include a combination of coffee, tea, other consumables, coffee machine, vending machines, crockery and support services. The combination of these products and services will depend on the needs and preferences of the customer.
- (32) Each of the elements provided in an out-of-home solution (the coffee, other consumables, coffee machine, crockery and services) can be sourced from one or multiple suppliers. Furthermore the regular delivery of ingredients can be made directly by the supplier or through the preferred logistical provider of the customer.
- (33) Some larger customers opt for a formal tender process, specifying requirements and inviting various players for bids. However, most customers will have an informal buying process, where they discuss their needs and preferences with sales representatives from their current supplier and from other suppliers. Each supplier will assess the needs of the customer and propose a solution from his portfolio of products and machines. Given the range of options and the different specialities of suppliers, the customer is rarely choosing between identical offers.
- (34) Both Parties internally divide their out-of-home customers into various groups according to their customer's businesses. However DEMB and Mondelēz do not split their customers into the same types of categories. DEMB follows a split focussed on sales effort, while Mondelēz splits the out-of-home customers based on a [...]*; as a result, the categories used are not comparable;¹⁵ moreover, the Parties do not consider that such divisions are appropriate for the purpose of defining relevant markets. The Parties also claim that there is no need to separate the various distribution channels within the out-of-home channel as separate product markets. Instead, according to the Parties, the relevant market should comprise all types of out-of-home coffee sales.

7.1.2. In-home

- (35) In the in-home channel, coffee manufacturers normally¹⁶ negotiate supply agreements with national and regional retailers in order to place their coffee products on the retailers' shelves for purchase by final consumers. Such negotiations normally encompass all types of coffee products and, in some cases all the products of the manufacturer across several categories (that is snacks and beverages). According to the Parties, negotiations tend to be annual.
- (36) Through retailers the Parties sell coffee in multiple formats compatible with various existing coffee brewing methods. Those formats include for instance R&G, instant coffee, filter pads, N-capsules and other consumables for single-serve systems.

Parties' arguments

- (37) The Parties submit that within each format, a consumer can find a considerable variety of coffee (for instance coffee made from Robusta or Arabica beans, from single country origin or mixed origin, fair trade, "long" coffee, espresso coffee).

¹⁵ DEMB's categories include: small business, medium business, large business, health and care, education, hotel and gaming, BaReCa, QSR and coffee houses, convenience and retail, and leisure. Mondelēz categories include: [...]*.

¹⁶ There might be exceptions, i.e. a manufacturer supplying private label products or Nestlé selling Nespresso capsules in dedicated shops and online.

- (38) Moreover, the price range of coffee products within each format and between formats varies (from low-priced to mid-priced to premium).
- (39) The popularity of a specific type of coffee (whether in terms of format or taste) varies from one Member State to another.
- (40) The further segmentation of the in-home channel is described in the following sections.

Commission's investigation and assessment

- (41) The Commission acknowledges the difference in customers and distribution (retail negotiation vs. service contracts) between the in-home and out-of-home channels. Those differences have been confirmed by interviews with market participants, which highlighted also the possibility of several segmentations among out-of-home customers (that is to say per size, per volume or per activity).¹⁷
- (42) Coffee manufacturers can be active in both the in-home and out-of-home channels. The out-of-home suppliers, however, also comprise a range of other players such as service companies, catering companies and vending operators selling hot beverage, cold beverage and snack solutions, which might have in-house roasting capabilities or might source their coffee from third-party manufacturers, while in-home suppliers are mainly coffee manufacturers and retailers via private labels products.

Conclusion

- (43) Although the available coffee formats tend to be broadly the same in both channels¹⁸, given the presence of different customer groups, different products or services offered, partly different competitors and the different competitive dynamics (that is to say yearly negotiations with retailers for in-home as opposed to a customised offers tailored at specific customers' needs for out-of-home), the Commission considers that for the purposes of this Decision, sales via the in-home and out-of-home channels form part of separate product markets.
- (44) Moreover, for the purposes of this Decision, the Commission considers that all out-of-home sales belong to the same product market given the individual needs of each out-of-home customer and the tailor made approach applied to each of their customers by the Parties.
- (45) In relation to in-home sales, the Commission considers that a further segmentation is necessary (see sections 7.2, 7.3, 7.5 and 7.6).

7.2. Private label vs. brands

- (46) The coffee sector is a differentiated sector which is characterised by the presence of brands and their perception by consumers. A coffee company might have multiple brands with different positioning in the market (for example, a premium brand sold at a higher price and a mainstream brand sold at a lower price).

¹⁷ See for instance the non-confidential minutes of a conference call with a competitor dated 18 November 2014 at 13.00 CET, non-confidential minutes of a conference call with a competitor dated 18 November 2014 at 10.45 CET, non-confidential minutes of a conference call with a competitor dated 19 November 2014 at 16.00 CET.

¹⁸ Coffee is usually provided in larger quantity formats to out-of-home customers. Another difference is that DEMB's out-of-home customers can have access to Liquid coffee, which is not available to in-home customers: this is proprietary DEMB technology where coffee is brewed under ideal circumstances and immediately concentrated, packed in a closed bag-in-box pack and deep-frozen, maintaining the coffee quality until the moment of serving.

- (47) Private label brands do exist but their penetration varies from country to country and retailer to retailer, and in many countries still remains relatively low, in particular in comparison to the penetration of private label brands in a number of other fast moving consumer goods such as frozen ready cooked meals, frozen vegetables, canned vegetables or edible oil.¹⁹ It should also be noted that penetration of private label brands may vary depending on the coffee format.

Parties' arguments

- (48) The Parties argue that private label brands are present at all levels of the coffee sector: in addition to offering the cheapest option to consumers, private label brands also compete with branded coffee across the full range of price, quality and variety of offerings, including high quality premium beans and single country origin coffee.²⁰ Furthermore private label brands often mirror the offering of branded coffee, are sold from the same shelves and sometimes have even better placements than branded coffee products on the shelves.
- (49) The Parties point to the high degree of supply side substitutability between branded coffee and private label products, as most coffee manufacturers supply retailers with both types of products. Also, in some instances the retailers have in-house roasting capabilities and are thus also coffee manufacturers.

Information obtained in the Commission's investigation

- (50) According to the majority of respondents to the market investigation, private label and branded coffee are substitutable to a certain extent in the eyes of the consumer²¹ and private label and branded coffee compete with each other on retailers' shelves.²²
- (51) Retailers in the course of the market investigation pointed out that in the majority of cases private label products do not have special²³ placements on retailers' shelves²⁴ and have lower but rather stable prices, while branded coffee is normally priced at a higher level but is characterised by temporary promotions that lower the price.²⁵ In general, retailers tend to obtain higher margins from the sale of private label products than from branded coffee products.²⁶
- (52) Lastly, for the majority of respondents to the Commission's questionnaires, the supply of private label products is different from the supply of branded goods in

¹⁹ See the "The Commission's final report on the economic impact of modern retail on choice and innovation in the EU food sector", published on 19 September, 2014, available at: <http://ec.europa.eu/competition/publications/KD0214955ENN.pdf>.

²⁰ In its recently published study on "The economic impact of modern retail on choice and innovation in the EU food sector", the European Commission stated: "*Private labels are increasingly being seen by retailers as important tools for building client loyalty and strengthening banner image. Thus, beyond generic and 'mimic' private labels, which are designed to provide low cost alternatives or directly compete with manufacturer's brands, retailers have increasingly developed high quality private label brands that compete side by side with manufacturer's brands or specifically positioned product ranges, such as organic.*" (see: European Commission, "The economic impact of modern retail on choice and innovation in the EU food sector: final report" *ibidem*, at p. 54).

²¹ Responses to question 35 of Questionnaire Q2-Retailers and responses to question 35 of Questionnaire Q1-Competitors.

²² Responses to question 36 of Questionnaire Q2-Retailers and responses to question 36 of Questionnaire Q1-Competitors.

²³ Special placement usually implies putting products in the so called "diamond area" that is in the upper middle of the retail shelf that provides the best product visibility – see Form CO par. 514.

²⁴ Responses to question 37 of Questionnaire Q2-Retailers.

²⁵ Responses to questions 38 and 38.1 of Questionnaire Q2-Retailers.

²⁶ Responses to questions 39 and 39.1 of Questionnaire Q2-Retailers.

general, given that a keen focus on price and multi-year contracts characterises the former and yearly negotiations with detailed promotion plans are typical for the latter.²⁷

- (53) The Parties' internal documents also show that coffee manufacturers monitor the performance of private label brands and thus consider private label as competing with both DEMB's and Mondelēz's brands.²⁸

Conclusion

- (54) Overall, taking into account the results of the market investigation and the Parties' arguments which have been confirmed by the Commission's investigation, the Commission considers for the purposes of this Decision that private label and branded coffee products, irrespective of the coffee format, belong to the same product market. However, given the differentiated nature of the relevant coffee markets, different penetration rates and ranges of offerings, as well as the fact that private labels are fragmented by nature (each retailer having a different strategy and policy), the competitive pressure exercised by private label brands on the Parties varies from country to country and format to format.

7.3. Conventional vs. non-conventional coffee

- (55) Given the presence of non-conventional coffee (that is to say organic, fair trade and other certified coffees) across several formats, the Commission investigated whether there is a separate market for non-conventional coffee across all the formats.

Parties' arguments

- (56) The Parties do not consider non-conventional coffee as a separate market, in particular since they do not gather data on coffee products by sustainability certification²⁹ and therefore were not able to provide market share estimates at that level.

Information obtained in the Commission's investigation

- (57) During the market investigation the majority of competitors indicated that the two coffee categories are perceived as potential alternatives by consumers³⁰ and are substitutable to a certain extent.³¹ On the other hand, the responses from retailers indicated that consumers might not necessarily switch between the two coffee categories in case of a small but permanent price increase³², and some consumers might perceive non-conventional coffee as fulfilling different needs from conventional coffee, such as the need for an organic product which is perceived as healthier or the need to feel more environmentally sustainable or to contribute to sustainable development, or again the need to have a higher quality products

²⁷ Responses to questions 40 and 40.1 of Questionnaire Q2-Retailers and responses to questions 38 et seq. of Questionnaire Q1-Competitors.

²⁸ See for instance Mondelēz internal document, dated 20 June 2014 "*Project Sequoia – Key Themes*" page 2, Mondelēz internal document, dated 15 April 2014 "*On Demand: how to boost mondelez performance?*" page 71 et seq., DEMB internal document, dated October 2013, "*Capsules market data / JvB*" page 5 and 6 and DEMB internal document, undated, "*Thank You for this new Exciting Challenge – Let's be Partners in Success*" page 118 et seq.

²⁹ Responses of 18 September 2014 to QP2, question 5(j) and Form CO paragraph 307.

³⁰ Responses to question 33 of Questionnaire Q1-Competitors.

³¹ Responses to questions 32 et. seq. of Questionnaire Q1-Competitors.

³² Responses to questions 32 et. seq. of Questionnaire Q2-Retailers.

produced in an environmentally-friendly way.³³ Respondents also noted differences in consumption patterns, prices and targeted consumer groups.³⁴

- (58) As regards supply-side substitutability, the majority of competitors who responded to the market investigation considered that a supplier active only in conventional coffee will be able to start, swiftly and without significant costs, production and sales of non-conventional coffee and vice-versa.³⁵

Conclusion

- (59) Taking into account the views expressed in the market investigation and in particular for reasons of supply-side substitutability, the Commission considers that for the purposes of this Decision, it is not necessary to differentiate between conventional and non-conventional coffee. Moreover, no competition concerns were raised during the investigation either by the Parties' customers or competitors in respect of the hypothetical non-conventional coffee segment.

7.4. Single-serve machines and consumables

7.4.1. Single-serve vs. multi-serve machines

Parties' arguments

- (60) The Parties maintain that they do not manufacture or sell coffee machines but they admit that they do own machine brands and participate in the marketing of machines. The Parties also state that coffee machines are differentiated by the number of servings they produce (single-serve or multi-serve), the type of coffee (filter or espresso), and whether they make other types of drinks (hot cocoa, tea and cold drinks). In particular the Parties note that the advantages of single-serve coffee machines over the multi-serve ones include: ease of use, consistent quality and in some instances additional variety.
- (61) The Parties also argue that when consumers buy a single-serve machine, they do not switch the entirety of their coffee consumption from the previous multi-serve machine to the new single-serve but rather keep using both machines (this is referred to as multi-homing). For that reason, the Parties claim that when it comes to the (after-)markets of consumables for single-serve machines, R&G coffee, which is used in multi-serve systems like drip filter machines, constrains in particular DEMB's Senseo (which produces filter coffee) and that therefore the line between multi-serve and single-serve is not clear (see section 9.7.1.4).

Commission's investigation and assessment

- (62) Coffee machines are various appliances used to produce coffee ranging between simple French press machines to the more complicated single-serve machines which can produce various types of beverages in addition to coffee (so called multi-drink machines).
- (63) The coffee machines sector can be further differentiated according to whether the brewing method used produces more than one cup at a time, like for instance traditional drip filter machines (so-called "multi-serve"), or only one cup at a time (so-called "single-serve").

³³ Responses to questions 33 and 33.1 of Questionnaire Q2-Retailers.

³⁴ Responses to question 34 of Questionnaire Q1-Competitors and responses to question 34 of Questionnaire Q2-Retailers.

³⁵ Responses to questions 31 et seq. of Questionnaire Q1-Competitors.

- (64) Each of these brewing methods requires a coffee machine and a coffee of a particular format, which can range from loose ground coffee (R&G) to ground coffee packed in soft pads, and from coffee sealed in N-capsules or other consumables to whole beans.
- (65) The most common multi-serve machines are drip filter machines, French presses and *cafetiers* which are normally used with R&G coffee.
- (66) The main single-serve machines in the EEA include: Senseo, Tassimo, Dolce Gusto and Nespresso. Other machines on the market, with more national or regional presence, include Cafissimo, Expressi and A Modo Mio.
- (67) Retailers and competitors in the course of the market investigation emphasised the following differences between single-serve and multi-serve coffee machines: the former are more premium and associated with better quality, they enable the final customer to prepare coffee in a much more convenient way, to choose not only black coffee but also milky coffees and other flavoured coffees.³⁶ Retailers and competitors also noted that single-serve machines are much more expensive than multi-serve machines and similarly the corresponding consumables for single-serve are more costly than the coffee formats used for multi-serve, which leads to higher cost per cup for the former.³⁷ As a result, retailers consider that single-serve machines are targeted at wealthier consumers. Due to the single-serve machines' qualities and in particular the ease of use and cleanliness they are also targeted at younger customers. An overwhelming majority of competitors does not consider that a supplier active in multi-serve coffee products could swiftly change into production of single-serve and cite investment into manufacturing lines and in "consumer communication package" as main obstacles for the switch.³⁸
- (68) Moreover, in their internal documents, the Parties consider the competitive dynamics pertaining to single-serve segment separately from those pertaining to multi-serve segment.³⁹

Conclusion

- (69) On the basis of differences in product characteristics, intended use and prices, as well as limited supply-side substitutability the Commission concludes that single-serve coffee machines belong to a different product market than multi-serve coffee machines. Since the Parties are not active in the latter, they will not be analysed further in this Decision. Since the Parties, as explained in the section 9.4.2, do have influence on the prices of single-serve machines even though they do not sell those machines, the Commission will consider the relevant market for single-serve machines in Section 7.4.2.

7.4.2. The relevant market for single-serve machines

- (70) As a general rule, the machine manufacturers (such as Bosch, Philips, Magimix, Krups and others) are responsible for the technical development, manufacturing and

³⁶ Responses to question 19 of Questionnaire Q2 – Retailers and to question 14 of Questionnaire Q1-Competitors.

³⁷ Responses to question 20 of Questionnaire Q2 – Retailers and to questions 14, 15 of Questionnaire Q1-Competitors.

³⁸ Responses to question 13 of Questionnaire Q1 – Competitors.

³⁹ See for instance Mondelez internal document, dated 15 April 2014, "On Demand: how to boost mondelez performance?" page 6, Mondelez internal document, dated 2011, "EU Coffee – KFE Management Overview" page 7, DEMB internal document, undated, "Multi Serve Benelux" and DEMB internal document, dated November 2013, "DEMB – Retail Sales – November 2013".

sale of the machines, for which they set the selling prices, whereas the coffee manufacturers (such as Mondelēz, DEMB, Tchibo, Nestlé) are responsible for the development, manufacturing and sales of consumables, for which they set the selling price. However, coffee manufacturers can and do allocate part of their marketing resources to subsidise machines sales. Due to the high interdependence between coffee machines and compatible consumables sales, the coffee manufacturers have a material interest to promote as much as possible the penetration of the single-serve system, for which they sell coffee consumables to maximise their sales of coffee consumables. The degree of collaboration and independence between the coffee manufacturer and the machine manufacturer can vary from one case to another, as described in section 9-4-2.

Parties' arguments

- (71) The Parties submit that single-serve machines are sold by their manufacturers and not by DEMB or Mondelēz. Whilst they admit that both DEMB and Mondelēz do provide certain levels of marketing and promotional support to incentivise sales of the machines in order to boost sales for their respective consumables, they submit that the market for the single serve machines is not relevant for the analysis of the effects of the Transaction given that they do not realise any machine sales.

Nestlé's arguments

- (72) According to Nestlé all single-serve machines belong to the same market for the following reasons: (i) all of them aim at fulfilling similar consumer needs, namely to produce a single portion of hot beverage (mainly coffee) in an easy, quick and convenient way, (ii) even the multi-drink machines are used predominantly to make coffee, (iii) they all compete with each other and promotion on one of the machines has an impact on sales of the others, (iv) there is supply-side substitution between them.

Previous decisions by the Commission and other competition authorities

- (73) The Commission has previously analysed the market for coffee machines, where it considered that electric filter coffee makers (also called drip filter coffee machines) and espresso machines belong to separate product markets⁴⁰ but when analysing single-serve filter pad machines, the Commission did not conclude whether such coffee machines are in the same market as espresso machines.⁴¹ In the same decision, the Commission stated that “[p]ad machines such as Senseo clearly appear as an improvement of the traditional drip filter machines”.⁴²
- (74) The French competition authority in its decision concerning an abuse of a dominant position by Nestlé considered the existence of a separate market for high pressure single-serve coffee machines.⁴³ It also concluded that coffee manufacturers are active in the market for such machines. Consequently the French competition authority attributed the share of sales of those machines to Nestlé and not to the relevant machine manufacturer.

⁴⁰ M.2621 - SEB / Moulinex paragraph 59.

⁴¹ M.5547 - Koninklijke Philips Electronics / Saeco International Group paragraph 30.

⁴² M.5547 - Koninklijke Philips Electronics / Saeco International Group paragraph 30.

⁴³ Decision No 14-D-09 of 4 September 2014.

Commission's investigation and assessment

- (75) As stated at Recital 22, DEMB owns the Senseo trademark and, together with Philips develops and markets the Senseo machines and filter pads (the "Senseo system"). Mondelēz owns the Tassimo trademark and, together with Bosch, develops and markets machines and T-discs (the "Tassimo system"). Details of the cooperation between the Parties and their respective machine partners are set out in Section 9.4.2.
- (76) As will be presented in more detail in Section 9.4.2, although the Parties (unlike Nestlé) do not directly sell single-serve coffee machines, they have both the ability and incentive to influence the machines' prices and they do actually influence it. They are also heavily involved in the marketing and promotion of those machines, consulted on their design and so on. Therefore, contrary to what the Parties argue, given the influence that the Parties exercise on the machine sales, the Commission takes the view that it is relevant to assess the effects of the Transaction on the market for single-serve machines.
- (77) As regards the issue whether all single-serve machines belong to the same product market, an overwhelming majority of electronic goods retailers and a majority of retailers and machine manufacturers that responded to the Commission's market investigation confirmed that final consumers view the various single-serve machines as broad substitutes because they all allow for brewing a cup of coffee with one click.⁴⁴ The common features shared by all single-serve machines and important for the final customers are: simplicity, convenience and speed.⁴⁵
- (78) As regards the importance for the final consumers of the level of pressure with which single-serve coffee machines functions, the results of the Commission's market investigation were not conclusive, with some of the retailers stating that in most cases the final consumers are not even aware of the pressure of the machine they purchase while other retailers took the view that the higher the level of pressure the better quality coffee can be made.⁴⁶ As a result it can be concluded that for some final customers the level of pressure of single-serve coffee machine can be one of the factors they take into account when deciding to purchase a single-serve machine. However the main product characteristics differentiating single-serve machines from other machines include their convenience, cleanliness, and their quick and easy operation.
- (79) On the other hand fully automated coffee machines or the bean-to-cup machines⁴⁷ are not considered as belonging to the same market as single-serve coffee machines due to their significantly higher prices. Furthermore they do not offer the same cleanliness, convenience and speed in preparing the hot beverage as single-serve machines, because for the latter the coffee is already pre-packaged in the pads, pods, capsules etc.
- (80) While different single-serve machines are positioned differently, with some of them being presented to final customers as offering in principle dark strong coffee (for instance Nespresso), while others as offering a variety of different drinks (such as

⁴⁴ Responses to question 2 of Questionnaire Q10 – Retailers and to question 6 of Questionnaire Q11 – Electronic goods retailers and to question 8 of Questionnaire Q12 – Machine manufacturers.

⁴⁵ Responses to question 2 of Questionnaire Q10 – Retailers and to question 8 of Questionnaire Q12 – Machine manufacturers.

⁴⁶ Responses to question 5 of Questionnaire Q10 – Retailers and to question 9 of Questionnaire Q11 – Electronic goods retailers.

⁴⁷ These machines grind coffee beans for each serving of coffee individually.

Tassimo and Dolce Gusto) this does not imply that they belong to different product markets. It is rather, as Nestlé argues, that in the eyes of final consumers they are broad substitutes, competing with each other. However the specific characteristics of a given single-serve machine (for instance offering only dark coffee or offering also a variety of other drinks) are important for the closeness of competition within the differentiated market. Thus they will be taken into account in Section 9.4.5.1.

Conclusion

- (81) On the basis of the foregoing, the Commission concludes that all single-serve machines belong to one differentiated product market. While the Parties do not directly sell their single-serve machines they are able and they do influence the prices of such machines. Therefore, although the market for single-serve coffee machines is not an affected market within the meaning of Section 6.3 Form CO⁴⁸, the Commission will consider it in its assessment in the Sections 9.4.5 and 9.4.6.

7.4.3. Consumables for single-serve machines (filter pads, N-capsules and other)

Introduction

- (82) Each type of single-serve machine requires a specific format of consumable. DEMB's Senseo machine, for example, requires filter pads though such pads can be produced by any coffee company as Senseo is an open system. Mondelēz' Tassimo machine requires T-discs which can be produced only by Mondelēz (Tassimo being a closed system). Nestlé's Dolce Gusto requires Dolce Gusto capsules which can be manufactured only by Nestlé (Dolce Gusto being a closed system). Nestlé's Nespresso machine requires Nespresso capsules which, can be produced by any coffee company which manages to develop a suitable technology to build compatible capsules (Nespresso being a semi-open system). There are a number of local or regional players having different single-serve systems comprising specific capsules, for example, Tchibo with Cafissimo, Aldi with Expressi and Paulig with Cupsolo.
- (83) As regards consumables for single-serve machines, the Parties' activities overlap in the production of filter pads and N-capsules.

Parties' arguments

- (84) As mentioned in Recital (24), the Parties claim that it is not necessary for the Commission to reach a conclusion as to the exact scope of the relevant product markets in this case. However, they describe their activities with respect to the narrowest segments of coffee consumables for single-serve coffee machines, that is filter pads and N-capsules separately.
- (85) The Parties also argue that no distinction should be made according to the different distribution channels and that original N-capsules belong to the same market as compatible N-capsules, since Nespresso has clearly reacted to the entry of compatible N-capsules on the market.
- (86) Specifically with respect to filter pads, the Parties claim they are very close to R&G in terms of product features, taste pattern, and production process; moreover they

⁴⁸ Form CO relating to the notification of a concentration pursuant to regulation (EC) no 139/2004, Annex 1 to Commission Regulation (EC) No 802/2004 of 21 April 2004 implementing Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (OJ L 133, 30.04.2004, p. 1-39), as amended by Commission Regulation (EC) No 1033/2008 (OJ L 279, 22.10.2008, p. 3-12) and by Commission Implementing Regulation (EU) No 1269/2013 of 5 December 2013 (OJ L 336, 14.12.2013, p. 1-36).

state that both types of products can be produced in the same production facilities, and that the production of both product types is not patent protected. The Parties therefore argue that R&G and filter pads belong to the same market or at least that R&G exercises a significant competitive constraint on filter pads. To support their claim, the Parties refer to a sector inquiry carried out by the German competition authority⁴⁹ which focuses on relative differences in production technologies between the different coffee formats and considers that instant coffee, cappuccino powders, coffee substitutes and N-capsules require more complex technologies than filter pads and R&G.

- (87) Furthermore, the Parties claim that filter pads consumers are highly price sensitive, which is evidenced by the increasing share of private label filter pads over time. Moreover, for instance in France, the majority of filter pads users also has a multi-serve machine and therefore could easily switch between the two types of coffee.

Nestlé's arguments

- (88) Nestlé submits that all consumables for the various single-serve machines (in particular filter pads, T-discs and N-capsules) belong to the same product market for the following reasons: (i) all consumables are aimed at satisfying the same need, that is to have a cup of hot beverage, (ii) there is demand-side substitution between all the different consumables which means that in particular the consumers owning a Senseo machine switch to Tassimo machine once the lifetime of their Senseo machine has lapsed, (iii) there is supply-side substitutability in terms of production, stocking and delivery of all types of consumables.

Commission's investigation and assessment

- (89) As regards single-serve coffee consumables, the Commission has never analysed the markets for coffee in those different formats.
- (90) It needs to be reiterated that within the single-serve category, there is (i) inter-system competition between providers of the various coffee systems and (ii) intra-system competition at the consumables level between providers of consumables for those coffee systems, whenever the system is not closed. Therefore, since each system has one specific consumable with which it operates (that is to say Senseo operates only with filter pads, Nespresso only with N-Capsules and Tassimo only with T-discs), once a consumer has bought a specific machine, that consumer is bound to the machine and its consumables. Whenever the same consumer would wish to switch to different consumables (that is to say switch from filter pads to N-capsules or from N-capsules to T-discs), it would need to purchase a new single-serve machine. Thus, despite Nestlé's claims, once a consumer has bought a single-serve machine, switching to consumables for another machine is not straightforward and requires the purchase of a new machine.
- (91) The Commission acknowledges that the relatively high subsidisation and the aggressive promotional activities exercised by coffee manufacturers on coffee machines result in lower prices of single-serve machines which might reduce the barriers to switching and thus entice consumers to purchase new single-serve machines. However, it seems unlikely that changes in relative prices of different consumables would trigger consumers to keep on switching their machines or have

⁴⁹ Bundeskartellamt, Sektoruntersuchung Lebensmitteleinzelhandel, September 2014, p. 201, (http://www.bundeskartellamt.de/Sektoruntersuchung_LEH.pdf;jsessionid=8621409BCB6D56A341A9EC2CAEAF9D8.1_cid371?_blob=publicationFile&v=7)

multiple single-serve machines in their household. This was also confirmed by retailers, electronic goods retailers, machine manufacturers and competitors.⁵⁰

- (92) Furthermore with the different levels of patent protection over the various consumables, supply-side substitutability is also questionable. This is reinforced by the fact that in order to start producing single-serve coffee consumables, most often a company needs to invest in new machinery with new or licensed intellectual property rights ("IP") (or to team up with a machine manufacturer to create a totally new system). In particular for closed systems, such as Tassimo and Dolce Gusto, for which only Mondelēz and Nestlé respectively produce consumables, other suppliers are not able to offer compatible consumables.

Conclusion

- (93) Due to limited demand and supply-side substitutability the Commission concludes that consumables for the various single-serve systems do not belong to the same market. Moreover, the Commission considers that ultimately, only those consumables that are compatible with a specific system compete with each other, that is for instance filter pads supplied by various coffee producers compete with each other. That, however, does not imply that the relative prices of different types of consumables have no significance since the price of consumables is one factor that the consumers may take into account when deciding which single-serve machine to purchase.⁵¹
- (94) In Sections 7.4.3.1 to 7.4.3.2 the Commission analyses in more detail the arguments put forward by the Parties and Nestlé with regard to N-capsules and filter pads, as those are the consumables for which the Parties' activities overlap.

7.4.3.1. N-capsules

- (95) Until very recently, Nespresso was a closed system, with Nestlé seeking to prevent other coffee producers from competing in the supply of N-capsules through legal action and various other means.⁵² The closed nature of the Nespresso system allowed Nestlé to charge high prices⁵³ for its N-capsules, supported by its unique distribution system in which Nestlé controls the distribution and prices through its boutique stores, its website and call centres.
- (96) The Nespresso system is now semi-open (pending the result of ongoing legal challenges), allowing other producers to compete for the supply of N-capsules. The "opening" of the Nespresso system has led to third party producers beginning to generate significant sales of N-capsules. Figure 2 shows the share of Nespresso of N-capsule sales in blue and that of third parties in red:

⁵⁰ Responses to question 9 of Questionnaire Q10 – Retailers, to question 10 of Questionnaire Q12 – Machine manufacturers, to question 13 of Questionnaire Q11- Electronic goods retailers and to question 8 of Questionnaire Q9- Competitors.

⁵¹ Responses to question 6 of Questionnaire Q10 – Retailers, to question 10 of Questionnaire Q11 – Electronic goods retailers, to question 6 of Questionnaire Q9 – Competitors and to question 6 of Questionnaire Q12 – Machine manufacturers.

⁵² See these measures in the French competition authority's recent preliminary report: (http://www.autoritedelaconurrence.fr/user/standard.php?id_rub=592&id_article=2343).

⁵³ Even after the compatible N-capsules were introduced on retailers' shelves, according to the Parties the average price per cup for Nespresso is between 35-42 cents, while the price of compatible N-capsules is approximately 30 cents – see Parties response to Article 6(1)(c) Decision and DEMB internal document, dated May 2014, "DEMB Category Strategy – Single serve" slide 10.

[...]*

Figure 2 – Nespresso EU N-capsules vs. Third party sales⁵⁴

- (97) Whereas Nestlé sells Nespresso products either on the internet or through a small number of boutique retail shops, the new entrants have introduced N-capsules through multiple traditional retail and grocery channels. While Nespresso remains the largest supplier by a very considerable margin, other brands are steadily eroding Nestlé's share with some brands (including strong retailer brands) having achieved significant success.⁵⁵
- (98) In the Sections 7.4.3.1.1 and 7.4.3.1.2 the Commission will assess whether (i) N-capsules should be considered as a separate market and (ii) original and compatible N-capsules belong to the same market

7.4.3.1.1 N-capsules as a separate relevant market

- (99) The Commission investigated in more detail the supply- and demand-side substitutability of N-capsules with filter pads and other capsules.

N-capsules vs filter pads

- (100) The majority of respondents to the Commission's questionnaires in the market investigation consider that N-capsules and filter pads are not substitutable in the eyes of the consumers⁵⁶ and that N-capsules are different from filter pads in consumption patterns, prices and targeted consumer groups.⁵⁷
- (101) Moreover, the majority of competitors who replied to the questionnaire are of the view that a supplier active only in filter pads would not be able to start swiftly and without significant costs the production and sale of N-capsules and vice versa.⁵⁸ The Commission also notes that any company wishing to start the production of N-capsules or filter pads would need to invest in new dedicated production lines. In addition, a company wishing to start production of N-capsules would need to develop a production technology or get a licence for an existing one.
- (102) Moreover, the Parties' internal documents show that there is a [...] difference in the profitability of filter pads and N-capsules, with the former averaging EUR [...] of gross margin per cup and the latter reaching an average gross margin [...] higher at EUR [...].⁵⁹

Conclusion

- (103) Given the lack of supply- and demand-side substitutability and the differences in prices, profitability, production processes and consumption patterns, the Commission considers, for the purposes of this Decision that N-capsules are in a separate market from filter pads.

⁵⁴ Mondelēz's estimates.

⁵⁵ For example, in Spain, Mercadona entered the N-capsules segment in July 2013 and within a year acquired at [30-40]* % segment share. (Source Form CO paragraph 280).

⁵⁶ Responses to questions 24 et seq of Questionnaire Q1-Competitors and responses to questions 26 et seq. of Questionnaire Q2-Retailers.

⁵⁷ Responses to question 26 of Questionnaire Q1-Competitors and responses to question 28 of Questionnaire Q2-Retailers.

⁵⁸ Responses to questions 23 et seq. of Questionnaire Q1-Competitors.

⁵⁹ Source: Annex 6-2 to Form CO.

N-capsules vs other capsules

- (104) Retailers who responded to the market investigation indicated that N-capsules and other capsules are not substitutable,⁶⁰ are considered a distinct product fulfilling specific needs⁶¹ and have different consumption patterns, prices and targeted consumer groups.⁶²
- (105) Although competitors responding to the market investigation suggested that other capsules (that is to say multi-drink capsules used in Tassimo or Dolce Gusto) could be perceived as potential alternatives to N-capsules⁶³ and do not differ significantly from N-capsules in consumption patterns, prices and targeted consumer groups,⁶⁴ the fact remains that a consumer can only buy capsules that are compatible with the system that the consumer has at home. Therefore, competition between different types of capsules really does not take place after the consumer has made a choice. This is different from competition for the single-serve machines where indeed different single-serve machines could be considered as broadly substitutable with each other, with some of them potentially competing closer with each other in this differentiated market.
- (106) Moreover, the Commission notes that the majority of other capsules are covered by IP rights making them a "closed system", in which only the owner(s) of the rights can manufacture and sell the capsules. On the contrary, as already explained, N-capsules can be manufactured and sold by any coffee company.

Conclusion

- (107) In conclusion, the Commission considers that for the purpose of this Decision, N-capsules belong to a separate product market.

7.4.3.1.2 Compatible vs. Original N-capsules

- (108) The Commission investigated whether original N-capsules, sold in Nespresso-dedicated shops and online or via call centres, belong to the same market as compatible N-capsules sold by other coffee companies via the traditional retail channels
- (109) The majority of respondents to the market investigation clearly consider that original and compatible N-capsules compete with each other.⁶⁵ They both address the same type of consumer, that is to say, a consumer who has a Nespresso machine in their household and is looking for certain values that can be represented by the original Nespresso brand but also values expressed by other coffee brands which the consumer knows from purchasing coffee in other formats.
- (110) Internal documents of the Parties and Nestlé show that both original and compatible N-capsules are monitored by market participants⁶⁶ and, although some market

⁶⁰ Responses to questions 29 et seq. of Questionnaire Q2-Retailers.

⁶¹ Responses to question 30 of Questionnaire Q2-Retailers.

⁶² Responses to question 31 of Questionnaire Q2-Retailers.

⁶³ Responses to question 29 of Questionnaire Q1-Competitors.

⁶⁴ Responses to question 30 of Questionnaire Q1-Competitors.

⁶⁵ Responses to question 35 of Questionnaire Q9-Competitors and responses to question 49 of Questionnaire Q10-Retailers.

⁶⁶ See for instance DEMB internal document, undated, "*L'Or Espresso – build the right strategy for a top brand*" pag 77 et seq., Mondelēz internal document, dated Q2 2013, "*Business Review DX Project – Launch of Nespresso Compatible Capsules*", Nestlé internal document, dated 15 April 2014, "*Coffee & machine market shares*" non-confidential version pag. 11-12 and Nestlé internal document, dated 15 April 2014, "*A focus on: Jacobs Douwe Egberts*" non-confidential version pag. 17-19.

participants highlight different purchasing patterns between the two,⁶⁷ it is clear that original and compatible N-capsules compete with each other.

Conclusion

(111) Given the clear market response and the fact that both original and compatible N-capsules can be used in the same coffee machines, the Commission considers, for the purposes of this Decision, that original and compatible N-capsules belong to the same product market.

7.4.3.2. Filter pads

(112) The Commission has previously considered the differences between filter pads and coffee used in multi-serve machines⁶⁸ and concluded that: (i) the coffee product used in those two types of coffee machines is different; (ii) R&G is used in principle in multi-serve coffee machines, while filter pads are used in pad machines; (iii) filter pads allow for preparing a single cup of coffee in a quick, convenient and clean manner (with one click of a button); (iv) filter pads are marketed and promoted by coffee companies as an upgrade from the traditional methods of coffee brewing and as a result, they are associated by consumers with a more modern product.

(113) As regards demand-side substitutability between filter pads and R&G, although the competitors' responses to the Commission's questionnaires indicated that a part of consumers might switch a minor portion of their purchases from one coffee format to the other in case of a small but permanent price increase, the majority of retailers replied that filter pads are not substitutable with R&G and vice versa. Moreover the majority of both retailers and competitors clearly indicated that filter pads are considered a distinct product from R&G coffee fulfilling specific needs.⁶⁹

(114) With regards to supply-side substitutability, the majority of competitors who replied to the Commission's questionnaire considered that a supplier active only in R&G would not be able to start swiftly and without significant costs the production and sale of filter pads and vice versa.⁷⁰

(115) Respondents to the market investigation suggested that many consumers who have a single-serve machine also have a multi-serve appliance.⁷¹ However on the basis of its market investigation the Commission cannot find evidence of a competitive constraint between filter pads and R&G. Moreover, there are many consumers who do not own multiple machines. For those consumers, a switch from R&G to filter pads would entail switching costs given the need to first purchase another machine.

(116) Market studies submitted by the Parties⁷² show that there is a switch from R&G to filter pads but not vice versa. That pattern combined with the marketing of filter pads as an upgrade from traditional brewing methods, show a trend whereby consumers who decided to switch to filter pads are not willing to "switch back" or "downgrade" to R&G.

⁶⁷ See for instance Mondelēz internal document, dated April 2012, "*Coffee Overview – Kantar Worldpanel*" p. 78.

⁶⁸ Case No COMP/M.5547 - Koninklijke Philips Electronics / Saeco International Group para. 30.

⁶⁹ Responses to questions 21 et seq. of Questionnaire Q1-Competitors and responses to questions 23 et seq. of Questionnaire Q2-Retailers.

⁷⁰ Responses to questions 20 et seq. of Questionnaire Q1-Competitors.

⁷¹ Responses to questions 10 et seq. of Questionnaire Q9-Competitors, responses to questions 11 et seq. of Questionnaire Q10-Retailers, responses to questions 14 et seq. of Questionnaire Q11-Electronic Retailers and responses to questions 15 et seq. of Questionnaire Q12-Machine Manufacturers.

⁷² Europanel 2013 – France switching behaviours.

- (117) The Parties' internal documents also show that the trend in the market is from traditional preparation methods (such as drip filter or instant coffee) to on-demand and single-serve systems (including the Senseo filter pad system), with a key driver of this trend being convenience. The Parties' internal documents and contact with market participants clearly show that customers also appreciate in filter pads the diversity of tastes offered and the various strengths of coffee proposed in comparison with R&G.⁷³ In conclusion, filter pads respond in a more convenient manner to consumers' needs.
- (118) The sector inquiry of the German competition authority put forward by the Parties focuses mainly on production technologies and supply-side substitutability and was not specifically carried out in a merger assessment context. The Commission considers that to define a product market for the purpose of assessing a concentration, a more holistic approach is needed and such approach might lead to a different conclusion than a narrow comparison between the technologies needed to produce different coffee formats. Moreover, even if one were to only consider the production side, it is clear that separate production lines are needed for manufacturing filter pads as opposed to R&G.
- (119) The Commission also notes that there are significant price differences between R&G coffee products and filter pads. According to the Parties' submission, the price per cup on average for R&G coffee products is [below 10]* cents, while for filter pads it is [10-20]*.⁷⁴ In France, the average price per kg of R&G coffee is EUR [below 10]* per kg whereas for filter pads it is EUR [10-20]* per kg. In Austria, the average price of R&G coffee is EUR [below 10]* per kg whereas in filter pads it is EUR [10-20]* per kg.⁷⁵ As a result, consumers already accept to pay a materially higher price per cup for filter pads and they would not in all likelihood decide to switch back to R&G should the price of filter pads increase by merely 5-10%. The Commission considers that in order to give up the convenience offered by filter pads and go back to R&G products, consumers would need to be faced with a much higher price increase than one of 5 to 10%.
- (120) During the course of the proceedings, the Parties submitted an economic study assessing the substitutability between filter pads and R&G in France. The Parties presented a demand estimation model showing that there is a strong degree of substitution between R&G and filter pads, and vice-versa.⁷⁶
- (121) For reasons explained in Annex I, the Commission considers that the Parties' demand estimation model suffers from serious identification and robustness issues. Therefore, the Commission cannot regard the Parties' study as informative for the current case.
- (122) In addition, the Commission notes that not only is the profitability different between filter pads and R&G but also the cost structures are different between the two products, with packaging costs being roughly three times higher and raw material costs being roughly half for filter pads when compared with R&G.

⁷³ See for instance DEMB internal document, undated, "*Senseo – Drive Senseo Brand to 1 Billion €*" page 20 et seq, and non-confidential minutes of a conference call with a retailer of 12 February 2015 11.00 CET.

⁷⁴ Parties submission on SiSe of 20 November 2014 paragraph 3.10 et seq.

⁷⁵ Figures based on 2013 data for total market; source: Annex 7-4AA to Form CO for R&G figures for both France and Austria, Annex 7-4a to Form CO for France filter pads figures and Annex 7-4b to Form CO for Austria filter pads figures.

⁷⁶ A detailed explanation of the Parties' economic study is present in Annex I.

Conclusion

- (123) Given the lack of supply-side substitutability, the low demand-side substitutability, the differences in use, purpose, prices and cost structure the Commission considers, for the purposes of this Decision, that filter pads constitute a separate market from R&G.
- 7.4.4. *Single-serve systems: the interplay between the relevant markets for single-serve machines and consumables*
- (124) Single-serve machines and single-serve coffee consumables, which together constitute single-serve systems, are complementary products. Moreover, each single-serve machine is based on a specific technology and, as a consequence, each machine needs specific consumables that are compatible with that machine. As set out in Recital (70), coffee machines are manufactured by one or more electrical appliance manufacturers while the compatible consumables are manufactured by one or more coffee manufacturers depending on whether the system technology is "open" or "closed": technology owners can make use of their intellectual property (IP) rights to prevent non-authorised manufacture of consumables (thus "closing" the system). Systems such as Senseo and Nespresso are "open" or "semi-open" systems, meaning that any or at least some competitors can manufacture compatible consumables. Other systems like Tassimo and Dolce Gusto are "closed" systems, meaning that only the coffee manufacturer owning specific IP rights can manufacture the consumables for the closed system.
- (125) The Commission has not assessed "coffee systems" in previous cases.
- (126) The Parties propose that different markets for the machines and the consumables be considered, and that given that their activities focus on the consumables' markets, only the consumables markets should be considered for the analysis of the Transaction. However, the Parties also recognise that there is a strong relationship between the machines and the consumables' markets and acknowledged that, due to the strong indirect involvement and interest of coffee manufacturers in the sales of machines, competition takes place not only within the consumables and machines markets separately but also at system level. Furthermore when presenting their arguments the Parties take into account both the consumables for single-serve systems and single-serve machines.
- (127) Similarly, Nestlé differentiates between markets for coffee machines and consumables, but also points to the strong interplay between the machines and consumables. According to Nestlé, such interplay is a key element to assess the effects of the Transaction that cannot be captured if the analysis were to focus only on the separate markets for machines and consumables respectively.
- (128) The Commission observes that the price and the choice of available consumables is one of the factors final consumers take into account when deciding which single-serve machine to purchase.⁷⁷ Given the strong dependence of coffee companies on machine sales and their consequent strong involvement in the marketing of the machines, the relevant markets for single-serve machines and consumables are inter-related.

⁷⁷ Responses to question 13 of Questionnaire Q2 – Retailers and to question 7 of Questionnaire Q1-Competitors.

- (129) In the light of what is stated in Recital (128), and also in order to address various parties' submissions, the Commission will consider the interplay between the relevant markets for single-serve machines and the markets for single-serve consumables in its competitive assessment. In particular and where appropriate, the Commission will have regard to the Transaction's effects on a wider segment for single-serve systems comprising both machines and consumables. At the same time, it does not appear necessary to define a distinct relevant market for single-serve systems, as the Transaction's effects on that market will be addressed in the assessment of the narrower markets for single-serve machines and consumables.

7.5. R&G coffee

- (130) R&G consists of coffee beans that have been roasted, ground and are mostly used in multi-serve machines. R&G coffee comprises a wide variety of flavours, aromas and intensities, depending on the specific blend of coffee varieties and origins of the beans, and how long they are roasted.
- (131) The Parties submit that for a manufacturer it is easy to produce different types of R&G coffee. Moreover, consumers will also switch between different R&G coffees depending on the occasion and individual preferences.

7.5.1. Whole beans

Parties' arguments

- (132) The Parties submit that whole beans are part of the R&G market given that they result from the same production process, with the only difference that the grinding is not done in advance by the coffee manufacturer but rather by the customer directly before brewing.
- (133) According to the Parties most consumers who purchase whole beans grind them and use them in any appliance that would normally use R&G coffee. For this reason the Parties consider that both supply- and demand-side substitutability exists between whole beans and R&G.

Information obtained in the Commission's investigation

- (134) The majority of competitors and customers who responded to the Commission's questionnaires stated that whole beans and R&G are considered by the final consumer as distinct products fulfilling different needs and a stronger majority noted significant differences in consumption patterns, prices and targeted consumer groups.⁷⁸
- (135) Moreover, the majority of competitors who replied to the market investigation considered that a supplier active only in R&G would not be able to start swiftly and without significant costs the production and sale of whole beans and vice-versa.⁷⁹

Commission's assessment

- (136) Taking into account the results of the market investigation, the Commission considers that it may be necessary to distinguish between whole beans and R&G. However, for the purpose of this Decision the precise product market delineation concerning R&G and whole beans can be left open since the assessment of the Transaction does not materially change under either alternative product market

⁷⁸ Responses to questions 11 et seq. of Questionnaire Q1-Competitors and responses to questions 16 et seq. of Questionnaire Q2-Retailers.

⁷⁹ Responses to question 9 of Questionnaire Q1-Competitors.

definition, namely under a broad product market definition comprising R&G and whole beans or under a narrower delineation where the two coffee products constitute different product markets.

7.5.2. *Greek Coffee*

- (137) In Greece there is a specific type of R&G coffee, ground in a slightly different way and producing finer grind, which is brewed following a specific process and which produces what is known as "Greek coffee". The Commission considered whether Greek coffee is a separate market from "normal" R&G.

Parties' arguments

- (138) The Parties are both active in the "normal" R&G segment, whereas only DEMB is active in Greek coffee and they consider that such narrow segmentation of the market would not form a relevant basis for the Commission assessment.
- (139) The Parties claim that there exists both demand- and supply-side substitutability between "normal" R&G coffee and "Greek coffee". They submit that the majority of consumers drinking "Greek coffee" also purchase "normal" R&G and that "normal" R&G manufacturers could easily start producing "Greek coffee".
- (140) The Parties also highlight also a decision by the Greek national competition authority⁸⁰ relating to an abuse of dominance which whilst reaching the conclusion that "*each type of coffee, meaning instant coffee, Greek coffee, filter coffee and espresso constitute a separate product market*", also elucidated that the definition of the relevant market could "*be given differently in a concentration case versus a case investigating a possible abuse of dominant position*". Consequently the Parties submit that segmenting the R&G further into Greek and "normal" R&G is not applicable for the purpose of analysing the Transaction.

Information obtained in the Commission's investigation

- (141) Although the majority of respondents to the Commission's questionnaires indicated that "Greek coffee" and "normal" R&G are not substitutable and are considered distinct products fulfilling specific needs,⁸¹ the respondents also highlighted that there is supply-side substitutability between "Greek coffee" and "normal" R&G and that a supplier active only in "normal" R&G would be able to start swiftly and without significant costs the production and sale of "Greek coffee" and vice versa.⁸²

Conclusion

- (142) The Commission considers that it might be necessary to distinguish between "Greek coffee" and "normal" R&G in Greece. However, for the purpose of this Decision, that issue can be left open as the Transaction would not significantly impede effective competition in the internal market under either alternative product market definition, namely under a broader market comprising "Greek coffee" and "normal" R&G or under a narrower delineation where the two coffee products are considered to constitute different product markets.

⁸⁰ Decision 434/V/2009 paragraph 12, page 13 ([http://oxcat.ouplaw.com/view/10.1093/law:ocl/cr016.case.16/OCL-CR016\(GR2009\).pdf](http://oxcat.ouplaw.com/view/10.1093/law:ocl/cr016.case.16/OCL-CR016(GR2009).pdf)).

⁸¹ Response to question 169 to 171 of Questionnaire Q1-Competitors and responses to question 278 et seq. and 279 of Questionnaire Q2-Retailers.

⁸² Response to question 168 of Questionnaire Q1-Competitors.

7.5.3. *Robusta vs. Arabica beans*

- (143) The two most widely cultivated varieties of the coffee plant are the *Coffea arabica* and the *Coffea canephora* (called also "Robusta"). In *Cafeteros de Colombia*,⁸³ the Commission made reference to "*the market for green coffee*" and identified three types of green coffee "*arabicas, robustas and mild arabicas*" but in the end did not define a relevant product market.

Parties' arguments

- (144) The Parties submit that there are no supply-side barriers to switching between Arabica and Robusta since each is a traded commodity.⁸⁴ The Parties also argue that within each of Arabica and Robusta, tastes and aromas will vary widely according to the quality of the specific plant: much like the different quality levels in the grape varieties used to make wines. Furthermore, most coffee products are a blend of Arabica and Robusta beans of different varieties and in different proportions to achieve a range of tastes and aromas, therefore in the majority of cases, the type of bean is not a significant part of consumer choice, which will focus more on the taste without the need for detailed knowledge of the blend's composition.⁸⁵ Indeed, data splits for Arabica or Robusta are not available in all countries because that aspect simply does not factor into supplier and customer decisions.⁸⁶

Commission's investigation and assessment

- (145) The Commission acknowledges the variety of blends available on the market and the fact that internal documents from the Parties, while showing a tracking of both the Arabica and Robusta green beans prices for supply reasons, do not indicate that the Parties give particular importance to the split between Arabica and Robusta in their final products.

Conclusion

- (146) Given the wide range of blends between Arabica and Robusta commercially available, and the limited role that the composition of the blend plays in consumers' choices, the Commission considers, for the purpose of defining the relevant market in this Decision, that it is not necessary to distinguish between Arabica and Robusta.

7.6. Instant coffee

Parties' arguments

- (147) The parties submit that instant coffee is a ready substitute for other coffee formats, given that it can be prepared in a short time and without the use of any dedicated appliances and that moreover it can be conserved for long periods.
- (148) The Parties submit that, due to the ease of transport, instant coffee can be sourced globally by retailers and such global reach is one of the reasons behind a strong penetration of private label brands in instant coffee.

⁸³ Case 82/860EEC (1982).

⁸⁴ According to the Parties, unroasted (that is to say green) beans are publicly traded on the New York International Commodities Exchange for Arabica green beans and the London LIFFE exchange for Robusta green beans and more than 95% of the final price is a reflection of the public trading price.

⁸⁵ Only in France the Arabica/Robusta distinction has been used prominently in the marketing of coffee products.

⁸⁶ Form CO paragraph 307.

Information obtained in the Commission's investigation

- (149) The majority of retailers who responded to the market investigation confirmed that instant coffee is not substitutable with any other coffee product while competitors' replies were mixed on that issue. However, the majority of both retailers and competitors clearly indicated that instant coffee is considered a distinct product fulfilling specific needs.⁸⁷
- (150) Moreover the majority of competitors who replied to the Commission's questionnaire, consider that a supplier active only in instant coffee will not be able to start swiftly and without significant costs the production and sale of any other coffee product and vice versa.⁸⁸

Conclusion

- (151) In conclusion, the Commission considers, for the purposes of this Decision, that instant coffee forms a separate product market from any other coffee product.

8. RELEVANT GEOGRAPHIC MARKETS

Parties' arguments

- (152) The Parties submit that, in line with previous Commission's decisions in the retail food sector,⁸⁹ the relevant geographic market for all coffee products is at least national in scope with customers purchasing products at the national level. Similarly, pricing and marketing of coffee products is considered national by the Parties. Moreover, the Parties consider that consumer national preferences vary according to Member State given different coffee drinking cultures which are reflected in different brands, types and tastes of coffee sold.
- (153) The Parties argue that one exception to such national markets is represented by Estonia, Latvia and Lithuania, which should be treated together as the Baltics for the following reasons:
- (1) the Commission has found that competition takes place throughout the Baltic cluster in previous cases involving wholesale supply of fast-moving consumer goods⁹⁰;
 - (2) there is a strong presence of pan-Baltic retailers, and of the same key competitors across the Baltics;
 - (3) coffee products are supplied in the same packaging across the Baltics;
 - (4) there is scope for transshipments of coffee products across the Baltics and into the Baltics from other countries both by coffee manufacturers and retailers;
 - (5) the pan-Baltic nature of the market has influenced the Parties' internal management structures, since they have one General Manager determining the strategy for the Baltics.

⁸⁷ Responses to questions 18 et seq. of Questionnaire Q1-Competitors and responses to questions 21 and 22 of Questionnaire Q2-Retailers.

⁸⁸ Responses to questions 17 et seq. of Questionnaire Q1-Competitors.

⁸⁹ M.5644 - Kraft Foods / Cadbury para. 42; M.4824 - Kraft / Danone Biscuits, para. 19; M.2072 - Philipp Morris / Nabisco, para. 17.

⁹⁰ M.6455 – SCA / Georgia Pacific Europe; M.4533 – SCA/P&G.

Information obtained in the Commission's investigation

- (154) With respect to all the product markets identified in Section 7 the Commission notes the high importance of national brands in the Member States despite the growing importance of some international brands.
- (155) In addition the Commission's market investigation, with respect to all the product markets confirmed *inter alia* the presence of national differences in terms of consumption by consumers;⁹¹ the divergence in market shares of the relevant suppliers in the different Member States; that negotiations with retailers regarding supply and pricing of coffee products are national⁹² and the presence of national and regional competitors.⁹³
- (156) In respect of the Baltics, market participants in the Baltic countries⁹⁴ highlighted national differences in consumption habits, limited transshipment and national-level budgeting for the promotion of coffee products. The different nature of each of the Baltic states is also highlighted by different market shares attained by each of the relevant players in each of Estonia, Latvia and Lithuania.

Conclusion

- (157) Given all the elements highlighted by the market investigation, and in line with previous decisions on fast moving consumer goods,⁹⁵ the Commission considers, for the purposes of this Decision, that the relevant geographic scope of all relevant markets defined in this Decision is national.

9. COMPETITIVE ASSESSMENT

- (158) The Commission reached the conclusion that the Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in: (i) the R&G markets in France, Denmark and Latvia; and (ii) filter pads markets in Austria and France. Moreover, for the reasons set out in Sections 9.4 to 9.7, the Commission has reached the conclusion that the Transaction would not significantly impede effective competition in the internal market in: (i) single-serve machines market in the countries where both Tassimo and Senseo are present and account for at least 25% of the market for single-serve machine sales⁹⁶ (that is to say Austria, Denmark, France, Germany, the Netherlands, Spain and the United Kingdom); (ii) the R&G markets in the Czech Republic, Greece, Poland, Bulgaria, Hungary, the Netherlands and Spain; (iii) instant coffee markets in the Czech Republic, Denmark, Estonia, Greece, Hungary, Latvia, Lithuania, the Netherlands, Poland, Slovakia, Spain or the United Kingdom; (iv) filter pads markets in Germany and the Netherlands and (v) out-of-home markets in Denmark, Germany, Sweden and the United Kingdom.

⁹¹ Responses to question 42 of Questionnaire Q1-Competitors and responses to question 43 of Questionnaire Q2-Retailers.

⁹² Responses to questions 41 and 44 of Questionnaire Q1-Competitors and responses to questions 41 and 42 of Questionnaire Q2-Retailers.

⁹³ Responses to questions 39 and 40 of Questionnaire Q1-Competitors.

⁹⁴ Non-confidential minutes from a conference call with a competitor on 18 November 2014 at 17.00 CET; non-confidential minutes from a conference call with a competitor on 18 November 2014 at 10.45 CET.

⁹⁵ See footnote 89.

⁹⁶ Tassimo's and Senseo' position has been calculated based on GfK sales data provided by the Parties.

9.1. General – market characteristics

(159) On the basis of its market investigation, the Commission notes that coffee products belong to differentiated markets, in which brands play an important role. Players in those markets invest in promotion and advertising to maintain the desired image of their brands and ensure final customers' loyalty. As a result the barriers to entry into the coffee products markets are not insignificant. Furthermore those markets are dynamic and subject to change. In Sections 9.1 to 9.9 those characteristics of coffee product markets will be analysed in more detail. For the retailers coffee products are important because they attract final customers to their retail outlets. Therefore their position in those markets will also be analysed.

9.1.1. Differentiated markets

(160) The various coffee product markets affected by the Transaction are characterised by a high degree of product differentiation, covering a spectrum of products with which coffee suppliers try to respond to the different expectations of final consumers.

(161) To some extent coffee products might differentiate according to objective characteristics reflecting personal coffee tastes and preferences, such as the strength of the beverage (for instance distinction between mild, medium and dark roast) or species of coffee bean (for instance the distinction between Robusta and Arabica).

(162) However the principal factors of differentiation are the "consumer need states", which are the reasons, contexts or motivations for final consumers to drink coffee, according to market intelligence reports, such as "BrandneXt study Coffee Market R&G (NL, Esp, FR)", prepared for coffee suppliers.⁹⁷ Those needs can range from "[...]*" to "[...]*" or from "[...]*" to "[...]*".⁹⁸ Other identified contexts might include: [...]*.⁹⁹

(163) The various coffee brands position themselves in order to correlate with the needs of the consumer. As soon as a brand "stands for something" it is also "making the communication faster and cheaper".¹⁰⁰ Thus within a given coffee market the high-end brands are meant to fit with the motivations centred on exclusivity and therefore serve as status symbols. On the other end the mid and low-range brands are meant to fit with the context of affinity and satisfy the need of belonging and homeliness.

9.1.2. Importance of brands, advertising and promotion

(164) Coffee suppliers create and successively maintain a desired set of correlations between their coffee brand and the consumers' needs and consequently the desired concept and image of the brand by means of advertising and promotion of their coffee products in various media – for example paper, electronic and social. As a result, final customers assume that a given coffee brand will guarantee the quality they associate with it and that it will match with a given set of coffee tastes and preferences. For those reasons brands are important in all the coffee product markets, as established in Section 7.

(165) Advertising and promotion efforts are also aimed at maintaining the awareness of the brand, which is the extent to which consumers can recognise and recall a brand. The

⁹⁷ DEMB internal document dated August 2012, "BrandneXt study Coffee Market R&G (NL, Esp,FR)", slide 3.

⁹⁸ *Ibidem*, slide 13.

⁹⁹ Mondelēz internal document, not dated, "Items to cover", slide 55.

¹⁰⁰ DEMB internal document, not dated, "A Marketing Training Seminar specially prepared for DE Master Blenders 1753 by Mike Philippon Associates", slide 13.

ultimate aim is to create brand loyalty which means, inter alia, that consumers will continue purchasing the branded products even in times of austerity and "not worry about (...) premium price".¹⁰¹ That strategy is successful in the coffee category. As one competitor put it, "[c]onsumers would probably not even switch from branded coffee (...) should the price of branded coffee increase, but will rather try to economise on other products in order to keep their purchasing power for branded coffee. Coffee is still considered as a small luxury, from which customers do not want to refrain even in the times of financial crisis."¹⁰²

- (166) The Parties themselves in internal documents refer to their coffee brands as "[...]*" and admit that they "[...]*". For example, consumers of Tassimo interviewed by a market research company for Mondelēz "[...]*".¹⁰³ On the other hand DEMB notes in its internal documents that thanks to its long history Douwe Egberts guarantees coffee quality.¹⁰⁴
- (167) Some of the particularly strong brands (such as Jacobs, Carte Noire, Tchibo, Nescafe, Senseo) serve as "umbrella brands" or "master brands" with various coffee products and formats being sold with the same brand and identification. That enables coffee suppliers to "transfer their brand equity" that is to say to leverage their strong position within one coffee market (for instance R&G) into a new market (for instance filter pads or N-capsules). In particular when an umbrella brand appears on a new or innovative product, the final customers might be more convinced to try it because they will believe the master brand guarantees the quality, taste and other features to which they are used to. In addition, with umbrella brands, advertising and promoting coffee products within one market increases brand awareness of products in other markets as well. Umbrella brands also allow for spreading and splitting of the brand promotion costs.
- (168) As a result coffee still remains a brand-oriented category, despite the introduction of private label coffee products by retailers. As it was mentioned in Recital (47), penetration of private label brands within coffee in most EEA countries is still relatively low as compared with other fast moving consumer goods and it has been rather stable over the last years.¹⁰⁵ Retailers confirm that final customers tend to be brand loyal.¹⁰⁶
- (169) Brand loyalty and awareness is maintained by continuous investment in advertising and promotion. That is important for existing coffee brands and the effectiveness of those investments is closely monitored.¹⁰⁷ However, advertising and promotion is

¹⁰¹ DEMB internal document, not dated, "A Marketing Training Seminar specially prepared for DE Master Blenders 1753 by Mike Philippon Associates", slides 13, 71.

¹⁰² Non-confidential minutes of a conference call with a competitor dated 18 November 2014 at 13.00 CET.

¹⁰³ Mondelēz internal document, "Tassimo Portfolio qualitative study -Ipsos Spain September 2010"

¹⁰⁴ DEMB internal document, dated 5 May 2009, "Make your move. Aroma Lady & Senseo. Equity Profiles and Interactions", slide 5.

¹⁰⁵ The Commission's final report on the economic impact of modern retail on choice and innovation in the EU food sector, published on 19 September 2014 considered, amongst other things, the penetration of PL in the coffee sector. For example, in Denmark, penetration of PL in coffee has only slightly grown from 12.1% to 14.8% between 2004 and 2012. Similarly, in Germany, PL penetration in the coffee sector has only grown by 2.9% between 2004 and 2012 (from 18.3% to 21.2%). In France, according to the report, PL penetration has in fact decreased from 7% to 5.3% between 2004 and 2012.

¹⁰⁶ Response to question 46 of Questionnaire Q2 – Retailers.

¹⁰⁷ For instance DEMB's internal document, undated, "Douwe Egberts Digital Performances Report for Q1 and Q2 of 2013" in which the effects of numerous digital media campaigns of the various DEMB

even more crucial at the time of launching new coffee products. For example, Mondelēz internal documents show that when preparing the introduction of Carte Noire branded N-capsules in France in 2013, the launch campaign included [...]*.¹⁰⁸ All those efforts are meant to [...]*.¹⁰⁹

- (170) The Parties admit that "[p]romotional spending is an important part of negotiations with retailers..."¹¹⁰ and that they "work with retailers to promote both the category and its brands" with particular arrangements being made for [...]*.¹¹¹ All those marketing and promotion elements – from sampling, through social media, digital and TV campaign to promotions in the point of sale - form the "*continued awareness and trial*" plan aimed at securing most shelf space against closely competing brands.¹¹² That aim is acknowledged by the overwhelming majority of retailers across various Member States as well as a majority of competitors, who confirm that marketing and promotions (discounts) offered by the coffee suppliers are the major parameters of competition.¹¹³

9.1.3. Barriers to entry and expansion

- (171) Since coffee products belong to differentiated markets dominated by brands, barriers to entry and expansion in those markets are not insignificant. Established positions of the incumbent coffee companies and the strength of their power brands to which customers remain loyal increase the risks and costs of potential entry.¹¹⁴
- (172) Critical factors for success in the coffee market, as identified by competitors and customers, include – apart from having a well-known brand – also financial strength to sustain investments; effective marketing strategy (in particular, TV advertising) and other PR activities.¹¹⁵ As it is stated in DEMB's internal document [...]*.¹¹⁶ For example, DEMB's expenditure for advertising and promotion of single-serve machines and consumables amounted to approximately EUR [...]* million in 2014, while that of Mondelēz amounted to approximately EUR [...]* million in 2014. The Parties themselves identify "*360° targeted media campaign: increased spend, geo-marketing & sampling*" as well as "*strong customer activation: improved in-store visibility and customer activation*" as key growth levers.¹¹⁷ Brand awareness has also been mentioned by competitors as one of the main obstacles for a coffee producer to gain access to retail shelf space (with the exception of the retailers' own brands).¹¹⁸

brands in the EEA are assessed in terms of conversion ratio, i.e. the extent to which site visitors can be converted into paying visitors.

¹⁰⁸ Mondelēz internal document, dated 25 October 2013, "*Boost plan Recommendation Q4 13-Q1 14*".

¹⁰⁹ *Ibidem*.

¹¹⁰ Response of DEMB to Request for Information - QP4 dated 11 September 2014.

¹¹¹ Response of Mondelēz to Request for Information - QP4 dated 11 September 2014.

¹¹² DEMB internal document, dated 3 September 2013, "*Country visit*", pp. 23-26.

¹¹³ Responses to question 48 of Questionnaire Q2 – Retailers and to question 46 of Questionnaire Q1 – Competitors.

¹¹⁴ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, paras. 70, 71 c).

¹¹⁵ Responses to questions 92, 107, 120, 133, 193, 206, 219, 252, of Questionnaire Q1 – Competitors and to questions 272, 309, 343, 481, 515, 586, of Questionnaire Q2 – Retailers.

¹¹⁶ DEMB internal document dated 2 March 2011, "FY12 AOP Sara Lee C&T France", slide 10.

¹¹⁷ For instance DEMB internal document, dated 23 May 2013, "*CDT Capsules. Strategic outlook 2013*", slide 22.

¹¹⁸ Responses to questions 93, 108, 121, 134, 194, 207, 220, 233, 246, 259, 272, 287 of Questionnaire Q1 – Competitors.

(173) As a result, new players or players wishing to expand are faced with the barriers resulting in particular from the necessary significant investment into advertising and promotion aimed at creating and maintaining brand awareness.

9.1.4. *Position of retailers*

(174) Another consequence of the fact that coffee is a brand-oriented category is that the bargaining power of retailers does not necessarily countervail the market position of suppliers of branded coffee products. Faced with the suppliers of the brands with the highest awareness, which cannot be easily replaced by alternative products, retailers will not credibly threaten to delist them in order to put pressure on their coffee suppliers in the course of negotiations. Since final consumers, incited by the advertising and promotion efforts carried independently by the coffee suppliers, request those brands, retailers cannot afford not to have them on their shelves. As a result retailers might not have the necessary buyer power to counter potential price increases. Furthermore retailers might simply pass-on the price increase, in particular if they assume that competing retailers are faced with a similar increase and their trade margin remains unchanged.¹¹⁹

9.1.5. *Future trends and innovation*

(175) Coffee markets are dynamic and subject to change. Although due to differences in consumer preferences, historical developments and the various coffee cultures, trends in the coffee markets are not uniform among the EEA countries, some common characteristics can be identified. First, there is a trend towards more premium coffee products. Second, the traditional coffee preparation methods are being gradually replaced by more sophisticated ones, in particular single-serve coffee machines. That trend was confirmed by retailers and competitors in all the affected geographic markets, who in the course of the market investigation expressed the view that in the future "*single serve and more convenient coffee products*"¹²⁰ will continue to increase.¹²¹

(176) The Parties agree that there is a trend towards differentiation and premiumisation, which is shown by the rise of products such as single-origin coffee, special blends, organic or fair trade products, local brands. Moreover the growth of the whole beans category can be considered as another manifestation of the move towards more premium products because whole beans are purchased by more sophisticated coffee connoisseurs, who either have a coffee machine which grinds beans or a separate grinder and are ready to devote time to the grinding process in order to obtain fresher coffee.

(177) In its internal strategy for the years 2014 to 2016 Mondelēz expects the global coffee category [...]*.¹²² Depending on the maturity of the coffee markets in a given country, this expected growth may be derived from different coffee products. In mature markets (that is to say markets with long established coffee cultures, such as France or the Netherlands) the trend is towards an increase in the more convenient and trendy single-serve segment. To some extent that trend is accompanied by a move away from the "traditional" coffee brewing methods (such as filter coffee or instant coffee) for which in principle R&G coffee is used. As a result the R&G

¹¹⁹ Responses to question 12 of Questionnaire Q2 – Retailers.

¹²⁰ Responses to question 167 of Questionnaire Q2 – Retailers.

¹²¹ Responses to question 76 of Questionnaire Q1 – Competitors.

¹²² Mondelēz internal document, dated 20 March 2013, "*Coffee Global Strategy 2014-2016 MLT Discussion*", slide 2.

markets are somewhat decreasing in those countries, due to the outflow of consumers towards the use of single-serve machines. The expected continuous growth of the single-serve segment was also confirmed by retailers and competitors when asked about future trends in coffee products. They stated that "*single serve and more convenient coffee products*"¹²³ will continue to increase.¹²⁴

- (178) However, there are also countries where R&G remains by far the largest coffee category (for instance Denmark, Latvia or Poland) with instant coffee being usually the second most popular coffee product. Nevertheless the Parties admit that in those countries the single-serve segment is also expected to increase in the future also as a result of the "lifestyle upgrade" by final consumers who become interested in more sophisticated coffee preparations.¹²⁵
- (179) Consumers associate single-serve products with greater quality, luxury and modernity, while R&G, used mainly for the drip filter machines, is considered more of a basic, routine product.¹²⁶ At the same time, single-serve coffee products generate higher margins since consumers are ready to pay a premium for the perceived better product. The Parties' internal documents show that single-serve coffee products are [...] * than the multi-serve ones.¹²⁷ Therefore, the Parties consider [...] *, while the plans as regards R&G and instant products are to simply [...] *".¹²⁸

9.2. Affected markets

- (180) The proposed Transaction leads to a number of affected markets, which will be analysed in turn below: (i) R&G markets¹²⁹ in France, Denmark, Latvia, the Czech Republic, Greece, Poland, Bulgaria, Hungary, the Netherlands and Spain; (ii) instant markets in Latvia, Lithuania, Estonia, Czech Republic, Denmark, Ireland, Poland, Slovakia, the United Kingdom; (iii) filter pads in France, Austria, Germany, the Netherlands and (iv) out-of-home markets in Denmark, Germany, Sweden and the United Kingdom. Furthermore, even though the market for coffee machine sales is not a technically affected market, for the reasons set out above (see Recitals (124) - (129)) the effects of the Transaction will be also assessed in relation to the market for single-serve machines. For this purpose the interplay between single-serve machines and consumables (that is within the single-serve systems) will be taken into account. Similarly, the Commission will assess also the effects of the Transaction on the market for N-capsules will also be assessed, as well as potential portfolio effects.

9.3. The Parties' economic studies (calibrated merger simulation models)

- (181) During the pre-notification period, as well as the Phase I and Phase II proceedings, the Parties submitted a set of economic studies with calibrated merger simulation models for a number of countries (Austria, the Czech Republic, Denmark, France, Greece, Spain and the United Kingdom). The aim of those models was to predict the price impact of the Transaction in the in-home consumables markets of those

¹²³ Responses to question 167 of Questionnaire Q2 – Retailers.

¹²⁴ Responses to question 76 of Questionnaire Q1 – Competitors.

¹²⁵ Response to question 483 of Questionnaire Q2 – Retailers.

¹²⁶ DEMB internal document dated August 2012 "*BrandneXt study Coffee Market R&G (NL, Esp,FR)*", pp. 13-15.

¹²⁷ For instance: Oct 2013 CI French Coffee Market Induction FINALE, p. 12; Mondelēz Confidential Annex 5-4a - Project Charger Update Audit Committee of 3 October 2013, pp. 3, 9; Annex 5-4s to the Form CO, Project Charger Discussion Materials Dec 15, 2013, p. 11.

¹²⁸ Mondelēz internal document, undated, "*Managing Innovation Funnel. Toolkit. Define growth drivers & innovation needs to deliver SP growth strategies*", slide 17.

¹²⁹ An affected R&G market arises also in Belgium, however the overlap amounts to [0-5]*%.

countries. However, for the reasons set out in Annex I to this Decision, the Commission finds that these merger simulation models of the Parties cannot be considered reliable as they likely underestimate the anti-competitive effect of the Transaction.¹³⁰

9.4. Single-serve coffee machines and systems

- (182) As further set out in Recitals (237) to (319), the Commission has reached the conclusion that the Transaction will not lead to a significant impediment to effective competition in the markets for single-serve coffee machines in the countries where both Tassimo and Senseo are present and account for at least 25% of the market for single-serve machine sales¹³¹ (that is Austria, Denmark, France, Germany, the Netherlands, Spain and the United Kingdom).
- (183) As regards markets for single-serve consumables, the Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position; in the filter pads markets in Austria and France (see sections 9.7.1 and 9.7.2 below).
- (184) For the reasons set out in Recitals (124) to (129), in order to address various parties' submissions, the Commission also considered the interplay between the market for the single-serve machines and the market for single-serve consumables. For this purpose, the Commission has in particular taken regard to the cooperation between the manufacturers of single-serve machines and consumables and the positioning of the Parties' brands within the single-serve segment comprising both machines and consumables. As a result of this analysis (see Recitals (237) to (349)), the Commission concludes that the Transaction would not give rise to competition concerns in relation to single-serve systems.

Parties' arguments

- (185) The Parties argue that the Transaction does not lead to a significant impediment to effective competition because Tassimo and Senseo do not constrain each other closely whether at the machines or consumables level. To support their argument the Parties advance the following reasons.
- (186) Firstly, the Parties argue that they do not manufacture or sell coffee machines. After the Transaction, machine manufacturers including those manufacturers (Bosch and Philips) which are the Parties' partners for the production and sale of single-serve systems, would continue to have an incentive to compete aggressively against each other and other machine producers. The Parties do admit that machine sales are a relevant consideration in understanding the dynamics of competition between single-serve products. However they also state that the machine sales realised by machine manufacturers are not always indicative of the sales achieved in coffee consumables and, in particular the share of Senseo machines achieved by Philips is not indicative of DEMB's competitive strength in relation to single-serve systems. The Parties further point out that, due to the fact that Senseo is an open system, if DEMB invests in increasing Senseo's machine park, it will only gain a part of the revenue from the associated increase in filter pad sales.
- (187) Secondly, the Parties argue that after the Transaction numerous other single-serve systems would still remain in the market, in particular those of Nestlé, in addition to

¹³⁰ For a detailed description and assessment of the submissions, see section 2 of Annex I to this Decision.
¹³¹ Tassimo's and Senseo's position has been calculated based on GfK sales data provided by the Parties.

Tchibo, Lavazza, Illy, Starbucks, Melitta, Paulig, Delta Café or Aldi. The Parties also note that fully automatic bean-to-cup machines are being introduced at substantially lower price points, thus increasing their accessibility to customers and rendering them a real alternative to single-serve machines. The Parties consider that single-serve is a new standard means of producing different coffee beverages in-home and most coffee manufacturers already actively participate in it. Therefore, the Parties argue that they would lose significant volumes to third party competitors if they were to compete less fiercely on price, quality or choice after the Transaction.

- (188) Thirdly, the Parties maintain that among single-serve systems Senseo and Tassimo each have a different positioning in the market and are not close competitors. In fact, since Tassimo was initially launched by Mondelēz as a response to Nestlé's Nespresso and triggered, in turn, the launch of Dolce Gusto by Nestlé as a response, the Parties consider Dolce Gusto as Tassimo's closest competitor. To justify those claims the Parties put forward a number of arguments.
- (189) The Parties note that the product positioning of Dolce Gusto and Tassimo is similar: they both have the multi-drink capability as their purchase driver, they cater for the needs of those consumers who value variety and are often used as supplementary machines to produce beverages for special occasions. On the other hand the Parties maintain that Senseo in the eyes of consumers is a convenient single-serve alternative to R&G drip filter coffee. Also the price per cup of Tassimo (amounting to [20-30]* to [30-40]* cents) is close to that of Dolce Gusto (amounting to [20-30]* to [30-40]* cents), but different from Senseo (which is significantly cheaper and amounts to [10-20]* to [10-20]* cents). That difference is also reflected in the throughput data¹³², which are much higher for Senseo than for Dolce Gusto and Tassimo, which also shows – according to the Parties – that the two latter systems are viewed by consumers as "*occasional treats*" as opposed to "*everyday long black coffee*", which is the domain of Senseo. The Parties further argue that Tassimo is not a closer constraint on Senseo than other single-serve machines because levels of switching from Senseo to Tassimo are low, that is customers who owned a Senseo machine and wish to purchase a new single-serve machine do not choose a Tassimo machine more often than for instance a Dolce Gusto one. The Parties also present marketing materials and strategy documents of Mondelēz, which demonstrate, in their view, Tassimo's positioning as a multi-drink system and its focus on Dolce Gusto as its main competitor. The Parties carried out an analysis of the effects of Tassimo's entry on prices of Senseo and Dolce Gusto single-serve machines over the past 10 years, which – according to their interpretation – indicates that Senseo machine prices have remained largely stable over time, while Tassimo and Dolce Gusto react to each other's entries by reducing machine prices.¹³³ Moreover, the Parties claim that Senseo and Tassimo are not close competitors but rather complementary products as shown by the fact that Mondelēz continues to sell filter pads in competition with DEMB and in addition to Tassimo T-discs. As a result, the Parties maintain that there can be no expectation that the Tassimo system would capture material amounts of consumers from the Senseo system or vice versa.
- (190) Fourthly, the Parties claim that they would have no ability (either through reducing support for Senseo machine purchases or through increasing prices of filter pads) or incentive to transfer consumers from Senseo to Tassimo after the Transaction.

¹³² That is data on how many cups of a given beverage are consumed in a given period of time.

¹³³ Response to Article 6(1)(c) decision, Annex 2, ID02428.

According to the Parties, that lack of ability results from two facts. In the first place, [financial argument of the Parties]* after the Transaction. In the second place, the open character of the Senseo system implies that competitors selling filter pads could defeat any attempt of a price increase of Senseo filter pads. The lack of incentive to move customers from Senseo to Tassimo is corroborated by the fact that [comparison between the two systems]*.

- (191) Fifthly, the Parties maintain that Tassimo is not a maverick and the Transaction will not lead to the loss of an important competitor to Senseo. Instead, the Parties argue that Dolce Gusto, similarly to Tassimo, has been promoting its machines aggressively and the Parties could not afford to decrease the intensity of their competitive efforts after the Transaction on either Senseo or Tassimo because they would lose customers to their various competitors.
- (192) Sixthly, the Parties argue that the Transaction will not lead to loss of innovation because if the Parties stopped innovating they would lose customers to their competitors. Existing suppliers of single-serve systems, system licensors^{134x} (such as Caffitaly or Krüger) as well as future potential entrants (for instance US company Keurig) are, in view of the Parties, also a source of innovation as regards single-serve systems. Finally the model of cooperation between DEMB and Mondelēz on the one side and their respective partner machine manufacturers on the other side also implies, according to the Parties, that the latter are driving the innovation in the market. The Transaction will not bring about any change in the machine manufacturers' incentives to innovate.

Nestlé's arguments

- (193) Nestlé maintains that the Transaction is likely to give rise to competition concerns, in particular with respect to single-serve systems (that is, coffee machines and consumables for those machines). To support its concerns the complainant raises a number of arguments.
- (194) Firstly, coffee companies are involved in the machine business – they carry out research and development (or at least finance it), manage and finance advertising and promotion of single-serve machines.
- (195) Secondly, single-serve machines constitute a point of entry for final consumers and the choice of machine influences the choice of consumables. Since most of the profits are made through sales of consumables it is critical for actors in the consumables market to be strong on the market for the machines.
- (196) Thirdly, Tassimo and Senseo systems are each other's closest competitors, because: (i) they have a similar strategy of capitalising on their brands to expand market shares through different coffee categories; (ii) they have a similar price positioning of their single-serve machines at the low end of the price spectrum; and (iii) their respective market shares have evolved in close correlation in opposite directions during the past years – in particular economic data shows that in Germany and in the Netherlands sales of Tassimo machines have increased at the expense of those of Senseo.
- (197) Fourthly, Tassimo is a maverick in the single-serve segment, with strong promotions, an aggressive commercial pricing policy, and significant investments in media

¹³⁴ Role of system licensors is described in [...]*.
x Should read: Section 9.4.5.5.

advertisement. As a result the sales of Tassimo machines increased in most countries, mainly to the detriment of Senseo. After the Transaction the "competitive animation" created by Tassimo and the competitive pressure currently exerted on Senseo will be lost. In addition, the entry of Tassimo in Member States where it is currently not present becomes less likely.

- (198) Fifthly, the elimination of Tassimo as a maverick is even more problematic due to existence of high barriers to entry in the single-serve segment resulting from: (i) the need for investment to develop and produce machines; (ii) the need for investment in brand promotion; (iii) the need for investment to convince retailers to grant shelf space; (iv) the long time required to achieve a return on investment; and (v) competition from existing well-known brands.
- (199) Sixthly, after the Transaction the JV will have increased incentives to raise prices of filter pads to make consumers switch from the open Senseo system to the closed Tassimo system. In addition, since Mondelēz currently also offers competing filter pads, the JV would capture some of the customers switching away from Senseo branded filter pads to other filter pads. The JV could then progressively remove Senseo single-serve system from the market, thereby reducing consumers' choice. Alternatively, promotions for Senseo and Tassimo could be synchronised to move all consumers from Senseo to Tassimo.

Commission's investigation and assessment

9.4.1. Introduction

- (200) In the late 1980s Nestlé launched its Nespresso single-serve system, which achieved significant commercial success in 1990s. DEMB's Senseo was launched in the early 2000s and subsequently Mondelēz introduced its Tassimo (2004), while Nestlé its Dolce Gusto (2006).
- (201) The value of the single-serve machines market in the EEA¹³⁵ in 2013 amounted to approximately EUR 1 558 million as compared with EUR 1 482 in 2011. The countries where the single-serve machines market is the largest and where it also grows significantly include: Germany where in 2013 value of machines' market amounted to EUR 629 million (EUR 594 million in 2011); France where in 2013 it amounted to EUR 268 million (EUR 257 million in 2011), the Netherlands where in 2013 it amounted to EUR 87 million (EUR 82 million in 2011) and the United Kingdom where in 2013 it amounted to EUR 94 million (EUR 57 million in 2011).
- (202) Machines which are able to produce a single portion of coffee, or of another hot beverage, at a click of a button are available at different price points, with their nominal retail prices ranging from EUR 30 to several hundred Euros. However coffee companies subsidise the prices of single-serve machines heavily, by using various promotional tools and thereby reducing the final price paid by the consumers at the cashier, or reducing the cost borne by the consumers by offering them additional perks. Those promotional tools include among others cash-back coupons or vouchers for free coffee consumables.
- (203) DEMB owns the Senseo trademark and other IP rights relating to the Senseo system. It also participates in the marketing of Senseo coffee machines, which are

¹³⁵ Estimates on the basis of GfK data, which does not include sales made by direct channels, such as Nestlé or Tchibo stores. The data are available for the following countries: Austria, Belgium, Czech Republic, Germany, Denmark, Spain, Finland, France, Greece, Hungary, Italy, Ireland, the Netherlands, Poland, Portugal, Romania, Sweden, Slovakia and the United Kingdom.

manufactured by Philips. Since patents for the consumables for the Senseo system filter pads have expired, Senseo is an open system and apart from DEMB also Mondelēz and other players offer filter pads which can be used in Senseo single-serve machines.

- (204) Mondelēz created the Tassimo system and it owns the Tassimo trademark and IP rights relating to essential technological features of Tassimo machine. The machines are manufactured and sold by Bosch, but Mondelēz participates in their marketing, in particular by offering cash-backs and other promotional support for Tassimo machines. Tassimo is a closed system and only Mondelēz produces its consumables, that is to say T-discs.

9.4.2. *Cooperation between machine manufacturers and coffee companies*

General remarks

- (205) Single-serve systems are in principle developed in cooperation between, on the one side, the appliance or machine manufacturers (such as AEG, Bosch, DeLonghi, Kitchen Aid, Miele, Philips) or system licensors (such as Caffita System for the Caffitaly technology or Perfect Steam Appliances in cooperation with Krüger for the K-Fee technology) and, on the other side, owners of coffee brands (that is coffee companies or coffee manufacturers), such as the Parties, Nestlé, Tchibo, Lavazza, Melitta, Starbucks or even retailers such as Aldi or Lidl. There are various models as to which entity (coffee company or machine manufacturer) sells the single-serve machines. For instance Nestlé sells its Nespresso machines in own boutiques and online, similarly to Tchibo selling its Caffissimo machines and Aldi selling its Expressi machines. On the other hand Senseo single-serve machines are sold by Philips, while Tassimo by Bosch.
- (206) Nestlé in the course of the market investigation emphasised that it is absolutely critical for the suppliers of consumables for single-serve systems (that is to say in principle the coffee manufacturers) to be strong in the single-serve machines (that is to say to have a high level of penetration of one's single-serve machines) because that is the entry point for the consumers, who have a tendency to stay with their purchased machines during the lifetime of the machine and consequently through this period they will continue purchasing compatible consumables. As a result, in the eyes of Nestlé, coffee manufacturers compete most intensively, fiercely and face the largest stakes with respect to single-serve machines and therefore are heavily involved in the development of those machines, their innovation, advertisement and commercial promotion, in particular by managing and financing those activities. Nestlé further notes that the single-serve machines are co-branded with the coffee brand and therefore consumers tend to identify them as coffee suppliers' products rather than those of machine manufacturers. Consequently Nestlé argues that both Parties are active, through their machine partners in the sale of single-serve machines.
- (207) Broadly speaking the primary responsibility of a machine manufacturer in the course of the cooperation with a coffee company is the production and marketing of the single-serve coffee machine, while the coffee company is primarily responsible for the marketing and production of the coffee consumables. However, since those two elements, that is to say single-serve machine and consumables, are closely interlinked, the cooperation is usually structured in such a way that both partners can be involved, they can among others support, intervene, finance each other in their respective roles. The degree of that intervention can however vary.

- (208) For instance Nestlé appears to be involved to a significant extent in the activities relating to the coffee machines, since it sells those machines via its network of Nespresso boutiques and on-line sales. It participates in the conception and development of not only consumables but also the machines; one of Nestlé's affiliates finances the costs of R&D related to their single-serve systems. Furthermore, Nestlé owns patents on the machines as well as on the moulds necessary for the manufacture of their different machines. The position of Nestlé in the coffee sector and in particular in relation to single-serve coffee machines appears to be so significant that machine manufacturers approach Nestlé to propose cooperation.¹³⁶
- (209) Even though the majority of machine manufacturers who participated in the Commission's investigation consider that they have discretion in setting prices for coffee machines, they also admit that their coffee partners are able in other ways (for instance by coupons, cash-back offers) to influence prices paid by final customers for the coffee machine.¹³⁷ Machine manufacturers, retailers and electronic goods retailers also stated that the driving force behind promotion and advertising of single-serve machines is either the coffee supplier exclusively or both the coffee supplier and appliance producer.¹³⁸ None of them indicated that it is solely the machine manufacturer driving the advertising and promotion of single-serve machines. An overwhelming majority of retailers and electronic goods retailers who participated in the Commission's investigation explained that the advertising and promotion of single-serve machines are decided together with both machine manufacturers and coffee companies and not only with the machines manufacturers.¹³⁹ Retailers and electronic goods retailers further confirm the involvement of coffee companies in the sale of single-serve machines. They also emphasise the importance of those sales because, as one of the respondents stated, the aim of coffee suppliers is to "*sell more machines and to achieve more customers*".¹⁴⁰ Therefore, it can be concluded that coffee manufacturers, such as the Parties, even if they do not directly sell single-serve coffee machines are able to influence their prices and are thus involved in the single-serve machines market.

Parties' cooperation with machine manufacturers

- (210) As regards the Senseo system, DEMB acquired sole ownership of the Senseo trademark in 2012. It also owns other IP rights relating to that single-serve system. On 30 March 2012 DEMB entered into a Partnership Agreement with Philips [...]*. On the basis of that agreement both DEMB and Philips [...]*.¹⁴¹ On the other hand one of DEMB's responsibilities is to define the brand vision and strategy for Senseo and to run the in-market activation and promotion, in particular the "*appliance + coffee promotions & displays & local media support*".¹⁴² [...]*.¹⁴³ [...]*.¹⁴⁴ DEMB

¹³⁶ Response to question 23.1 of Questionnaire Q12 Machine manufacturers.

¹³⁷ Responses to questions 27.1, 27.2 of Questionnaire Q12 Machine manufacturers.

¹³⁸ Response to question 26 of Questionnaire Q12 Machine manufacturers and to question 25 of Q10 Retailers and to question 27 of Questionnaire Q11 Electronic goods retailers.

¹³⁹ Responses to question 24 of Questionnaire Q10 Retailers and to question 26 of Questionnaire Q11 Electronic goods retailers.

¹⁴⁰ Response to question 26.1 of Questionnaire Q12 Machine manufacturers.

¹⁴¹ Annex 6-1a, Partnership Agreement, par. 2.5.

¹⁴² Schedules 1-3 to the Partnership Agreement.

¹⁴³ Schedules 1-3 to the Partnership Agreement.

¹⁴⁴ Annex 6-1a, Partnership Agreement, par. 2.7.

also admitted that it is consulted by Philips in the course of establishing prices for Senseo machines to ensure that they are competitively positioned.

- (211) In the course of the market investigation Philips admitted that it is in charge of, inter alia, setting the recommended retail price for Senseo machines and that it receives revenues from these sales. However it also stated that "[t]he division of responsibilities between [DEMB and Philips] regarding the promotion of the Senseo machines is [...]*" Philips explained further that "[w]hen joint promotions are done, costs are often split [between Philips and DEMB]*. Promotion on machines are normally issued and sponsored by Philips; promotions on pads by DEMB; for promotions on the brand or on a combination of machine & pads, costs are split as outlined above."¹⁴⁵ This evidences that DEMB is also able to influence the prices of Senseo machines.
- (212) Mondelēz owns the Tassimo trademark as well as IP rights [...]*.¹⁴⁶ Specific provisions govern the influence of Mondelēz over the prices of Tassimo machines. [...]*.¹⁴⁷
- (213) In the course of the market investigation Bosch confirmed that its cooperation with Mondelēz was initiated by the latter and that "usually the coffee producers (...) take the lead in the development of new coffee systems and also later on sit in the driving seat".¹⁴⁸ It also stated that vouchers for coffee machines, which form part of an overall promotion scheme, are mainly issued at the discretion of Mondelēz.¹⁴⁹
- (214) The Parties themselves admit that the level of sales of Tassimo and Senseo machines are relevant to the sale of consumables and for that reason they support single-serve machines' sales through promotional funding. Moreover internal documents of the Parties demonstrate that they are vividly interested in pushing the sales and penetration of "their" single-serve coffee machines. Mondelēz states that in order to "[...]*" one of their priorities is to provide "[...]*¹⁵⁰ "151, and it aims at "[...]*".¹⁵² In another internal document Mondelēz plans to [...]*.¹⁵³ Moreover DEMB's internal documents indicate that it is constantly trying to increase the penetration of Senseo machines, in particular through "[...]*".¹⁵⁴

Conclusion

- (215) Consequently, on the basis of the Commission's investigation it can be concluded that although they indeed do not manufacture or sell single-serve machines, both Mondelēz and DEMB have an ability to influence the machine prices of Tassimo and Senseo machines respectively. That influence takes the form of promotional support aimed at pushing the penetration of their machines. However in practice and as will be further explained, Mondelēz appears to be engaged in [...]* than DEMB.

¹⁴⁵ Non-confidential minutes of a conference call with machine manufacturer dated 1 December 2014 at 16.00 CET.

¹⁴⁶ Annex 6-3a, Agreement for the development, manufacture, packaging, sale and distribution of Bosch-branded Tassimo advanced one cup in-home brewers, par. 21.

¹⁴⁷ Annex 6-3a, Agreement for the development, manufacture, packaging, sale and distribution of Bosch-branded Tassimo advanced one cup in-home brewers, par. 24.2.

¹⁴⁸ Non-confidential minutes of a conference call with Bosch dated 1 December 2014 at 15.00 CET.

¹⁴⁹ *Ibidem*.

¹⁵⁰ That is single-serve coffee machine.

¹⁵¹ Mondelēz internal document, dated 31 March 2011, "KFE Coffee Strategic Plan 2012-2014", p. 12.

¹⁵² Mondelēz internal document, dated 23 September 2013, "AC14 CE Coffee", p. 9.

¹⁵³ Mondelēz internal document, dated February 2014, "Link Meeting Spain", p. 9.

¹⁵⁴ DEMB internal document submitted as Annex 7-Netherlands-5 to the Form CO, p. 8.

Mondelēz appears to be [...] * than DEMB monitors the sales of Senseo machines. This is evidenced by the fact that – according to the Parties – DEMB does not [...] *, while Mondelēz does.¹⁵⁵

- (216) The analysis of cooperation between the Parties and their respective machine manufacturer partners also shows the great degree of importance which coffee companies attach to the level of penetration of their single-serve machines in the market.

9.4.3. Positioning of brands in single-serve systems

- (217) This section 9.4.3 will first discuss the importance of brands within the single-serve segment (that is both for single-serve machines and consumables for those machines) and it will subsequently deal with the positioning of those different brands.

- (218) According to retailers who participated in the Commission's market investigation, having a well-established coffee or other beverage brand is one of the main criteria in order for a single-serve system to achieve a substantial presence in a given country.¹⁵⁶ A well-known system brand is also one of the main factors customers take into account when purchasing their single-serve machine.¹⁵⁷

- (219) Mondelēz provides T-discs for Tassimo with various brands, including its numerous coffee brands (Carte Noire, Jacobs, Gevalia, Kenco) but also other Mondelēz/Kraft brands such as Milka, Oreo, Twining's and Cadbury.

- (220) Towards the end of 2010 Tassimo changed the image and strategy for its brand (that is to say it rebranded itself), moving away from espresso-focused premium coffee proposition towards a multi-brand, multi-drink and more mainstream positioning. That change meant that it was moving away from the Nespresso single-serve machines and emphasizing instead its multi-beverage functions, which brought it closer to Dolce Gusto. It was also aiming at increasing the easiness to shop for consumers (in view of its rapidly expanding range) as well as easier identification of different drink types available. The key marketing message of Tassimo is now "choose not to choose" or "be indecisive" offering "limitless branded beverage possibilities".¹⁵⁸ The power brands offered for T-discs are also meant to drive the throughput of consumables.¹⁵⁹ As a result Tassimo's main selling point is the variety of drinks it offers with the various brands.

- (221) Tassimo machines are available at different price points (spanning between entry price segment, through core, core plus and premium)¹⁶⁰ and with different characteristics in order to meet various consumer needs, for instance for quick brewing process consumers are offered Tassimo Sunny, while those who have limited space in their kitchens can choose the compact Tassimo Vivy.

- (222) DEMB considers that core strengths of the Senseo brand image are its functional qualities, that is to say being fast, easy and affordable, and relate to the emotional

¹⁵⁵ Responses of the Parties to Request for Information - QP4 dated 11 September 2014.

¹⁵⁶ Responses to question 18 Questionnaire Q10 – Retailers.

¹⁵⁷ Responses to question 7 Questionnaire Q1 – Competitors and to question 13 Questionnaire Q2 – Retailers.

¹⁵⁸ Mondelēz internal document, dated 2 May 2013, "Tassimo", slide 58.

¹⁵⁹ Mondelēz internal document, dated 9 October 2013, "AC'14 Beverages. Brewing delicious moments of joy", slide 22.

¹⁶⁰ Mondelēz internal document, dated March 2014, "Tassimo brewer launch program", slide 9.

and coffee pleasure appeal.¹⁶¹ Senseo customers are quite loyal to the brand, to a large extent replacing their Senseo machine with a new one once its lifetime lapses. However it was also noticed in DEMB's internal documents that they become [...] with the Senseo brand since [...]”¹⁶².

(223) The extract from DEMB's internal document presented in Figure 3 [...]*

[...]*

Figure 3 Shopper study 2014. Summary and final report.¹⁶³

(224) In order to prevent customers' switching away from Senseo and to differentiate Senseo from its competitors, DEMB was considering different strategies, including [...]”¹⁶⁴ ”¹⁶⁵.

(225) On the other hand Nestlé's Nespresso is positioned as a high-end, luxurious brand offering in principle strong, dark, espresso-type coffee. It is a social status symbol, a stylish item. Nestlé's Dolce Gusto positions itself as a trendy, playful, fun brand offering consumers a wide variety of drinks.¹⁶⁶

9.4.4. The structure of the market for single-serve machines

(226) Table 1 presents shares of the sales of the machines of the Parties' single-serve systems in the countries where both Tassimo and Senseo are present and account for at least 25% of the market for single-serve machine sales. These figures do not take into account the current penetration rates of each single-serve machine, rather simply the additional sales made by each machine in 2013. It should also be noted that France, Germany, the Netherlands and the United Kingdom jointly represent more than 60% of the EEA market for consumables for single-serve coffee systems. Data are presented both in volume and value, since, due to significant promotions applied to the prices of coffee machines, those two factors often differ significantly.

¹⁶¹ DEMB internal document, dated 30 June 2014, "Senseo – reunion Philips-DEMB", p. 60.

¹⁶² DEMB internal document, undated, "Shopper study 2014. Summary and final report. E2E Coffee Benelux", slide 2.

¹⁶³ DEMB internal document, undated, "Shopper study 2014. Summary and final report. E2E Coffee Benelux", slide 2.

¹⁶⁴ DEMB internal document, dated 13 January 2014, "Senseo NSC Philips-DEMB", p. 14.

¹⁶⁵ *Ibidem*, p. 14.

¹⁶⁶ DEMB internal document, undated, "Challenge 1: Develop brand equity & hierarchy for the masterbrand Senseo and its segments", slide 61.

Table 1 Single-serve coffee machines market shares for 2013¹⁶⁷

Single-serve machines market shares for 2013 ¹⁶⁸														
System	Austria ¹⁶⁹		France		Denmark		Germany ¹⁷⁰		Netherlands		Spain		United Kingdom	
	volume	value	volume	value	volume	value	volume	value	volume	value	volume	value	volume	value
Senseo	[10-20]* %	[10-20]* %	[40-50]* %	[30-40]* %	[10-20]* %	[5-10]* %	[40-50]* %	[30-40]* %	[50-60]* %	[40-50]* %	[5-10]* %	[5-10]* %	[5-10]* %	na
Tassimo	[10-20]* %	[5-10]* %	[10-20]* %	[10-20]* %	[20-30]* %	[10-20]* %	[10-20]* %	[10-20]* %	na ¹⁷¹	na ¹⁷²	[20-30]* %	[10-20]* %	[30-40]* %	[30-40]* %
Combined	[30-40]* %	[20-30]* %	[60-70]* %	[50-60]* %	[30-40]* %	[20-30]* %	[60-70]* %	[40-50]* %	-	-	[20-30]* %	[10-20]* %	[40-50]* %	-
Dolce Gusto	[10-20]* %	[5-10]* %	[10-20]* %	[10-20]* %	[30-40]* %	[20-30]* %	[10-20]* %	[10-20]* %	[10-20]* %	[10-20]* %	[40-50]* %	[30-40]* %	[30-40]* %	[20-30]* %
Nespresso	[40-50]* %	[60-70]* %	[20-30]* %	[20-30]* %	[20-30]* %	[40-50]* %	[10-20]* %	[30-40]* %	[30-40]* %	[40-50]* %	[20-30]* %	[40-50]* %	[10-20]* %	[30-40]* %
Others	[0-5]**% %	[0-5]* %	[0-5]**% %	[0-5]* %	[0-5]**% %	[0-5]* %	[0-5]**% %	[0-5]* %	[0-5]**% %	[0-5]* %	[0-5]**% %	[0-5]* %	[0-5]**% %	[5-10]* %
Cremesso	[0-5]**% %	[0-5]* %	-	-	-	-	-	-	-	-	-	-	-	-

(227) As is apparent from [...] the combined share of machine sales of Senseo and Tassimo would be particularly high in France ([60-70]*% in volume and [50-60]*% in value), with an overlap of approximately [10-20]*% resulting from Tassimo sales. Sales of Tassimo machines have also been increasing in France in the past three years starting at the level of [10-20]*% in volume and [10-20]*% in value in 2011. Senseo's shares of sales also slightly increased in value (from [30-40]*% in 2011 to

¹⁶⁷ Commission's estimates on the basis of GfK sales data.

¹⁶⁸ The market shares displayed do not include the full automated machines. Machines with a volume or value share lower than [0-5]*% have been aggregated in the "OTHERS" category.

¹⁶⁹ In Austria the underlying sales figures do not fully cover the Cafissimo system (which in the table falls within the category of "Others"). Caffissimo's share might amount to approximately [10-20]*%.

¹⁷⁰ In Germany the underlying sales figures do not fully cover certain systems (Cafissimo, Aldi and Lidl). Consequently, the reported market shares are overestimated, while the share of Caffissimo is underestimated and might amount to approximately [20-30]*% to [20-30]*%.

¹⁷¹ Tassimo Data for 2014: volume [5-10]*%.

¹⁷² Tassimo Data for 2014: value [5-10]*%.

x Should read: Table 1.

[30-40]*% in 2013) but declined in volume (from [40-50]*% in 2011 to [40-50]*% in 2013). The next strongest player in France is Nestlé with its Nespresso (the sales of which decreased in value from [30-40]*% in 2011 to [20-30]*% in 2013) and Dolce Gusto (the sales of which have been stable over the past 3 years) machines. Other players in the market occupy a niche position with a share of approximately [0-5]*% which is a slight increase in value from [0-5]*% in 2011.

- (228) The combined sales of Senseo and Tassimo machines are also very high in Germany ([60-70]*% in volume and [50-60]*% in value), again with Nestlé occupying the second position. Senseo has lost significant sales in volume as compared with 2011 ([50-60]*%); while Tassimo increased its position in volume from [10-20]*% in 2011. Also Dolce Gusto has slightly increased its sales in volume from [10-20]*% in 2011. GfK data for Germany do not track sales of single-serve systems by entities that operate private label brands, such as Aldi (with its Expressi system) as well as those sold through dedicated Tchibo boutiques (Caffissimo system). As a result the position of the players in Germany as presented is likely overstated.
- (229) In the Netherlands the share of sales of Senseo machines in 2013 was quite significant ([50-60]*% in volume and [40-50]*% in value), though decreasing in volume as compared with 2011 (when it amounted to [50-60]*%). Tassimo entered the Dutch market only in 2013 and on the basis of data for 2014, which covers only until October/November and therefore does not take into account the Christmas period sales, it achieved a share of [10-20]*% in volume and [5-10]*% in value. Nespresso maintained its position throughout the past three years in volume, although it decreased in value (from [40-50]*% in 2011).
- (230) In Denmark the combined sales of Tassimo and Senseo machines in volume are the largest in the market, however on the basis of value data Nestlé with Nespresso machines occupies the first position. Senseo and Dolce Gusto have lost significant sales over the past three years in Denmark (Senseo [10-20]*% in volume and [10-20]*% in value in 2011; Dolce Gusto [40-50]*% in volume, [30-40]*% in value in 2011), while Tassimo has increased its share of machine sales in this period (from [5-10]*% in volume and [5-10]*% in value in 2011).
- (231) Similarly in Austria Nestlé's sales of Nespresso are the largest with Tassimo's and Senseo's combined share of sales amounting to [30-40]*% in volume and [20-30]*% in value. It should be further noted that in Austria a Swiss player Cremesso – which has entered the Austrian market in 2013 - has a non-insignificant presence in that market with approximately [0-5]*% of single-serve machines' sales.
- (232) In Spain Senseo's and Tassimo's combined share of machines' sales occupies the second position after Nestlé. Nespresso and Senseo have lost sales over the past three years, in particular in volume– from [40-50]*% for Nespresso and from [10-20]*% for Senseo in 2011. On the other hand Dolce Gusto and Tassimo increased their sales in volume as compared with 2011, from [30-40]*% and [5-10]*% respectively.
- (233) In the United Kingdom Senseo is not particularly strong (with the volume share of approximately [5-10]*%); while Tassimo and Nestlé's Dolce Gusto are the leaders in the machines market with the former having a share of [30-40]*% in volume and [30-40]*% in value and the latter having a share of [30-40]*% in volume and [20-30]*% in value. Tassimo's position has increased from [20-30]*% in volume in 2011, while that of Dolce Gusto decreased from [40-50]*%.
- (234) Table 2 presents levels of penetration, that is to say, the percentage of households which own a given machine of the main coffee machines, in the EEA countries,

where both Tassimo and Senseo are active and account for at least [20-30]**% of the market for single-serve machine sales.¹⁷³

Table 2 Penetration of single-serve machines in Q4 2013¹⁷⁴

Penetration of single-serve machines in Q4 2013				
Country	Senseo	Tassimo	Dolce Gusto	Nespresso
Denmark	[5-10]**%	[0-5]**%	[5-10]**%	[5-10]**%
France	[30-40]**%	[10-20]**%	[5-10]**%	[10-20]**%
Germany	[30-40]**%	[10-20]**%	[5-10]**%	[5-10]**%
Netherlands	[50-60]**%	[0-5]**%	[5-10]**%	[10-20]**%
Spain	[5-10]**%	[5-10]**%	[10-20]**%	[20-30]**%
United Kingdom ¹⁷⁵	[0-5]**%	[5-10]**%	[5-10]**%	[0-5]**%

(235) As evidenced in Table 2, Senseo is the clear leader in terms of machine penetration in France, Germany and the Netherlands, with no other single-serve machine achieving similar levels. The penetration of Tassimo is highest in France ([10-20]**%) whilst both Nespresso and Dolce Gusto achieve highest levels of machine penetration in Spain (Nespresso [20-30]**%; Dolce Gusto [10-20]**%).

(236) The data in Table 2 can also be considered as a proxy for the strength and popularity of the various single-serve machines. As such, they clearly show that Senseo and Tassimo, together with the single-serve machines of Nestlé are the most prevalent in Austria, Denmark, France, Germany, the Netherlands, Spain and the United Kingdom. In fact all other players have a very small presence in those countries with the share of machine sales not exceeding 5%. However, as evidenced by the sharp increases in the value of the market for single-serve machines in the concerned Member States, mentioned in Recital (201), as well as the volatility of sales (in particular the growth of Tassimo and Dolce Gusto in some countries), the market for single-serve machines and consequently the segment of single-serve systems appears to be highly dynamic in character and therefore its structure can be unstable due to innovation and further growth.¹⁷⁶

9.4.5. *Non-coordinated effects*

(237) The Commission guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (the "Horizontal Merger Guidelines")¹⁷⁷ distinguish between two main ways in which mergers between actual or potential competitors on the same relevant market might

¹⁷³ According to the Parties the penetration data for Austria are not available.

¹⁷⁴ Parties' estimates.

¹⁷⁵ Data for the United Kingdom are for Q3 2013.

¹⁷⁶ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, par. 15.

¹⁷⁷ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings.

significantly impede effective competition, namely non-coordinated and coordinated effects. Non-coordinated effects might result from eliminating important competitive constraints on one or more firms, which consequently would have increased market power, without resorting to coordinated behaviour. In that regard, the Horizontal Merger Guidelines consider not only the direct loss of competition between the merging firms, but also the reduction in competitive pressure on non-merging firms in the same market that could be brought about by the merger.¹⁷⁸

- (238) The Horizontal Merger Guidelines list a number of factors which might influence whether or not non-coordinated effects are likely to result from a merger, such as the large market shares of the merging firms, the fact that the merging firms are close competitors, the limited possibilities for customers to switch suppliers, or the fact that the merger would eliminate an important competitive force. That list of factors applies equally if a merger would create or strengthen a dominant position, or would otherwise significantly impede effective competition due to non-coordinated effects. Furthermore, not all of those factors need to be present to make significant non-coordinated effects likely and it is not an exhaustive list.¹⁷⁹
- (239) After the Transaction the Parties would have influence over two of the four main single-serve systems (that is, Tassimo and Senseo) and Nestlé would have influence over the other two systems (that is, Nespresso and Dolce Gusto). Elimination of the current competition between Senseo and Tassimo could potentially lead to non-coordinated effects through (i) higher prices and (ii) less innovation in the single-serve systems.
- (240) Firstly, as already explained, the Parties – even though they do not sell coffee machines directly – do have some influence over machine prices by various means. Therefore, as further evidenced in section 9.4.2, they theoretically have the ability to increase prices for their single-serve machines by decreasing or stopping promotion efforts. Alternatively or in addition to increasing machine prices the Parties could increase also the prices of consumables (filter pads) for the Senseo machines.¹⁸⁰ In addition, the Parties could theoretically have incentives to engage in such price increases post-merger. For example some of the customers who would have been lost, pre-merger, from Tassimo would, post-merger, be captured through sales of Senseo. This could result in a general price increase for all single-serve machines and consumables. With horizontal mergers, in particular mergers concerning concentrated, oligopolistic markets, it is often the case that even non-merging firms can benefit from the reduction of competitive pressure which results from the merger. This is because the merging firms' price increase may switch some demand to the rival firms, which, in turn, may find it profitable to increase their prices¹⁸¹. Likewise, the main remaining player in the single-serve segment - Nestlé - would likely follow possible price increases because it would achieve higher profits from its increased prices as compared with the profits it could gain from undercutting the JV.
- (241) Secondly, combining two out of the four main single-serve systems in the hands of the JV could also lead to less innovation, in particular through limiting or blocking the development of a new single-serve system by one of the Parties or through

¹⁷⁸ Horizontal Merger Guidelines, par. 24.

¹⁷⁹ Horizontal Merger Guidelines, par 25.

¹⁸⁰ Consumables for Tassimo are currently supplied exclusively by Mondelēz and the transaction does not change anything in that respect.

¹⁸¹ Horizontal Merger Guidelines, par. 24.

decreasing the competitive pressure on the other players, which therefore might be less prone to innovate as well.

- (242) The Commission assessed the theories of harm referred to in Recital 239 and 240 in relation to single-serve systems, taking into account in particular the interplay between the market for single-serve machines and the market for single-serve consumables. On the basis of that assessment and for the reasons set out in Sections 9.4.5.1 to 9.4.5.6, the Commission has reached the conclusion that the Transaction would not give rise to competition concerns in relation to single-serve systems or to single-serve coffee machines in the countries where both Senseo and Tassimo are present and account for at least 25% of the market for single-serve machine sales (that is to say Austria, Denmark, France, Germany, the Netherlands, Spain and the United Kingdom). In reaching that conclusion, the Commission analysed (i) the closeness of competition between Tassimo and Senseo (Sections 9.4.5.1 and 9.4.5.2 below); (ii) the consequences of loss of competition between Tassimo and Senseo (Section 9.4.5.3 below); (iii) the competitive constraints exercised by other suppliers of single-serve coffee machines (Section 9.4.5.4 below); (iv) entry and expansion of the existing players (Section 9.4.5.5 below); and (v) the importance of the machine penetration (Section 9.4.5.6 below). As regards markets for single-serve consumables, the Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the filter pads markets in Austria and France (See sections 9.7.1 and 9.7.2 below).
- (243) In Sections 9.4.5.1 to 9.4.5.6 the general arguments that apply to all relevant geographic markets are set out and analysed. Thereafter in Sections 9.4.6.1 to 9.4.6.7 set out an assessment of the Parties' positions in each of those countries.

9.4.5.1. Closeness of competition

Introduction

- (244) In differentiated markets, the degree of substitutability between the products of the merging parties is a strong indicator of the likelihood of the implementation of price increases by the merged entity post-merger. The merging firms' incentive to raise prices is more likely to be constrained when rival firms produce close substitutes to the products of the merging firms than when they offer less close substitutes. For example, a merger between two producers offering products which a substantial number of customers regard as their first and second choices could generate a significant price increase. Thus, the fact that rivalry between the merging firms has been an important source of competition on the market might be a central factor in the analysis of the effects of the mergers.
- (245) As explained in Section 9.1.1, single-serve systems comprise differentiated products. As such, it is necessary to assess whether Senseo and Tassimo are close substitutes. The Commission has in its investigation paid particular attention to arguments put forward by Nestlé to the effect that Tassimo and Senseo could be each other's closest competitors because (i) they have a similar strategy of using their already well-known brands across coffee categories in order to capitalise on those brands and expand market share, (ii) they are positioned similarly in particular as regards their single-serve machines' prices, as they both occupy the low price spectrum and (iii) there is a negative relation between the relative volumes and the relative prices of Tassimo's and Senseo's machines, suggesting that there is substitution between those two machines and that Senseo and Tassimo are close competitors.
- (246) In its assessment on closeness of competition, the Commission has taken into account the responses of market participants (retailers, electronic goods retailers,

competitors and machine manufacturers) to the market investigation as well as the Parties' internal documents, which discuss Senseo's and Tassimo's current and anticipated positioning in the market vis-à-vis their competitors. Those internal documents also contain marketing studies, consumer preference surveys and analyses of purchasing patterns.

- (247) The Commission also analysed three economic studies submitted by Nestlé during the course of the proceedings which are claimed to show the closeness of Senseo and Tassimo. The Commission found that they are affected by serious shortcomings undermining the reliability of their results, and, hence, the conclusions of such studies. A detailed assessment of those studies can be found in Annex I. The Commission also carried out its own quantitative analysis on Tassimo's entry events which are further discussed in Section 9.4.5.2.
- (248) For reasons explained in Recitals (249) to (270), the Commission considers that Senseo and Tassimo cannot be considered to be particularly close competitors on the market for single-serve machines or on the single-serve system segment as a whole. Rather, the Commission considers that Tassimo's closest competitor on the machines market is in fact Dolce Gusto.

Information obtained in the Commission's investigation

- (249) Considering first the replies given by market participants to questions on the closeness of the four single-serve systems, the Commission notes that the majority of retailers in Denmark and in Germany as well as all French retailers consider that Tassimo would be the second choice for final customers whose first option is Senseo.¹⁸² However, when asked about the second choice of customers for whom Tassimo would be the first option, all of responding retailers in Denmark, Germany and the Netherlands mention Dolce Gusto; while those in Spain and the United Kingdom name either Dolce Gusto or Nespresso.¹⁸³ In France only the responses are more diverse and inconclusive with some retailers mentioning Senseo as the second best option to Tassimo, while others state it is rather Dolce Gusto or Nespresso.¹⁸⁴
- (250) Electronic goods retailers, when asked about the best alternatives to Senseo, in terms of targeted consumer groups, product characteristics, prices, brand strategy and perception by consumers, mention Nespresso in Austria and Dolce Gusto in Denmark and the United Kingdom.¹⁸⁵ In Germany and France the responses point in different directions with some retailers mentioning Tassimo, while others mention both Nestlé systems.¹⁸⁶ As regards the best alternative to Tassimo, in the eyes of Danish electronic goods retailers it is Dolce Gusto. By contrast, respondents from France and Netherlands mention Senseo and those from Germany and Austria are divided between Senseo and Dolce Gusto.¹⁸⁷ As for competitors, while most of them consider that Tassimo is the second best alternative for customers if they do not buy Senseo, their responses are not conclusive when asked which is the best alternative to Tassimo, with some of them mentioning Senseo, others Nespresso or Dolce Gusto.¹⁸⁸

¹⁸² Responses to question 26 of Questionnaire Q10 – Retailers.

¹⁸³ *Ibidem.*

¹⁸⁴ *Ibidem.*

¹⁸⁵ Responses to question 29 of Questionnaire Q11 – Electronic goods retailers.

¹⁸⁶ *Ibidem.*

¹⁸⁷ Responses to question 30 of Questionnaire Q11 – Electronic goods retailers.

¹⁸⁸ Responses to question 16 of Questionnaire Q9 – Competitors.

- (251) The Parties in their internal documents analyse and assess the threats posed by different single-serve systems to their own system. A large number of documents mention all four systems when analysing the single-serve systems segment. [...]*.¹⁸⁹ That implies that customers moving away from Senseo (that is to say soft pads) choose in principle the Tassimo single-serve system and therefore DEMB considers Tassimo as an important threat. [...]*.¹⁹⁰
- (252) However, there are many more internal documents of Mondelēz in which Mondelēz in particular [...]*.¹⁹¹ [...]*.¹⁹² [...]*,¹⁹³ . [...]*.¹⁹⁴ [...]*.¹⁹⁵

Commission's assessment

- (253) As mentioned in Section 9.4.3 the main selling point of both Tassimo and Dolce Gusto machines and systems is their multi-drink functionality. That key selling point is confirmed by retailers and electronic goods retailers who consider that the main reasons final customers choose a Tassimo machine relate to the multi-drink functionality, brand and price; while for Dolce Gusto those reasons relate to multi-drink functionality, price and quality.¹⁹⁶ An external study prepared for Mondelēz by a research company also established that Tassimo and Dolce Gusto are chosen by the consumers for the same reason, namely, that they can produce a variety of beverages and therefore they are also perceived similarly across Europe, whereas Nespresso and Senseo have a clear and distinct positioning.¹⁹⁷ One of the slides from this study is presented in Figure 4.

Figure 4 [...]*.¹⁹⁸

- (254) In this respect, the Commission notes that although milky or other flavoured filter pads (that is to say chocolate, caramel and speculoos among others) are available also for the Senseo system, there is still a difference in the perception of the two systems. Whilst it is not so clear-cut that – as the Parties' claim - the Senseo system is only perceived by consumers as a convenient alternative to filter coffee (and therefore associated primarily with long black coffee),¹⁹⁹ the majority of retailers who responded to Commission's market investigation, believe that Tassimo and

¹⁸⁹ DEMB internal document, undated, "*Kantar Worldpanel. High definition inspiration*", pages 14, 18.

¹⁹⁰ Mondelēz internal document, dated January 2012, "*Coffee Pods Platform Funnel 2014+*", p. 88, 89, 92.

¹⁹¹ Mondelēz internal document, dated 28 February 2013, "*Tassimo TDiscs Performance analysis 2012*". It is worth noting that this internal document does not mention Senseo at all.

¹⁹² Mondelēz internal document, undated, "*Tassimo current platforms*", slides 25, 26, 27.

¹⁹³ Mondelēz internal document dated 9 October 2013, "*AC'14 Beverages. Brewing delicious moments of joy*", slides 21, 22.

¹⁹⁴ For instance Mondelēz internal document, dated 20 September 2011, "*2012 Annual Contract. Germany*", slide 38. [...]*.¹⁹⁵

¹⁹⁵ Mondelēz internal document, dated 7 December 2010 "*Global sales council Vienna 2010 Competitive systems analysis*", slide 13.

¹⁹⁶ Responses to questions 37, 38 of Questionnaire Q10 – Retailers and to questions 32-33 of Questionnaire Q11 – Electronic goods retailers.

¹⁹⁷ Mondelēz internal document dated 9 February 2011, "*Benchmarking Tassimo against competition and across markets to identify opportunities and levers for growth*", slide 18.

¹⁹⁸ Mondelēz internal document dated 9 February 2011, "*Benchmarking Tassimo against competition and across markets to identify opportunities and levers for growth*", slide 18.

¹⁹⁹ Some respondents stated that "*Senseo is easier to use with different beverages variety and prepares beverages with foam (such as long coffee, espresso...) which is not the case for filter coffee makers*", and that "*Senseo's advertising (...) suggests that Senseo allows consumers to prepare espresso*" (as opposed to long black coffee) as well as emphasised the importance of easy dosage due to single portion which differentiates Senseo from filter coffee.

Senseo appeal to different types of customers.²⁰⁰ For example, a French retailer stated that differences in price, quality and the choice of drinks available indicate that Senseo and Tassimo are aimed at different customers, while a Dutch retailer noted that since they see people moving from Senseo to Tassimo "[p]robably Tassimo is the next step after Senseo".²⁰¹

(255) That difference in perception is further supported by Mondelēz's internal documents. In one particular document Mondelēz specifically notes that, [...]*.²⁰² In an analysis of Senseo carried out in 2006 it is further stated that "[...]*²⁰³ "204

(256) What came through from the responses to the market investigation is that consumers' perception of Tassimo and Dolce Gusto is very similar. As one French competitor highlighted, while "each single-serve system has specificities and may address different kinds of customers (...) Tassimo and Dolce Gusto systems target the same kind of customers because these two systems are based on machines that can provide not only coffee but also other beverages like chocolate or tea..."²⁰⁵ Another competitor also perceives Tassimo and Dolce Gusto as being in direct competition with each other due to their multi-beverage selling point.²⁰⁶

(257) That direct competition perception is also supported by the machine manufacturers who consider either that Dolce Gusto and Tassimo compete mostly with each other in terms of attracting the same customers or because all major suppliers of single-serve systems compete with each other.²⁰⁷ One of those respondents stated "Tassimo and Nescafé Dolce Gusto have the most similar product offer, being both multi beverage systems and competing often head to head on price. Then, as previously stated the big players in the single-serve are Senseo, Tassimo, Nescafé Dolce Gusto and Nespresso, and they all compete targeting for the same customer."²⁰⁸

(258) DEMB itself in its internal documents appears [...]*.²⁰⁹

[...]*

Figure 5 FY12 AOP Sara Lee C&T France²¹⁰

(259) Internal documents of Mondelēz also show that [...]*.

[...]*

[...]*

Figure 6 BSH and Kraft Brewer Workshop²¹¹

(260) Moreover, some of Nestlé's internal documents indicate that it similarly monitors, targets and benchmarks its Dolce Gusto against Tassimo. For instance, in the

²⁰⁰ Responses to question 40.1 of Questionnaire Q10 – Retailers.

²⁰¹ Response to question 40.1 of Questionnaire Q10 – Retailers.

²⁰² Mondelēz internal document dated June 2012 "Kraft Coffee Pods Ambition", p. 7.

²⁰³ That is single-serve.

²⁰⁴ Mondelēz internal document "Senseo Overall Analysis", pages 7-8.

²⁰⁵ Response to question 5 of Questionnaire Q5 – Market test France.

²⁰⁶ Response to question 5 of Questionnaire Q5 – Market test France.

²⁰⁷ Responses to question 30 of Questionnaire Q12 – Machine manufacturers.

²⁰⁸ *Ibidem*.

²⁰⁹ Internal document of DEMB, undated, entitled "Kantar Worldpanel. High definition inspiration", page 33.

²¹⁰ DEMB internal document, dated 2 March 2011, "FY12 AOP Sara Lee C&T France", slide 16.

²¹¹ Mondelēz internal document, dated 3 May 2010, "BSH and Kraft Brewer Workshop no app", slides 15 and 19.

Netherlands, Nestlé has prepared a special "*welcome plan Tassimo*" for the launch of Mondelēz's system.²¹² It also plans detailed responses to various types of promotional activities it expects from Tassimo, including pricing of machines, presentation in points of sale and TV advertising.²¹³ Those internal documents show the preparation of "*anti-Tassimo*" plans²¹⁴ and analyse in detail Tassimo's offer, including photos with the presentation of both machines and consumables on retailers' shelves.²¹⁵

- (261) The differences in throughput (referred to in Recital (188)), which are broadly confirmed by the Parties' internal documents, also further support the Parties' claim that Senseo and Tassimo address different consumer needs: the former, which is drunk more often, is more of a regular, daily beverage; while the latter with lower throughput is considered by consumers as suitable for their moments of indulgence.
- (262) The Parties also argue that levels of switching from Senseo machines to Tassimo machines are low, which further proves that those two are not close competitors. To substantiate their argument they cite an analysis of French customers' switching behaviour in 2013. [...]*.²¹⁶ The results of the analysis imply that users of all investigated single-serve machines – excluding Nespresso – seem interested in the various alternative machines to a similar extent (between 20% and 30%) and no clear pattern of switching between particular single-serve machines can be found. That appears to suggest that the various single-serve machines all compete with each other to the same extent.
- (263) As regards the argument put forward by Nestlé that both Senseo and Tassimo have a similar strategy of using their well-known brands across coffee categories in order to capitalise on those brands and expand the market share, it should first be noted that, the fact that DEMB and Mondelēz use their already strong coffee brands across different coffee products (in other words, the same brands appear across for example R&G, filter pads and N-capsules) is not in itself an indication of closeness. In a differentiated market, where brands are important that seems to be not only reasonable but also the prevalent strategy. In particular Nestlé uses its Nescafé brand (particularly strong in the instant coffee market) to endorse Dolce Gusto single-serve machines; Tchibo coffee brand is put on the Cafissimo single-serve machines, while Lavazza's brand is on the A Modo Mio machines. Moreover, whilst Mondelēz uses a multi-brand strategy for Tassimo consumables (in other words manufacturers sell consumables compatible with the Tassimo system under a number of different Mondelēz brands), DEMB does not use this multi-brand strategy. In fact, both Tassimo and Dolce Gusto capitalise on their owners' strong non-coffee related brands in their consumables offerings (Tassimo uses Mondelēz brands such as Oreo, Milka or Twining's and Dolce Gusto uses Nestlé brands such as Nestea or Nesquik).
- (264) As regards price positioning of single-serve machines, an analysis of the price chart submitted by Nestlé to evidence that Tassimo and Senseo are closest competitors due to their similar price positioning indicates that, while players in the single-serve machines markets offer machines at all various price points, there seems to be a continuum of single-serve machines beginning with Senseo as an entry-level and

²¹² Nestlé internal document, undated, "*Tassimo launch in NL*", slide 16-ff.

²¹³ Nestlé internal document, dated March 2014, "*Operational meeting – the Netherlands*", slide 6.

²¹⁴ Nestlé internal document, dated 8-9 September 2011, "*Operational meeting – Czech & Slovak Republics*", slide 4.

²¹⁵ Nestlé internal document, dated 8-9 September 2011, "*Operational meeting*", slide 14.

²¹⁶ DEMB internal document, undated, "*Brand tracking report 2013*", slide 19.

most affordable machine, followed by Tassimo and Dolce Gusto, with Nespresso positioned at the end of the continuum, offering the most expensive machines. That continuum seems to be confirmed by the fact that Senseo is particularly strong in the price range below EUR 50, Tassimo and Dolce Gusto between EUR 50 and 100 and Nespresso above EUR 100. However it should also be added that Figure 7 is based on retail ticket prices, that is to say, it does not take into account cash-backs, coupons and other promotional measures which are widely used in the single-serve machines market. With respect to price positioning it is also worth noting that, as per the Parties' submission, the consumables for Senseo and Tassimo are priced at different points, with the latter being two to three times more expensive. Therefore the comparison presented in Figure 7 does not, contrary to Nestlé's view, prove closeness of competition between Tassimo and Senseo.

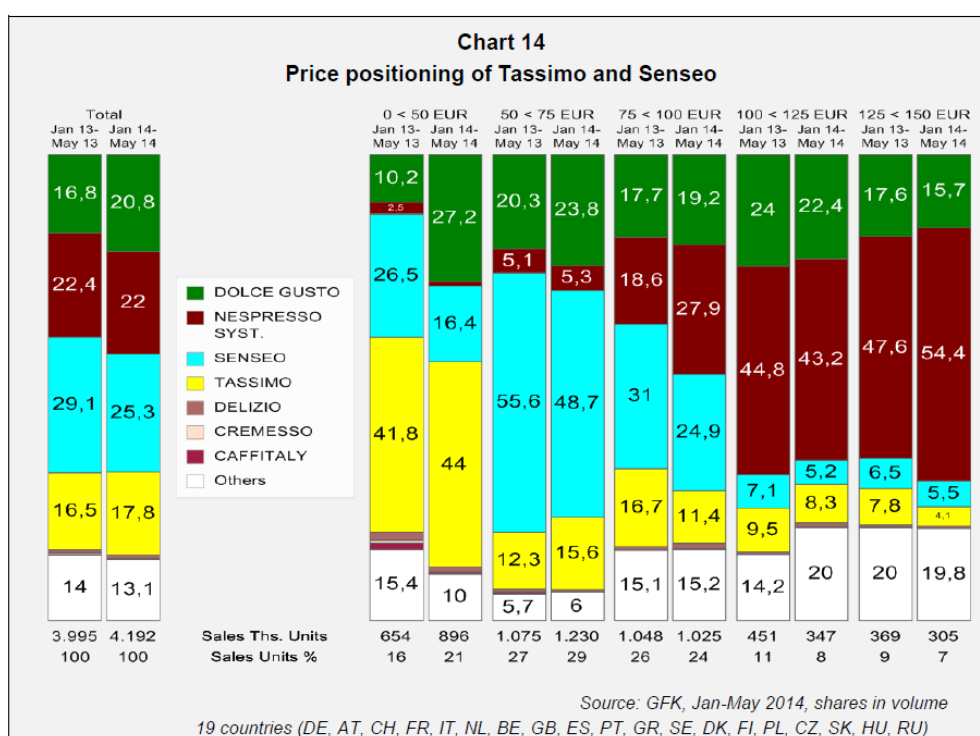


Figure 7 Price positioning of Tassimo and Senseo machines²¹⁷

- (265) Moreover, positioning in the market place and thus closeness of competition is not only price related but rather depends on multiple other factors relating to the image and functionalities of a given system.
- (266) As regards Nestlé's third argument of, namely that the Parties are close competitors because there is a negative correlation between the relative prices and volumes of Tassimo and Senseo machines, the Commission notes that such a correlation is not directly informative for the purpose of assessing the closeness of competition between Tassimo and Senseo, as it might be driven by factors unrelated to competition. In addition, unilateral variations in the price of one machine, keeping the price of the other machine constant, result in the same negative relation.
- (267) Finally, the Parties also submitted an analysis of the effects of Tassimo's entry on the price of Senseo and Dolce Gusto machines.²¹⁸ The Commission notes that that

²¹⁷ Nestlé's compilation on the basis of GfK data.
²¹⁸ Response to Article 6(1)(c) decision, Annex 2.

analysis is not based on a systematic analytical comparison of the underlying prices. Rather, it is a purely graphical comparison of the price series. Even though a graphical representation is not necessarily unreliable in general, particularly for the purposes of carrying out a preliminary analysis of price series, an in-depth assessment requires a more systematic approach in order to rule out the possibility of drawing erroneous conclusions due to spurious relations between the price series and entry events. The Commission, however, carried out a systematic, analytic comparison the methodology and conclusions of which are summarised in Section 9.4.5.2.

- (268) On the basis of what has been said, the Commission considers that there seems to be a heterogeneity of single-serve systems, possibly on a sliding scale, with some being perceived as more suitable for first-time buyers who do not yet have experience with single-serve machines, while others appear targeted rather at consumers willing to further upgrade and wishing to satisfy additional needs (such as the need for the availability of drinks other than coffee). That could be reinforced by the fact that Tassimo was considered as an alternative option to Senseo but not necessarily vice versa. Moreover it could also be confirmed by the fact that Senseo sells most of its machines – as compared with other players – in the lower price spectrum. Furthermore, one of the machine manufacturers in the course of the market investigation noted that it would be difficult to establish clear segmentations according to consumer preferences, since each company has its own strategy and therefore one could rather speak of a “*continuum along which consumer would be placed*”.²¹⁹ Moreover a retailer confirmed that within the single-serve machines there are more premium products and that “*customers will generally trade up*” to those products.²²⁰ That could potentially imply that on the sliding scale Senseo would be the entry-level machine followed by Tassimo or Dolce Gusto, or both, with Nespresso being perceived as the high level machine.
- (269) On the basis of the evidence available, the Commission considers that on the continuum of single-serve systems, Tassimo and Dolce Gusto are closer competitors to each other than each is to Senseo or Nespresso. That is because they both share the same key selling point, which is offering a variety of drinks and utilising a multi-brand strategy for their consumables. That is the message delivered to consumers in Tassimo's and Dolce Gusto's marketing campaigns. Consumers are receptive of that message and perceive them as close competitors. Dolce Gusto, similarly to Tassimo and unlike Senseo, also engages in extensive promotional activities with respect to its machines, heavily subsidising their sales. As a result, much of the “competitive animation” in the single-serve segment results from the rivalry between Tassimo and Dolce Gusto. Moreover, although DEMB [...]*

Conclusion

- (270) The Commission therefore concludes that Senseo and Tassimo cannot be considered as particularly close competitors. In fact, the Commission considers that all the main four single-serve systems compete with each other and within those systems, Tassimo's closest competitor is in fact Dolce Gusto.

²¹⁹ Response to question 5.1 of Questionnaire Q12- Machine manufacturers.

²²⁰ Response to question 5 of Questionnaire Q6 – Market test Denmark.

9.4.5.2. Closeness of competition: Quantitative Assessment

- (271) The Commission performed a quantitative analysis on Tassimo's entry events and found that Tassimo machines exert a competitive constraint on both Senseo machines and Dolce Gusto machines. The Commission notes that the presence of a degree of competition across coffee machines is a necessary but not sufficient condition to conclude that the merger would give rise to non-coordinated effects in the coffee system market. In fact, DEMB has a very limited ability to raise Senseo machines' prices, and Mondelēz has little or no incentives to raise Tassimo machines' prices.
- (272) In this particular case the Commission's entry analysis should be seen as a one-sided test. That means that it provides information about the potential (lack of) merger effect only if it shows that the different coffee machine systems do not compete with each other. However, if the analysis finds that the different coffee machines (and in particular Tassimo and Senseo) compete against each other further evidence would be needed to show that the merger would have an anti-competitive effect. In other words, the finding that the different coffee machines compete with each other is a necessary but not sufficient ingredient for building a theory of harm showing anti-competitive effects on the market for coffee machines. That is due to the particular complementarity structure between coffee machines and coffee consumables of the single-serve coffee systems already described.
- (273) The Commission performed a fixed effect regression model (in this application the model is also called *difference in differences estimation*) using GfK data provided by the Parties.²²¹ The data included coffee machines' sales and prices in 20 countries on a monthly basis from January 2004 to November 2014.^{222,223} The model quantifies the relationship between the (log) monthly average price of the coffee machine on the one hand and indicator variables for the presence of a rival coffee machine in a country for a given period and control variables on the other hand.^{224,225,226} The model was performed on Senseo machines' prices ("Senseo regression") and Dolce Gusto machines' prices ("Dolce Gusto regression").
- (274) The regression model captures how the average price of a coffee machine is affected by the presence of a rival coffee machine. To properly capture that effect the model requires some variation in the variable indicating the presence of a rival machine during the period considered. In other words, the estimation of the model requires observations of entry or exit events, or both, of the rival machine systems. The variable of interest in the present case is the presence of Tassimo. In the data there

²²¹ See Response to RFI of 19 December 2014, 9 January 2015.

²²² Countries included: Austria, Belgium, Switzerland, Czech Republic, Germany, Denmark, Spain, Finland, France, Greece, Hungary, Ireland, Italy, Netherlands, Poland, Portugal, Romania, Sweden, Slovakia, United Kingdom.

²²³ For some countries the data were not available for the full period. However, this limitation did not hinder the reliability of the analysis.

²²⁴ The estimation method was linear regression. The other control variables were country specific control variables in logarithms (exchange rate, HICP index for coffee, tea and cocoa products, GDP and GDP per capita), and time and country fixed effects.

²²⁵ The GfK data include also sales of coffee machines that are due to parallel imports from other countries. To avoid the inclusion of parallel imports in the analysis, the Commission excluded those coffee machines that did not reach 5% market share in any year of the analysis.

²²⁶ The regressions employed heteroskedasticity robust standard errors. As a robustness check, the Commission also clustered the standard errors on a country level. The conclusions of this specification do not differ from the conclusions using robust standard errors.

are eight Tassimo entry events for the Senseo regression, and eight Tassimo entry events for the Dolce Gusto regression.

- (275) Intuitively, the effect of Tassimo's entry on Senseo or Dolce Gusto machines' prices is identified as the difference of the average machine's price before and after Tassimo's entry in a given country, relative to other countries where entry did not occur. Such countries where Tassimo did not enter are called control (or comparator) countries. In the Senseo regression there are two such control countries, while in the Dolce Gusto regression there are five control countries. The main estimated coefficient of the model represents the average effect of Tassimo's entry across the countries the markets of which it entered.
- (276) It should be noted that because of the usage of that comparator country (or difference-in-differences) methodology, and also taking into account the effect of other variables, the Commission's analysis is more systematic than the entry analysis presented by the Parties.²²⁷
- (277) It might be expected that the effect of Tassimo's entry on Senseo's and Dolce Gusto's prices would also depend on the relative strength of Senseo and Dolce Gusto in a given a country. In other words, it is possible that Senseo and Dolce Gusto may react differently to Tassimo's entry in those countries where they have a stronger presence. To account for that possibility, the Commission also estimated a specification where the regression model is weighted by a proxy measure of the machine penetration in each country.²²⁸
- (278) An examination of the GfK data evidenced a sharp decrease in Tassimo machines' prices from 2012 onwards in all the countries of the analysis. The Parties explained that that sharp decrease was due to the implementation of the "[...]*" by Mondelēz. [...] In the Commission's view, part of the decrease in Tassimo's prices may be also due to the spin-off of Mondelēz from Kraft Foods announced in early 2012 and occurred in October 2012.²²⁹
- (279) In its regression analysis, the Commission took the increase in Tassimo's aggressive behaviour into account by including in the model an indicator variable equal to one from 2012 onwards in those countries where Tassimo was present before 2012. In the countries where Tassimo entered after 2012 the dummy is equal to zero as the effect is already captured by the presence indicator variable.
- (280) The results show that in both the Senseo and Dolce Gusto regressions, the effect of Tassimo's presence is negative and statistically significant. That is, the entry of Tassimo is associated with an average decrease in the prices of both Senseo machines and Dolce Gusto machines. That indicates that Tassimo represents a significant competitive constraint for both machines.²³⁰ However, the Commission finds that the effect of Tassimo's entry on Dolce Gusto's prices is higher (in absolute value) than the effect of Tassimo's entry on Senseo's prices. The Commission's finding is consistent with Tassimo being closer to Dolce Gusto than to Senseo, as indicated by the qualitative evidence.

²²⁷ Response to Article 6(1)(c) decision, Annex 2.

²²⁸ This proxy penetration was the total machine sales over the period divided by the sum of the population over the period.

²²⁹ See Response to RFI of 30 January 2015, 5 February 2015.

²³⁰ The effects slightly differ in magnitude between the weighted and the unweighted regressions, but the negative sign and the statistical significance are the same in both specifications.

- (281) The Commission employed several methodologies to test the robustness of the analysis. In particular, following approaches recommended in economic literature, different bootstrap methods were used to assess the statistical significance of the estimates (those methods were the so called classic²³¹ and wild bootstrap²³² methods).²³³ Overall, the outcome of such checks reinforces confidence in the robustness of the estimated coefficients. Furthermore, the wild bootstrap indicated that Tassimo's presence is not statistically significant in the Senseo regression and is statistically significant in the Dolce Gusto regression. The finding gives some further indication that Tassimo is closer to Dolce Gusto than to Senseo.
- (282) It is important to point out, however, that the results of the analysis are not directly indicative of the merger effect, or even of the likelihood of the merger effect. What can be learned from the results is that the different single-serve systems compete with other systems. However, the merging Parties are active in the aftermarket, in the production of consumables, and, as it will be explained in more detail below, only Mondelēz has a significant ability to increase the Tassimo machines' prices by reducing the subsidies of the promotional activity (that is to say coupons and "Direct Pricing"). The amount of machine subsidisation that DEMB spends on a yearly basis is minimal. Therefore DEMB is not able to substantially increase Senseo machine prices.
- (283) Furthermore, Mondelēz would have a limited incentive to increase Tassimo machine prices post-merger. The lost demand that the merged entity could recapture after the price increase would be limited to the amount of consumers who would switch to Senseo (among the other systems) and would use Senseo's filter pads currently produced by DEMB (among the other filter pads producers). Hence, the recapture would not be only limited by switching to coffee machines other than Senseo, but it would be further fractioned because the market for filter pads is an open market, and only the portion of consumers who switch to Senseo *and* buy DEMB's filter pads will count as recaptured lost demand. Particularly, if the market for filter pads has a high degree of competition, the recapture would represent a small percentage of the loss in demand. Additionally, the market investigation evidenced the current rush for increasing the installed machine base, as the market for single-serve is growing. The willingness to attract new customers incentivises coffee manufacturers to decrease the price of the coffee machines by subsidising them through coupons. That incentive would not disappear post-merger.
- (284) For the reasons set out, although the quantitative analysis indicates a degree of competition across different single-serve machines and systems, for the particular complementarity of machine and consumables in the coffee systems, and the particular incentives of the coffee manufacturers, the Commission cannot conclude

²³¹ See, for example, Bertrand, Marianne, Esther Duflo, and Sendhil Mullainathan. "How Much Should We Trust Differences-In-Differences Estimates?." *The Quarterly Journal of Economics* 119.1 (2004): 249-275.

²³² See Cameron, A. Colin, Jonah B. Gelbach, and Douglas L. Miller. "Bootstrap-based improvements for inference with clustered errors." *Review of Economics and Statistics* 90.3 (2008): 414-427.

²³³ The estimated coefficient of Tassimo's presence in the Senseo regression was found significant at 10% level using the classic bootstrap with replacement, and non-significant using the wild bootstrap. The estimated coefficient of Tassimo's presence in the Dolce Gusto regression was found significant at 5-10% level using the classic bootstrap, and significant at 10% level using the wild bootstrap. In general, the bootstrap methodologies will always decrease the significance level of the estimated coefficients. As the estimated coefficients still maintain a degree of statistical significance, the results can be considered robust.

with the requisite degree of certainty that the merger will give rise to a price increase in respect of single-serve machines or systems.

9.4.5.3. Consequences of loss of competition between Tassimo and Senseo

Introduction

(285) Irrespective of the level of closeness existing between Tassimo and Senseo, the Transaction still leads to a loss of competition between those two single-serve systems. The Commission has therefore assessed whether the Transaction leads to a significant impediment to effective competition, in particular by removing an important competitive force from the market.

Arguments of Nestlé and other competitors

(286) Some of the Parties' competitors argued potential anti-competitive non-coordinated effects could derive from the loss of the current competition between Tassimo and Senseo. In particular, those competitors claimed that the Parties, after the Transaction, could try to shift their customers from the open Senseo system to the closed Tassimo system (with the latter being potentially more profitable to the Parties given that only Mondelēz can manufacture the consumables for that system). Those competitors suggest that the Parties would have the ability to make the shift through: (i) cash-back promotions or bring-in programs for customers willing to trade their Senseo machine for a Tassimo machine, or otherwise synchronising promotions on the machines or consumables; and (ii) increasing the prices of Senseo consumables or machines, or both. As a result, according to those competitors, the open market for Senseo consumables would shrink and competing suppliers of filter pads would be foreclosed, while the JV would progressively remove the Senseo system from the market thereby reducing consumers' choice. The Parties' would have, according to those competitors, significant incentives to implement such a strategy given that the profits they would make from the closed Tassimo system would more than offset the losses they would incur by limiting their sales of Senseo.

(287) Furthermore Nestlé submitted in the course of market investigation that Tassimo is a very aggressive player (so called "maverick") in the single-serve segment, applying an aggressive commercial pricing policy and significant promotions, as well as investing strongly in advertising in various media. All those efforts, according to Nestlé, created "competitive animation" which was not only increasing the awareness of consumers of single-serve systems as a whole but also their willingness to purchase single-serve machines. That in turn resulted in growing the entire demand for single-serve machines. After the Transaction the competitive dynamic and pressure currently exerted by Tassimo in particular on Senseo will, according to Nestlé, be lost. Nestlé further argues that the entry of Tassimo in countries where it is currently not present becomes less likely after the Transaction.

Commission's assessment

(288) The Commission has assessed the potential anti-competitive effects of the Transaction resulting from shifting consumers from the open Senseo system to the closed Tassimo system, and has analysed whether the JV would be likely to implement such a strategy.

(289) First of all, the scope for DEMB to influence prices of Senseo machines is limited to the extent of the promotional support it offers for the Senseo single-serve machines. Moreover, although DEMB does have a contractual possibility to offer such support, in practice it is not using that possibility and its promotional efforts for Senseo machines are limited. As per the Parties' submission, on the basis of aggregate EEA

2013 sales, DEMB's direct investment per machine sold (that is to say machine price support) amounts to EUR [...]*. In 2014 DEMB spent approximately EUR [...]* in the EEA on promotion of Senseo machines, which amounted to [...]**% of the average Senseo machine price. To put those numbers into perspective, Mondelēz, which is a player aggressively promoting its single-serve machines, in 2014 spent EUR [...]* on promoting Tassimo machine sales, which amounted to [...]**% of the average machine price. DEMB also does not make money transfers to Philips in order to support or influence Senseo machine prices or promotions. In view of its current minimal support for the sales of Senseo machines, the JV would not have significant scope of manoeuvre for increasing Senseo machine prices (notably by reducing the support of those machines) with the hope that that would lead the customers to move to the closed Tassimo system.

- (290) Similarly, the Commission notes that the likelihood that the JV would increase the prices of Senseo consumables to shift its customers to Tassimo is also very limited. That is because, due to the open character of the Senseo system, it would be significantly constrained in most countries by the presence of other suppliers of competing filter pads. As regards in particular countries, such as Austria or France, where the JV would possess significant market power in the filter pads market, the competitive situation in these countries is analysed in sections 9.7.1 to 9.7.2.
- (291) Furthermore, as concerns the potential promotions by which the customers would be encouraged to bring in their Senseo machine and replace it with a Tassimo machine, the Commission notes that that situation is not merger specific, since nothing would prevent Mondelēz, absent the Transaction, from using such promotion methods immediately and the Transaction does not strengthen anyhow its ability to do so.
- (292) Finally, as presented in Section 9.4.2, the commercial policy with regard to single-serve systems, including Senseo, is shaped in cooperation between coffee companies and machine manufacturers. Therefore DEMB cooperates with Philips in that respect and, due to the fact that Philips' profits are derived from the sales of Senseo machines, it is very likely that Philips would oppose any efforts by the JV aimed at "progressively removing Senseo system from the market".
- (293) In conclusion, it seems unlikely that the Parties would be able to shift their customers from Senseo to Tassimo machines or system following the Transaction.
- (294) As regards the Parties' incentives to shift their customers from Senseo to Tassimo machines or system, it can also be noted that given the differentiated nature of the markets in question, the Parties would not be able to capture all the customers outflowing from Senseo as a result of possibly increased prices of either Senseo machines or consumables, since at least some of them might decide to purchase the competing single-serve systems, particularly taking into account that rivals' products (for example Dolce Gusto) are, as explained in section 9.4.5.4 close substitutes to each of Senseo and Tassimo. That would diminish the JV's incentives to increase Senseo prices (machines or consumables) and renders those price increases further unlikely.
- (295) The Parties also claim that they would not have incentives to transfer customers from Senseo towards Tassimo, [...]*. Nevertheless the lack of ability to implement a strategy of moving consumers from Senseo to Tassimo still constitutes the critical reason why it is unlikely that the anti-competitive effects evoked by Nestlé and described in Recital (286) would materialise.
- (296) With respect to Nestlé's claim that following the Transaction Tassimo would decrease its promotional efforts and thus increase prices of the machines for

consumers, the Commission considers that whilst Mondelēz, unlike DEMB, has the ability to increase those prices, it is unlikely that it will do so. The Commission found that Mondelēz is currently investing heavily in supporting sales of its Tassimo machines. In fact historical evolution of shares of sales of single-serve machines indicates that Mondelēz's efforts were quite successful and its aggressive promotional spending translated into an increase in Tassimo machines' sales. Therefore, Mondelēz could theoretically stop its aggressive promotion of the machines. Nonetheless in a growing and dynamic market, as evidenced in Section 9.4.4, where the positions of market players are shifting in time and where one of the critical success factors is achieving a sufficient level of penetration of machines, decreasing aggressiveness in recruiting customers would be a harmful and thus irrational strategy. The Parties' claim that the JV could not afford to let up the intensity of its competitive efforts for both Tassimo and Senseo because it would lead to losses to different sets of competitors seems in this context founded. In addition, high prices for single-serve machines would also slow down the shift of consumers from multi-serve to single-serve systems, thus slowing down the growth of the entire single-serve category to the detriment of all single-serve suppliers, as described in Section 9.4.5.6.

Conclusion

(297) The Commission therefore concludes that it is not likely that the Parties – after the Transaction – would be able and incentivised to shift customers from Senseo machines and system to Tassimo machines and system.

9.4.5.4. Competitive constraint exercised by other suppliers of single-serve systems

Competitive constraint exercised by Nestlé

(298) The Parties' single-serve systems, as presented in Table 1, are particularly strong at least in France, Germany and the Netherlands. Sales of Nestlé's Dolce Gusto and Nespresso systems constitute in essence the remaining part of the single-serve systems markets in those countries, while in the other countries where both Senseo and Tassimo are present, that is to say in Austria, Denmark, Spain and the United Kingdom, Nestlé occupies the first position.

(299) In fact competitors in Denmark, Austria, Spain, Greece, consider Nestlé's systems as their primary competitors in the single-serve systems.²³⁴ As regards suppliers of single-serve systems active in multiple EEA countries two of them view Nestlé as their main competitor, while the remaining two mention Tassimo.²³⁵

(300) Nestlé was the first coffee company to introduce a single-serve machine for in-home consumption into the market and maintained that first mover advantage by maintaining a constantly high level of investment in advertising and promotion on points of sales of its single-serve brands.²³⁶ Its strong position results also from the "premium brand image" of their Nespresso system; which is marketed as "affordable luxury", the fact that it maintains the quality level of both the machines and consumables, has a good distribution network and offers a broad range of

²³⁴ Responses to question 19 of Questionnaire Q9-Competitors.

²³⁵ *Ibidem.*

²³⁶ Responses to questions 15.3 and 15.4 of Questionnaire Q9 – Competitors.

machines.²³⁷ As a result it is perceived by other suppliers of single-serve systems as the market leader.²³⁸

- (301) The apparent fierce pre-Transaction rivalry between Tassimo and Dolce Gusto also implies that following the creation of the JV, despite increased concentration in the single-serve segment, both the JV and Nestlé will remain incentivised to compete with each other. This was also noted by some of the retailers and electronic goods retailers who participated in the Commission's investigation and stated that, in particular for the Netherlands, there would be more competition between Nestlé and JV after the Transaction,²³⁹ and that prices will remain low.²⁴⁰ For the reasons mentioned in this Section, if the JV were to increase prices of Tassimo machines or consumables after the Transaction, it would likely lose sales to Nestlé (in particular to Tassimo's closest competitor Dolce Gusto) and therefore the latter will still constrain the JV after the Transaction.

Competitive constraint exercised by other players

- (302) Furthermore, in addition to Nestlé, there are also other players in the single-serve segment, although they currently occupy niche positions and are not necessarily present across the EEA. However their positions are not insignificant, which is confirmed by their presence on retailers' shelves. Those other players include: Tchibo in Germany and Austria, Aldi in Germany, and Lavazza and Illy in France.
- (303) In the course of market investigation machine manufacturers indicated that they expect private label single-serve systems as well as those of Lavazza or Illy to increase their market share in the coming years.²⁴¹

Conclusion

- (304) Consequently in the countries where the combined share of machine sales of the Parties' system is the largest, in addition to the competitive constraint exercised by Nestlé, the Parties also face constraint from the smaller players. Should the JV decrease its promotional efforts thereby increasing prices of machines there could be *"an opportunity for smaller local players to find their niche and penetrate the markets of the machines more easily."*²⁴² The competitive constraint exercised by Nestlé and other suppliers of single-serve systems also implies that the Parties will remain incentivised to maintain investment into innovation (by means of introducing new single-serve machines and upgrading existing ones) in order not to be outgrown by their competitors.

9.4.5.5. Entry and expansion of existing players

- (305) The entry of new players in a market as well as the expansion of existing ones act as a competitive constraint on the merged entity. However, for entry to be considered a sufficient competitive constraint on the merging parties, it must be shown that entry is likely, timely and sufficient to deter or defeat any potential anti-competitive effects of the merger.

²³⁷ *Ibidem.*

²³⁸ *Ibidem.*

²³⁹ Response to question 51 of Questionnaire Q10 – Retailers.

²⁴⁰ Response to question 43 of Questionnaire Q11 – Electronic goods retailers.

²⁴¹ Non-confidential minutes of a conference call with a machine manufacturer dated 1 December 2014 at 15.00 CET and of a conference call with machine manufacturer dated 1 December 2014 at 15.00 CET.

²⁴² Non-confidential minutes of a conference call with a competitor dated 6 February 2015 at 16.00 CET.

- (306) Barriers to enter and expand in the single-serve machines market are certainly not insignificant. First of all, those are the barriers resulting from the general characteristics of the market, referred to in Section 9.1, such as the importance of brands and the need to devote substantial financial resources to advertising and promotion. Retailers and electronic goods retailers consider that in order to achieve a substantial presence within a given country with a single-serve system one needs to have a well-known brand and invest in promotion and advertising.²⁴³ Secondly additional barriers result from the need to finance the single-serve technology and the penetration of single-serve coffee machines, since only a sufficiently large machine park allows for recoupment of the investment made into development of the single-serve system. Competitors confirm that the main driver for purchasing a new single-serve system is promotion of the coffee machine.²⁴⁴ Furthermore the high costs of introducing new single-serve system into the market result also from the need to offer a range of coffee machines and a range of consumables, positioned at different price points in order to match the wide ranges already offered by the existing players.
- (307) The Parties themselves in their internal documents take the view that high barriers exist in relation to single-serve systems: "[...]*".²⁴⁵
- (308) Nevertheless the majority of retailers and electronic goods retailers as well as all machine manufacturers who responded to the Commission's questionnaire confirmed that there have been entries into the single-serve segment in the past three years.²⁴⁶ In that context, Segafredo is mentioned in France, Aldi in Germany, Lavazza with A Modo Mio in the United Kingdom and Germany, Illy in the United Kingdom and Starbucks with Verismo system in France.²⁴⁷
- (309) As regards future entry, the vast majority of machine manufacturers expect a new single-serve system to be introduced into the market in the next 2–3 years.²⁴⁸ In particular the US company Keurig is viewed as a potential new entrant into Europe (in particular into the United Kingdom, Poland and Sweden), for instance by Bosch. That entry is also expected by Mondelēz because Keurig is viewed as a strong player in the US with a "[...]*" and thus, according also to Mondelēz internal documents, potentially "[...]*".²⁴⁹ A Dutch electronic goods retailer states that Tchibo with its Cafissimo system might become active in the Netherlands. It also adds that Dutch retailers might follow the example of the German retailers and also introduce their own single-serve systems.²⁵⁰ Another competitor expects that "[c]ompetition will continue to be fierce, with 2 systems potentially merging into one there is another 10 ready to step in."²⁵¹ In its market investigation the Commission found also evidence of plans of entry or expansion of offer of single-serve systems by a number of players within the EEA.
- (310) The reason why, despite relatively high barriers to entry, a number of companies have decided to start marketing single-serve systems in the past – and for which

²⁴³ Responses to question 18, Q10 – Competitors and question 20 of Q11 – Electronic goods retailers.

²⁴⁴ Responses to question 5 Q9 - Retailers.

²⁴⁵ DEMB internal document Strategy, February 2014 submitted as Annex 6-2 to Form CO, pp. 64, 69.

²⁴⁶ Responses to question 43 of Questionnaire Q12- Machine manufacturers, question 38 of Questionnaire Q11 – Electronic goods retailers and question 41 of Questionnaire Q9 – Retailers.

²⁴⁷ *Ibidem*.

²⁴⁸ Responses to question 48 of Questionnaire Q12- Machine manufacturers.

²⁴⁹ Mondelēz internal document, dated 23 May 2012, "*Tassimo Product Council*", slide 10.

²⁵⁰ Responses to question 40 of Questionnaire Q11 – Electronic goods retailers.

²⁵¹ Response to question 6.1 of Questionnaire Q6 – Market test Denmark.

entries are expected in the future – lays in the attractiveness of the market. Single-serve is a dynamic and growing market, with potential for substantial margins. Therefore incentives to enter, expand, participate in it are indeed high. As a machine manufacturer has noted, single-serve "[is] not saturated leaving room for other entrants [which will] accelerate single serve penetration".²⁵²

- (311) In addition, the entry barriers resulting from the investment into single-serve technology are less significant since that technology is becoming more easily available. For instance, entry and expansion in single-serve segment can also take place in cooperation with licensors of single-serve technology, which are ready to pair with a coffee supplier or with a retailer. Tchibo's Caffissimo system is, for instance, an example of collaboration between Tchibo and the system licensor – Caffitaly. Similarly Krüger licenses its K-Fee technology for instance to Aldi, but also to Starbucks. Those systems are semi-open, which means for instance that all licencees of the technology can offer compatible consumables. As a result final consumers have more choice and variety, which can constitute a good selling point for its suppliers, who can thus gain easier access to retailers' shelves.²⁵³ This is reflected in Mondelēz internal documents, where Mondelēz notes that Caffitaly "[...]".²⁵⁴

Conclusion

- (312) Consequently, while barriers to entry and expansion in the single-serve segment are relatively high it remains attractive for potential and expanding players. The market for single-serve machines experienced a significant growth in the last years, as explained in Recital (201), and is likely to experience a growth in the future, both in terms of higher consumer penetration in the EAA countries where those systems are already present and expansion to other countries. As a result entry is still likely,²⁵⁵ as confirmed by the market participants who responded to the Commission's investigation. Therefore the potential entrants and expanding players are likely to exercise a competitive constraint on the JV also after the Transaction.

9.4.5.6. Importance of machine penetration

- (313) For the reasons previously mentioned in Recital (201), the demand for single serve machines is far from being mature and stable and is expected to grow rapidly in the future. At the same time the pace of growth of that demand depends on the conditions under which single-serve machines are offered. If those conditions worsen (for instance by decreasing the promotional efforts – not offering cash-backs, coupons) the development of the demand for single serve machines risks a significant slowdown. Consequently also the shift of consumers from multi-serve to single-serve systems would be hampered. As it has been shown in Section 9.1.5 single-serve is much more profitable than multi-serve for coffee companies. Therefore also in light of the need to recoup the high investments incurred to start marketing a single serve system it is unlikely that the coffee companies would run the risk of slowing down the development of the demand for single-serve machines.

²⁵² Response to question 43 of Questionnaire Q12- Machine manufacturers.

²⁵³ Non-confidential minutes of a conference call with a competitor dated 6 February 2015 at 16.00 CET.

²⁵⁴ Mondelēz internal document, dated 22 November 2011, "*Tchibo ATC – Caffitaly system*", slide 2.

²⁵⁵ Horizontal Merger Guidelines, paragraph 69.

- (314) As a result, in order to ensure high levels of sales in coffee consumables, coffee companies are incentivised to increase demand for single-serve machines and thus the machine penetration.
- (315) The Parties' competitors stated in the course of market investigation that the promotion of coffee machines is one of the main drivers for consumers to purchase a new single-serve system.²⁵⁶ That confirms that the levels of inflow of new consumers into the single-serve system depend on the aggressiveness of promotional efforts. As a result a supplier of single-serve systems, which decides to tone down its promotional efforts, might have difficulties recruiting new customers. A competitor explained that since in principle the majority of households will only purchase one single-serve machine, which will then determine the choice of compatible consumables for the lifetime of this machine, *"the competition among single-serve systems is very aggressive"*.²⁵⁷ Another competitor noted *"The key in this business model is to achieve high penetration of coffee machines so it is expected that the owners of the main SiSe will continue to push machine sales by aggressive promotions. Only this way they will also ensure their consumables are placed on retailers' shelves (i.e. retailers will welcome consumables for systems with high machine park, since this will guarantee high turnaround for the consumables)"*.²⁵⁸ When asked about the impact of the Transaction on single-serve machines prices a machine manufacturer submitted that *"the trend is to 'buy' consumers to the systems; we don't expect this to change significantly. The pressure on prices will continue"*.²⁵⁹
- (316) Internal documents of Mondelēz confirm [...]*.²⁶⁰ [...]*.²⁶¹ That suggests that JV will continue its aggressive promotion strategy also after the Transaction because it considers it crucial for its success in the market.
- (317) Moreover, a competitor in the market investigation noted that one of the competitive advantages of Tassimo is the price of its machines, since Mondelēz subsidises them strongly, which *"leads to high level of machine penetration"*.²⁶²
- (318) A survey carried out for DEMB [...]*.²⁶³ Such consumers would purchase a Tassimo machine only because it was offered at a low price but would not afterwards buy the consumables. It has concluded that the new Tassimo buyers are not less regular consumers of T discs than the new buyers of Dolce Gusto or Senseo of the respective consumables and they are not less loyal. That implies that in fact such consumers are not "less qualitative".²⁶⁴ Therefore the strategy of Mondelēz is rational and effective and as such likely to be continued.

Conclusion

- (319) The importance of pushing the penetration of single-serve machines is a feature of the single-serve segment largely confirmed by the market participants in the course of the Commission's investigation and corroborated by the Parties' internal

²⁵⁶ Responses to question 5 of Questionnaire Q9 – Competitors.

²⁵⁷ Response to question 5 Questionnaire Q5 – Market test France.

²⁵⁸ Non-confidential minutes of a conference call with a competitor dated 6 February 2015 at 16.00 CET.

²⁵⁹ Response to question 48 of Questionnaire Q12 – Machine manufacturers.

²⁶⁰ Mondelēz internal document dated 9 October 2013, "AC'14 Beverages. Brewing delicious moments of joy", slide 11.

²⁶¹ Mondelēz internal document dated 3 December 2014, "BSH- Mondelēz 2nd GSCM 2014 Minutes", p. 1.

²⁶² Response to question 15.2 of Questionnaire Q9 – Competitors.

²⁶³ DEMB internal document, undated, entitled "Kantar Worldpanel. High definition inspiration", pages 40-41.

²⁶⁴ *Ibidem*.

documents. That feature influences market dynamics and indicates that even after the Transaction, [...]*, the JV will have to remain aggressive in order not to lose its market position to existing strong players, which include Nestlé, or those entering or expanding in the single-serve segment. Another reason not to decrease promotional efforts lays in the necessity to ensure the inflow of customers into the single-serve segment. Importance of machine penetration also implies that the Parties will remain incentivised to innovate and offer new, upgraded versions of their machines in order to convince final customer to choose their single-serve systems over those of competitors or to switch to them from multi-serve systems.

9.4.6. *Country analysis*

(320) For the reasons presented in Section 9.4.5, the Commission has reached the conclusion that the Transaction would not give rise to competition concerns in relation to single-serve systems or to single-serve coffee machines in the countries where both Senseo and Tassimo are present and account for at least 25% of the market for single-serve machine sales (that is to say Austria, Denmark, France, Germany, the Netherlands, Spain and the United Kingdom). Those reasons apply to all the relevant countries. In addition, Sections 9.4.6.1 to 9.4.6.7 analyse in more detail the effects of the Transaction in each of those countries.

9.4.6.1. Austria

(321) In Austria the combined sales of Tassimo and Senseo machines amount to [20-30]% in value. The clear leader in the single-serve machines market is Nestlé with its Nespresso and Dolce Gusto machines.

(322) Furthermore in Austria Tchibo is active with its Cafissimo system. As mentioned in footnote 169 the competitive significance of Tchibo's single-serve machines is not reflected in market shares presented in Table 2 due to the fact that GfK data does not capture sales made through Tchibo's own boutiques. Furthermore in Austria another important player is Cremesso with its share increasing in value from [0-5]*% in 2011 to [0-5]*% in 2013.

(323) Machine manufacturers in Austria confirm even though Tassimo is closest competitor to Senseo, it is in fact Dolce Gusto which is the closest competitor to Tassimo.²⁶⁵

(324) As a result those other players in addition to Nestlé will continue to exercise competitive constraint on Tassimo and Senseo in Austria. The effects of the Transaction on the filter pads market in Austria are analysed in section 9.7.2. Therefore the Transaction does not lead to competition concerns in relation to single-serve systems in Austria.

9.4.6.2. Denmark

(325) In Denmark the combined sales of Tassimo and Senseo machines amount to [20-30]*% in value, while sales of Nestlé's machines are much larger and amount to [70-80]*%.

(326) While the majority of Danish retailers which responded to the Commission's questionnaire consider Tassimo to be the closest competitor to Senseo, they all consider Tassimo's closest competitor to be, in fact, Dolce Gusto.²⁶⁶ The majority of

²⁶⁵ Responses to question 31, 32 of Questionnaire Q12 – Machine manufacturers.

²⁶⁶ Responses to question 26 of Questionnaire Q10 – Retailers.

machine manufacturers also view Dolce Gusto as the closest competitor to Tassimo.²⁶⁷

- (327) Furthermore the sales value of Senseo machines have been decreasing in Denmark, from [10-20]*% in 2011 to [5-10]*% in 2013. The main player in Denmark remains Nestlé.
- (328) As a result the Transaction does not lead to competition concerns in relation to single-serve systems in Denmark.

9.4.6.3. France

- (329) In France, although Tassimo and Senseo jointly would have the highest share of single-serve machine sales amounting to [50-60]*% in value, Nestlé's position is also quite significant. Therefore for the reasons set out in Section 9.4.5, Nestlé will continue to exercise competitive constraint on the Parties' single-serve systems in France.
- (330) Retailers in France confirmed that they do not only allocate shelf space to single-serve machines of Tassimo, Senseo and Nestlé. In particular, those retailers stated that shelf space is also allocated to other suppliers of single serve machines, in particular, Malongo (owner of "1,2,3 Spresso" system) and Lavazza.²⁶⁸
- (331) As regards the Italian competitors, that is Lavazza (with its A Modo Mio) and Illy (with its Iperespresso) Mondelēz in its internal documents [...].²⁶⁹
- (332) In terms of market shares Lavazza is slowly but gradually increasing its presence in France, while in 2011 its value market share amounted to [0-5]*% in 2013 it amounted to [0-5]*% (in volume it grew from [0-5]*% in 2011 to [0-5]*% in 2013).
- (333) Machine manufacturers perceive Dolce Gusto as the closest competitor to Tassimo in France. Views were, however, mixed as to who represented Senseo's closest competitor. Certain respondents mentioned Tassimo, while others referred to Nestlé.²⁷⁰
- (334) Consequently players such as Lavazza will, in addition to Nestlé, continue to exercise competitive constraint on Tassimo and Senseo in France. The effects of the Transaction on filter pads market in France are analysed in Section 9.7.1. Therefore the Transaction does not lead to competition concerns in relation to single-serve systems in France.

9.4.6.4. Germany

- (335) In Denmark the combined sales of Tassimo and Senseo machines amount to [50-60]*% in value, closely followed by Nestlé's with its sales of machines amounting to [40-50]*%.
- (336) In Germany retailers allocate shelf space to competing single-serve systems of Lavazza Krüger, Tchibo and Illy.²⁷¹
- (337) Retailers and machine manufacturers also confirmed that in Germany the closest competitor to Tassimo is Dolce Gusto.²⁷²

²⁶⁷ Responses to question 31 of Questionnaire Q12 – Machine manufacturers.

²⁶⁸ Response to question 22 of Q10 – Retailers and to question 24 of Q11– Electronic goods retailers.

²⁶⁹ Mondelēz internal document, dated 26 February (no year indicated), "*Tassimo SP 14/16. WIP Assumptions*", slide 2.

²⁷⁰ Responses to question 31 of Questionnaire Q12 – Machine manufacturers.

²⁷¹ Response to question 22 of Q10 – Retailers and to question 24 of Q11– Electronic goods retailers.

- (338) In Germany, similarly to Austria²⁷³ Tchibo is active with the Cafissimo system and sells its single-serve machines and consumables not only through retailers but mostly through its own network of dedicated Tchibo boutiques. The competitive significance of Caffissimo is confirmed by the fact that it is analysed in the internal documents of the Parties²⁷⁴ but also those of Nestlé²⁷⁵. Smaller competitors present in Germany also view Tchibo's Cafissimo as an important player and estimate its share in Germany at [20-30]*%.²⁷⁶ Tchibo itself admits that single-serve segment is the fastest developing coffee market at the moment and it is very attractive for Tchibo to be present and expand.²⁷⁷
- (339) Furthermore in Germany retailer Aldi offers its own single-serve system Expressi. Although that system certainly is positioned differently from those of the Parties and Nestlé, its presence in the market and thus certain competitive constraint it exercises is acknowledged and monitored in [...] internal documents.²⁷⁸
- (340) As a result the Transaction does not lead to competition concerns in relation to single-serve systems in Germany.

9.4.6.5. Netherlands

- (341) Tassimo entered the Netherlands in 2014 and achieved sales of [5-10]*% in value. The strongest player in the Dutch single-serve machines market is Nestlé with the combined share of sales of its Nespresso and Dolce Gusto machines amounting to [50-60]*% in value.
- (342) One of the main retailers in the Netherlands stated that Tassimo's closest competitor is in fact Dolce Gusto and not Senseo.²⁷⁹ Similarly the majority of machine manufacturers mentioned Nestlé's single-serve machines as closest competitors to Senseo in the Netherlands.²⁸⁰
- (343) As a result in the Netherlands, where Tassimo has entered only recently the key competition will continue to take place between the system of Mondelēz and Dolce Gusto. This is also evidenced by Nestlé's internal documents describing a "welcome plan" for Tassimo in the Netherlands cited in Recital (260). Therefore the Transaction does not lead to competition concerns in relation to single-serve systems in the Netherlands.

9.4.6.6. Spain

- (344) Combined shares of sales of Tassimo and Senseo machines in Spain are not very significant and amount to only [10-20]*% in value. Nestlé remains the clear leader in Spain and it will exercise a significant competitive constraint on the JV.

²⁷² Responses to question 3.1 and to question 26 of Questionnaire Q10 – Retailers and to question 31 of Questionnaire Q12 – Machine manufacturers.

²⁷³ In addition to other countries, including inter alia Poland, Czech Republic, Romania, Slovakia.

²⁷⁴ See for instance Mondelēz internal document, dated January 2012, "*BSH and Kraft Tassimo Strategy Alignment Workshop. Anticipating competition*", slide 26-ff and DEMB internal document, dated 19 November 2012, "*Senseo in Poland. Single serve market overview*", slide 12 and ff.

²⁷⁵ With respect to Poland – see Nestlé internal document dated 8-9 September 2011, "*Operational meeting*", slide 15.

²⁷⁶ Non-confidential minutes of a conference call with a competitor dated 6 February 2015 at 16.00 CET.

²⁷⁷ Non-confidential minutes of a conference call with a competitor dated 6 February 2015 at 12.30 CET.

²⁷⁸ For instance Mondelēz internal document dated August 2014, "*Brewer sales opportunity. Germany*", slide 11 and ff.

²⁷⁹ Response to question 3.1 of Questionnaire Q10 – Retailers.

²⁸⁰ Responses to question 32 of Questionnaire Q12 – Machine manufacturers.

(345) The Transaction will not lead to anti-competitive effects in Spain also due to the lack of closeness of competition between Tassimo and Senseo in Spain. Spanish retailers consider Nestlé's systems as competing most closely with both Senseo and Tassimo.²⁸¹ Consequently the Transaction does not lead to competition concerns in relation to single-serve systems in Spain.

9.4.6.7. United Kingdom

(346) The share of Senseo machine sales, decreased in value from [0-5]*% in 2011 to [0-5]*% in 2013. As a result the combined share of Tassimo and Senseo sales amounts to [30-40]*% in value.

(347) Retailers in the United Kingdom view Tassimo and Dolce Gusto as the closest competitors.²⁸² One of them further explained "*Although Senseo was the first single serve brand in the UK with its pads, it was not sufficiently promoted and has been overtaken by Dolce Gusto and Tassimo. Senseo remains very small in the UK. Tassimo on the other hand is very big in the UK. [name of the retailer] does not perceive Tassimo and Senseo (...) as close competitors (...)*"²⁸³

(348) On the other hand Lavazza's presence in the United Kingdom is gradually increasing with its share of machine sales growing in value from [0-5]*% in 2011 to almost [0-5]*% in 2013.

(349) Thus the Commission concludes that the Transaction does not lead to competition concerns in relation to single-serve systems in the United Kingdom.

9.4.7. Conclusion

(350) On the basis of the foregoing and the available evidence, the Commission concludes that the Transaction will not lead to competition concerns in relation to single-serve systems. In particular, it will not lead to a significant impediment to effective competition in the markets for single-serve machines in Austria, Denmark, France, Germany, the Netherlands, Spain and the United Kingdom.

(351) However, as regards the markets for single-serve consumables, the Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the filter pads markets in Austria and France (as set out at sections 9.7.1 to 9.7.2).

9.5. R&G

(352) For the reasons set out in Recitals (353) to (421), the Commission has reached the conclusion that the Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the R&G markets in France, Denmark and Latvia. Moreover, for the reasons set out in Recitals (422) to (454), the Commission has reached the conclusion that the Transaction would not significantly impede effective competition in the internal market in the R&G markets in the Czech Republic, Greece, Poland, Bulgaria, Hungary, the Netherlands and Spain.

²⁸¹ Response to question 26 of Questionnaire Q10 Retailers.

²⁸² Response to question 3.1 of Questionnaire Q10 – Retailers.

²⁸³ Non-confidential minutes of a conference call with a retailer dated 24 September 2014 at 16.00 CET.

9.5.1. France

- (353) R&G represented [30-40]*% of the total coffee market in France in 2013, with the total value amounting to approximately EUR 1,062 million. DEMB supplies the French market with R&G coffee products mainly under L'Or, Ma Tradition and Maison du Café brands. The R&G brands of Mondelēz include Carte Noire, Grand'Mère, Jacques Vabre and Velours Noir.

Parties' arguments

- (354) The Parties do admit that DEMB's L'Or brand and Mondelēz's Carte Noire brand could be viewed as closely competing within R&G coffee products. Nevertheless they argue that in France they face strong competition in this market originating mostly from retailers' brands but also from other suppliers of branded coffee products, such as Lavazza, Segafredo, Malongo and Legal. As to private label products the Parties claim that they are present throughout the entire product range, they offer the same quality as branded products.
- (355) Secondly, the Parties claim that entry into R&G market in France is easy, given that coffee is a globally traded commodity, and that roasting and packaging process does not require substantial investment or technical expertise. Alternatively a new entrant could outsource in particular roasting to a third party supplier, since there is an overcapacity in roasting in France.
- (356) Thirdly, the Parties argue that retailers in France are able to exercise significant buyer power. That would be maintained after the transaction in particular since retailers are linked by buying alliances, which reinforces their position against suppliers. The Parties further claim that French retail market is also witnessing price wars as a result of fierce competition between the different retail groups, and that such competition drives retailers to negotiate lower prices by means of various negotiation levers, such as delisting threats, stopping orders, refusing to agree prices, cancelling promotion slots. The Parties cite examples when such negotiation techniques were used in their relations with French retailers.

Commission's investigation and assessment

- (357) In general the overall R&G market in France appears to be rather stable and mature. While the total value of the market decreased by approximately EUR 41 million, various competitors maintained their positions over the course of the past three years.

Table 3 R&G market in France²⁸⁴

Manufacturer	Brand	2013		2014	
		Value('000 €)	Share	Value ('000 €)	Share
DEMB	L'OR	[...]*	[5-10]**%	[...]*	[5-10]**%
	MA TRADITION	[...]*	[0-5]**%	[...]*	[0-5]**%
	OTHER	[...]*	[0-5]**%	[...]*	[0-5]**%
DEMB TOTAL	-	[...]*	[10-20]**%	[...]*	[10-20]**%
MONDELEZ	CARTE NOIRE	[...]*	[20-30]**%	[...]*	[20-30]**%
	GRAND'MÈRE	[...]*	[5-10]**%	[...]*	[10-20]**%
	JACQUES VABRE	[...]*	[0-5]**%	[...]*	[0-5]**%
	VELOURS NOIR	[...]*	[0-5]**%	[...]*	[0-5]**%
	OTHERS	[...]*	[0-5]**%	[...]*	[0-5]**%
MONDELEZ TOTAL	-	[...]*	[40-50]**%	[...]*	[40-50]**%
COMBINED	-	[...]*	[50-60]**%	[...]*	[50-60]**%
RETAILERS	PRIVATE LABELS	[...]*	[20-30]**%	[...]*	[20-30]**%
REGIONAL BRANDS	-	[...]*	[0-5]**%	[...]*	[0-5]**%
LAVAZZA	LAVAZZA	[...]*	[0-5]**%	[...]*	[0-5]**%
SEGAFREDO	-	[...]*	[0-5]**%	[...]*	[0-5]**%
LEGAL	-	[...]*	[0-5]**%	[...]*	[0-5]**%
OTHER	OTHER	[...]*	[0-5]**%	[...]*	[0-5]**%
TOTAL	-	[...]*	100%	[...]*	100%

Source: the Parties.

9.5.1.1. Parties have high market shares

(358) In general the overall R&G market in France appears to be rather stable and mature. While the total value of the market decreased by approximately EUR 41 million, various competitors maintained their positions over the course of the past three years.

²⁸⁴

There would be no material change in the market shares, if coffee beans were included.

- (360)
- (361) Table 3 shows that the Parties are significant players in the R&G market in France. In fact they are number one (Mondelēz) and number two (DEMB) providers of branded R&G products. Their market shares have been stable over the past three years, with Mondelēz slightly strengthening its position from [40-50]*% in 2011 to [40-50]*% in 2014, due to an increase in Carte Noire's share.
- (362) The combined market share of the Parties amounts to more than [50-60]*% ([50-60]*% in 2014). After the Transaction the various retailers' brands would jointly hold the second largest market share and in any case be twice smaller than the JV (with a share of approximately [20-30]*% which has slightly decreased over the past three years). Furthermore the degree of competitive constraint exercised by private label brands cannot be considered as equivalent to that of a market player with the same market share, since it represents an aggregation of sales of various retailers with some of them having stronger private label brands and others weaker.
- (363) It should be also noted that over the past three years none of the suppliers of branded R&G coffee products (other than the Parties) was able to achieve market share in excess of [0-5]*%. French retailers also confirmed in the market investigation that their mix of suppliers of coffee products has been relatively stable over the past three years.²⁸⁵
- (364) With respect to branded consumer goods the position and competitive importance of a given player depends on whether it is able to target the differentiated consumers, providing a full portfolio of brands, including those catering for price-driven (value) customers as well as less (premium) cost-conscious customers. In the French market the distinction between the value range and the more premium range is also reflected in a distinction between, respectively, Robusta and Arabica. Both Mondelēz and DEMB have indeed in their offering brands positioned as value or mid-range Robustas (Ma Tradition for DEMB and Grand'Mere for Mondelēz) and as premium Arabicas (L'Or for DEMB and Carte Noire for Mondelēz). As regards private label brands, since their market share in volume exceeds by [5-10]*% their market share in value, it could be concluded that they are particularly focused on customers purchasing the mid-range R&G coffee products. Lavazza and Segafredo, the next strongest suppliers of branded R&G coffee products after the Parties appear to address a specific niche in the market, namely high-premium Italian coffee.
- (365) As a result the Parties appear as the two strongest players in the French R&G market, with the high market shares and full portfolio of brands cutting across various price points and catering to the needs of different consumers. The fact that the positions of the Parties remained almost unchanged in the course of the past three years implies that the French R&G market is rather stable and mature and none of the competing suppliers of R&G coffee products (either branded or private label) was able to challenge the positions of the Parties and take their market share. Post-Transaction it is even less likely that the strong combined position of the JV will be successfully challenged.

9.5.1.2. Parties are close competitors

- (366) The Parties do admit that DEMB's L'Or brand and Mondelēz's Carte Noire brand could be viewed as closely competing within R&G coffee products. Also the market

²⁸⁵ Responses to question 207.2 of Questionnaire Q2-Retailers.

investigation and the analysis of the Parties' internal documents confirm that the Parties are each other's close competitors in the French R&G market.

- (367) As regards internal documents a study entitled "Coffee consumption in France" prepared for DEMB, [...]*.²⁸⁶ Another internal document of DEMB, [...]*.²⁸⁷ 288 289 Review of DEMB's internal documents corroborates the conclusion that in the French R&G market Parties' brands are closet competitors.
- (368) Similarly, internal documents of Mondelēz [...]*.²⁹⁰ 291 292 293 Consequently analysis of internal documents of Mondelēz confirms that in France the R&G brands of the Parties are close competitors.
- (369) Retailers in France view in particular the brands L'Or and Carte Noire as competing vigorously with each other.²⁹⁴ They also consider Mondelēz as closest competitor to DEMB and *vice versa* in France in coffee products in general and with respect to R&G in particular.²⁹⁵ Moreover, the majority of competitors active in France perceive Carte Noire as closest competitor to L'Or and vice versa.²⁹⁶
- (370) In the differentiated R&G market in France, the products of the Parties appear to be close substitutes. Indeed, that is not contested by the Parties themselves. As a result the loss of competition between the brands of DEMB and Mondelēz could potentially lead to higher prices for the French customers for the R&G products.

9.5.1.3. Insufficient constraint exercised by other players in the market, including private label brands

- (371) As noted in Recital (354), the Parties argue that competitors, in particular private label products as well as other suppliers of branded coffee products, exercise competitive constraint on DEMB and Mondelēz in France and will continue to do so after the Transaction. Therefore, it would follow from this that private label, Lavazza, Segafredo or Legal could increase supplies of R&G products in France in reaction to a price increase after the Transaction and the final customers could switch to those competing R&G products therefore making the price increase unprofitable for the JV.
- (372) Nevertheless, as set out in Section 9.1.2, the Commission's investigation has shown that one of the features of the coffee sector is the importance of brands. That is apparent from the Parties' internal documents, [...]*.²⁹⁷ Also the retailers in France confirm that market characteristic. One of the retailers stated that a supplier with a stronger brand is granted more shelf space and cited Carte Noire as an example.²⁹⁸

²⁸⁶ DEMB internal document, undated, "*Coffee consumption in France*", slide 14.

²⁸⁷ DEMB internal document, dated 7 November 2013, "*France short term rebound*", slides. 26, 31, 33, 45, 52 and 54.

²⁸⁸ *Ibidem*, slide 84.

²⁸⁹ DEMB internal document, undated, "*Introduction to French multiserve business*", slides 30 and 31.

²⁹⁰ Mondelēz internal document "*CCE ordinaire 12 decembre 2013 Categorie Boissons Chaudes*", slide 6.

²⁹¹ Mondelēz internal document, undated, "*S&I Budget Agreement AP 09-26 of August*", slides 27 and 28.

²⁹² Mondelēz internal document, undated, "*R&G French market overview*", slides 6 and 14.

²⁹³ *Ibidem*, slides 40-44.

²⁹⁴ Non-confidential minutes of a conference call with a retailer, dated 23 September 2014 at 11.00 CET and with retailer dated 19 September 2014 at 10.00 CET.

²⁹⁵ Responses to questions 209, 210 of Questionnaire Q2-Retailers.

²⁹⁶ Responses to questions 139, 140 of Questionnaire Q1 – Competitors.

²⁹⁷ Mondelēz internal document, dated 17 March 2008, "*EU Coffee Category Preliminary 2009 Strategic Plan*", slide 64.

²⁹⁸ Response to question 46.1 of Questionnaire Q2-Retailers.

Retailers also mention Parties' brands as must-have brands for R&G coffee.²⁹⁹ French retailers in the course of market investigation confirmed that having brands with high awareness (such as L'Or and Carte Noire) is one of the competitive advantages of both Parties.³⁰⁰ Since the final customers in the R&G market in France are attached to brands, that constitutes a barrier to their switching. At the same time the Parties own must-have brands, which are requested by the customers. Therefore other suppliers of branded R&G products would not necessarily be able to constrain the Parties by successfully attracting customers in reaction to a price increase by the JV after the Transaction.

- (373) As regards private label products, the Parties do acknowledge their presence in their internal documents [...]*.³⁰¹ In a study prepared for Mondelēz, [...]*.³⁰² The same document measured "attraction rate" of Grand'Mere as [...]*% and "loyalty rate" as [...]*%, while for private label products those rates amount to [...]*% and [...]*% respectively. Furthermore a French retailer admitted that due to the private label brands' limited presence in the coffee category (amounting to 20% at most) they are not real and strong challengers to the branded products.³⁰³ French retailers also note that the share of private label brands in the coffee products has been decreasing over the past years.³⁰⁴ These pieces of evidence suggest that while private label brands do have some presence in the French R&G market, it is not able to truly challenge the position of the Parties. In fact they are rather more likely to follow any price increase endorsed by the Parties.

9.5.1.4. Lack of countervailing buyer power

- (374) Another countervailing factor raised by the Parties is the buyer power of retailers. However the power of retailers *vis-à-vis* suppliers with 'must-have' brands (and Parties' brands in R&G in France are clearly must-have) is obviously limited. The more a given brand is requested by the final customers, the more difficult it will be for the retailers to demonstrate their buyer power by threatening or actually switching to alternative suppliers. [...]*³⁰⁵ Also French retailers admit that it would be difficult to find alternatives to Mondelēz brands (in particular to Carte Noire) in case they would no longer be able to stock them.³⁰⁶ As regards DEMB's brands one of the retailers stated it would be able to replace them with those of Mondelēz.³⁰⁷ That implies that in the eyes of French retailers Mondelēz, at least, has 'must-have' brands and DEMB is perceived as its key challenger. As a result the ability (due to the must-have character of the JV's brands and limited number of credible alternatives) and incentives of retailers to switch to alternative suppliers after the Transaction are both questionable.

²⁹⁹ Responses to question 211 of Questionnaire Q2-Retailers and non-confidential minutes of a conference call with a retailer, dated 23 September 2014 at 11.00 CET.

³⁰⁰ Responses to questions 49.1.1, 149.2.1 of Questionnaire Q2 – Retailers.

³⁰¹ DEMB internal document "*R&G market review by country*", slide 32; and "*Plan per country*", slide 36.
³⁰² Mondelēz internal document, "*Brand Health Tracking - All Coffee 2012 Review France, January - December 2012*", slide 97.

³⁰³ Response to question 213.1 of Questionnaire Q2 – Retailers.

³⁰⁴ Responses to question 215 of Questionnaire Q2 – Retailers.

³⁰⁵ Mondelēz internal document, dated 14 October 1, Aix-en-Provence, slides 22, 33, 35.

³⁰⁶ Responses to question 58 of Questionnaire Q2 – Retailers.

³⁰⁷ Response to question 57.1 of Questionnaire Q2 – Retailers.

(375) With regard to the various negotiation levers the Parties submit the French retailers are applying in their negotiations with coffee suppliers, they are in fact factored into the Parties' strategies. [...] ³⁰⁸ [...] ^{*}.

9.5.1.5. Barriers to entry

(376) Finally, as regards the Parties' claim of an absence of barriers to entry, such absence was not in fact confirmed by the Commission's investigation. ³⁰⁹ Whilst neither competitors nor retailers mentioned access to coffee beans, roasting or packaging capacity as potential entry barriers into the overall coffee market and in particular into R&G market, strong brand image and high financial resources were identified as necessary requirements for a successful entry into R&G in particular by one of the competitors. ³¹⁰ Similarly a French retailer stated that high brand awareness is needed for a successful entrant, while communication and promotion efforts are required from a supplier wishing to expand in the R&G market. ³¹¹ All French retailers confirmed that lacking brand image is the principal obstacle for a supplier of coffee products to get access to their shelves. ³¹² In addition, none of the competitors in France or of the French retailers was able to identify any potential entrant into the R&G market in France. The [...] ^x of those barriers to entry and expansion confirmed by the results of the Commission's market investigation implies that the Parties' strong market position after the Transaction would not be countervailed by potential entry or expansion of rivals.

9.5.1.6. Conclusion on R&G in France

(377) The Commission concludes that the proposed Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the French R&G market.

9.5.2. Denmark

(378) The sales of R&G in Denmark in 2013 amounted to approximately EUR 194 million and represented [70-80]*% of the total value of the coffee market in the country. DEMB supplies the Danish market with R&G coffee products mainly under the Merrild and Café Noir brands, while Mondelēz is present with its Gevalia, Karat and Ali Kaffe brands.

Parties' arguments

(379) The Parties maintain that the Danish R&G market is highly competitive and dynamic and therefore any attempt to raise prices after the Transaction would lead to substantial volume losses making the price increase unprofitable. The Parties view retailers' brands as their strongest competitors in Denmark, followed by the largest Danish coffee manufacturer – BKI and the Swedish supplier Peter Larsen.

(380) The Parties claim that private label products are particularly successful in Denmark. They also note that retailers in Denmark use the same raw materials as DEMB or Mondelēz to produce their coffee products. The Parties further claim that private

³⁰⁸ For instance DEMB internal document, dated 19 May 2014, "*Tariff increase DEMB France*"; pp. 11, 21.

³⁰⁹ Responses to question 234 of Questionnaire Q2 – Retailers and to question 144 of Questionnaire Q1 – Competitors.

³¹⁰ Response to question 146 of Questionnaire Q1- Competitors.

³¹¹ Responses to question 235 of Questionnaire Q2 – Retailers.

³¹² Responses to question 236 of Questionnaire Q2 – Retailers.

^x Should read: existence.

label products are given a better position on the shelves by retailers and use packaging which closely resembles packages of branded coffee products. As a result, private label products exercise a strong constraint on Parties' products.

- (381) The Parties further argue that Danish consumers are highly price sensitive and have low brand loyalty.
- (382) Another argument raised by the Parties with respect to the Danish R&G market is that there are low barriers to entry, because access to raw materials is easy and the presence of spare capacity for roasting coffee in Denmark could give the opportunity to outsource roasting activities at competitive prices to any new entrant. The Parties cite Starbucks and another coffee shop chain, Baresso, as having recently started partnership and cooperation agreements with Danish retailers and claim that both companies could be potential entrants into the Danish R&G market.
- (383) Lastly the Parties state that retailers' buyer power imposes a substantial constraint on them and will continue to do so after the Transaction.

Commission's investigation and assessment

- (384) Table 4 and the analysis below are based on the premise that in Denmark private label brands compete with branded R&G coffee products.

Table 4 R&G market in Denmark³¹³

Manufacturer	Brand	2013		2014	
		Value ('000 €)	Share	Value ('000 €)	Share
DEMB	MERRILD	[...]*	[20-30]**%	[...]*	[20-30]**%
	CAFE NOIR	[...]*	[5-10]**%	[...]*	[5-10]**%
	OTHER			[...]*	[0-5]**%
DEMB TOTAL	-	[...]*	[30-40]**%	[...]*	[30-40]**%
MONDELEZ	KARAT	[...]*	[5-10]**%	[...]*	[5-10]**%
	GEVALIA	[...]*	[5-10]**%	[...]*	[10-20]**%
	ALI	[...]*	[0-5]**%	[...]*	[0-5]**%
MONDELEZ TOTAL	-	[...]*	[10-20]**%	[...]*	[20-30]**%
COMBINED	-	[...]*	[50-60]**%	[...]*	[50-60]**%
RETAILERS	PRIVATE LABEL	[...]*	[20-30]**%	[...]*	[10-20]**%
BKI TOTAL	VARIOUS BRANDS	[...]*	[10-20]**%	[...]*	[10-20]**%

³¹³ If coffee beans are included the combined market share of the Parties drops to [40-50]**% in 2014.

Manufacturer	Brand	2013		2014	
		Value ('000 €)	Share	Value ('000 €)	Share
PETER LARSEN TOTAL	VARIOUS BRANDS	[...]*	[5-10]*%	[...]*	[5-10]*%
EMDRUPLUND	EMDRUPLUND	[...]*	[0-5]*%	[...]*	[0-5]*%
OTHER	OTHER	[...]*	[0-5]*%	[...]*	[0-5]*%
TOTAL	-	[...]*	100%	[...]*	100%

Source: the Parties

9.5.2.1. Parties have high market shares and the constraint exercised by other players and operators of private label brands is limited

(385) The Parties maintain that the Danish R&G market is highly competitive and dynamic and therefore any attempt to raise prices after the Transaction would lead to substantial volume losses making the price increase unprofitable. The Parties view retailers' brands as their strongest competitors in Denmark, followed by the largest Danish coffee manufacturer – BKI and the Swedish supplier Peter Larsen.

(386) The R&G market in Denmark has been declining in its value constantly since 2011. The shares of the Parties have increased between 2013 and 2014, while the share of private label brands has declined sharply in the same period. While the positions of BKI and Peter Larsen have strengthened slightly, both of those players are still much smaller than any of the Parties individually and significantly smaller than the JV.

(387) Therefore it is apparent that the Parties are the main two market players in R&G in Denmark and have increased their market shares in the last years. Other competitors are the regional players, with the main contender being operators of private label products, which, on top of having declined sharply in the last year, as discussed previously, are fragmented in nature and pose a lower competitive constraint as compared to branded coffee products.

(388) Moreover, as regards private label brands, the retailers clearly indicated that they expect an increase in the market share of such brands in the coming years while competitors were a bit more cautious on the future growth of private label brands.³¹⁴ Furthermore hard discounters are not considered to pose any competitive constraint on branded coffee products sold via traditional retail channels.³¹⁵ Therefore the constraint posed by private label branding does not seem to be as strong as the Parties submit.

9.5.2.2. Parties are close competitors

(389) When looking at closeness of competition between the Parties, DEMB's internal document states that [...]*³¹⁶ ³¹⁷.

³¹⁴ Responses to questions 115 et seq. Of Questionnaire Q1-Competitors and responses to questions 141 et seq of Questionnaire Q2-Retailers.

³¹⁵ Responses to questions 163 et seq of Questionnaire Q2-Retailers.

³¹⁶ [...]*.

- (390) When looking at average prices per kilo³¹⁸ the competitive landscape is the following:
- (1) Peter Larsen has a value brand sold at an average price of 7.37 EUR/kg;
 - (2) Merrild Special Regular has a weighted average price of [below 10]* EUR/kg, while Mondelēz's Karat has a weighted average price of [below 10]* EUR/kg; BKI main brand is sold at an average of [below 10]* EUR/kg;
 - (3) Merrild Roed Regular has a weighted average price of 9.49 EUR/kg, and Gevalia Roed Regular has a weighted average price of 9.95 EUR/kg;
 - (4) The main Peter Larsen brands are sold at an average of 10.48 EUR/kg;
 - (5) At the high end of the market BKI premium brand is sold at an average of 13.14 EUR/kg and DEMB's Café Noir brand has a weighted average price of 12.48 EUR/kg
- (391) In view of the price positioning and some indication from the market investigation, the Commission considers that DEMB and Mondelēz are close competitors for the bulk for their R&G activities in Denmark.

9.5.2.3. Barriers to entry

- (392) Another argument put forward by the Parties with respect to the Danish R&G market is that there are low barriers to entry, because access to raw materials is easy and the presence of spare capacity for roasting coffee in Denmark could give the opportunity to outsource roasting activities at competitive prices to any new entrant. The Parties cite Starbucks and another coffee shop chain, Baresso, as having recently started partnership and cooperation agreements with Danish retailers and claim that both companies could be potential entrants into the Danish R&G market.
- (393) With regards to the argument of potential entry in the Danish market, the respondent to the market investigation did not mention any company that could be considered – in their view – as a potential entrant.³¹⁹
- (394) Elaborating further on the possible entry, the respondent to the market investigation highlighted the importance of having a well-known brand and sufficient financial resources as a key success factor and the minimum sales volume to be attained by the new entrant as a main barrier to entry.³²⁰
- (395) Given the relative size of the Danish market and the declining trend of the R&G market highlighted by the Parties' data and the respondent to the market investigation³²¹, even if an entry were to happen in the near future, it seems unlikely that such new entrant would reach a market penetration sufficient to be a competitive constraint on the Parties.

³¹⁷ Responses to questions 113 and 114 of Questionnaire Q1-Competitors and responses to questions 138 and 139 of Questionnaire Q2-Retailers.

³¹⁸ These prices were provided by the Parties in the Form CO paragraphs 760 to 766.

³¹⁹ Responses to question 119 of Questionnaire Q1-Competitors and responses to question 164 of Questionnaire Q2-Retailers.

³²⁰ Responses to questions 120 and 121 of Questionnaire Q1-Competitors and responses to questions 165 and 166 of Questionnaire Q2-Retailers.

³²¹ Annex 7-4aa of Form CO, submission of 10 March 2015 and Responses to question 122 of Questionnaire Q1-Competitors and responses to question 167 of Questionnaire Q2-Retailers.

9.5.2.4. Lack of countervailing buyer power

- (396) The Parties state that retailers' buyer power imposes a substantial constraint on them and will continue to do so after the Transaction, in particular since [70-80]*% of downstream coffee sales is controlled by two retail groups – Dansk Supermarked and Fællesforeningen for Danmarks group. Furthermore the Danish R&G market is highly promotion driven and therefore obtaining access to promotion slots³²² is of crucial importance for coffee suppliers. The Parties argue that any attempt to increase prices or reduce promotional support after the Transaction would be met with retailers' reactioning and cancelling of JV promotion slots. Finally the Parties claim that retailers would also be ready to support growth of a competitor to the disadvantage of the JV as they had already done so in other categories.
- (397) With regards to the Parties' argument on the retailers' buyer power, the Commission notes that the JV will have more than half of the market and the respondents to the market investigation indicated that both Parties have 'must-have' brands³²³. Therefore the Commission considers that both the size of the JV and the 'must-have' brands it possesses, constitutes a counter-weight to the bargaining power of the retailers *vis-à-vis* the JV.
- (398) With regards to the importance of promotions, the respondents to the market investigation confirmed the importance of promotions for coffee sales in Denmark, especially for R&G, for which approximately 85% of the volumes are sold on promotion.³²⁴ Those results confirm the importance of promotions in order to be a successful player in Denmark in the coffee market in general and especially in the R&G market. Furthermore, in case of overall price increases, promotion prices could also go up. Moreover, any price increase is likely to be passed on to consumers.³²⁵

9.5.2.5. Conclusion

- (399) The Commission therefore concludes that the proposed Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the Danish R&G market.

9.5.3. Latvia

- (400) The sale of R&G in Latvia in 2014 reached an amount of approximately EUR 31 million and represented [50-60]*% of the total value of the coffee market in the country.³²⁶ DEMB supplies the Latvian market with R&G coffee products exclusively under the Merrild brand³²⁷, while Mondelēz is present almost exclusively with its Jacobs brand.

Parties' arguments

- (401) The Parties maintain that the Latvian R&G market is highly competitive and dynamic and therefore any attempt to raise prices after the Transaction would lead to

³²² Promotion slots are the dedicated areas in retail outlets where consumer goods on promotion are displayed, advertised etc.

³²³ Responses to question 140 of Questionnaire Q2-Retailers.

³²⁴ Responses to questions 147 and 148 of Questionnaire Q2-Retailers.

³²⁵ Responses to question 12 of Questionnaire Q2 – Retailers.

³²⁶ Calculation made on the base of the Parties submission of 10 March 2015 and following the Parties' assumption in the Form CO (i.e. paragraph 567 et seq and 603) that the only coffee products sold in Latvia are R&G including whole beans and instant coffee.

³²⁷ With the exception of a very limited amount of whole beans sold under other brands, i.e. Douwe Egberts.

substantial volume losses making the price increase unprofitable. As evidence of the dynamic nature of the market, the Parties point to the volatility of market shares in the past years and also during the same calendar year.

- (402) According to the Parties, their R&G products are also not each other's closest competitors because Mondelez benchmarks its prices against [...]*, while DEMB benchmarks against [...]*.
- (403) Furthermore, the Parties submit that competition in the wholesale supply of coffee takes place across all three Baltic States given that the same large retailers are present in all these countries and the same competitors are also active across all the Baltics.
- (404) The Parties argue that Rimi and Maxima, the main Baltic retailers, have significant buyer power.
- (405) Finally the Parties claim that there are no significant barriers to entry or expansion in R&G in the Baltics in general; furthermore the Parties claim that manufacturers already present in the Baltics could expand in response to any attempt to increase prices by the Parties, facilitated by the price sensitive nature of consumers.

Commission's investigation and assessment

- (406) The table and the analysis below are based on the premise that in Latvia private label brands compete with branded R&G coffee products.

Table 5 R&G market in Latvia³²⁸

Manufacturer	Brand	2013		2014	
		Value ('000 €)	Share	Value ('000 €)	Share
DEMB TOTAL	MERRILD	[...]*	[20-30]*%	[...]*	[20-30]*%
MONDELĒZ	JACOBS	[...]*	[20-30]*%	[...]*	[...]*%
	OTHER	[...]*	[0-5]*%	[0-5]*	[0-5]*%
MONDELĒZ TOTAL	-	[...]*	[20-30]*%	[...]*	[20-30]*%
COMBINED	-	[...]*	[40-50]*%	[...]*	[40-50]*%
PAULIG TOTAL	VARIOUS BRANDS	[...]*	[10-20]*%	[...]*	[10-20]*%
TCHIBO TOTAL	VARIOUS BRANDS	[...]*	[10-20]*%	[...]*	[10-20]*%
DALLMAYR	DALLMAYR	[...]*	[5-10]*%	[...]*	[5-10]*%
LOFBERGS LILA TOTAL	VARIOUS BRANDS	[...]*	[5-10]*%	[...]*	[5-10]*%
LAVAZZA	LAVAZZA	[...]*	[5-10]*%	[...]*	[5-10]*%

³²⁸ There would be no material change in the market shares, if coffee beans were included.

Manufacturer	Brand	2013		2014	
		Value ('000 €)	Share	Value ('000 €)	Share
DAISENA TOTAL	VARIOUS BRANDS	[...]*	[0-5]**%	[...]*	[0-5]**%
RETAILERS	RETAILER BRANDS	[...]*	[0-5]**%	Incl. In "OTHER"	Incl. In "OTHER"
JULIUS MEINL	JULIUS MEINL	[...]*	[0-5]**%	Incl. In "OTHER"	Incl. In "OTHER"
EESTI PAKEND IP TOTAL	VARIOUS BRANDS	[...]*	[0-5]**%	Incl. In "OTHER"	Incl. In "OTHER"
ALVORADA	ALVORADA	[...]*	[...]**%	Incl. In "OTHER"	Incl. In "OTHER"
OTHER	OTHER	[...]*	[0-5]**%	[...]*	[5-10]**%
TOTAL	-	[...]*	100%	[...]*	100%

Source: the Parties

9.5.3.1. Parties have high market shares

- (407) The R&G market in Latvia has been declining in its value constantly since 2011. Despite the decline in its market share, DEMB is still the main market participant by value, closely followed by Mondelēz. The main competitor is Paulig with a market share similar to that of Mondelēz.
- (408) The sharp decline in Tchibo's share and the relatively small and fragmented market share of the other competitors present in the Latvian R&G market indicate that the JV will be the main player in the Latvian market with very limited competitive constraints posed by the other incumbents.
- (409) The overall value of the Latvian R&G market decreased between 2013 and 2014 and in particular Mondelēz's share dropped by [0-5]*. However the positions of the remaining players remained rather stable and both Parties remain the two main suppliers of R&G products in Latvia.

9.5.3.2. Parties are close competitors

- (410) According to the Parties, their R&G products are also not each other's closest competitors. They observe that Mondelēz benchmarks its prices against [...]*, while DEMB benchmarks against [...]*.
- (411) As regards the closeness of competition, the respondents to the market investigation gave indications that Jacobs and Merrild are close competitors.³²⁹ Further interviews with market participants did not give clearer indications with one competitor highlighting how Jacobs is positioned as a premium brand and at a higher price point

³²⁹ Responses to questions 199 and 200 of Questionnaire Q1-Competitors and responses to questions 351 and 352 of Questionnaire Q2-Retailers.

than Merrild³³⁰ and another competitor stating that both Merrild and Jacobs are mainstream brands.³³¹

- (412) Given the high market share obtained by Jacobs, the Commission considers that it cannot be positioned as a premium brand, which, by definition, would appeal to a minority of the market. Therefore, it can be inferred that at least the bulk of both Merrild's and Jacobs' target customers are the mainstream consumers and hence the Parties are close competitors.
- (413) The majority of respondents to the market investigation indicated that private label brands are not close competitors of branded coffee products in Latvia.³³² The Commission therefore considers that private label brands are not exercising a competitive constraint on branded R&G in Latvia.

9.5.3.3. Insufficient constraint exercised by players from other Baltic states

- (414) Furthermore, the Parties submit that competition in the wholesale supply of coffee takes place across all three Baltic States given that the same large retailers are present in all of the three countries and the same coffee suppliers are also active across all the Baltics. Furthermore the Parties claim that they supply the same coffee products in the same packaging in all three countries and therefore there is scope for transshipment of coffee products between Estonia, Latvia and Lithuania.
- (415) As regards the arguments of "pan-Baltics" competition, one retailer stated that there are separate contracts for Latvia for the supply of coffee products.³³³ Furthermore follow-up interviews with market participants gave a clear indication that Estonia, Latvia and Lithuania are considered by coffee companies as separate markets, having each a different leading incumbent, different coffee cultures and different consumer preferences.³³⁴

9.5.3.4. Lack of countervailing buyer power

- (416) The Parties argue that Rimi and Maxima, the main retailers in Latvia have significant buyer power, since they account for [60-70]*% of retail coffee sales in Latvia. They further state that coffee is a key traffic driver for retailers which take a proactive role in seeking to offer the lowest prices and use strong negotiations levers (such as delisting, freezing or reducing promotions, unilaterally imposing promotions) towards that end.
- (417) With regards to the buyer power exercised by retailers, the Commission's investigations confirmed the presence of a strong buyer power concentrated in the hands of the main retailers.³³⁵ The Commission considers nonetheless that the JV will be having important brands accountable for considerable volumes which will serve as a counter-weight to the buying power of the retailers.³³⁶

³³⁰ Non-confidential minutes of a conference call with a competitor of 18 November 2014 at 10.45 CET.

³³¹ Non-confidential minutes of a conference call with a competitor of 18 November 2014 at 17.00 CET.

³³² Responses to question 201 of Questionnaire Q1-Competitors and responses to question 335 of Questionnaire Q2-Retailers.

³³³ Responses to question 376 of Questionnaire Q2-Retailers.

³³⁴ Non-confidential minutes of a conference call with a competitor of 18 November 2014 at 10.45 CET and at 17.00 CET.

³³⁵ Non-confidential minutes of a conference call with a competitor of 18 November 2014 at 10.45 CET and at 17.00 CET.

³³⁶ For instance the Merrild brand has a very strong historic heritage in Latvia, where it was the first foreign coffee brand and still in 2014 accounts for one quarter of all the R&G sales in the country.

9.5.3.5. Barriers to entry

- (418) Finally the Parties claim that there are no significant barriers to entry or expansion in R&G in the Baltics in general. Furthermore, the Parties claim that manufacturers already present in the Baltics could expand in response to any attempt to increase prices by the Parties, facilitated by the price sensitive nature of consumers.
- (419) When looking for trends in the Latvian R&G market, the Parties' data show a decline in the years 2011 to 2014 but the responses to the market investigation are mixed indicating, according to the respondents, a stabilisation, an increase and a decline of the R&G sales.³³⁷
- (420) With regards to potential new entrants in the Latvian R&G market, the respondents to the market investigation did not mention any company that could be considered, in their view, as a potential entrant.³³⁸

³³⁷ Responses to question 208 of Questionnaire Q1-Competitors and responses to question 380 of Questionnaire Q2-Retailers.

³³⁸ Responses to question 205 of Questionnaire Q1-Competitors and responses to question 377 of Questionnaire Q2-Retailers.

- (421) Further interviews with market participants highlighted that a regional coffee company active in instant coffee in Latvia was planning to enter the R&G Latvian market from January 2015.³³⁹ The Commission considers that such entry, even if successful, is unlikely to reach a scale which could pose a competitive constraint to the JV.
- (422) Elaborating further on the possible entry, the respondent to the market investigation highlighted the importance of having a well-known brand and sufficient financial resources to support the promotional activities as a key success factor and the minimum sales volume to be attained by the new entrant as an additional barrier to entry.³⁴⁰

9.5.3.6. Conclusion

- (423) The Commission concludes that the proposed Transaction would lead to a significant impediment of effective competition, in particular through the creation of a dominant position, in the Latvian R&G market.

9.5.4. *The Czech Republic*

Parties' arguments

- (424) The Parties argue that the Transaction would not lead to anti-competitive effects due to their low combined market share in the R&G market in the Czech Republic. They also state their activities will be constrained by other players in particular Tchibo. Furthermore the Parties claim that their pricing strategies do not indicate any closeness of competition between their brands in the Czech Republic and present extracts from internal documents which show that [...]*

Commission's investigation and assessment

- (425) Table 6 shows the Parties' and their competitors' market shares by value in 2014 within the R&G segment in the Czech Republic including private label brands.³⁴¹

³³⁹ Non-confidential minutes of a conference call with a competitor of 18 November 2014 at 10.45 CET.

³⁴⁰ Responses to questions 206 and 207 of Questionnaire Q1-Competitors and responses to questions 378 and 379 of Questionnaire Q2-Retailers.

³⁴¹ The Parties' combined market share excluding PL would be slightly higher, namely [30-40]*%.

Table 6 R&G market in the Czech Republic³⁴²

Manufacturer	Brand	2014	
		Value ('000 €)	Share
DEMB	DOUWE EGBERTS	[...]*	[10-20]**%
	OTHERS	[...]*	[0-5]**%
DEMB TOTAL		[...]*	[10-20]**%
MONDELĚZ	JACOBS	[...]*	[10-20]**%
	DADAK	[...]*	[5-10]**%
	OTHERS	[...]*	[0-5]**%
MONDELĚZ TOTAL		[...]*	[20-30]**%
COMBINED		[...]*	[30-40]**%
TCHIBO	JHLAVANKA	[...]*	[30-40]**%
	TCHIBO	[...]*	[10-20]**%
	OTHERS	[...]*	[0-5]**%
TCHIBO TOTAL		[...]*	[40-50]**%
RETAILERS	PRIVATE LABEL	[...]*	[5-10]**%
MOKATE	MARILA	[...]*	[5-10]**%
	OTHERS	[...]*	[0-5]**%
MOKATE TOTAL		[...]*	[5-10]**%
LAVAZZA	LAVAZZA	[...]*	[0-5]**%
SEGAFREDO ZANETTI	SEGAFREDO ZANETTI	[...]*	[0-5]**%
OTHERS	OTHERS	[...]*	[0-5]**%
TOTAL		[...]*	100%

Source: Parties

³⁴²

There would be no material change in the market shares, if coffee beans were included.

- (426) The joint venture would be second on the market with a combined market share of [30-40]*% in 2014. Tchibo would remain the market leader post-Transaction with a market share of approximately [40-50]*%. In addition, a number of other competitors are present in the Czech Republic with smaller market shares, including Mokate ([5-10]*%), Lavazza ([0-5]*%) and Segafredo ([0-5]*%).
- (427) The market investigation confirmed that the rivals' products are close substitutes to the products of the merging parties. Tchibo, the market leader, is closer to Mondelēz than DEMB is.³⁴³ Respondents to the market investigation also did not raise any concerns related to the R&G segment in the Czech Republic.
- (428) DEMB has an arrangement with [...] for the manufacture of instant coffee to sell under [...] own brand. Mondelēz does not supply any retailer with coffee for resale under retailer brands in the Czech Republic. There is therefore no overlap between the Parties' activities in supply of coffee to retailers to re-sell under their own brands. However, due to DEMB' supply arrangement with [...], the market for the upstream coffee supply to retailers and the downstream market for the retail supply of branded coffee products are a vertically affected market.
- (429) The combined entity would not have the ability to foreclose Coop from supplies of coffee since it would lack any significant market power in the upstream supply of retail branded coffee. DEMB estimates that its share of retailer coffee supplies in the Czech Republic are approximately [10-20]*% by volume. There are many manufacturers in the upstream segment likely to supply in the Czech Republic who would be able to supply instant coffee under the same terms. Moreover, the combined entity would have no incentive to foreclose Coop, since it would be sacrificing revenues in the upstream supply without any reasonable prospect of increasing margins on its own branded products or to increase consumer prices of coffee on the retail market for the sale of coffee to final customers.

Conclusion

- (430) The Commission concludes that the proposed Transaction does not give rise to a significant impediment to effective competition in the R&G market in the Czech Republic.

9.5.5. Greece

Parties' arguments

- (431) The Parties submit that the Transaction does not give rise to any competition concerns in Greece. The Parties further submit that “Greek” coffee imposes a constraint on normal R&G and that the Parties are not each other’s closest competitors.
- (432) With respect to normal R&G, the Parties argue that DEMB positions its main brand Douwe Egberts as a premium coffee while Mondelēz’ main brand Jacobs is a value-for-money product. The difference between those brands would also be seen in the fact that Douwe Egberts is seldom sold at a discount while Jacobs often is, and that the average unit price (taking into account promotions) of Douwe Egberts is significantly higher than that for Jacobs. The Parties provided data according to which between September 2011 and September 2013, Douwe Egbert’s unit price remained above [10-20]* EUR/kg with the sole exception of November 2012 when the average price was [10-20]* EUR/kg. During the same period, Jacobs’ prices

³⁴³ Responses to questions 100 and 101 of the questionnaire Q1 – Competitors.

remained below [10-20]* EUR/kg, with the sole exception of March 2012 when the price was [10-20]* EUR/kg.

- (433) In the potential sub-segment of “Greek” coffee, there would not be any overlap as Mondelēz is not present in the market. DEMB achieved a market share of [5-10]*% in 2014 in value while the clear market leader was Nestlé with a market share of [70-80]*%.

Commission's investigation and assessment

- (434) The Commission assessed the R&G market in Greece as a whole as well as the potential sub-segment of “normal” R&G. There is no overlap in the potential sub-segment of “Greek” coffee as Mondelēz is not active.

Table 7 R&G – without coffee beans in Greece, including private label and Greek coffee³⁴⁴

Manufacturer	Brand	2014	
		Value ('000 €)	Share
DEMB	Bravo	[...]*	[5-10]*%
	Douwe Egberts	[...]*	[0-5]*%
	La Meloise	[...]*	[0-5]*%
DEMB total		[...]*	[5-10]*%
Mondelēz	Jacobs	[...]*	[10-20]*%
	Others	[...]*	[0-5]*%
Mondelēz total		[...]*	[10-20]*%
COMBINED		[...]*	[20-30]*%
Nestlé	Loumidis Papagalos	[...]*	[40-50]*%
	Others	[...]*	[0-5]*%
Nestlé total		[...]*	[40-50]*%
Retailers	Private Label	[...]*	[10-20]*%
AO	AO	[...]*	[5-10]*%
Lavazza	Qualita Rossa	[...]*	[0-5]*%
	Others	[...]*	[0-5]*%
Lavazza total		[...]*	[0-5]*%
Illy	Illy	[...]*	[0-5]*%
Melitta	MelitaSL	[...]*	[0-5]*%
	Others	[...]*	[0-5]*%
Melitta total		[...]*	[0-5]*%
Others	Others	[...]*	[0-5]*%
TOTAL		[...]*	100%

Source: Parties

³⁴⁴ There would not be a material change if whole coffee beans were to be included; the Parties’ combined market share in 2014 would have been [20-30]*% if beans were included.

Table 8 R&G – without coffee beans in Greece including private label products, excluding Greek coffee

Manufacturer	Brand	2014	
		Value ('000 €)	Share
DEMB	Douwe Egberts	[...]*	[0-5]**%
	La Meloise	[...]*	[0-5]**%
	Other	[...]*	[0-5]**%
DEMB total		[...]*	[5-10]**%
Mondelēz	Jacobs	[...]*	[50-60]**%
	Carte Noire	[...]*	[0-5]**%
	Maxwell House	[...]*	[0-5]**%
Mondelēz total		[...]*	[50-60]**%
COMBINED		[...]*	[60-70]**%
Retailers	Retailer brands	[...]*	[10-20]**%
Lavazza	Qualita Rossa	[...]*	[0-5]**%
	Lavzqlor	[...]*	[0-5]**%
	Others	[...]*	[0-5]**%
Lavazza total		[...]*	[10-20]**%
Illy	Illy	[...]*	[5-10]**%
Melitta	MelitaSL	[...]*	[0-5]**%
	Others	[...]*	[0-5]**%
Melitta total		[...]*	[0-5]**%
Dallmayr	Prodomo	[...]*	[0-5]**%
	Others	[...]*	[0-5]**%
Dallmayr total		[...]*	[0-5]**%
Others	Others	[...]*	[0-5]**%
TOTAL		[...]*	100%

Source: Parties

- (435) In all R&G market consisting of both “normal” and “Greek” R&G coffee, the joint venture would become the second largest player, after the market leader Nestlé. Nestlé’s market share of [40-50]*% is significantly higher than the Parties’ combined market share of [20-30]*%. A number of other competitors will remain on the market, including various retailer brands ([10-20]*%) and AO ([5-10]*%). Greek coffee represents around [...] of the overall R&G market in Greece (approximately EUR [...] and [...] tonnes out of a total R&G market of EUR [...] and [...] tonnes in 2014)³⁴⁵, and it is therefore far more important in terms of volume and value to both coffee manufacturers and retailers.
- (436) In the potential sub-segment of “normal” R&G coffee (excluding “Greek” coffee), the Parties would achieve a high combined market share of [60-70]*% in value in 2014. The remaining main competitors would include the various retailer brands ([10-20]*%), Lavazza ([10-20]*%) and Illy ([5-10]*%).
- (437) A high market share in the potential sub-segment of “normal” R&G coffee is, however, unlikely to be indicative of the Parties’ actual market power in the market. Even if “Greek” coffee and “normal” R&G were considered to be in separate markets, due to the low demand-side substitutability, “Greek” coffee places an out of market competitive constraint on “normal” R&G in Greece. That conclusion is supported by the finding that there is significant supply-side substitutability between “Greek” and “normal” R&G coffee.³⁴⁶
- (438) The results of the market investigation appear to support the view that rivals products are close to the Parties' products and even closer than the parties' products are to each other. Multiple customers mention Nestlé and private label brands for being closer to each of the Parties than the Parties are to each other.³⁴⁷
- (439) A significant share of customers that responded also appears to consider that private label products are close competitors to branded R&G coffee in Greece.³⁴⁸ The majority of customers further considered that the share of private label products has been increasing in Greece, and that it would continue to increase.³⁴⁹ This is in line with the market share estimates provided by the Notifying Parties that show an increase in the market share of private label products from [5-10]*% in 2011 to [10-20]*% in 2014 for all R&G and from [5-10]*% in 2011 to [10-20]*% for the potential sub-segment of “normal” R&G in Greece. At the same time, the Parties’ combined market share in “normal” R&G dropped from [70-80]*% to the 2014 figure of [60-70]*%.

³⁴⁵ See the Parties reply to the Commission’s request for information of 13 March 2015.

³⁴⁶ See, e.g. responses to question 168 of Questionnaire Q1 – Competitors.

³⁴⁷ Responses to questions 283 and 284 of Questionnaire Q2 – Customers.

³⁴⁸ Responses to questions 287 and 288 of Questionnaire Q2 – Customers.

³⁴⁹ Responses to questions 289 and 290 of Questionnaire Q2 – Customers.

- (440) Customers replying to the market investigation did not consider that the proposed Transaction would give rise to increased prices or any other competition concerns with respect to any of the potential sub-segments of R&G coffee in Greece.³⁵⁰ To the contrary, some customers considered the Transaction to be generally positive, commenting for instance that the proposed Transaction “*is estimated to have a positive effect on competition and may balance to a certain degree Nestle’s leading position on the coffee market in Greece*”³⁵¹.

Conclusion

- (441) The Commission therefore concludes that the proposed Transaction does not give rise to a significant impediment to effective competition in the R&G market, or in any of its potential sub-segments, in Greece.

9.5.6. Poland

Parties' arguments

- (442) The Parties submit that the Transaction does not give rise to competition concerns with respect to the market for R&G coffee in Poland, which is highly competitive and dynamic. First of all the Parties maintain that they are not each other’s closest competitor, with their two main brands Jacobs Kroenung and Prima positioned differently. Furthermore the Parties meet strong competition from suppliers of branded products, such as Tchibo, Polish coffee supplier – Elite/MK Café and Mokate – as well as from private label brands. Finally [...]× Parties submit that their combined market shares have been decreasing from [30-40]*% in 2011 to [30-40]*% in 2014.

Commission's investigation and assessment

- (443) Polish R&G market has remained relatively stable over the past years. The positions of the Parties and their rivals are set out in Table 9.

³⁵⁰ See, e.g. responses to questions 312–314 of Questionnaire Q2 – Customers.

³⁵¹ Response to question 312 of Questionnaire Q2 – Customers.

× Should read: the.

Table 9 R&G market in Poland³⁵²

Manufacturer	Brand	2013		2014	
		Value('000 €)	Share	Value ('000 €)	Share
DEMB	PRIMA	[...]*	[10-20]*%	[...]*	[10-20]*%
	DOUWE EGBERTS	[...]*	[0-5]*%	[...]*	[0-5]*%
DEMB TOTAL	-	[...]*	[10-20]*%	[...]*	[10-20]*%
MONDELĒZ	JACOBS	[...]*	[10-20]*%	[...]*	[10-20]*%
	MAXWELL HOUSE	[...]*	[0-5]*%	[...]*	[0-5]*%
	CARTE NOIRE	[...]*	[0-5]*%	[...]*	[0-5]*%
MONDELĒZ TOTAL	-	[...]*	[20-30]*%	[...]*	[20-30]*%
COMBINED	-	[...]*	[30-40]*%	[...]*	[30-40]*%
TCHIBO	TCHIBO	[...]*	[20-30]*%	[...]*	[20-30]*%
	GALA	[...]*	[0-5]*%	[...]*	[0-5]*%
	OTHER	[...]*	[0-5]*%	[...]*	[0-5]*%
TCHIBO TOTAL	-	[...]*	[20-30]*%	[...]*	[20-30]*%
ELITE/MK CAFE	MK CAFE	[...]*	[10-20]*%	[...]*	[10-20]*%
	ELITE			[...]*	[5-10]*%
	FORT	[...]*	[0-5]*%	-	-
	PEDROS	[...]*	[0-5]*%		
	SAHARA	[...]*	[0-5]*%		
	OTHER	[...]*	[0-5]*%		
ELITE/MK CAFÉ TOTAL	-	[...]*	[10-20]*%	[...]*	[10-20]*%
WOSEBA ODOLANOW	WOSEBA	[...]*	[5-10]*%	[...]*	[5-10]*%
RETAILERS	PRIVATE LABEL	[...]*	[5-10]*%	[...]*	[5-10]*%
MOKATE	LAVAZZA	[...]*	[0-5]*%	[...]*	[0-5]*%
	OTHER	[...]*	[0-5]*%	[...]*	[0-5]*%
MOKATE TOTAL		[...]*	[0-5]*%	[...]*	[0-5]*%
DALLMAYR	DALLMAYR	[...]*	[0-5]*%		
ASTRA	ASTRA	[...]*	[0-5]*%	[...]*	[0-5]*%
SIDO & PARTNER	SIDO	[...]*	[0-5]*%		
OTHER	OTHER	[...]*	[0-5]*%	[...]*	[5-10]*%
TOTAL	-	[...]*	100%	[...]*	100%

Source: Parties

- (444) As is apparent from Table 9, the JV would become the market leader in the Polish R&G market with an estimated market share of [30-40]*%. However, two significant competitors, Tchibo ([20-30]*%) and Elite / MK Café ([10-20]*%) would remain on the market after the Transaction, together with private label products and a number of other branded products suppliers such as Woseba with [5-10]*% share or Mokate with more than [0-5]*%. A Polish retailer confirmed that the Polish R&G market is a difficult and competitive one.³⁵³
- (445) Polish retailers do not view the Parties as close competitors in R&G coffee. With respect to DEMB, Tchibo, Woseba and MK Café are indicated as close competitors, whereas for Mondelēz, Tchibo was also the primary competitor identified.³⁵⁴ One

³⁵² There would be no material change in the market shares, if coffee beans were included.

³⁵³ Non-confidential minutes of a conference call with a retailer dated 18 November 2014 at 16.00 CET.

³⁵⁴ Responses to questions 455, 456 of Questionnaire Q2- Retailers.

Polish retailer stated that the main brand of Mondelēz in Poland – Jacobs Kroenung is an A brand, while that of DEMB- Prima is a B brand.³⁵⁵

- (446) Internal documents of the Parties confirm that *[quotes from internal documents on brand positioning]** are positioned differently. The former is a [...]*.³⁵⁶ On the other hand [...]*.³⁵⁷

Conclusion

- (447) The Commission therefore concludes that the proposed Transaction does not give rise to a significant impediment to effective competition in the R&G market in Poland.

9.5.7. Other Member States with affected markets in R&G coffee

- (448) The Parties' activities give rise to horizontally affected markets for R&G coffee in a number of other Member States, including Bulgaria, Hungary, the Netherlands and Spain.
- (449) The Parties submit that the Transaction does not give rise to any competition concerns in the R&G coffee markets in any of the mentioned territories.

9.5.7.1. Market shares and market structure, R&G coffee

- (450) In Bulgaria, the Parties achieved a combined market share of [60-70]*% in 2014 (DEMB [0-5]*%, Mondelēz [60-70]*%). However, the market share increment is only [0-5]* due to DEMB's limited market presence. Other competitors include, for instance Lavazza ([10-20]*%) and Tchibo ([5-10]*%).
- (451) In Hungary, the Parties achieved a combined market share of [40-50]*% in 2014 (DEMB [30-40]*%, Mondelēz [0-5]*%). However, the market share increment is [0-5]* due to Mondelēz' limited market presence. Other competitors include, for instance Tchibo ([20-30]*%) and various retailer brands ([10-20]*%).
- (452) In the Netherlands, the Parties achieved a combined market share of [60-70]*% in 2014 (DEMB [60-70]*%, Mondelēz [0-5]*%). However, the market share increment is only [0-5]* due to Mondelēz' limited market presence. Other competitors include, for instance various retailer brands ([30-40]*%) and Lavazza ([0-5]*%).
- (453) In Spain, the Parties achieved a combined market share of [20-30]*% in 2014 (DEMB [10-20]*%, Mondelēz [5-10]*%). Other competitors include, for instance various retailer brands ([30-40]*%) and Nestlé ([10-20]*%).

Commission's investigation and assessment

- (454) The Commission notes that while the Parties achieve a significant combined market share in R&G coffee in Bulgaria, Hungary and the Netherlands, the market share increment in each of the markets in question is notably small. In light of that, and taking into account the number of remaining competitors, the Commission considers that merger-specific competition concerns can be excluded.
- (455) As to Spain, the Parties' combined market shares remain modest. In light of that, and taking into account the number of remaining competitors, the Commission considers that competition concerns can be excluded.

³⁵⁵ Non-confidential minutes of a conference call with a retailer dated 18 November 2014 at 10.00 CET.

³⁵⁶ DEMB internal document, dated January 2013, entitled "*Prima Jan 13*", slides 6 and 10.

³⁵⁷ Mondelēz internal document, undated, entitled "*Countries – PL*", slide 22.

9.5.7.2. Conclusion

(456) The Commission concludes that the proposed Transaction does not give rise to a significant impediment to effective competition in the markets for R&G coffee in Bulgaria, Hungary, the Netherlands or Spain.

9.6. Instant coffee

(457) For the reasons set out in Recitals (456) to (496), the Commission has reached the conclusion that the Transaction would not significantly impede effective competition in the markets for instant coffee in the Czech Republic, Denmark, Estonia, Greece, Hungary, Latvia, Lithuania, the Netherlands, Poland, Slovakia, Spain or the United Kingdom.

9.6.1. Latvia

(458) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Latvia.

(459) DEMB is active in the instant coffee market in Latvia with its brand Merrild, while Mondelēz serves the [...] instant coffee market with its brand Jacobs.

(460) The combined market share of the Parties in instant coffee in Latvia will amount to [20-30]*%. However the increment brought about by the Transaction is small ([0-5]*%) as DEMB's instant coffee sales in Latvia in 2014 amounted only to EUR [...]*. Other players active in the Latvian market are Nestlé ([20-30]*%), Daisena ([10-20]*%) and Unilever ([5-10]*%)

(461) No specific concerns were voiced by Latvian customers as regards the impact of the Transaction on the Latvian market for instant coffee.³⁵⁸

9.6.2. Lithuania

(462) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Lithuania.

(463) DEMB is active in the instant coffee market in Lithuania with its brand Merrild, while Mondelēz serves the Lithuanian instant coffee market with its brand Jacobs.

(464) The combined market share of the Parties in instant coffee in Lithuania will amount to [30-40]*%. However the increment brought about by the Transaction is small ([0-5]*%) as DEMB's instant coffee sales in Lithuania in 2014 amounted only to [...]*. Other players active in the Lithuanian market are Nestlé ([20-30]*%), Daisena ([10-20]*%) and Maspex Wadowice ([5-10]*%).

(465) No specific concerns were voiced by Lithuanian customers as regards the impact of the Transaction on the Lithuanian market for instant coffee.³⁵⁹

9.6.3. Estonia

(466) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Estonia.

³⁵⁸ Responses to questions 381, 382 and 383 of Questionnaire Q2-Retailers.

³⁵⁹ Responses to questions 416,417 and 418 of Questionnaire Q2-Retailers.

- (467) DEMB is active in the instant coffee market in Estonia with its brands Merrild and Douwe Egberts, while Mondelēz serves the Estonian instant coffee market with its brand Jacobs.
- (468) The combined market share of the Parties in instant coffee in Estonia will amount to [30-40]*%. However the increment brought about by the Transaction is negligible ([0-5]*%) as DEMB's instant coffee sales in Estonia in 2014 amounted only to EUR [...]*. Other players active in the Estonian market are Nestlé ([50-60]*%), JFK ([0-5]*%) and Unilever ([0-5]*%).
- (469) No specific concerns were voiced by Estonian customers as regards the impact of the Transaction on the Estonian market for instant coffee.³⁶⁰

9.6.4. *The Czech Republic*

- (470) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in the Czech Republic.
- (471) DEMB is active in the instant coffee market in the Czech Republic with its brand Douwe Egberts, while Mondelēz serves the Czech instant coffee market with its brand Jacobs.
- (472) The combined market share of the Parties in instant coffee in Czech Republic will amount to [30-40]*%. However the increment brought about by the Transaction is relatively small ([0-5]*%). The new entity will continue facing competition from the market leader Nestlé ([40-50]*%), as well from private label products ([10-20]*%) and Tchibo ([5-10]*%). Rivalry between Nestlé and Mondelēz has spurred competition in the Czech market recently, according to the findings of a GfK study on consumer switching commissioned by Mondelēz.³⁶¹ That study demonstrates clearly that the most significant constraint on the Jacobs brand in instant coffee is posed by Nestlé.
- (473) No specific concerns were voiced by Czech customers as regards the impact of the Transaction on the Czech market for instant coffee.³⁶²

9.6.5. *Denmark*

- (474) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Denmark.
- (475) DEMB is active in the instant coffee market in Denmark with its brand Café Noir, while Mondelēz serves the Danish instant coffee market with its brands Karat and Gevalia.
- (476) The combined market share of the Parties in instant coffee in Denmark will amount to [20-30]*% (Douwe Egberts [10-20]*%, Mondelēz [10-20]*%). The new entity will continue facing competition from the market leader Nestlé ([50-60]*%), as well as from private label products ([5-10]*%) and Peter Larsen ([5-10]*%). Rivalry between Nestlé and Mondelēz has spurred competition in the Danish market recently, as Nestlé has been the primary focus of the launch of the new Mondelēz' instant coffee product range.

³⁶⁰ Responses to questions 204,205 and 206 of Questionnaire Q2-Retailers.

³⁶¹ Commission's Request for Information of 18 July 2014 (QP2) - Annex Question 17 at p. 8.

³⁶² Responses to questions 133, 134 and 135 of Questionnaire Q2-Retailers.

(477) No specific concerns were voiced by Danish customers as regards the impact of the Transaction on the Danish market for instant coffee.³⁶³

9.6.6. *Ireland*

(478) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Ireland.

(479) DEMB is active in the instant coffee market in Ireland with its brand Douwe Egberts, while Mondelēz serves the Irish instant coffee market with its brands Kenco, Maxwell House and Carte Noire.

(480) The combined market share of the Parties in instant coffee in Ireland will amount to [40-50]*%. However the increment brought about by the Transaction is negligible ([0-5]*%) as DEMB's instant coffee sales in Ireland in 2014 amounted only to EUR [...]*. DEMB has significantly lost sales in Ireland between 2011 and 2014, from the amount of EUR [...]* and market share of [0-5]*% in 2011 to the figures of 2014, which shows that its competitive strength is declining. Other players active in the Irish market include Nestlé ([50-60]*%) and private label products ([5-10]*%).

(481) No specific concerns were voiced by Irish customers as regards the impact of the Transaction on the Irish market for instant coffee.

9.6.7. *Poland*

(482) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Poland.

(483) DEMB is active in the instant coffee market in Poland with its brands Douwe Egberts and Prima, while Mondelēz serves the Polish instant coffee market with its brands Jacobs, Maxwell and Carte Noire.

(484) The combined market share of the Parties in instant coffee in Poland will amount to [30-40]*%. However the increment brought about by the Transaction is relatively modest ([0-5]*%). The new entity will continue facing competition from the market leader Nestlé ([30-40]*%), as well as from private label products ([10-20]*%), Tchibo ([5-10]*%) and Mokaté ([5-10]*%).

(485) No specific concerns were voiced by Polish customers as regards the impact of the Transaction on the Polish market for instant coffee.³⁶⁴

9.6.8. *Slovakia*

(486) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in Slovakia.

(487) DEMB is active in the instant coffee market in Slovakia with its brands Douwe Egberts, while Mondelēz serves the Slovakian instant coffee market with its brand Jacobs.

(488) The combined market share of the Parties in instant coffee in Slovakia will amount to [20-30]*%. However the increment brought about by the Transaction is negligible ([0-5]*%) as DEMB's instant coffee sales in Slovakia in 2014 amounted only to

³⁶³ Responses to questions 168, 169 and 170 of Questionnaire Q2-Retailers.

³⁶⁴ Responses to questions 484,485 and 486 of Questionnaire Q2-Retailers.

EUR [...]*. Other players active in the Slovak market are Nestlé ([40-50]*%), private label products ([10-20]*%) and Tchibo ([0-5]*%).

(489) No specific concerns were voiced by Slovakian customers as regards the impact of the Transaction on the Slovakian market for instant coffee.³⁶⁵

9.6.9. United Kingdom

9.6.9.1. Commission's assessment: horizontal overlap

(490) For the reasons set out in this Section, the Commission finds that the Transaction would not lead to a significant impediment to effective competition in the instant coffee market in the United Kingdom.

(491) DEMB is active in the instant coffee market in the United Kingdom with its brand Douwe Egberts, while Mondelēz serves the United Kingdom instant coffee market with several brands, notably Kenco and Carte Noire, the largest brands of its portfolio and three smaller ones: Rappor, Maxwell House and Mellow Bird's.

(492) The combined market share of the Parties in instant coffee in the United Kingdom will amount to [30-40]*% (Douwe Egberts [5-10]*%, Mondelēz [20-30]*%). The new entity will continue to face competition from the market leader Nestlé with its brand Nescafé ([50-60]*%), as well as from private label products ([10-20]*%).³⁶⁶

(493) DEMB and Mondelēz do not appear to be closest competitors as they both target [...] as a specific point of reference. Douwe Egberts takes [...] Gold Blend stock keeping unit as the main benchmark when it is planning strategy and pricing for its DEMB Pure Gold, which accounts for the vast majority of DEMB's sales in instant coffee. This is due to the fact that Kenco and Carte Noire do not offer any similar products with the positioning of a medium or 'gold' roast, but it is only [...] that offers that type of product.³⁶⁷

(494) From a comparison of the two brands portfolio³⁶⁸, it is evident that Mondelēz assumes that [*positioning versus Nestle*] across the product range. Internal documents on the British instant market follow that approach, focussing on the comparison between Kenco and Nestlé.³⁶⁹

(495) No specific concerns were voiced by United Kingdom customers as regards the impact of the Transaction on the United Kingdom market for instant coffee.³⁷⁰

9.6.9.2. Commission's assessment: vertical link

(496) Mondelēz has an arrangement for the manufacture of instant coffee for [...] to sell under [...] own brand. DEMB does not supply any retailer with coffee for resale under retailer brands in the United Kingdom. There is therefore no overlap between the Parties' activities in the supply of coffee to retailers to re-sell under their own brands.

(497) The combined entity would not have the ability to foreclose [...] from supplies of coffee since it would lack any significant market power in the upstream supply of retail branded coffee. Mondelēz estimate that its share of retailer coffee supplies in

³⁶⁵ Responses to questions 518, 519 and 520 of Questionnaire Q2-Retailers.

³⁶⁶ Private labels have increased their market share by [0-5]* between 2013 and 2014.

³⁶⁷ DEMB internal document, undated "DE Instants : Preparing for battle" annex -7 UK-2, slides 2-3.

³⁶⁸ Form CO, paragraph 1209.

³⁶⁹ Form CO, Annex-7-UK-3, slides 1-15.

³⁷⁰ Responses to questions 590, 591 and 592 of Questionnaire Q2-Retailers.

the United Kingdom amounts to approximately [5-10]*% by volume and approximately [10-20]*% by value. There are many manufacturers in the upstream segment in the United Kingdom who would be able to supply instant coffee under the same terms. Moreover, the combined entity would have no incentive to foreclose [...]*, since it would be sacrificing revenues in the upstream supply without any reasonable prospect of increasing margins on its own branded products sold through [...]* or any other retailers, or to increase consumer prices of coffee.

9.6.10. *Other Member States*

(498) The activities of the Parties overlap in other EEA Member States in instant coffee but none of those markets are affected. The states concerned are Greece (combined market share of [5-10]*%), Hungary ([5-10]*%), the Netherlands ([5-10]*%) and Spain ([0-5]*%).

9.7. **Filter pads**

(499) For the reasons set out in Recitals (498) to (584), the Commission has reached the conclusion that the Transaction would lead to a significant impediment to effective competition, in particular as a result of the creation of a dominant position, in the markets for filter pads in France and Austria. On the other hand the Commission concludes for the reasons presented in Recitals (585) to (596) that the Transaction would not significantly impede effective competition in the internal market in the filter pads markets in Germany and the Netherlands.³⁷¹

9.7.1. *France*

9.7.1.1. Merging firms have high market shares

(500) According to the Nielsen data submitted by the Notifying Parties, the filter pad coffee market in France had a total value of EUR 449.1 million in 2014, 74.1% of which is covered by supplier brands and the remaining 25.9% by private label brands.

(501) DEMB is active in the filter pads coffee market in France mainly with its brand Senseo and to a very limited extent with Ma Tradition and L'Or, while Mondelēz serves the French filter pad coffee market with its brands Carte Noire, Grand-Mère and Milka.

(502) Table 10 shows the market shares of the Parties and their main competitors on the filter pads coffee market in 2014 in France.

³⁷¹ The Transaction leads also to an affected market in Spain, however the overlap in the Spanish filter pads market amounts to [0-5]*% in 2013 and there is no overlap in 2014 as Mondelēz has ceased selling filter pads in the Spanish market. Private label products account for almost 70% of the filter pads in market in 2014. No specific concerns were voiced by Spanish customers as regards the impact of the Transaction on the Spanish market for filter pads.

Table 10 Filter pads in France

Manufacturer	Brand	2014	
		Value (‘000 EUR)	Share
DEMB	<i>SENSEO</i>	[...]*	[40-50]*%
	<i>OTHERS</i>	[...]*	[0-5]*%
DEMB TOTAL	-	[...]*	[40-50]*%
MONDELÉZ	<i>CARTE NOIRE</i>	[...]*	[10-20]*%
	<i>GRAND MÈRE</i>	[...]*	[0-5]*%
	<i>MILKA</i>	[...]*	[0-5]*%
MONDELÉZ TOTAL	-	[...]*	[10-20]*%
COMBINED	-	[...]*	[60-70]*%
RETAILERS	<i>PRIVATE LABEL</i>	[...]*	[20-30]*%
LAVAZZA	<i>LAVAZZA</i>	[...]*	[0-5]*%
OTHER	<i>OTHER</i>	[...]*	[5-10]*%
TOTAL	-	[...]*	100%

Source: the Parties

- (503) Post-Transaction, the new entity would achieve a combined market share of [60-70]*% which has increased by [0-5]* between 2011 and 2014. The overlap between the Parties' activities ([10-20]*%) is also significant. The Transaction will combine the two main suppliers of branded filter pads in the market, with private label products as a distant follower (market share of [20-30]*%). Another branded player with a very limited share of the market is Lavazza ([0-5]*%).
- (504) The filter pad coffee market in France has experienced an increase in value of [10-20]*% between 2011 and 2014, and [10-20]*% in volume. The most successful supplier in that market is Mondelēz with its brand Carte Noire, whose sales increased during the same period by [30-40]*% in value and [30-40]*% in volume. The other brand of Mondelēz, Grand-Mère, has achieved lower, albeit quite positive, results (increase of [0-5]*% in value and [10-20]*% in volume).
- (505) Senseo, DEMB's major brand in filter pads, has also grown between 2011 and 2014 although to a more limited extent than Carte Noire ([10-20]*% in value and [10-20]*% in volume). Finally sales of private label products have increased significantly less than the overall market in: [0-5]*% in value and [10-20]*% in volume. Their market share has consequently slightly decreased from [20-30]*% in 2011 to [20-30]*% in 2014.

9.7.1.2. Merging firms are close competitors

- (506) An important aspect for assessing unilateral effects arising from the proposed merger is the degree of substitutability between the Parties' filter pad coffee products. The higher the degree of substitutability between their products, the more likely it is that

the Parties will be able to significantly raise prices to retailers for filter pad coffee products.

Commission's investigation and assessment

- (507) Retailers in France who responded to the market investigation consider, in particular, the brands Senseo and Carte Noire to be competing vigorously with each other in the filter pad coffee market.³⁷² They also consider Mondelēz as the closest competitor to DEMB and *vice versa* in France in coffee products in general and with respect to filter pads in particular.³⁷³ Also the majority of competitors having responded to the market investigation perceive Carte Noire as closest competitor to Senseo as regards filter pads and *vice versa*.³⁷⁴ The Parties appear as the two strongest players in the French filter pads market, with the high market shares and full portfolio of brands cutting across various price points.
- (508) Retailers have explained in that regard that the main branded suppliers like DEMB and Mondelēz tend to adopt similar policies as regards the supply of their products. Since filter pads are not perishable products and can be kept by customers for long periods, branded suppliers tend to launch very aggressive promotion campaigns in order to induce end-consumers to stock significant volumes of filter pads.³⁷⁵ All branded suppliers follow that strategy but DEMB and Mondelēz are the largest players in the market and each of them react significantly to promotions campaigns launched by the other party. As explained by one retailer "*Competition is very fierce between national brands and it eliminates any price differences [with private label brands]. For example, the entry of Carte Noire in the N-capsules market in 2013 has triggered a new price war*".³⁷⁶ [...]*.³⁷⁷

[...]*

- (509) An analysis of the Parties' other internal documents confirms the conclusion that the Parties are each other's close competitors in the French filter pads market.
- (510) For example, an internal document of DEMB assessing Senseo brand's performance in filter pads in 2012 and way forward notes that "*Senseo has a similar price structure than Carte Noire*"³⁷⁸ and compares price per cup of Senseo and Carte Noire.³⁷⁹ In terms of positioning, that document indicates that "*Senseo is the higher (sic) brand of the Fr. Market (strong emotional dimension) and is in the same area as Carte Noire*".³⁸⁰ Likewise, the portfolio structure is very similar for Senseo and Carte Noire with respectively [60-70]*% and [80-90]*% of volumes respectively

³⁷² Non-confidential minutes of a conference call with a retailer dated 23 September 2014 at 11.00 CET. Non-confidential minutes of a conference call and with a retailer dated 19 September 2014 at 10.00 CET.

³⁷³ Responses to questions 209 and 210 of Questionnaire Q2-Retailers.

³⁷⁴ Responses to questions 139 and 140 of Questionnaire Q1 – Competitors.

³⁷⁵ Non-confidential minutes of a conference call with a retailer, 18 February 2015 at 16.30 CET.

³⁷⁶ Non-confidential minutes of a conference call with a retailer, 9 February 2015 at 17.30 CET. The French original reads "*Il existe une concurrence très forte entre les marques nationales elles-mêmes qui font donc fondre les écarts de prix (l'arrivée de Carte Noire en 2013 par exemple sur le marché des capsules Nespresso a contribué à relancer la guerre des prix)*".

³⁷⁷ Mondelēz internal document, dated 27 March 2014, "*Understand and optimize promotional efficiency on the coffee market*", slide 138.

³⁷⁸ DEMB internal document "France 2a" attached as, Annex 7 to the Form CO, slide 102.

³⁷⁹ *Ibidem*, slide 103.

³⁸⁰ *Ibidem*, slide 137.

achieved in the "mainstream" range (between EUR [...] and [...] per pad), whereas private label products achieve 90% of their volumes in the value range (less than EUR 0.10 per pad).³⁸¹ Another internal document from DEMB related to filter pads notes as a strategic objective "[...]".³⁸²

Conclusion on closeness of competition

(511) On the basis of what has been said in Recitals (498) to (508), the Parties' brands are the closest substitutes in the filter pads market in France.

9.7.1.3. Private label products do not exert sufficient competitive constraint

Parties' arguments

(512) The Parties have argued that retailer brands impose a substantial constraint on DEMB and Mondelēz in filter pads coffee. According to the Parties, there is no difference in the quality of Filter Pad coffee offered by retailer brands and manufacturer brands. Retailer brands are in the process of successfully expanding their portfolio, recording significant sales increases for organic and premium coffee products in private label products. As with R&G, retailer and manufacturer brands may be made by the same companies, such as Legal and Segafredo.

(513) The Parties submit that retailer brands offer a full range of products at the same quality and in the same variations as manufacturer brands, with comparable packaging, and often better on-shelf visibility. Retailers' packaging often closely mimics manufacturer brands for the same variations and in addition to adopting the traditional approach of retailer branding, some retailers use a differentiated brand strategy for filter pads.

Commission's investigation and assessment

(514) The Commission has carefully assessed the arguments brought forward by the Parties and considers that competition from private label products will not be sufficient to offset the adverse effects of the merger. On the contrary, it appears that Carte Noire has been a growing and dynamic competitor in the French filter pads coffee market that has spurred competitive rivalry and that private label products have played a minor role in this competitive setting.

(515) In the first place and similarly to R&G, the Commission's investigation has shown that one of the features of the coffee sector is the importance of brands. That importance is documented in the Parties' internal documents, in which they refer to their brands as "[...]", admit that they "[...]" and aim at "[...]".³⁸³

(516) Moreover, retailers in France confirm the importance of brands in the market. One of the retailers stated that a supplier with a stronger brand is granted more shelf space and cited Carte Noire as an example.³⁸⁴ Retailers also mention Parties' brands as 'must-have' brands for filter pads coffee (brands that need to be kept on shelves otherwise the retailer would lose a significant share of turnover in this category).³⁸⁵

³⁸¹ *Ibidem*, slide 145.

³⁸² DEMB internal document, dated 13 February 2014, "France, Board of Directors" attached as Annex 7 France 1-b to the Form CO, slide 21.

³⁸³ Mondelēz internal document, dated 17 March 2008, "EU Coffee Category Preliminary 2009 Strategic Plan", slide 64.

³⁸⁴ Response to question 46.1 of Questionnaire Q2-Retailers.

³⁸⁵ Responses to question 211 of Questionnaire Q2-Retailers and non-confidential minutes of a conference call with a retailer, dated 23 September 2014 at 11.00 CET.

On the basis of the results of the market investigation, it can also be concluded that having brands with high awareness (such as L'Or, Senseo and Carte Noire) is one of the competitive advantages of both Parties. The fact that the Parties are considered by retailers to hold 'must-have' brands relativizes the competitive constraint exerted by private label products on the Parties' filter pads products.

- (517) The Parties' internal documents also show that 90% of private label filter pads portfolio can be found in the value range, while for Carte Noire it is only [10-20]*% and for Senseo only [5-10]*%, implying that private label products indeed target rather the value segment of the market (up to a price of EUR 0.10 per pad)³⁸⁶, as it is further confirmed by the much lower share in value of private label filter pads in France as compared with its volume share ([30-40]*% in volume and [20-30]*% in value)
- (518) Moreover, the relative strength of private label products compared to branded products tends to stabilise in France in the recent years. The graph in Figure 8 shows the evolution of penetration of private label products in the French retail market in the last 15 years. Although those figures represent penetration of such products across all categories of food and personal care products sold in supermarkets, they are indicative of the current slowing of growth of private label branding in France.³⁸⁷

[...]*

Figure 8 Nielsen, conjoncture 2013 tendance et perspectives³⁸⁸

- (519) Private label products in filter pads coffee have followed the same trend. As mentioned in Section 9.7.1.1, sales of private label products have increased significantly less between 2011 and 2014 than the size of the overall market: [0-5]*% in value ([10-20]*% for the total market) and [10-20]*% in volume ([10-20]*% for the total market). The private label's market share has consequently slightly decreased from [20-30]*% in 2011 to [20-30]*% in 2014. It follows that the competitive pressure exerted by private label filter pads on branded products has decreased in the last years.
- (520) As explained in Section 9.7.1.1., the most successful brand over the same period has been Carte Noire, the sales of which have increased during the same period by [30-40]*% in value and [30-40]*% in volume.
- (521) During the market investigation, French retailers have explained that this drop of private label brands' penetration is the direct consequence of fierce competition between branded producers. As the filter pads category has been growing to a more limited extent than other single serve coffee products available on the market (like N capsules), branded producers have increased their marketing and advertisement expenses in order to get a larger share of a rather sluggish market. By doing so, they have improved the awareness of their filter pads brands and increased barriers to expansion for private label products. As explained by one French retailer, customers are attached to their brands and the filter pad market (as well as single-serve coffee products in general) is driven by technical evolution, which is led by branded producers like Nestlé, DEMB or Mondelēz.³⁸⁹

³⁸⁶ DEMB internal document undated, submitted as Annex 7 France 2a to the Form CO.

³⁸⁷ DEMB internal document, dated 31 January 2013, "*Nielsen, conjoncture 2013 tendance et perspectives*", slide 11.

³⁸⁸ *Ibidem*.

³⁸⁹ Non-confidential minutes of a conference call with a retailer dated 20 February 2015 at 9.30 CET.

- (522) Moreover, branded products suppliers have intensified their promotional activity in the French filter pad market recently, particularly because of the slowing down of the category's growth and in the light of the specific features of coffee filter pads. As one retailer explained: "*Promotion works quite well because the unit price of filter pads is high, filter pads are non-perishable and consumers use them frequently and regularly*".³⁹⁰ Promotional activity has decreased the average price of branded filter pads and narrowed down the price differences between branded filter pads and PL products. Consequently "*[Private label] sales have remained stable in the last years, because of the very aggressive pricing policy of branded suppliers. This very liberal attitude tends to downgrade the brand because it eliminates the price gap between branded and [private label] products*".³⁹¹
- (523) Another retailer noted that in the situation where price differences between branded products and private label products is gradually disappearing end-consumers tend to reduce their private label purchases, since they can afford to buy branded products sold at lower price points.³⁹² That has been confirmed by all French retailers that participated in the market investigation
- (524) One retailer has also explained that its private label product range is narrower than Senseo's or Carte Noire's: "*The [private label] filter pads range is more limited than the range of national brands (half the number of references). National brands are frequently launching new products whereas branded producers cannot afford this. To the best of our knowledge, this is also the case for other retailers*".³⁹³
- (525) The Parties' internal documents of the Parties confirm the decrease of penetration by private label brands coffee filter pads. In a document assessing Senseo's performance in 2012 in filter pads, DEMB notes that private label brands have been the "*looser [sic] of the year*" with a decreasing volume share from [30-40]*% to [30-40]*% whereas there has been a "*stronger long-term push for Carte Noire*" with an increasing volume share from [10-20]*% to [10-20]*%.³⁹⁴ That strong long-term push of Carte Noire is due according to DEMB to two main factors: "*a very strong*

³⁹⁰ Non-confidential minutes of a conference call with a retailer dated 20 February 2015 at 9.30 CET. The French original reads "*La promotion fonctionne très bien, puisque les dosettes sont des produits chers à l'unité, qui se conservent longtemps et que les clients consomment avec une grande fréquence*".

³⁹¹ Non-confidential minutes of a conference call with a retailer dated 12 February 2015 at 11.00 CET. The French original reads "*Du côté des marques de distributeurs (MDD), les ventes sont stagnantes depuis plusieurs années, ce qui est lié à la politique très agressive des marques nationales sur les prix. Cette politique excessivement libérale en matière de promotion a tendance à dévaloriser la marque en annulant l'écart de prix entre la marque et la MDD la marque*".

³⁹² Non-confidential minutes of a conference call with a retailer dated 9 February 2015 at 17.30 CET. "*Les marques de distributeurs ne peuvent pas se permettre de faire des promotions aussi agressives et donc elles perdent des parts de marché. Il en résulte que les marques nationales sont parfois vendues au même prix que les marques de distributeurs. Les consommateurs ont donc tendance à diminuer leurs achats de marques de distributeurs, compte tenu de l'absence de différence notable de prix*". See also non-confidential minutes of a conference call with a retailer dated 18 February 2015 at 14.00 CET "*Par exemple, lorsque Carte Noire est entrée sur le marché des dosettes souples, elle a proposé des prix particulièrement bas. Les dosettes Carte Noire en promotion se vendaient donc au même prix que les marques de distributeurs*".

³⁹³ Non-confidential minutes of a conference call with a retailer dated 9 February 2015 at 17.30 CET. The French original reads "*Chez [name of retailer], la gamme de produits disponible en dosettes est plus limitée que pour les marques nationales (nombre de références deux fois plus faible). Les marques nationales se renouvellent sans cesse, alors que les marques de distributeurs ne peuvent pas se le permettre. A la connaissance de [name of retailer], c'est aussi le cas chez les autres distributeurs*".

³⁹⁴ DEMB internal document undated, submitted as Annex 7 France 2a to the Form CO, slide 16.

increase in media spending ([...])" and "Promotion as a key driver of the growth : Promo volumes : [...]*%".³⁹⁵*

Conclusion on private label competition

(526) On the basis of what has been said in Recitals (510) to (523), private label products do not exert sufficient competitive constraint on the Parties' brands.

9.7.1.4. R&G products do not exert sufficient competitive constraint on filter pads products

Parties' arguments

(527) The Parties have argued that there is clear evidence that R&G coffee exerts a significant competitive constraint on filter pads. For example, DEMB conducted a research in 2013 which purportedly showed that the effect of a reduction in the price of filter pads was to make the price of R&G coffee and filter pads more comparable, leading to increased substitution between R&G coffee and filter pads. In particular, the Parties submitted that that has accelerated net switching from R&G to filter pads. According to the Parties, this may be driven by the fact that in France the majority of consumers use more than one coffee format and machine, with French households using an average of 1.7 coffee machines. Of the consumers that own a Senseo machine, just 28% use that machine exclusively, with the remaining 72% using alternative machines in addition to their Senseo machine, the most common alternative being R&G brewers (55%).

(528) In addition to the lower price differential between filter pads and R&G coffee, the Parties argued that switching to R&G is likely to be particularly pronounced for consumers using Senseo machines because Senseo machines produce a coffee that is more similar to that produced using R&G coffee, compared to machines such as Nespresso that produce espresso-type coffee. Moreover, the Parties put forward that this trend is likely to intensify as French consumers are becoming more price conscious – DEMB's research suggests that most French consumers have in recent years adapted their behaviour to save money on coffee, by buying more coffee products on promotion or buying cheaper products.

Commission's investigation and assessment

(529) The Commission has carefully assessed the Parties' arguments and found no evidence that R&G products exert sufficient competitive constraint on filter pads.

(530) The French retailers which responded to the market investigation did not confirm such a competitive interaction between R&G and filter pads. One retailer explained that it is not expected that French consumers would switch away from filter pads to R&G products even if filter pads prices increase by 5 to 10%. Filter pads have significant advantages compared to R&G: filter pads are easier to use, convenient and include many references among which the end-consumer can choose. Moreover consumers having purchased a filter pad machine want to use it and it is more difficult to make them switch towards another product.³⁹⁶

³⁹⁵ *Ibidem*, slide 123.

³⁹⁶ Non-confidential minutes of a conference call with a retailer dated 12 February 2015 at 11.00 CET "Il n'est plus possible d'imaginer un retour en arrière sur le marché français, à savoir que les consommateurs ne se tourneraient plus vers le café moulu si le prix des dosettes augmentait de 5 à 10%. Les dosettes souples et les capsules présentent de nombreux avantages. Le dosage est juste (alors que dans le café moulu, le consommateur doit faire son dosage lui-même en fonction de l'intensité du café qu'il veut obtenir- ce qui est très aléatoire), l'utilisation est pratique et l'offre est flexible et diversifiée,

- (531) Another retailer submitted that whilst it is true that most of the households own a filter coffee machine and a single-serve system, usages differ significantly. Filter coffee machines are mostly used for breakfast coffee whereas the use of single-serve machines is more diversified. Both types of machines (and therefore both types of coffee) thus cater to different needs.³⁹⁷
- (532) Moreover, from a commercial perspective, producers enjoy higher margins from the sales of filter pads and N-capsules than from the sales of coffee beans and R&G products. It appears from the Parties' internal documents that single-serve coffee products generate higher margins and require premium brands, while R&G coffee products are low margin products.³⁹⁸ That is also evidenced by the stability of the overall French coffee market between 2011 and 2013 (207 000 tonnes) which has grown in value by 10% over the same period thanks to single-serve products such as filter pads and N-capsules. Coffee companies have therefore an interest in maintaining the current level of advertising and promotion (provided that the competitive environment remains dynamic) rather than incentivise customers to switch to R&G products.³⁹⁹
- (533) Finally, there are significant price differences between filter pads and R&G products that limit substitution. According to the Parties' internal documents, the price per cup on average for R&G coffee products is EUR [0-5]*, while for filter pads it is EUR [0-5]*. In France, the average price per kg of R&G coffee is EUR [5-10]* whereas for filter pads it is EUR [10-20]* per kg. It is not very likely that customers that already accept to pay a higher price per cup for filter pads would decide to switch to R&G should the price per cup of filter pads increase by 5 to 10%, since they already pay a higher price.

Conclusion on R&G competition

- (534) On the basis of what has been said in Recitals (525) to (531), R&G products do not exert sufficient competitive constraint on filter pads products.

9.7.1.5. Lack of countervailing buyer power

Parties' arguments

- (535) The Parties have argued that retailers in France are able to exercise buyer power through a wide range of "negotiation levers". According to the Parties, those levers impose, and would continue following the proposed Transaction to impose, a substantial constraint on the Parties. The Parties argued that the French food retail market is characterised by a combination of relatively high levels of concentration with fierce competition for market share amongst the key retail groups.

avec de nombreuses références parmi lesquelles le consommateur peut choisir. De surcroît, les consommateurs investissent dans une machine et souhaitent l'utiliser et il donc d'autant plus difficile de les faire basculer vers un autre produit'.

³⁹⁷ Non-confidential minutes of a conference call with a retailer dated 17 February 2015 at 9.40 CET. "*Beaucoup de ménages ont aujourd'hui des machines à dosette et des machines à filtre. Les usages sont différents, la machine à filtre étant réservée pour les petit déjeuner, la machine à dosette pour un moment de convivialité après le repas*".

³⁹⁸ For instance: Mondelēz internal document dated October 2013, "CI French Coffee Market Induction FINALE, p. 12; dated 3 October 2013 "Project Charger Update Audit Committee vf", pp. 3, 9 and dated 15 December 2013 "Project Charger Discussion Materials", p. 11.

³⁹⁹ Non-confidential minutes of a conference call with a retailer dated 12 February 2015 at 11.00 CET "*Il n'est donc pas non plus dans l'intérêt de la marque de retourner en arrière et l'intensité de la guerre commerciale entre les marques sur les dosettes montre leur volonté de faire croître la catégorie des dosettes et de la capsule, au détriment du café moulu*".

- (536) The Parties submitted that buyer power is reinforced by the highly competitive nature of downstream retail markets, with retailers in France engaged in a “price war”, led by Leclerc, Carrefour and Géant Casino, where offering coffee products at low prices is seen as an important traffic generator. This, it is claimed, puts pressure on retailers’ downstream margins, and in turn on wholesale pricing. The Parties believe that this trend is likely to increase, in particular as a result of the recently announced buying alliances between Auchan and Système U (currently fourth and fifth in the French market) in September 2014, between Casino and Intermarché in October 2014 and between Carrefour and Cora in October 2014.

Commission's investigation and assessment

- (537) In the first place, as regards buying alliances, despite the fact that three alliances have been announced in the last three months of 2014, it is too early to assess their real impact, especially considering that none of these buying alliances have been implemented and the expected changes in the retail landscape brought by the "Macron law", currently under discussion in the French Parliament.⁴⁰⁰
- (538) Moreover, as explained in Recitals (512) to (524), the market investigation pointed out that Parties filter pads' brands (Senseo and Carte Noire) are ‘must-have’ brands that cannot be excluded from the shelves otherwise retailers would lose substantial turnover in that category. Therefore retailers will not replace those power ‘must-have’ brands with other smaller brands. Considering the significance of brands in the filter pads coffee market and the relative decline of their market position, private label products are not an alternative either.
- (539) It is in any event not sufficient that buyer power (if any) exists prior to the merger; it must also exist and remain effective following the merger. A merger between two suppliers may reduce buyer power if it thereby removes a credible alternative. In assessing buyer power, it is essential to look at the alternatives available to French retailers. In the filter pad market where DEMB's and Mondelēz' brands are close competitors or even the sole competitors on the market, supermarkets could not switch to alternative brands with the required level of recognition to compete with those of the Parties. If the retailer is not willing to entirely eliminate the JV's's products from the shelves, even a partial delisting of important JV brands such as Carte Noire or Senseo would clearly endanger the retailer's turnover in the coffee category.
- (540) As to the threat of delisting and other negotiation levers, [...]*. This suggests they negotiate with retailers as equal partners and not from a position of a weaker player. This is consistent with the fact that the Parties hold must-have brands which give them an influence on the retailers’ bargaining position – in case of failure to reach an agreement, the retailer has as much to lose as the branded supplier.

Conclusion on countervailing buyer power

- (541) On the basis of what has been said in Recitals (533) to (538), buyer power does not appear to be sufficient to counter the increase in market power that the transaction is likely to create.

⁴⁰⁰ For example, the "Macron law" specifies that any retail buying alliances should be submitted to the French Competition Authority before its implementation.

9.7.1.6. Entry unlikely to occur

Parties' arguments

- (542) The Notifying Parties have also argued that there are no material barriers to entry in the filter pad market for other competitors, given the ease of obtaining supply of good quality pads and coffee, and the open nature of the Senseo system. The Parties submit that there are a number of manufacturers that produce or offer filter pads production for use in retailer brands in France, including: Fichaux, United Coffee, Meo, Legal, Malongo, Segafredo and Warca.

Commission's investigation and assessment

- (543) As mentioned in the general Section 9.1 related to the coffee sector as a whole, since coffee products belong to differentiated markets dominated by brands, barriers to entry and expansion in those markets are not insignificant. Established positions of the incumbent coffee companies and the strength of their power brands to which customers remain loyal increase the risks and costs of potential entry.
- (544) Critical factors for success in the coffee market, as identified by competitors and customers, include, apart from having a well-known brand, also financial strength to sustain investments, effective marketing strategy (television advertising) and other public relation activities.
- (545) The barriers to entry referred to in Recital (542) have been confirmed by French retailers as regards filter pads in the market investigation. The retailers have indicated that entering the filter pad markets requires substantial marketing and promotion overheads and would only be achievable by a company able to afford significant expenditure.⁴⁰¹
- (546) Finally, retailers have not confirmed in the market investigation that they would be ready to sponsor a new entrant in the filter pad market as their primary objective is to rationalise their coffee shelves and make their coffee offering easier to grasp and to understand by the end-consumers.⁴⁰²

Conclusion on market entry

- (547) On the basis of what is said in Recitals (540) to (544), market entry is not considered as likely to exert sufficient competitive constraint on the merging Parties.

9.7.1.7. Conclusion on filter pads in France

- (548) The Commission concludes that the proposed Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the French filter pads market.

⁴⁰¹ Non-confidential minutes of a call with a retailer dated 18 February 2015 at 14.00 CET " *Deuxièmement, les marques nationales ont des moyens marketings plus importants que les distributeurs pour promouvoir les marques de distributeurs. Ce qui compte pour réussir sur un tel marché est la promotion et la publicité*".

⁴⁰² Non-confidential minutes of a call with a retailer dated 20 February 2015 at 9.30 CET " *le rayon café est devenu difficile à comprendre et à appréhender pour le consommateur avec beaucoup de marques et de formats différents L'objectif du distributeur comme [name of retailer] aujourd'hui est de clarifier et de rationaliser ce rayon. Dans ce contexte, l'arrivée de nouvelles marques risquerait de complexifier encore davantage le rayon et donc de perdre le consommateur. Le coût qu'un distributeur doit assumer afin de faire de la place pour une nouvelle marque est particulièrement important.*"

9.7.2. Austria

9.7.2.1. Merging firms have high market shares

- (549) According to the Nielsen data submitted by the Parties, the filter pad coffee market in Austria had a total value of EUR 15.8 million in 2014, [80-90]*% of which is covered by supplier brands and the remaining [10-20]*% by private label brands.
- (550) DEMB is active in the filter pads coffee market in Austria mainly with its brand Senseo, while Mondelez serves the Austrian filter pad coffee market with its brands Jacobs and to a lesser extent with its brand Hag.
- (551) Table 11 shows the market shares of the Parties and their main competitors on the filter pads coffee market in 2014 in Austria.

Table 11 Filter pads in Austria

Manufacturer	Brand	2014	
		Value ('000 EUR)	Share
DEMB	<i>SENSEO</i>	[...]*	[30-40]*%
DEMB TOTAL	-	[...]*	[30-40]*%
MONDELÉZ	<i>JACOBS</i>	[...]*	[30-40]*%
	<i>HAG</i>	[...]*	[0-5]*%
MONDELÉZ TOTAL	-	[...]*	[30-40]*%
COMBINED	-	[...]*	[70-80]*%
RETAILERS	<i>PRIVATE LABEL</i>	[...]*	[10-20]*%
TCHIBO	<i>EDUSCHO</i>	[...]*	[0-5]*%
	<i>TCHIBO</i>	[...]*	[0-5]*%
TCHIBO TOTAL	-	[...]*	[0-5]*%
ILLY	<i>ILLY</i>	[...]*	[0-5]*%
DALLMAYR	<i>DALLMAYR</i>	[...]*	[0-5]*%
MEINL	<i>MEINL</i>	[...]*	[0-5]*%
OTHERS	-	[...]*	[0-5]*%
TOTAL	-	[...]*	100%

Source: the Parties

- (552) The new entity will achieve a combined market share of [70-80]*% which has remained quite stable between 2011 and 2014 ([70-80]*% in 2011). The overlap between the Parties' activities ([30-40]*%) is also particularly significant. The Transaction will combine the two main suppliers of branded filter pads in the market, with private label products as a very distant follower (market share of [10-20]*%). Other branded players with a particularly limited share of the market are German

player Tchibo ([0-5]*%) with its brand Eduscho and Tchibo, Illy from Italy ([0-5]*%), Dallmayr ([0-5]*%) and local supplier Meinel ([0-5]*%).

(553) The filter pad coffee market in Austria lost [0-5]*% of its value between 2011 and 2014 (and a small increase, [0-5]*% in volume).

(554) Mondelēz' market presence has decreased over the period 2011-2014 ([0-5]*% in value). Senseo, DEMB's major brand in filter pads, has remained stable during the same period. Branded producer Tchibo has also reduced its market presence, with a drop of [40-50]*%. Finally, sales of private label products have increased by [10-20]*% in value.

9.7.2.2. Parties are close competitors

(555) An important aspect for assessing unilateral effects arising from the proposed merger is the degree of substitutability between the Parties' filter pad coffee products. The higher the degree of substitutability between their products, the more likely it is that the Parties will be able to significantly raise prices to retailers for filter pad coffee products.

Commission's investigation and assessment

(556) Retailers in Austria that responded to the market investigation view in particular the brands Senseo and Jacobs as competing vigorously with each other in the filter pad coffee sector. They also consider Mondelēz as closest competitor to DEMB and *vice versa* in Austria in coffee products in general and with respect to filter pads in particular.⁴⁰³ Also the majority of competitors having responded to the market investigation perceive Jacobs as the closest competitor to Senseo as regards filter pads and *vice versa*.⁴⁰⁴ The Parties appear as the two strongest players in the Austrian filter pads market, with the high market shares and full portfolio of brands cutting across various price points.

(557) An analysis of the Parties' other internal documents confirms the conclusion that the Parties are each other's close competitors in the Austrian filter pads market.

(558) For example, an internal document of Mondelēz assessing brand awareness and penetration in Austria notes that "[...]*". In another internal document on Mondelēz dealing with filter pads, [...]*.⁴⁰⁵

Conclusion on closeness of competition

(559) The Parties' brands are the closest substitutes in the filter pads market in Austria.

9.7.2.3. Other brands, private label products and R&G products will not exert sufficient competitive constraint.

Parties' arguments

(560) The Notifying Parties have argued that nineteen manufacturers are active in the filter pads segment, including well-established manufacturer brands like Eduscho, Tchibo, Meinel, and Dallmayr. Together those manufacturer brands account for [10-20]*% of the Austrian filter pads segment. According to the Parties, some of those filter pads manufacturers have only very recently entered the segment which shows that the

⁴⁰³ Responses to questions 66 and 67 of Questionnaire Q2-Retailers.

⁴⁰⁴ Responses to questions 85 and 86 of Questionnaire Q1 – Competitors.

⁴⁰⁵ Mondelēz, Link meeting Coffee, 25 March 2014, slide 11.

filter pads category in Austria is a dynamic segment and that there are no material barriers to enter.

- (561) Likewise, the Parties have argued that retailer brands compete with manufacturer brand products in all areas of the filter pads segment. According to the Notifying parties, retailer brands compete with products from all price points, quality levels and varieties, are marketed with similar packaging and are sold on the same shelves as manufacturer brands.
- (562) The Parties further argued that at the end of 2011, DEMB raised list prices of filter pads and as a result retailers increased the average retail prices of filter pads which led to a loss in volumes of about [30-40]*%. As a consequence, DEMB took back the list price increase and retailers followed, taking back the average retail price rise. According to the Notifying Parties, a significant part of the lost volumes was absorbed by retailer brands which experienced the largest increase in sales around that period

Commission's investigation and assessment

- (563) As regard other brands, it is clear from the figures shown in Table 11 that they have a minor role in the Austrian market. Tchibo, which achieves a market of [5-10]*% in filter pads in neighbouring Germany, has a share of [0-5]*% in Austria. Dallmayr, which has a share of [0-5]*% in Germany, holds a negligible market presence in Austria ([0-5]*%). None of the brands listed by the Notifying Parties has a share above [0-5]*% and the main alternative brands active in Austria (Tchibo brands, Illy) have seen their sales declining between 2011 and 2014.
- (564) Similarly, it is unlikely that private label products will exercise a significant competitive constraint on the merged entity.
- (565) In the first place and as explained in Section 9.1, the Commission's investigation has shown that one of the features of the coffee sector is the importance of brands. That is documented in the Parties' internal documents, in which they refer to their brands as "[...]*", admit that they "[...]*" and aim at "[...]*".⁴⁰⁶ Competitive constraint by private label products is in this context mitigated by the importance of brands.
- (566) In the second place, private label products play a relatively limited role in the Austrian filter pads market. Market share of private label products in Austria is only [10-20]*%. In neighbouring Germany, PL products achieve a much higher share of supply ([40-50]*%). Even assuming that Austrian final customers are price sensitive, it does not appear that price-sensitivity has led Austrian consumers to resort more frequently to private label products, unlike German consumers.
- (567) As regards the market situation when DEMB raised list prices of filter pads late 2011, Senseo's sales have dropped from EUR 4.8 million in 2011 to EUR 4.5 million in 2012. Yet, the available data shows that Mondelēz and its brand Jacobs have achieved the most significant growth in the same year (from EUR 6.6 million to EUR 7 million) whilst private label products achieved a more steady growth (EUR 2.6 million in 2011, EUR 2.7 million in 2012).
- (568) Similarly to what is explained in Section 9.7.1.4, the Commission has not found, in relation to the Austrian market, any evidence that R&G products exert enough competitive constraint on filter pads.

⁴⁰⁶ Mondelēz internal document, dated 17 March 2008, "EU Coffee Category Preliminary 2009 Strategic Plan", slide 64.

Conclusion on competition from other brands, private label products and R&G products

(569) Other brands, private label products and R&G products do not exert sufficient competitive constraint on the Parties' brands.

9.7.2.4. The competitive outlook in Germany does not affect the competitive situation in Austria

Parties' arguments

(570) The Parties have argued that price negotiations for filter pads in Austria are heavily influenced by German prices. German retailers, Rewe, Spar and Lidl, have a strong presence in Austria through their retail subsidiaries. As a result, the Parties contended that German prices have a strong impact on the prices which DEMB negotiates for Austria with Germany-based retailers. That allegedly means that DEMB's respective prices in Austria are the result of the competitive constraints that prevail in the German filter pads segment and this would also be the case following the Transaction. In the German filter pads segment, the Parties' combined share is significantly lower ([20-30]*%), retailer brands hold a share of [40-50]*%, and Aldi is the price leader. Therefore, according to the Parties, sales by the Parties of filter Pads to German retailers in Austria face similar competitive conditions as in Germany. As there is fierce competition in filter pads in Germany, the Parties submitted that such competition should impose competitive constraints on prices in Austria as well.

Commission's investigation and assessment

(571) The Commission does not share the Parties' view on the effects of German competition on the competitive situation in Austria. First, as explained in Section 8, the relevant geographic markets for coffee products in general and filter pads in particular are national due to specific differences between countries in terms of consumption habits, market presence of various players, sales and marketing policies and procurement behaviour.

(572) Germany and Austria are not an exception to what has been said in Recital (569). First there are differences between Germany and Austria in terms of retail market structure. Aldi has much more weight in Germany than in Austria where Rewe and Spar have the highest shares. Moreover, the share of private label products is three times higher in Germany than in Austria. Although the Parties are not directly active at retail level (since they sell their coffee products to retailers), the structure of the downstream retail has an influence on the way the Parties run their coffee business at the upstream level.

(573) With respect to the upstream level where the Parties are active, there are differences between Germany and Austria as regards presence of competitors (Melitta is active in Germany but not in Austria, Tchibo is stronger in Germany than in Austria), structure of the market (filter pads represent [5-10]*% of the Austrian coffee market but [10-20]*% in Germany) or even the regulatory environment (there is a coffee tax in Germany but not in Austria).

(574) During the market investigation, suppliers active in both countries indicated that negotiations with retailers were conducted on a national basis and not on a cross-border basis.⁴⁰⁷

⁴⁰⁷ Non-confidential minutes of a conference call with a competitor, dated 6 February 2015 at 12.30 CET.

Conclusion on the influence of the German market on the Austrian situation

(575) The Commission concludes that the competitive outlook in Germany does not affect the competitive situation in Austria.

9.7.2.5. Lack of countervailing buyer power

Parties' arguments

(576) The Parties have argued that retailers in Austria are able to exercise buyer power through a wide range of “negotiation levers”. The Parties submitted that those levers impose, and would continue following the proposed Transaction to impose, a substantial constraint on the Parties. The Austrian food retail market is characterised by a combination of relatively high levels of concentration with fierce competition for market share amongst the key retail groups.

Commission's investigation and assessment

(577) As explained in Recitals (563) to (567), market investigation pointed out that Parties filter pads' brands (Senseo and Jacobs) are ‘must-have’ brands that cannot be excluded from the shelves otherwise retailers would lose substantial turnover in this category. Therefore retailers will not replace those power ‘must-have’ brands with other smaller brands. Considering the significance of brands in the filter pads coffee market and the lack of growth of their market position, private label products are not an alternative either.

(578) It is in any event not sufficient that buyer power (if any) exists prior to the merger; it must also exist and remain effective following the merger. A merger between two suppliers could reduce buyer power if it thereby removes a credible alternative. In assessing buyer power, it is essential to look at the alternatives available to [...] retailers. In the filter pad market where DEMB's and Mondelēz' brands are close competitors or even the sole competitors on the market, supermarkets could not switch to alternative brands with the required level of recognition to compete with those of the Parties. If the retailer is not willing to entirely eliminate the JV's products from the shelves, even a partial delisting of important JV brands such as [...] would clearly endanger the retailer's turnover in the coffee category.

(579) As to the threat of delisting and other negotiation levers, [...] This suggests they negotiate with retailers as equal partners and not from a position of a weaker player. This is consistent with the fact that the Parties hold must-have brands which give them an influence on the retailers' bargaining position – in case of failure to reach an agreement, the retailer has as much to lose as the branded supplier.

Conclusion on countervailing buyer power

(580) Buyer power does not appear to be sufficient to counter the increase in market power that the transaction is likely to create.

9.7.2.6. Entry unlikely to occur

Parties' arguments

(581) The Parties have also argued that there are no material barriers to entry in the filter pad market for other competitors, given the ease of obtaining supply of good quality pads and coffee, and the open nature of the Senseo system. The Parties argued that there are a number of manufacturers that have recently entered the filter pads market in Austria, including: Bellarom (2009), Rewe (2010), Gunz (2012), Markant (2013), and Pfeiffer (2013).

Commission's investigation and assessment

- (582) As mentioned in the general part related to the coffee sector as a whole, since coffee products belong to differentiated markets dominated by brands, barriers to entry and expansion in those markets are not insignificant. Established positions of the incumbent coffee companies and the strength of their power brands to which customers remain loyal increase the risks and costs of potential entry.
- (583) Critical factors for success in the coffee market, as identified by competitors and customers, include, apart from having a well-known brand, also financial strength to sustain investments, effective marketing strategy (television advertising) and other public relation activities.
- (584) The barriers to entry referred to in Recital (581) have been confirmed by Austrian retailers as regard filter pads in the market investigation. The retailers have indicated that entering those markets requires substantial marketing and promotion overheads and would only be achievable by a company able to afford significant expenses.⁴⁰⁸

Conclusion on market entry

- (585) Market entry is not considered as likely to exert sufficient competitive constraint on the merging Parties.

9.7.2.7. Conclusion on filter pads in Austria

- (586) The Commission concludes that the proposed Transaction would lead to a significant impediment to effective competition, in particular through the creation of a dominant position, in the Austrian filter pads market.

9.7.3. Germany

- (587) For the reasons set out in this Section, the Commission considers that the Transaction would not lead to a significant impediment of effective competition in the filter pads coffee market in Germany.
- (588) According to the Nielsen data submitted by the Notifying Parties, the filter pad coffee market in Germany had a total value of EUR 425.1 million in 2014, [50-60]*% of which is covered by supplier brands and the remaining [40-50]*% by private label brands.
- (589) DEMB is active in the filter pads coffee market in Germany with its brand Senseo, while Mondelēz serves the German filter pad coffee market with its brand Jacobs.

⁴⁰⁸ Responses to questions 93 and 94 of Questionnaire Q2-Retailers.

(590) Table 12 shows the market shares of the Parties and their main competitors on the filter pads coffee market in 2014 in Germany.

Table 12 Filter pads in Germany

Manufacturer	Brand	2014	
		Value ('000 EUR)	Share
DEMB	<i>SENSEO</i>	[...]*	[20-30]*%
DEMB TOTAL	-	[...]*	[20-30]*%
MONDELÉZ	<i>JACOBS</i>	[...]*	[5-10]*%
MONDELÉZ TOTAL	-	[...]*	[5-10]*%
COMBINED	-	[...]*	[30-40]*%
RETAILERS	<i>PRIVATE LABEL</i>	[...]*	[40-50]*%
TCHIBO	<i>EDUSCHO</i>	[...]*	[0-5]*%
	<i>TCHIBO</i>	[...]*	[0-5]*%
TCHIBO TOTAL	-	[...]*	[5-10]*%
MELITTA	<i>MELITTA</i>	[...]*	[0-5]*%
DALLMAYR	<i>DALLMAYR</i>	[...]*	[0-5]*%
OTHERS	-	[...]*	[0-5]*%
TOTAL	-	[...]*	100%

Source: the Parties

- (591) Following the Transaction, the new entity would hold a market share of [30-40]*% with an overlap of [5-10]*%. The German filter pad market will remain dominated by private label products, which hold a market share of more than [40-50]*%. Unlike other European markets where branded filter pads retain a prominent role, private label products hold a leading position in Germany, primarily due to the specific retail structure and in particular the dense network of hard discounters in Germany, notably Aldi (which accounts for half of the private label market share in Germany) and Lidl. The gap between private label and the new entity's market share is in that regard particularly significant (more than [20-30]*%).
- (592) The share of retailer brands has also been growing in Germany. While the merging Parties' share decreased by [0-5]*% between 2011 and 2014 retailer brands were not only able to maintain their share, but managed even to increase their share slightly between 2011 ([40-50]*%) and 2014 ([40-50]*%), demonstrating the continuing trend of retailer brands' leadership in the filter pads market in Germany. Some Alternative brands have also managed to increase their sales over the same period, notably Tchibo ([10-20]*%), whereas the overall market has slightly declined. That demonstrates that competition in the German filter pads market is primarily characterised by alternative brands and private label products.

- (593) This trend is also acknowledged in the Parties' internal documents. For example, DEMB notes in one internal document assessing Senseo's performance that the volume of lost sales of Senseo filter pads was mainly recaptured by Aldi, other retailer brands and Tchibo (Gala sub-brand).⁴⁰⁹
- (594) Finally, no specific concerns were voiced by German customers as regards the impact of the Transaction on the German market for filter pads.⁴¹⁰

9.7.4. *The Netherlands*

- (595) For the reasons set out in this Section, the Commission considers that the Transaction would not lead to a significant impediment to effective competition in the filter pads coffee market in the Netherlands.
- (596) DEMB is active in the filter pads coffee market in Germany with its brands Douwe Egberts and Kanis&Gunnink, while Mondelēz serves the Dutch filter pad coffee market with its brand Velours Noir.
- (597) The combined market share of the Parties in filter pads in the Netherlands will amount to [50-60]*%. However the increment that would be brought about by the Transaction is negligible ([0-5]*%) as Velours Noir's filter pad sales in the Netherlands in 2014 amounted only to EUR [...]*. Other players active in this market are private label products, Beyers with its brand Moreno and Nestlé with Nescafé.
- (598) No specific concerns were voiced by Dutch customers as regards the impact of the Transaction on the Dutch market for filter pads.⁴¹¹

9.8. **N-capsules**

- (599) Following the market definition for N-capsules as defined earlier in this Decision, the Transaction does not give rise to any affected market in N-capsules in the EEA.
- (600) In several Member States the Parties are the main market participants in the traditional retail channel with Nespresso compatible capsules, while Nespresso is the clear market leader and it is present with its original capsules in its own distribution channels (that is to say dedicated shops and online).
- (601) The Parties submit that the N-capsules market is growing at a very high pace and, also in view of its higher margin, is attracting numerous new entrants which act as a competitive constraint on the Parties and will keep acting as constraint also towards the JV.
- (602) The Commission recognises the presence of numerous new entrants in the market for N-capsules among branded coffee producers, operators of private label products or companies active in related markets. The majority of respondents to the market investigation indicated that the number of competitors in this market will remain high and some respondents indicated the possibility for some of these players to achieve considerable market shares in the next five years.⁴¹²

⁴⁰⁹ DEMB internal document, dated 12 March 2013, "*Pods Workshop 2012 Douwe Egberts Retail Germany GMBH*", slides 2 and 4.

⁴¹⁰ Responses to questions 275, 276, 277 of Questionnaire Q2-Retailers.

⁴¹¹ Responses to questions 450, 451, 452 of Questionnaire Q2-Retailers.

⁴¹² Responses to question 36 of Questionnaire Q9-Competitors and responses to question 50 of Questionnaire Q10-Retailers.

(603) Moreover internal documents of Nestlé show that Nespresso considers compatible capsules as competition.⁴¹³

9.9. Out-of home

(604) The Commission considers that the Transaction would not significantly impede effective competition in the internal market with respect to the out-of-home coffee markets.

Parties' arguments

(605) The Parties submit that the Transaction would not raise competition concerns in the out-of-home market mainly due to their low combined market shares and presence of considerable number of competitors. According to the Parties, each of the elements provided in an out-of-home solution (the coffee, other consumables, coffee machine, crockery and services) can be sourced from one or multiple suppliers and the regular delivery of ingredients can be made directly by the supplier or can be made through the preferred logistical provider of the customer.

(606) Furthermore the Parties argue that most customers will have an informal buying process, where they discuss their needs and preferences with sales representatives from their current supplier and from other suppliers. Each supplier will assess the needs of the customer and propose a solution from its portfolio of products and machines. Given the range of possible options and the different specialities of suppliers, the customer is rarely choosing between like-for-like propositions.

Commission's investigation and assessment

(607) In the out-of-home market, the proposed Transaction will give rise to affected markets in (i) Denmark, with a combined market share of [20-30]*% (with an increment of [5-10]*%); (ii) Germany, with a combined market share of [20-30]*% (with an increment of [5-10]*%); (iii) Sweden, with a combined market share of [30-40]*% (with an increment of [5-10]*%); and (iv) the United Kingdom, with a combined market share of [20-30]*% (with an increment of [0-5]*%).

(608) The main competitors of the Parties in the out-of-home market include Nestlé (present in Sweden and the United Kingdom), as well as regional players, such as Tchibo, Dallmayr, BKI, Frelsen and Löfberg Lila. The majority of competitors responding to the market investigation confirmed that each offer is tailored to the specific needs of the customer and those needs vary across customer sectors and also among customers in the same sector.⁴¹⁴

(609) As regards the competitive landscape in the out-of-home market, the Commission acknowledges that several competitors would continue to be present following the Transaction.

(610) With regards to multi-sourcing, the competitors responding to the market investigation gave mixed results on whether their customers would source from multiple suppliers at the same time. Among the customers who responded to the

⁴¹³ Nestlé internal document dated 15 April 2014 "Coffee & machine market shares" non-confidential version page 11-12 and Nestlé internal document dated 15 April 2014 "A focus on: Jacobs Douwe Egberts" non-confidential version page 17-19. of 2 March 2015.

⁴¹⁴ Responses to question 10, 11 and 12 of the Questionnaire Q4 –Competitors.

market investigation, the vast majority confirmed to multi-source either the same product or different out-of-home products.⁴¹⁵

- (611) Concerning the way contracts are awarded in the out-of-home market, the competitors responding to the market investigation gave mixed results on whether it is by call for tender or through individual negotiation. The majority of customers who responded to the market investigation indicated a clear tendency towards engaging a negotiation process.⁴¹⁶
- (612) The replies to the market investigation indicated that for both competitors and customers the main competition drivers among out-of-home suppliers are price and quality.⁴¹⁷
- (613) Both some customers and some competitors raised initial concerns about the impact of the proposed Transaction on competition in the out-of-home market⁴¹⁸ in view of the Parties' combined market share and in view of the strong brand that would form part of the JV's portfolio.
- (614) The Commission contacted the relevant market participants and after further investigation it became apparent that also after the Transaction, there would be a sufficient number of relevant alternative suppliers in all the affected markets.⁴¹⁹

Conclusion

- (615) Taking into account the overall market investigation, the strong presence of several competitors in each of the affected markets, the relatively small market share in certain affected markets and the little increment brought about in some other affected markets, the Commission considers that the Transaction would not significantly impede effective competition in the internal market with respect to the out-of-home coffee markets.

9.10. Potential conglomerate effects

- (616) For the reasons presented in this Section, the Commission considers that the proposed Transaction is not likely to lead to foreclosure of competitors as a result of the Parties' enlarged portfolio.
- (617) According to previous Commission's decisions conglomerate effects might arise from the Parties' significant portfolio of brands and the fact that they have significant market shares in numerous product markets where their activities do not overlap.⁴²⁰
- (618) It is proposed that the JV would own a number of 'must-have' brands in the various coffee markets. The Commission has therefore examined whether following the Transaction the JV would be able to impose weak brands on the retailers and

⁴¹⁵ Responses to question 16 of the Questionnaire Q3 –Customers and responses to question 16 of the Questionnaire Q4 – Competitors.

⁴¹⁶ Responses to questions 18 et seq of the Questionnaire Q3 –Customers and responses to question 18 et seq. of the Questionnaire Q4 – OOH Competitors.

⁴¹⁷ Responses to question 19 of the Questionnaire Q3 –Customers and responses to question 19 of the Questionnaire Q4 – Competitors.

⁴¹⁸ Responses to question 26 of the Questionnaire Q3 – Customers and responses to question 29 of the Questionnaire Q4 – Competitors.

⁴¹⁹ Non-confidential minutes from a follow up calls with out-of-home customers from 18 to 21 November 2014.

⁴²⁰ See for example, M.3732 Procter &Gamble/Gillette, paragraphs 110 – ff.

therefore foreclose competitors from access to limited shelf space using bundling practices.⁴²¹

- (619) First of all, the Commission observes that being active with a portfolio of various coffee products is not a particularity of the Parties, but their competitors also follow the same strategy. In particular Nestlé is active not only with its single-serve systems and their consumables but is also strong in instant markets; Tchibo is present and strong not only in R&G but also in instant coffee and in some countries in filter pads; Lavazza is present in R&G and N-capsules; BKI and Peter Larsen are present in R&G and instant.
- (620) With the exception of one German retailer, no other retailer in the course of market investigation raised concerns resulting from the JV having a wide portfolio of brands and coffee products. As regards Germany, it should be noted that the position of retailers in coffee products in Germany is somewhat stronger as compared with other EEA countries. In particular combined private label brands are the strongest player in the R&G market (with a share of [20-30]*%, followed by Tchibo with [20-30]*%), filter pads market (with a share of almost [50-60]*%, followed by the JV with [20-30]*%) and instant coffee market (with a share of [40-50]*%, followed by Nestlé with [20-30]*%). As a result in particular in Germany the retailers are likely to have an ability and incentive to mitigate any portfolio effects that could result from the proposed Transaction.
- (621) It also appears that at least retailers in France, Greece, some in Germany and in the Netherlands actually negotiate each of the coffee products (that is to say R&G, instant etc.) separately.⁴²² Furthermore an overwhelming majority of retailers who responded to the Commission's questionnaire stated that while negotiating with their coffee product suppliers, it does not make a significant difference that those suppliers have a broader portfolio covering many coffee brands and formats, since "*each product is important and plays its own role*",⁴²³ or covering other product categories.⁴²⁴ Some of the retailers clearly stated that it is the market share of a given brand which is more important than the breadth of the supplier's portfolio and therefore brands are more significant than the portfolio.⁴²⁵ Therefore it seems unlikely that the JV would be able to impose its weak brands on the retailers in order to occupy more shelf space and foreclose its competitors by bundling practices.
- (622) Consequently the Transaction is not likely to lead to foreclosure of competitors as a result of the JV's enlarged portfolio.

10. CONCLUSION ON THE TRANSACTION'S COMPATIBILITY WITH THE INTERNAL MARKET

- (623) The Commission considers that the Transaction leads to a significant impediment to effective competition, in particular through the creation of a dominant position, in the following markets:
- (a) R&G market in France, Denmark and Latvia;
 - (b) Filter pads market in France and Austria.

⁴²¹ *Ibidem*, par. 115 – ff.

⁴²² Responses to question 10 of Questionnaire Q2- Retailers.

⁴²³ Responses to question 52 of Questionnaire Q2- Retailers.

⁴²⁴ Responses to question 53 of Questionnaire Q2- Retailers.

⁴²⁵ Responses to question 52 of Questionnaire Q2- Retailers.

11. MODIFICATIONS TO THE TRANSACTION

11.1. Framework for the Commission's assessment of commitments

- (624) Where a concentration raises serious doubts as to its compatibility with the internal market, the Parties could undertake to modify the concentration so as to remove the grounds for the serious doubts identified by the Commission with a view to having the Notified Transaction approved in phase I of the merger review procedure. In this respect, the Commission has the power to accept commitments provided that they will remove the grounds for serious doubts.
- (625) As set out in the Commission's Remedies Notice,⁴²⁶ the commitments have to eliminate the competition concerns entirely⁴²⁷ and have to be comprehensive and effective from all points of view.⁴²⁸
- (626) In assessing whether commitments will maintain effective competition, the Commission considers all relevant factors including, *inter alia*, the type, scale and scope of the proposed commitments, judged by reference to the structure and particular characteristics of the market in which the competition concerns arise, including the position of the Parties and other participants on the market.⁴²⁹
- (627) In order for the commitments to comply with those principles, they must be capable of being implemented effectively within a short period of time.⁴³⁰ Where, however, the Parties submit proposals for remedies that are so extensive and complex that it is not possible for the Commission to determine with the requisite degree of certainty, at the time of its decision, that they will be fully implemented and that they are likely to maintain effective competition in the market, an authorisation decision cannot be granted.⁴³¹
- (628) Concerning the form of acceptable commitments, the Regulation (EC) No 139/2004 gives discretion to the Commission as long as the commitments meet the requisite standard.⁴³² Structural commitments will meet the conditions set out in Recitals (623) to (625) only in so far as the Commission is able to conclude with the requisite degree of certainty that it will be possible to implement them and that it will be likely that the new commercial structures resulting from them will be sufficiently workable and lasting to ensure that effective competition will be maintained.⁴³³ Divestiture commitments are generally the best way to eliminate competition concerns resulting from horizontal overlaps, although other structural commitments, such as access remedies, may be suitable to resolve concerns if those remedies are equivalent to divestitures in their effects.⁴³⁴

⁴²⁶ Commission Notice on remedies acceptable under Council Regulation (EEC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (OJ C 267, 22.10.2008, p. 1-27).

⁴²⁷ See also Case C-202/06 P *Cementbouw Handel & Industrie v Commission* [2007] ECR 2007 I-12129, paragraph 54.

⁴²⁸ Remedies Notice, paragraphs 9 and 61.

⁴²⁹ Remedies Notice, paragraph 12.

⁴³⁰ Remedies Notice, paragraph 9.

⁴³¹ Remedies Notice, paragraphs 13, 14 and 61 *et seq.*

⁴³² Case T-177/04 *easyJet v Commission* [2006] ECR II-1913, paragraph 197.

⁴³³ Remedies Notice, paragraph 10.

⁴³⁴ Remedies Notice, paragraph 19.

11.2. Process

- (629) To address the competition concerns identified by the Commission, the Notifying Parties submitted commitments on 24 November 2014 and revised them on 26 November 2014 ('the Commitments of 26 November 2014').
- (630) After the Commission decided to open proceedings, the Notifying Parties submitted new commitments on 23 February 2015 ('the Commitments of 23 February 2015'). Having received feedback from the Commission on its assessment of the Commitments of 23 February 2015, including the results of the market test, the Parties submitted final commitments on 20 March 2015 ('the Final Commitments').

11.3. Commitments of 26 November 2014

11.3.1. Description of the Commitments of 26 November 2014

- (631) The Commitments of 26 November 2014 included measures relating to the coffee markets in (i) France ('the French Divestment Businesses of 26 November 2014'), (ii) Denmark and Latvia ('the Danish and Latvian Divestment Business of 26 November 2014'), and (iii) Austria (the 'Austrian Licence of 26 November 2014').

11.3.1.1. French Divestment Businesses of 26 November 2014

- (632) The French Divestment Businesses of 26 November 2014 would have consisted of the divestment of (i) the business DEMB currently operates under the brand L'Or (including R&G, N-capsules, filter pads and instant coffee) in the EEA, with the exception of the L'Or out-of-home business, and (ii) the business that Mondelez currently operates under the brand Grand'Mère (including R&G, filter pads and instant coffee) in the EEA, with the exception of Grand'Mère Tassimo T-discs and the Grand'Mère out-of-home business.
- (633) The French Divestment Businesses of 26 November 2014 would also have included various tangible and intangible assets, relevant personnel, as well as DEMB's Andrézieux manufacturing plant, including, at the expiry of the re-configuration period, the necessary number of roasters and manufacturing lines as well as all necessary licences, permits and authorisations to support both the current level of operations and the expansions envisaged in DEMB's business plan. Various transitional support arrangements were also envisaged, in particular to take account of the re-configuration period, such as manufacturing and packing L'Or and Grand'Mère products for the purchaser.
- (634) For products excluded from the French Divestment Businesses of 26 November 2014 but currently marketed under the brands to be divested, such as out-of-home products, the purchaser would have been required to grant the Parties and the joint venture a one-year transitional licence for the purpose of rebranding.

11.3.1.2. Danish and Latvian Divestment Business of 26 November 2014

- (635) The Danish and Latvian Divestment Business of 26 November 2014 would have consisted of the divestment of the business DEMB currently operates under the brand Merrild in the EEA, with the exception of the Merrild out-of-home business and certain Café Noir and Senseo-products that are primarily marketed under those brands. The in-home products marketed under the Merrild brand are primarily R&G and instant coffee, but there are also filter pads that carry primarily the Merrild brand and those would have been included in the divestment.

- (636) With respect to the excluded products, such as the Merrild out-of-home products, the purchaser would have been required to grant the Parties and the joint venture a one-year transitional licence for the purpose of rebranding.
- (637) In addition, the Danish and Latvian Divestment Business of 26 November 2014 would have included a number of transitional measures aimed at supporting the purchaser in starting operating the divestment business, such as co-manufacturing of the Merrild products for a transitional period on a reasonable cost-plus basis.

11.3.1.3. Austrian Licence of 26 November 2014

- (638) The Austrian Licence of 26 November 2014 would have consisted of granting a three-year exclusive licence for the use of the DEMB brand Senseo for filter pads and N-capsules sold to in-home customers in Austria.
- (639) That licence would have been followed by a two year black-out period for the Notifying Parties and the joint venture. During that black-out period neither the Notifying Parties nor the joint venture would have been permitted to use the Senseo brand for filter pads or N-capsules sold to in-home customers in Austria.
- (640) In addition, the Austrian Licence of 26 November 2014 would have included a number of transitional measures aimed at supporting the purchaser in starting operating the licence and the rebranding exercise, such as co-manufacturing of the Senseo filter pads and N-capsules on a reasonable cost-plus basis.

11.3.2. *Assessment of the Commitments of 26 November 2014*

11.3.2.1. French Divestment Businesses of 26 November 2014

- (641) The Commission launched a market test on the French Divestment Businesses of 26 November on 26 and 27 November 2014.
- (642) The results of the market test indicated that (i) while the French Divestment Businesses of 26 November 2014 seemed, subject to further improvements, to address the competition concerns identified by the Commission in the R&G coffee market in France, they (ii) failed to sufficiently address the competition concerns in the market for filter pads in France.
- (643) The Commission found that the French Divestment Businesses of 26 November 2014 would have removed all the overlap brought about by the Transaction with respect to R&G coffee in France. However, the businesses to be divested would only have had a very small market share in filter pads, leading to a marginal impact on the market. As a result, and in light of the results of the market test, the purchaser would most likely not have been able to establish itself as a viable competitor in filter pads in France and the remedy would thus have been insufficient to dispel the competition concerns identified for this market.

11.3.2.2. Danish and Latvian Divestment Business of 26 November 2014

- (644) The Commission launched a market test on the Danish and Latvian Divestment Business of 26 November 2014 on 26 and 27 November 2014.
- (645) The results of the market test were generally positive. For instance, the majority of respondents considered that the remedy was suitable to remove the competition concerns and that the purchaser would be able to effectively compete on the markets

on a lasting basis.⁴³⁵ The majority of respondents taking a position during the market investigation also considered the Danish and Latvian Divestment Business of 26 November 2014 as capable of attracting suitable purchasers.⁴³⁶

- (646) Negative comments were mainly voiced by one competitor who also viewed, for instance that the divestment would not be interesting due to a declining R&G market.⁴³⁷ Negative comments were also made by competitors concerning the transitional services, such as the ‘cost-plus’ basis for transitional co-manufacturing services.⁴³⁸
- (647) The Commission found that the Danish and Latvian Divestment Business of 26 November 2014 would remove more than the overlap in R&G coffee in Denmark and Latvia as Merrild’s 2014 market share (Denmark: [20-30]*%, Latvia: [20-30]*%) was higher than the market share increment brought about by the Transaction (Denmark: [10-20]*%, Latvia [10-20]*%). Therefore it would have likely been able to, *prima facie*, remove the competition concerns in the markets in question.
- (648) The Danish and Latvian Divestment Business of 26 November 2014 included not only R&G coffee, where competition concerns had been identified by the Commission, but instant coffee and filter pads as well. The commitment therefore went beyond what would be strictly necessary to remove the impediment to effective competition while giving the purchaser the ability to compete with a wider product portfolio. The Commission considers this to significantly improve the viability and attractiveness of the divestment business. Even if the different coffee consumables constitute distinct product markets, being able to offer retailers a wide range of products increases brand visibility. Moreover, cost-synergies may be gained in brand promotion and marketing.
- (649) The Commission noted that the Merrild brand is a well-established brand that generates a notable turnover in Denmark and Latvia. Respondents to the market investigation also did not point to factors that would have called the divestment’s suitability into question.
- (650) The purchaser’s ability to start operations immediately after taking over the brand would be supported by the Notifying Parties and the joint venture through the provision of transitional co-manufacturing services. While such services would inevitably create a link and a certain level of dependency between the purchaser and the Parties or the joint venture, such effects, which are not expected to be permanent, are inherent to those types of transitional services and a Monitoring Trustee would be in place to supervise the relationship.
- (651) In light of the above, the Commission concluded that the Danish and Latvian Divestment Business of 26 November 2014 would be capable of removing the competition concerns identified by the Commission in the markets for R&G coffee in Denmark and Latvia as such.

⁴³⁵ Responses to questions 1–3 of the Questionnaire Q6 Denmark; and responses to questions 1–3 of the Questionnaire Q7 Latvia.

⁴³⁶ Responses to question 24 of the Questionnaire Q6 Denmark; and responses to question 24 of the Questionnaire Q7 Latvia.

⁴³⁷ See, e.g. responses to question 1 of the Questionnaire Q6 Denmark; and responses to question 1 of the Questionnaire Q7 Latvia.

⁴³⁸ See, e.g. responses to questions 9, 12, 21, 23 and 24 of the Questionnaire Q6 Denmark; and responses to questions 16, 21, 23 and 25 of the Questionnaire Q7 Latvia.

- (652) However, the fact that the transitional services were to be provided at a ‘cost-plus’ basis was considered to potentially hamper the ability of the purchaser to be competitive in the market. The arrangement might effectively result in a double margin problem which could only be fully avoided if the purchaser forewent its margin. The problem is aggravated in the present case by the fact that the Parties or the joint venture would be supplying the purchaser with finished goods. Consequently, the purchaser would not be engaged in any production that would add any value to those products.
- (653) As the Danish and Latvian Divestment Business of 26 November 2014 would not have included production facilities, the viability of the business would inherently have required that the purchaser had access to suitable production capacity after the transitional period during which the Notifying Parties and the joint venture would be obliged to provide the co-manufacturing service.

11.3.2.3. Austrian Licence of 26 November 2014

- (654) The Commission launched a market test on the Austrian Licence of 26 November 2014 on 27 November 2014.
- (655) The results of the market test were mixed. While the majority of respondents submitted that the remedy was suitable to remove competition concerns,⁴³⁹ a number of respondents also questioned the viability or details of the licence.
- (656) Nestlé was particularly negative of the Austrian Licence, suggesting that a Senseo licence without the Senseo brewing machines was insufficient and unviable as a remedy. Nestlé also submitted that the purchaser’s ability to compete would depend on the joint venture’s goodwill in developing the Senseo machines and that there could be confusion among consumers.⁴⁴⁰ In addition, other market participants also expressed doubts, for instance, in relation to the risks related to re-branding and the ‘cost-plus’ basis at which the transitional services, such as co-manufacturing, were to be provided to the purchaser by the Parties or the joint venture.⁴⁴¹
- (657) While respondents to the market investigation were generally sceptical about the attractiveness of the Austrian Licence of 26 November 2014, one market participant expressed its interest in acquiring the licence.⁴⁴²
- (658) The Commission found that the Austrian Licence of 26 November 2014 would have removed all the overlap brought about by the proposed Transaction. Therefore, it could *prima facie*, have removed the competition concerns identified by the Commission in the market for filter pads in Austria. However, in light of the results of the market test, the Commission considered that the licence would likely be viable and attractive only subject to further improvement.

11.4. Commitments of 23 February 2015

11.4.1. Description of the Commitments of 23 February 2015

- (659) The Commitments of 23 February 2015 include three measures: (i) the divestment of the brand Merrild in the EEA (‘the Merrild Divestment Business’), (ii) the divestment of the brand Carte Noire in the EEA (‘the Carte Noire Divestment Business’) and (iii) a licence of the Senseo brand in Austria (‘the Austrian Licence’).

⁴³⁹ Responses to question 1 of the Questionnaire Q8 Austria.

⁴⁴⁰ See, e.g. responses to questions 1–4 and 7–10 of the Questionnaire Q8 Austria.

⁴⁴¹ See, e.g. responses to questions 2, 6 and 10 of the Questionnaire Q8 Austria.

⁴⁴² Responses to questions 18 and 19 of the Questionnaire Q8 Austria.

11.4.1.1. Merrild Divestment Business

- (660) The Merrild Divestment Business aims at remedying the competition concerns identified by the Commission in the R&G coffee markets in Denmark and Latvia. It is identical to the divestment offered as part of the Commitments of 26 November 2014 ('Danish and Latvian Divestment Business of 26 November 2014').

11.4.1.2. Carte Noire Divestment Business

- (661) The Carte Noire Divestment Business aims at remedying the competition concerns identified by the Commission in the R&G coffee and filter pad markets in France. It consists of the divestment of the business currently operated in the EEA by Mondelēz under the brand Carte Noire, including in-home R&G coffee, filter pads and N-capsules – but excluding instant coffee, Tassimo T-discs and out-of-home products as well as the related Velours Noir brand. The purchaser would be required to grant a transitional licence-back for the excluded products in favour of the Notifying Parties and the joint venture for the purpose of allowing them to rebrand those products. The duration of the licence would be one year for the Velours Noir products and two years for the other excluded products.
- (662) The divestment would further include Mondelēz' Lavérune production facility that, after a reconfiguration period of 18 months, would house the production lines currently primarily employed in the manufacture of Carte Noire R&G, filter pads and N-capsules, including production lines currently located at other factories. The Notifying Parties or the joint venture would also provide the purchaser with certain transitional services, including the manufacturing of products not at present produced at the Lavérune facility, on a 'reasonable cost-plus' basis. During the reconfiguration period, production lines employed in the production of other than divested products would be removed from the Lavérune site.
- (663) The Carte Noire Divestment Business would only include those IP rights currently owned by Mondelēz and would therefore not cover all the IP rights required to produce Carte Noire N-capsules as Mondelēz does not own all those rights. Instead, the Notifying Parties would have committed to making all reasonable efforts to facilitate a licence between the proprietor of the technologies, an Italian company Tuttoespresso S.r.l, and the purchaser at terms no less favourable than those currently enjoyed by Mondelēz.

11.4.1.3. Austrian Licence

- (664) The Austrian Licence aims at remedying the competition concerns identified by the Commission in the filter pads market in Austria. It consists of a five-year exclusive licence for the Senseo brand for use in filter pads and N-capsules, during which period the purchaser can re-brand the products.
- (665) The five-year licence period would be followed by a five-year black-out period during which the Notifying Parties and the joint venture would be barred from using the Senseo brand for the sale of filter pads or N-capsules to in-home customers in Austria.
- (666) The Austrian Licence has been developed from the one offered as part of the Commitments of 26 November 2014 by lengthening the duration of both the licence period (from three to five years) and the following black-out period (from two to five years), and by including express obligations for the Notifying Parties and the joint venture to facilitate direct contacts and cooperation between the purchaser and Philips to allow joint planning between them for support of the Senseo brewer park in Austria.

11.4.2. Assessment of the Commitments of 23 February 2015

11.4.2.1. Merrild Divestment Business

- (667) The Commission had launched a market test on the Commitments of 26 November 2014, including the divestment of the Merrild brand ('the Danish and Latvian Divestment Business'), on 26 and 27 November. As the Merrild Divestment Business offered as part of the Commitments of 23 February 2015 was identical to the one offered and market-tested as part of the Commitments of 26 November 2014, the Commission did not launch a new market test on it during Phase II.
- (668) A detailed assessment of the Merrild Divestment Business is included under the heading 11.3.2 "11.3.2. Assessment of the Commitments of 26 November 2014".
- (669) The Commission concluded that the Merrild Divestment Business would constitute a viable and competitive business that would be able to compete effectively with the Notifying Parties and the joint venture in the market for R&G coffee in Denmark and Latvia, subject to the transitional services and, in particular, the co-manufacturing being offered to the purchaser at a price level that does not hamper the purchaser from establishing itself on the market.

11.4.2.2. Carte Noire Divestment Business

Results of the market test

- (670) The Commission launched a market test on the Carte Noire Divestment Business on 25 February 2015.
- (671) The market test was generally positive. The majority of respondents considered that the remedy was suitable to remove the competition concerns and that the purchaser would be able to effectively compete on the markets on a lasting basis.⁴⁴³
- (672) However, market participants commented particularly on (i) the uncertainty of acquiring the required N-capsules technologies from their third-party proprietor, (ii) the 'cost-plus' basis for the transitional services and (iii) the exclusion of the Velour Noir brand and excluded Carte Noire products from the remedy. Negative comments were made primarily by two competitors. In particular Nestlé submitted that the divestment should be "coupled with the sale of a portion coffee system"⁴⁴⁴, including both the machine and the corresponding pods".⁴⁴⁵ In Nestlé's view, the Commitments of 23 February 2015 fail to address competition concerns on the level of single-serve systems.
- (673) The lack of the divestment of the N-capsules technologies received negative feedback from a number of competitors, submitting that without the technology the purchaser would not be able to compete efficiently, if at all, in N-capsules. The requirement for the Notifying Parties or the joint venture to make all reasonable efforts to procure a licence between the proprietor of the relevant technologies and the purchaser was considered inadequate.⁴⁴⁶

⁴⁴³ Responses to questions 1–3 of the Questionnaire Q14 France – Retailers; and responses to questions 1-3 of the Questionnaire Q16 France – Competitors.

⁴⁴⁴ That is single-serve system.

⁴⁴⁵ See, e.g. responses to question 1 of the Questionnaire Q16 France – Competitors.

⁴⁴⁶ Responses to questions 3, 5 and 6 of the Questionnaire Q16 France – Competitors.

- (674) Some competitors also questioned whether the ‘cost-plus’ basis for the transitional services would enable the purchaser to establish itself as a viable and effective competitor to the Notifying Parties and the joint venture. Other market participants nonetheless also commented that such terms are acceptable as long as they are in line with market standards.⁴⁴⁷
- (675) Two competitors considered that the Velours Noir brand related to the Carte Noire brand should be included in the remedy.⁴⁴⁸ Two competitors also commented negatively on the exclusion of certain Carte Noire products, such as out-of-home products.⁴⁴⁹
- (676) No customer commented negatively on the exclusion of the Velours Noir or excluded Carte Noire products during the market test.
- (677) Finally, the majority of competitors taking a position replied that they would be interested in acquiring the Carte Noire Divestment Business⁴⁵⁰ and all of the customers replying considered that a suitable purchaser will likely be found⁴⁵¹.

Commission’s assessment

- (678) The Commission finds that the Carte Noire Divestment Business would remove more than the overlap brought about by the Transaction in R&G and would remove almost all of the overlap in relation to filter pads (R&G: Carte Noire’s market share [20-30]*%, overlap [10-20]*%; filter pads: Carte Noire’s market share [10-20]*%, overlap [10-20]*%, all in 2014). The Carte Noire Divestment Business would therefore be able to remove the competition concerns in the markets concerned.
- (679) The Commission further notes that the Carte Noire brand is a well-established and successful brand in France and together with the related production assets and IP rights appears to be capable of being a self-standing business.
- (680) The Carte Noire Divestment Business includes not only R&G coffee and filter pads, where competition concerns have been identified by the Commission, but also N-capsules. The commitment therefore goes beyond what would be strictly necessary to remove the impediment to effective competition in order to enable the purchaser to effectively compete with the Parties through a wider product portfolio. The Commission considers, however, that this is necessary to ensure the viability and attractiveness of the divestment business. Even if the different coffee consumables constitute distinct product markets, being able to offer retailers a wide range of products increases brand visibility and may provide for cost-synergies in brand promotion and marketing. The addition of a product such as N capsules that are growing at a high pace and provide a high margin also contribute to the viability and attractiveness of the divestment business.
- (681) The Commission nonetheless notes that, whilst ensuring that the Purchaser is able to offer a wide variety of products is key to improve the viability of the divested business, it is not necessary to include *all* different coffee consumables and formats in the remedy package to ensure that the purchaser of the Carte Noire brand obtains the benefits related to a wide product range. For instance, Tassimo T-discs have not been offered by brands other than Mondelēz’ but that has not prevented other

⁴⁴⁷ Responses to questions 13 and 19 of the Questionnaire Q16 France – Competitors.

⁴⁴⁸ Responses to questions 1, 2, 14 and 24 of the Questionnaire Q16 France – Competitors.

⁴⁴⁹ Responses to questions 1, 14, 23, 24, 30 and 32 of the Questionnaire Q16 France – Competitors.

⁴⁵⁰ Responses to question 31 of the Questionnaire Q16 France – Competitors.

⁴⁵¹ Responses to question 15 of the Questionnaire Q14 France – Retailers.

competitors, such as DEMB or Nestlé, from being successful in the French (and other) coffee markets with their brands. Moreover, Nestlé is not at all present in R&G but it has been very successful in instant coffee with its Nescafe brand.

- (682) In particular, the Commission does not consider that the exclusion of the Velours Noir brand, which has a very limited presence in the French market for R&G coffee products, would hamper the viability and effectiveness of the divestment business or otherwise give rise to unacceptable risks of customer confusion.
- (683) Currently, the Velours Noir packages carry an endorsement from Carte Noire in the form of a label stating, e.g. ‘created by Carte Noire’. Velours Noir is a self-standing brand and Carte Noire merely plays the role of an umbrella brand with respect to Velours Noir. The proposed divestment would include a one-year licence to the Parties and the JV to enable them to remove *inter alia* those endorsements from the Velours Noir products.
- (684) Therefore, considering the small size of the Velours Noir brand and the short time period available for the Notifying Parties and the joint venture to carry out the rebranding (one year), it is also unlikely that the arrangement proposed by the Notifying Parties with respect to Velours Noir would result in significant confusion among consumers.
- (685) As to the other excluded Carte Noire products, such as the out-of-home and Tassimo T-discs, the proposed divestment would include a two-year licence to the Notifying Parties and the joint venture for the purpose of rebranding.
- (686) The two-year rebranding period for the excluded Carte Noire products is unlikely to give rise to significant consumer confusion. The rebranding period is limited in time and the rebranding concerns only a limited part of the in-home Carte Noire products while the market characteristics between in-home and out-of-home products are significantly different. This finding is also supported by the fact that no customers raised the issue in the market test.
- (687) With regard to Nestlé’s claim that the divestment should include single-serve systems, it is sufficient to recall that following its market investigation, the Commission found that the Transaction would not lead to a significant impediment to effective competition in respect of single-serve systems. As such, no remedy is necessary in this respect.
- (688) Moreover, the fact that the remedy does not come with a divestment of the single-serve machines in which the filter pads are used cannot render the divestment business unviable or ineffective. It is adequate to recall in this respect that the Carte Noire brand in filter pads is already at present separate from the Senseo brand under which the brewers are marketed and the owners of the two brands are also different. However, that has not prevented Carte Noire from establishing itself in the filter pads market.
- (689) As commented by some market participants in the market test, the Carte Noire Divestment Business would not include the necessary IP rights for the production of N-capsules as Mondelēz only licenses the technologies from their third-party proprietor.
- (690) The purchaser could theoretically access the technologies in two ways: either through a sub-licence from Mondelēz, or through a direct licence from the proprietor of the technology. Mondelēz currently has an exclusive worldwide licence though with some exclusions. The licence agreement prohibits sub-licensing to third parties.

- (691) Given that the technology is likely crucial for the ability of the purchaser to produce N-capsules, the Commission considers that the mere obligation for the Parties and the JV to take all reasonable actions to procure the licence between the purchaser and the third-party proprietor would likely not be adequate in the present case. This finding is supported by the comments made by a number of competitors in the market test.
- (692) The Carte Noire Divestment business would come with the Lavérune production plant where the Carte Noire products are primarily produced. Some production lines are located elsewhere, and they would be relocated to the Lavérune plant during the reconfiguration period, which would also see non-Carte Noire production lines removed from the plant. The Commission considers that concentrating the production in one location can best provide for economies of scale in the present case. According to information provided by the Notifying Parties, the Lavérune facility has adequate capacity and space available for housing all the present, and increased, production of the divested Carte Noire products. The Monitoring Trustee will supervise the reconfiguration to limit risks related to, for example, interruptions and production efficiencies.
- (693) The purchaser's ability to start full operations without unnecessary delay is supported by the Notifying Parties or the joint venture providing the purchaser certain transitional services, including manufacturing of those Carte Noire products that are not currently produced at the Lavérune production facility. While such services inevitably create a link and a certain level of dependency between the purchaser and the Notifying Parties or the joint venture, such effects are temporary (limited to 18 months) and a Monitoring Trustee will be in place to supervise the relationship.
- (694) However, the fact that the transitional services are provided at 'cost-plus' basis might affect negatively the ability of the purchaser to be competitive in the market. The arrangement may effectively result in a double margin problem which could only be fully avoided if the purchaser forewent its margin. The problem is aggravated in the present case by the fact that the Parties or the JV joint venture would be supplying the purchaser with finished goods, the purchaser not making any value-adding production on them.
- (695) In light of the above, the Commission concludes that the Carte Noire Divestment Business will constitute a viable and competitive business that will be able to compete effectively with the Parties and the JV in the markets for R&G coffee and filter pads in France, subject to (i) the transitional services and, in particular the co-manufacturing being offered to the purchaser at a price level that does not hamper the purchaser establishing itself on the market and (ii) increased level of certainty concerning the purchaser's access to the relevant N-capsules technologies.

11.4.2.3. Austrian Licence

Results of the market test

- (696) The Commission launched a market test on the Austrian Licence on 25 February 2015.
- (697) The market test was generally positive. Many market respondents taking a position considered that the remedy was suitable to remove the competition concerns and that its effectiveness, viability and workability had been improved from the Commitments of 26 November 2014 so as to enable the licensee to effectively

compete.⁴⁵² A majority of market participants taking a position also replied that the licence and black-out periods would be sufficient or at least the minimum required, even if not all respondents shared this view.⁴⁵³

- (698) Negative comments were voiced in the market investigation mainly by two competitors. In particular, Nestlé considered that a divestment, including the divestment of the Senseo machines and a production plant for consumables, would have been required instead of a licence for the remedy to be effective and in order to avoid risks associated with re-branding. The same respondent also called for the divestment to cover the whole EEA instead of only Austria, for instance because of economies of scale and the avoidance of confusion among consumers.⁴⁵⁴ Another competitor also viewed that the licence would need to be Union-wide.⁴⁵⁵
- (699) Two market participants replied they would be interested in acquiring the Austrian Licence, one at the conditions offered by the Parties and another one on condition that the remedy was further developed with regard, for instance to the purchaser being able to fully control key variables such as pricing.⁴⁵⁶

Commission's assessment

- (700) The Commission found that the Austrian Licence would remove all the overlap in filter pads in Austria as Senseo's market share ([30-40]*% in 2014) equals the market share increment brought about by the Transaction. The Austrian Licence would therefore *prima facie* be able to remove the competition concerns in the markets concerned.
- (701) The Austrian Licence includes not only filter pads, where competition concerns have been identified by the Commission, but also N-capsules. The commitment therefore goes beyond what would be strictly necessary to remove the competition concerns while giving the purchaser the ability to compete with a wider product portfolio. The Commission considers this to significantly improve the viability and attractiveness of the licence. Even if the different coffee consumables constitute distinct product markets, being able to offer retailers a wide range of products increases brand visibility. Moreover, cost-synergies may be gained in brand promotion and marketing.
- (702) The Commission notes that while structural remedies are often preferable, other types of commitments may also be capable of preventing a significant impediment to effective competition.⁴⁵⁷ The Commission further notes that the commitments should not only remove the competition concern but be proportionate to it as well.⁴⁵⁸
- (703) The Austrian Licence is essentially a re-branding remedy. Such remedies may be acceptable in circumstances where the brand at stake is widely used and a high proportion of its turnover is generated in markets outside those in which competition

⁴⁵² Responses to questions 1–3 of the Questionnaire Q13 Austria – Retailers; and responses to questions 1–3 of the Questionnaire Q15 Austria – Competitors.

⁴⁵³ Responses to questions 4 and 5 of the Questionnaire Q13 Austria – Retailers; and responses to questions 4 and 5 of the Questionnaire Q15 Austria – Competitors.

⁴⁵⁴ Responses to questions 1–11 of the Questionnaire Q15 – Competitors.

⁴⁵⁵ Responses to question 5 of the Questionnaire Q15 Austria – Competitors.

⁴⁵⁶ Responses to questions 2, 3 and 16 of the Questionnaire Q15 Austria – Competitors.

⁴⁵⁷ See, e.g. paragraphs 15 and 61 of the Remedies Notice.

⁴⁵⁸ See, e.g. recital 30 of the Regulation (EC) No 139/2004 and paragraph 85 of the Remedies Notice.

concerns have been identified.⁴⁵⁹ In such circumstances it could be disproportionate to require that the whole brand is divested.

- (704) In the present case, the Senseo brand is employed by DEMB in the sale of filter pads in a number of EEA countries. In 2013, the turnover accumulated by DEMB through the sale of Senseo-branded filter pads in Austria was EUR [...]*, which was approximately only [0-5]*% of the respective EEA turnover of EUR [...]*. The vast majority of the turnover is therefore generated in markets outside the filter pads market in Austria.
- (705) The Notifying Parties are also active in the market for filter pads in Austria with Mondelēz' brand Jacobs. The turnover generated by Mondelēz through the sale of Jacobs-branded filter pads in Austria in 2013 was EUR [...]*, which was only [0-5]*% of the total EEA turnover of the brand in 2013, EUR [...]* (including all coffee formats). The proportion of turnover generated outside the filter pads market in Austria is therefore even higher than for DEMB's Senseo brand.
- (706) The Commission therefore considers that an EEA-wide measure would be disproportionate to the competition concern in the filter pads market in Austria.
- (707) In assessing the suitability of the Austrian Licence as a remedy, the Commission has taken into account factors pertaining to the likelihood of the purchaser being able to establish itself as an active competitor in the market. To this effect, it should first be noted that the brand to be transferred enjoys the second largest market share in the Austrian filter pads market and is widely-known. The Austrian Licence also includes measures related to production and marketing that would support the purchaser in establishing itself in the market, such as IP-rights related to the production and marketing of the products.
- (708) The fact that the licence does not come with a divestment of the brewer machines in which the filter pads are used cannot render the divestment business unviable or ineffective. It is sufficient to recall that filter pads are sold in Austria by a number of competitors with brands unrelated to the Senseo brand. For instance, Mondelēz is – independently of DEMB – present in the market with the brand Jacobs and has been able to achieve in 2014 a market share clearly in excess of the market share DEMB reached with the Senseo-branded filter pads.
- (709) The Austrian Licence would result in a situation where the Senseo-brand is controlled by a different entity in and outside of Austria during the licence period. However, the Commission does not consider this to give rise to significant consumer confusion risks, given that the relevant markets are national. Moreover, to the extent different Senseo products, such as in-home and out-of-home, are controlled by different entities in Austria, the Commission does not consider that in the present case the risk of confusion would be significant given that the characteristics and dynamics of the markets are different.
- (710) The Commission further considers that the duration of the licence and black-out periods are likely to be adequate in the present case which concerns fast-moving consumer goods. The duration of the licence is also significantly longer than the duration in which the Parties themselves have considered to be able to rebrand the excluded Carte Noire and Velours Noir products in the R&G and filter pad markets in France without a black-out period.

⁴⁵⁹ See, e.g. paragraph 40 of the Remedies Notice.

- (711) The purchaser's ability to start operations immediately after taking over the brand is supported by the Notifying Parties or the joint venture providing the purchaser transitional co-manufacturing services. While such services inevitably create a link and a certain level of dependency between the purchaser and the Notifying Parties or the joint venture, such effects are inherent to these types of transitional agreements and a Monitoring Trustee will be in place to supervise the relationship.
- (712) However, the fact that the transitional services are provided at a 'cost-plus' basis might affect negatively the ability of the purchaser to be competitive in the market. The arrangement may effectively result in a double margin problem which could only be fully avoided if the purchaser forewent its margin. The problem is aggravated in the present case by the fact that the Parties or the joint venture would be supplying the purchaser with finished goods. Consequently, the purchaser would not be engaged in any production that would add value to those products.
- (713) As the Austrian Licence does not include production facilities, the viability of the Austrian Licence therefore requires that the purchaser has access to suitable production capacity also after the transitional period during which the Notifying Parties and the joint venture are obliged to provide the manufacturing service. Moreover, the nature of the Austrian Licence as a rebranding remedy calls for the purchaser to have adequate financial resources to undertake the rebranding exercise, including promotion expenses.
- (714) In light of the considerations laid down in Recitals (695) to (711), the Commission concludes that the Austrian Licence will constitute a viable and competitive business that will be able to compete effectively with the Notifying Parties and the joint venture in the market for filter pads in Austria, subject to the transitional services and, in particular, the co-manufacturing being offered to the purchaser at a price level that does not hamper the purchaser establishing itself on the market and carrying out the rebranding.

11.5. Final Commitments

11.5.1. Description of the Final Commitments

- (715) The Final Commitments submitted on 20 February 2015 differ from the Commitments of 23 February 2015 in the following ways:
- (a) It is proposed that transitional co-manufacturing services for the purchaser(s) will be provided by the Parties and the joint venture on a cost basis instead of a 'cost-plus' basis with respect to the Merrild Divestment Business, the Carte Noire Divestment Business and the Austrian Licence;
 - (b) Mondelēz expressly waives, but only in favour of the purchaser of the Carte Noire Divestment Business, the exclusivity it enjoys in the EEA for the N-capsules technologies employed in the production of Carte Noire N-capsules; and
 - (c) the Notifying Parties must be able to demonstrate, prior to purchaser approval, that the proprietor of the N-capsules technologies has consented to grant the purchaser of the Carte Noire Divestment Business an EEA-wide licence to the technologies on terms no less favourable than currently enjoyed by Mondelēz.

11.5.2. Commission's assessment of the Final Commitments

- (716) The Commission considers that the Final Commitments sufficiently address the issues raised in the Commission's assessment of and the market test on the Commitments of 23 February 2015.

- (717) The provision of the transitional services, including co-manufacturing, to the purchaser(s) of the Merrild Divestment Business, the Carte Noire Divestment Business and the Austrian Licence on a cost basis will enable the purchasers to acquire the goods at a price that does not hamper the purchaser's ability to compete or set its own pricing on the market. A Monitoring Trustee will be in place to supervise the provision of the transitional services, including pricing.
- (718) The requirements concerning the technology used to produce Carte Noir N-capsules remove possible uncertainties related to the purchaser of the Carte Noir Divestment Business ability to conclude an agreement with the provider of the license and guarantee that the purchaser will have access to the technologies on terms no less favourable than currently enjoyed by Mondelēz.
- (719) The Commission therefore concludes that the Final Commitments are adequate and sufficient to eliminate the significant impediment to effective competition that the Transaction would have led to in the markets for R&G coffee in Denmark, France and Latvia, and in the markets for filter pads in Austria and France.

11.6. Conclusion on the modifications to the Transaction

- (720) The Commission finds that following modifications by the Parties through the Final Commitments the Transaction would not significantly impede effective competition in the internal market or in a substantial part of it.

12. CONDITIONS AND OBLIGATIONS

- (721) Pursuant to the second subparagraph of Article 8(2) of the Regulation (EC) No 139/2004, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into *vis-à-vis* the Commission with a view to rendering the concentration compatible with the internal market.
- (722) The fulfilment of the measure that gives rise to the structural change of the market is a condition, whereas the implementing steps which are necessary to achieve that result are generally obligations on the parties. Where a condition is not fulfilled, the Commission's decision declaring the concentration compatible with the internal market is no longer applicable. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(6) of the Regulation (EC) No 139/2004. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2) and 15(1) of the Regulation (EC) No 139/2004.
- (723) In accordance with the basic distinction described in Recital (720) as regards conditions and obligations, this Decision should be made conditional on the full compliance by the Parties with the Section B (including Schedules A to D of the Final Commitments submitted by the Parties on 20 March 2015 and all other Sections should be obligations within the meaning of Article 8(2) of the Regulation (EC) No 139/2004. The full text of the commitments is attached as an Annex II to this Decision and forms an integral part thereof.

HAS ADOPTED THIS DECISION:

Article 1

The notified operation whereby D.E. Master Blenders 1753 and Mondelēz [...]× acquire joint control of Charger OpCo B.V. within the meaning of Article 3(1)(b) of the Council Regulation (EC) No 139/2004 is hereby declared compatible with the internal market and the EEA Agreement.

Article 2

Article 1 is subject to compliance with the conditions set out in Section B of Annex II.

Article 3

D.E. Master Blenders 1753 and Mondelēz [...]× shall comply with the obligations set out in the Sections A, C, D, E and F of Annex II.

Article 4

This Decision is addressed to:

Acorn Holdings B.V.

Oosterdoksstraat 80

1011 DK Amsterdam

The Netherlands

and

Mondelēz International, Inc.

Three Parkway North

Deerfield, IL 60015

United States of America

Done at Brussels, 5.5.2015

For the Commission

(Signed)

Margrethe VESTAGER

Member of the Commission

× Should read: International, Inc.
× Should read: International, Inc.

ANNEX I:
ASSESSMENT OF THE ECONOMIC SUBMISSIONS

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1. This Annex presents the economic studies that the Commission received and assessed during the course of the proceedings. It is divided into three sections. Section 1 sets out the estimated demand model submitted by the Parties to assess the substitutability between roast and ground coffee ('R&G') and filter pads. Section 2 deals with the Parties' calibrated merger simulation models to estimate the likely effects of the Transaction. Finally, Section 3 discusses several economic studies submitted by the Parties and by Nestlé that aimed to assess the closeness of competition among coffee systems by analysing, in particular, the competitive effect of Tassimo's entry in a market.
2. The Commission's quantitative analysis of Tassimo's entry effect can be found in Section 9.4.5.2 of the Decision.

1. ESTIMATED DEMAND MODEL

3. During the course of the proceedings, the Parties submitted a series of estimated demand models for the purpose of assessing the substitutability across coffee segments and to draw insights on the likely effect of the Transaction. The Commission considers that the Parties' demand estimation models cannot be relied upon for the purposes of the present decision as they suffer from a number of substantial shortcomings, the details of which are set out in the following subsections.

1.1. The Parties' First Set of Submissions on Demand Estimation

4. During the pre-notification period and Phase I of the proceedings, the Parties submitted an economic paper on demand estimation for France to assess the substitutability between R&G and filter pads, and to gain more insight into the potential effect of the Transaction in the French coffee markets (the "First Set of Submissions on Demand Estimation").^{1, 2} In the First Set of Submissions on Demand Estimation, the Parties' presented estimates of own and cross price elasticities³ for R&G brands and filter pad brands which are based on the empirical "Almost Ideal Demand System" ('AIDS') model.⁴ The Parties use weekly retail scanner data at national level collected by AC Nielsen for this estimation.
5. In the First Set of Submissions on Demand Estimation, the Parties use their demand estimation results in an Indicative Price Rise ('IPR') calculation. The IPR uses the own and cross price elasticities estimated by the AIDS model to predict the price effect of the Transaction in the post-Transaction scenario.⁵

¹ M.7292 –DEMB/MONDELÉZ/CHARGER JV, Economic Submission: demand estimation results – France, ID00186.

² M.7292 DEMB/Mondelez/Charger JV, Demand estimation for in-home coffee in France, ID00187.

³ The elasticities measure the price sensitivity of demand. The own-price elasticity gives the percent change in the demand for a product as a response to a 1% increase in the price of the product. The cross-price elasticity between two products gives the percent change in the demand for the first product as a response to a 1% increase in the price of the other product. Normally, the own-price elasticity is negative (demand decreases as the product becomes more expensive) and cross-price elasticities are positive between substitute products (a product's demand is increasing if its substitute becomes more expensive). Elasticities can be calculated on product, brand, segment or even more aggregated level.

⁴ Deaton, A., J. Muellbauer. 1980. Economics and Consumer Behavior. Cambridge University Press.

⁵ The results of the IPR are only a first-order approximation of the magnitude of the effect on the Parties' price because the methodology does not account for the reactions of the competitors in the market.

6. The IPR results proposed by the Parties indicate strong price increases resulting from the Transaction in both R&G and filter pads in France. Nevertheless, the estimated cross price elasticities across the products of the two segments are relatively high, suggesting a high degree of substitution and, hence, a strong competitive constraint between the segments. In fact, once the methodology accounts for the commitments proposed by the Parties on 26 November 2014 (the "Commitments of 26 November 2014"), that is to say, the divestiture of the l'Or and Grand Mere brands, referred to in paragraph (8) of the Decision, the price increases estimated by the IPR become negligible in both segments.

1.2. The Commission's assessment of the First Set of Submissions on Demand Estimation

7. The Commission assessed the Parties' First Set of Submissions on Demand Estimation and found that the model is not able to capture the consumers' inventory behaviour present in the market. This limitation severely biases the estimated own and cross price elasticities, making the inferences based on those estimated elasticities unreliable.
8. The AIDS model is one approach used in economic literature to estimate demand for consumer products. The AIDS model is "flexible" in the sense that it imposes relatively few restrictions on the substitution patterns across products. However, the model often delivers results, such as negative cross price elasticities of demand, that are difficult to reconcile with standard economic theory. While in principle those results can be an indication that the data does not support the basic assumptions of standard economic theory, it is equally or even more likely that they might be the consequence of imprecisely measured data and inadequate estimation methodology⁶.
9. The Parties' demand estimation contains well-known econometric problems that are frequently encountered in demand estimations in industries of this type. Firstly, prices may be "endogenously" determined with demand (that is to say they are determined by reasons or elements not incorporated in the model). Secondly, the observed consumer behaviour may reflect the inventory behaviour in the form of stock-piling by consumers during promotional periods. Both issues are difficult to deal with and can lead to potentially serious biases in the estimated elasticities. Importantly, in the present case, the Commission found that the conclusions from these estimates vary substantially depending on how one "trades-off" the two types of problems against each other.
10. According to the Parties, the use of weekly level data in the demand estimation minimises the biases in the estimation which are due to the endogeneity of prices⁷. The Commission notes that the economic literature argues that the use of high frequency (that is to say

⁶ Such as lack of instrumentation or poor instrumental variables. The use of instrumental variables is an estimation methodology developed to prevent the so-called endogeneity bias of the parameter estimates. See point 9. The Parties argue that no instrumentation is needed, see point 10.

⁷ The endogeneity problem here refers to the case where prices and quantities are simultaneously determined in the market. That is to say, the prices and quantities observed in the data are generated by multiple instances where demand and supply meet; hence, each pair of price and quantity is determined simultaneously (that is to say one determines the other and vice-versa). That "simultaneous causality" introduces a bias in the estimation of the causal relation between quantities and prices (that is to say it is not possible to disentangle how changes in quantities are *caused* by changes in prices). The Parties argue that using high-frequency data (that is to say weekly data) solves the endogeneity problem because the observed prices are pre-determined, in the sense that they are not determined simultaneously with the quantities.

weekly) data can in some specific cases alleviate the problem of endogeneity. More specifically, the use of high frequency data relies on the assumption that the price setters (that is to say, the retailers) do not form expectations of future consumption and are not able to change the prices in a week's time⁸.

11. As regards inventory behaviour by consumers, the Commission notes that coffee is a storable good that can be stocked for at least 18 to 24 months before it becomes non-consumable regardless of the format. In addition, the Commission's investigation found that coffee was often put on promotional sale on the retailers' shelves, and the vast majority of the respondents to the Commission's market investigation indicated that consumers stockpiled coffee products during the promotional sale period. This is consistent with the price and quantity movements over time in the observed data, which show high spikes during periods with strong promotional activity and low quantities during regular price periods.
12. Consumers' inventory behaviour is a form of inter-temporal substitution. Consumers purchase more during promotional sales periods in order to substitute future purchases and consumption. The estimated demand based on the AIDS model is static. It measures simultaneous substitution patterns, but it is not able to capture the dynamic nature of consumers' stockpiling behaviour. This limitation of the model introduces an upward bias in the price elasticities estimates⁹. In other words, the results might erroneously imply that there is a strong reaction to price changes, and also a strong inter-segment substitution (such as, for example, between R&G and filter pad products). A similar critique was accepted by the Commission in the merger case *Friesland/Campina*¹⁰.
13. The Commission notes that a similar limitation would arise in contexts of consumer heterogeneity, namely, where a proportion of consumers are strongly influenced by the retailers' promotional activity and purchases coffee only when the product is on promotional sale, while the rest of the consumers purchase coffee on a regular basis. In such circumstances the size of the coffee market would increase during promotional periods and fall during non-promotional periods, leading to a similar upward bias in price elasticities as estimated by the AIDS model.
14. The Commission attempted to deal with the likely serious stock-piling issue by aggregating the data to monthly and quarterly levels. The use of more aggregated data should average out part of the effect of promotional activity and consumers' stockpiling behaviour. However, aggregating the data potentially reintroduces or reinforces the endogeneity problem mentioned in paragraph 10¹¹.

⁸ Capps, Oral, Jr., Jeffrey Church, and H. Alan Love (2003). "Specification Issues and Confidence Intervals in Unilateral Price Effects Analysis." *Journal of Econometrics*, 113, 3-31.

⁹ Hosken, Daniel, Daniel O'Brien, David Scheffman, and Michael Vita (2002). "Demand System Estimation and its Application To Horizontal Merger Analysis." Federal Trade Commission, Bureau of Economics, Working Paper 246, available at <http://www.ftc.gov/be/workpapers/wp246.pdf>. In particular, Hosken et al point out that "[i]f inventory effects are important (this is likely to be the case if the predominate source of price variation are the sales which generate inventory effects), the estimated elasticities will likely be too large".

¹⁰ Commission Decision in Case No COMP/M.5046 – *Friesland/Campina*, Annex 1, section 5.3.2.2.

¹¹ The assumption that prices are pre-determined mentioned in footnote 7 is unreasonable in case of low frequency data (i.e. monthly or quarterly).

15. The Commission found that the estimated unconditional cross price elasticities across the R&G brands and the filter pads brands were substantially lower using lower frequency (that is to say monthly and quarterly) data, suggesting a low degree of substitutability between R&G brands and filter pads brands. In fact, the corresponding IPR results indicate a strong price increase in filter pads even after taking into account the Commitments of 26 November 2014. Therefore, the Parties' argument that the Commitments of 26 November 2014 would also address competition concerns in relation to filter pads is not supported by using lower frequency data, which reduces the likely serious bias due to inventory behaviour (although, at the expense of potentially increasing the endogeneity problem).
16. The Commission therefore considered, in the Article 6(1)c Decision, that the results of the First Set of Submissions on Demand Estimation are unreliable.

1.3. The Parties' Second Set of Submissions on Demand Estimation

17. In their response to the Article 6(1)(c) Decision ("Response No. 1") and in a subsequent response to a request for information ("Response No. 2") (together with Response No 1 the "Second Set of Submissions on Demand Estimation"), the Parties contest the Commission's arguments on the limitations of the First Set of Submissions on Demand Estimation and conclude that "the concerns [...] are unfounded and the Commission can safely rely on the demand estimation results"^{12, 13, 14}. The Commission finds that the arguments put forward by the Parties to sustain such conclusion do not alleviate the severe limitations of the Parties' demand estimation analysis. Points 18 to 26 set out the Parties' arguments and the Commission's assessment.
18. Firstly, in Response No. 1 the Parties argue that promotional sales on coffee in France are relatively infrequent. The Parties show that in France the promotional sales at segment level amount to a [...] proportion (less than [30-40]*% in R&G and less than [20-30]*% in filter pads) of the total coffee sales during the period of the analysis. Questioned on the reliability of the promotion's indicator in the AC Nielsen data and on the proportion of promotional sales divided by brand, in Response No. 2 the Parties provided the share of promoted and non-promoted sales by segment and brand for 2014, based on new data provided by AC Nielsen.¹⁵ Based on those figures the Parties conclude that "Approximately [30-40]*% of total volume sales of the products were sold under promotion."¹⁶
19. However, having reviewed the Parties' argument the Commission concludes that the segments' share of promotional sales over the period of the analysis is not informative enough to assess the impact of consumers' inventory behaviour¹⁷. The Commission notes

¹² Response No. 1: Parties' response to Article 6(1)(c) decision, Annex 5, ID02431.

¹³ Response No. 2: Response to RFI of 21 January 2015, ID02988.

¹⁴ Response No. 1, pp.2 par. 5.

¹⁵ In Response No. 2 the Parties explain that AC Nielsen may not record some promotional activity in their data. AC Nielsen provided the Parties with data for 2014 including estimates of the amount of promoted and non-promoted sales considering all promotional activities.

¹⁶ Response No. 2, pp. 5.

¹⁷ The segments' share of promotional sales may be informative of consumers' inventory behaviour in case it was very close to 0% (i.e. no promotional sales) or very close to 100% (i.e. all sales are promotional sales).

that the bias in the demand estimation's coefficients stems directly from the spikes observed in the brands' sales and price figures during periods of high promotional activity. Therefore, as infrequent as the promotions may be, the bias in the estimated elasticities determined by the consumers' inventory behaviour is due to the share of promotional sales *during* highly promotional periods. In addition, the promotional share figures provided by the Parties in Response No. 2 already show that several brands in all segments have a [...] * proportion of promoted sales in 2014 (above [40-50] *%), suggesting that the brands' share of promotional sales during highly promotional periods is likely to be even higher.

20. Secondly, the Parties argue that promotions do not impact upon consumer behaviour in a significant way. To support this argument, the Parties submitted a correlation study in Response No. 1 investigating the simultaneous co-movement of brand's volume sales in period t and in period $t-1$ ¹⁸. The Parties argue that if promotions had a significant impact on the consumers' inventory behaviour one would expect to find a negative correlation coefficient, as consumers who stockpile during promotions in period $t-1$ would deplete their inventory in period t . Hence, periods with a spike in sales (that is to say sales promotions periods) should be followed by periods with a "dip" in sales (that is to say consumers depleting their inventory), which would result in a negative correlation between the sales in period t and $t-1$. Since such negative relation was not found in the data, the Parties concluded that promotions are unlikely to change consumer behaviour.
21. After receiving questions from the Commission on the possibility that other factors might influence the sales' co-movement over time (for example trends, seasonality, different duration of promotions, and aggregate nature of the data), the Parties refined their correlation study in Response No. 2. The Parties included yearly, quarterly and monthly fixed effects in the analysis to take into account unobservable time-varying factors and they aggregated the data from weekly to fortnightly levels to take into account longer duration of the promotions. From the results of the correlation study, the Parties conclude that there is no evidence of strong and negative inter-temporal correlation in the brands' volume sales.
22. However, the Commission found that the Parties' analysis suffered from a number of different shortcomings, notably, with respect to the aggregate nature (across shops, not over time) of the data. Although the Commission agrees that in case of consumer stockpiling behaviour there should be such negative inter-temporal relation of the sales volume at a very granular level of aggregation (for example household level), this relation is likely not to be visible in the highly aggregated country level data used in the analysis. At country level, in order to observe the negative inter-temporal correlation sought by the Parties, all the promotional activity of all the retailers in the country should be simultaneous in time. However, it is very unlikely that the promotional activities of all the retailers are carried out simultaneously. In fact, for a given brand the data show a continuum of promotional activity throughout the period of the analysis. That could be explained by promotional activities which vary in different micro-areas depending on observable and unobservable factors (for example the level of competition in the area and the average wage of the inhabitants). The continuum of promotional activity for each brand is formed by weeks of intensive promotional activity (which could be explained by many micro-areas offering promotions simultaneously) and weeks of low promotional activity (that is to say few micro-areas offering promotions simultaneously). In such

¹⁸ The simultaneous co-movement of two time series is measured by the *correlation coefficient*.

circumstances, the evolution of the brands' sales volume over time will not follow a clear pattern of "spikes followed by dips". Different retailers may, for example, offer the same promotion in subsequent weeks, keeping the brands' volume sales at a relatively high level. Ultimately, the evolution of the brands' volume sales will depend upon unobservable factors governing the likelihood that the retailers in many micro-areas offer the same promotion simultaneously. As a result, the negative inter-temporal relation in a brand's sales volume that one would expect to find in disaggregated data will not be visible and will not be measurable in the country level data used by the Parties. As the Parties acknowledge in Response No. 2, "[i]f promotional activity does not occur simultaneously across retailers, then testing correlation of sales over time is less informative".¹⁹

23. Thirdly, in Response No. 1 the Parties argue that the demand estimation is robust as regards the aggregation at monthly level. As explained in paragraph 14, aggregating the data at monthly or quarterly level alleviates the stockpiling or consumer heterogeneity issue. The Parties present the segment level elasticities, claiming that "[t]he changes in the estimated elasticities using monthly data compared to those obtained using weekly data are quantitatively small, and, most importantly, do not change [...] the conclusion that there is significant substitution between R&G and filter pads."²⁰ The Commission sent several questions to the Parties to clarify the robustness of the results. In Response No. 2, the Parties submitted two robustness checks, one using monthly data and the other using weekly data, where the Parties included yearly and quarterly fixed effects in all the equations of the segment level system of equations. According to the Parties, the results of those robustness checks confirm the conclusions reached by the original specification submitted in Response No. 1, that there is significant substitution effect between R&G and filter pads.
24. However, the Commission assessed Response No. 1 and Response No. 2 and concluded that the Parties' argument is not able to dispel the Commission's doubts on the reliability of the demand estimation's results.
- a. In the first place, in Response No. 2 the Parties' argue that the endogeneity problem in the demand estimation's results using monthly data is expected to bias own and cross price elasticities downward, suggesting that the estimated elasticities are an upper bound of the true elasticities. However, in the Commission's view it is not possible to deduce the direction of the endogeneity bias a priori when several price coefficients are estimated within the same equation. Hence, it is not possible to determine whether the estimated elasticities represent a lower bound or an upper bound of the true parameter.
 - b. In the second place, the Commission notes that the Parties estimated only the segment-level system of equations in their submissions made after the adoption of the Article 6(1)(c) Decision²¹. However, when estimating also the brand-level

¹⁹ Response No. 2, pp. 7.

²⁰ Response No. 1, pp. 5 par. 16.

²¹ The AIDS model can be formed by several systems of equations, each representing a level of aggregation of the products. In the First Set of Submissions on Demand Estimation, the Parties estimated a two level AIDS, where the levels were "segment" and "brand", while in the Second Set of Submissions on Demand Estimation the Parties estimated only the segment level.

system of equations, the brands' cross price elasticities are not consistent with the segments' cross price elasticities²². For example, all the brands of the segment Robusta have a negative cross price elasticity relative to the brands of the segment Arabica, suggesting that Arabica and Robusta are in different markets. This contradicts the segment-level cross price elasticities estimated by the segment-level system of equations.

- c. In the third place, in the specification submitted by the Parties' in Response No. 2 that includes yearly and quarterly fixed effects and with the data aggregated at monthly level, the estimated segment-level cross price elasticities are mostly not statistically different from zero. That is, in a statistical sense, the results of the analysis do not call into question the hypothesis that there is no cross-segment substitution. Even if the methodology was not subject to the econometric problems identified, this finding would reduce the importance that can be assigned to the interpretation of the elasticities estimated by this model, particularly in presence of other evidence on cross-segment substitution.

25. Overall the Commission takes the view that considerable bias is likely in the results of the Parties' demand estimation resulting from endogeneity of prices and, in particular, consumer stock-piling behaviour. While the alternative estimations using monthly data rather than weekly data for the estimation cannot fully solve these problems, the fact that using more aggregate data leads to different implications (in particular in terms of the unconditional brand level elasticities and, in many cases, non-significant segment level results) further indicates that such a bias is likely to be serious.

26. The Commission concludes that the econometric demand estimates cannot be considered reliable in the current case and are relatively uninformative compared to other evidence on file regarding switching (or the absence thereof) between R&G and filter pads.²³

2. MERGER SIMULATION MODELS

27. The Parties submitted calibrated merger simulation models for several coffee product markets in a number of countries to predict the Transaction's likely impact on price. The Commission, however, for the reasons set out below, has found that they cannot be considered reliable as they are likely to underestimate the anti-competitive effect of the Transaction.

2.1. The Parties' First Set of Merger Simulation Models

28. During the pre-notification period, the Parties submitted calibrated merger simulation models for a subset of the affected national markets (Austria²⁴, the Czech Republic²⁵, Denmark²⁶, France^{27,28,29}, Greece³⁰, Spain^{31,32,33} and the United Kingdom³⁴) (the "First Set

²² The segment and brand levels systems of equations estimate, respectively, the conditional segment-level own and cross price elasticities and the conditional brand-level own and cross price elasticities.

²³ See Section 6.7 of the Decision.

²⁴ Coffee market in Austria: merger simulation, 30 September 2014, ID00144.

²⁵ Coffee market in the Czech Republic: merger simulation, 29 July 2014, ID00038.

²⁶ Coffee market in Denmark: merger simulation, 30 September 2014, ID00145.

²⁷ Coffee market in France: merger simulation analysis, 8 August 2014, ID00041.

²⁸ Additional merger simulation results - France and Spain, 8 September 2014, ID00063.

of Merger Simulation Models"). The aim of these models is to predict the price impact of the Transaction in the R&G coffee, filter pads, instant coffee and N-capsules coffee markets (or some subsets of those markets) of those countries.

29. The models share some general features across the countries. The two key components of the models are the demand side and the supply side. The demand side attempts to describe, in a simplified way, how consumers behave when choosing between different coffee consumable products such as a Carte Noire R&G coffee package, a pack of Senseo filter pads or a Private Label product. In particular, the Parties use the nested logit demand models³⁵. Those models take into account the perceived differences between products by grouping them into nests or segments. The nesting is an attempt to capture the differentiation across the different coffee products. For example, one nest could include R&G products, a second filter pad products, a third instant products. The products in the nest can be closer substitutes of each other than of products outside their nests. In some cases, the Parties use two-level nested logit demand models. For example, in some cases within the R&G nest further subsets are specified for Arabica and Robusta products. The set of segments or nests included in the models vary from one country to another³⁶.
30. The supply side describes, in a simplified way, how firms behave. In particular, a Nash-Bertrand price equilibrium concept is used where the manufacturers are assumed to set their prices to maximise profits, taking into account the competitive responses of their rivals as well as the demand side. The model is used to predict post-Transaction prices by assuming that during the post-Transaction period the merged entity maximises the profits generated by all of its products.
31. The demand parameters of those models are calibrated using three sources of information. Firstly, prices and quantities of the products are obtained from the AC Nielsen retail scanner data. Secondly, the Parties use the observed cost-price ratio of DEMB and Mondelēz and select the models' parameters so that the model's implied pre-Transaction cost-price ratios are consistent with the observed cost-price ratios within a certain range, a practice referred to as "cost calibration". Thirdly, the Parties use an assumption on the aggregate demand elasticity, that is to say, the price sensitivity of coffee demand³⁷ which

²⁹ Coffee market in France: additional merger simulation results, 17 October 2014, ID00293.

³⁰ Coffee market in Greece: merger simulation, 17 October 2014, ID00304.

³¹ Coffee market in Spain: merger simulation, 24 July 2014, ID00030.

³² Additional merger simulation results - France and Spain, 17 October 2014, ID00063.

³³ Coffee market in Spain: additional merger simulation results, 17 October 2014, ID00294.

³⁴ In-home coffee market in UK: merger simulation, 20 October 2014, ID00316.

³⁵ See, for example, McFadden, D., (1981): "Econometric Models of Probabilistic Choice," in C.F. Manski, D. McFadden (eds), *Structural Analysis of Discrete Data with Econometric Applications*, MIT Press, Cambridge, Massachusetts, pages 198-272.

³⁶ R&G, Filter Pads and Instant (Austria); R&G and Instant (the Czech Republic, Denmark, Greece, Spain); R&G or Instant (the UK). The subnests also differ from country to country, especially within R&G: Coffee beans and Ground (the Czech Republic); Espresso and Traditional (Denmark and the UK); Greek and Non-Greek (Greece); Mezcla&Torrefacto and Natural (Spain).

³⁷ The aggregate elasticity is the percent change in the overall coffee demand as a response to a 1% overall increase in the coffee products' price. The Parties use two scenarios in their models. The first with aggregate elasticity of -1 and the second with -0.75. This implies, hence, that the model assumes that in response to a 1% overall price increase the coffee demand decreases by 1% (or 0.75%, respectively).

they argue is supported by the economic literature³⁸. The calibrated parameters of the model determine the brand level substitution patterns between brands in the same segment and between brands in different segments. Together with an assumption on the aggregate elasticity, the parameters also imply how sensitive the demand is to overall price changes. The calibration approach is unusual in that it leaves one degree of freedom for the two demand parameters. This means that for each model specification considered, there is a range of combinations of demand parameters that is consistent with the Parties' calibration approach. The Parties first perform a search over a chosen set of parameter combinations to determine all combinations of parameters within that set that are consistent with the observed cost-price ratios³⁹. They then simulate the merger effects for all those consistent parameter combinations.

32. The overall price increases predicted in the First Set of Merger Simulation Models are below 1% for Austria, the Czech Republic, Spain and the UK, and around 1.3-1.5% for Greece in the R&G coffee, filter pads and instant coffee markets. The predicted overall price increases across those three coffee markets for the Parties' products still tend to be low for Austria, the Czech Republic, Spain and the UK. However, the overall price increases for Denmark and France are more substantial at 2.9% to 3.4% for Denmark, and 3.5% to 4.2% for France without taking into account any commitments. The predicted price increases for the Parties' products are even higher in those two countries at 6.6% to 7.8% and 5.4% to 6.3%, respectively. For France, the Parties also present merger simulations for scenarios including the divestiture of the l'Or and Grand Mere brands, as proposed by the Parties earlier in the proceedings. With those alternative specifications, the models predict a 1.9% to 2.1% price increase in the filter pads market in France which is due to the fact that the envisaged divestments affected mainly the R&G coffee market of the models.
33. In the assessment below, the results take into account such a divestment of the l'Or and Grand Mere brands. It is important to point out, however, that the Final Commitments provide for a different divestment in relation to France, that is to say, that of the Carte Noire brand. Yet, the assessment had to be done based on the previous divestment proposal because the earlier commitment proposal did not alleviate the Commission's concerns in the French filter pads market in a clear cut manner. It would have eliminated the overlap between the Parties' activities in the R&G coffee market but not in the filter pad market.

2.2. The Commission's assessment of the Parties' First Set of Merger Simulation Models

34. In its Article 6(1)(c) Decision, the Commission considered that First Set of Merger Simulation Models was not sufficient to allow it to conclude that no serious doubts would arise as to the compatibility of the proposed Transaction with the internal market in all of the countries modelled. In particular, the Commission had taken the view that the merger

³⁸ Note on the aggregate elasticity of coffee, 14 November 2014. ID01664 This submission cites papers that present aggregate elasticity estimates closer to -1. Hence, the Parties argue that the aggregate elasticity assumptions in the First Set of Merger Simulation Models (-1 and -0.75) are supported by this literature. For discussion of these arguments see point 35 and footnote 52 below.

³⁹ Hence, there is not one pair of parameters matching the observed cost-price ratios but several pairs. In this sense, the calibration of the parameters is up to one degree of freedom.

simulation models raised several issues that called into question their reliability as tools not underestimating the likely effect of the Transaction.

35. Firstly, the Commission considered that the Parties applied aggregate elasticity assumptions which were not consistent with established academic literature. In particular, the Parties' assumptions depict an overall coffee segment where demand is not particularly inelastic. On the other hand, the academic literature with focus on the markets in the US^{40,41}, France⁴², Germany^{43,44}, Greece⁴⁵, the Netherlands^{46,47}, and the Nordic countries^{48,49} that is to say Denmark, Sweden^{50,51} and Finland, estimates quite inelastic coffee demand, with aggregate elasticity in the range of -0.2; -0.5⁵². The aggregate elasticity is a measure of the price sensitivity of the overall demand for coffee products. An inelastic demand, that is to say an aggregate elasticity close to zero, means that in case of a small price increase of all coffee products the total coffee quantity sold would decrease only to a small extent: the demand is not sensitive to the price change. The aggregate elasticity is an input, that is to say, an assumption, to the Parties' models (see also point 31 above). A less elastic aggregate demand, that is to say, an aggregate elasticity assumed to be closer to zero, would result in higher predicted post-merger price increases when using the Parties' models. That is because a less elastic demand means that consumers are less willing to substitute towards non-coffee consumer goods as the average price of coffee increases, and this gives the merging firms a stronger incentive to raise prices than in a more elastic aggregate demand scenario. On the contrary, a more elastic aggregate demand, that is to say an aggregate demand elasticity with a large absolute value, leads to lower predicted

⁴⁰ Okunande, A. A., and P. E. McLean-Meynise (1992): "Reliability test of elasticity estimates from alternative specifications of the US demand for coffee," *Journal of Agribusiness*, 10(2): 19-35.

⁴¹ Bhuyan, S., and R. A. Lopez (1997): "Oligopoly power in the food and tobacco industries," *American Journal of Agricultural Economics*, 79: 1035-1043.

⁴² Aiyama, T., and P. N. Varangis (1990): "The impact of the international coffee agreement on producing countries," *The World Bank Economic Review*, 4: 157-173.

⁴³ Feuerstein, S., (2002): "Do coffee roasters benefit from high prices of coffee?," *International Journal of Industrial Organization*, 20: 89-118.

⁴⁴ See footnote 42.

⁴⁵ See footnote 42.

⁴⁶ Bettendorf, L., and F. Verboven (2000): "Incomplete transmission of coffee bean prices: evidence from the Netherlands," *European Review of Agricultural Economics*, 27: 1-16.

⁴⁷ See footnote 42.

⁴⁸ Durevall, D., (2003): "Competition in the Nordic Coffee Markets," *working paper*, Göteborg University.

⁴⁹ See footnote 43.

⁵⁰ Durevall, D., (2005): "Demand for Coffee Prices: The Role of Preferences and Market Power," *Food Policy*, 32: 5-6.

⁵¹ Durevall, D., (2007): "Competition in the Swedish Coffee Market 1978-2002," *International Journal of Industrial Organization*, 25:4.

⁵² The Parties' submission on aggregate elasticities (see footnote 38) cites, with one exception unpublished, papers that present aggregate elasticity estimates closer to -1. Those papers, however, do not estimate the aggregate elasticity of demand but rather only conditional elasticities (mostly using AIDS models), which are expected to be larger in absolute value than the unconditional aggregate elasticity. Interestingly, one of those papers, (Alamo, C. "Implications of product differentiation in food demand: the case of coffee in the United States", PhD Dissertation in Agricultural and Applied Economics – Texas Tech University. December, 2012) cites an academic paper (see footnote 40) which reviews estimates of unconditional aggregate elasticities for the US implying inelastic aggregate demand.

post-merger price increases in the models. The Parties' submissions assumed a more elastic aggregate demand than what is found by the above cited academic literature. Hence, it follows that the Parties' submissions use assumptions on the aggregate elasticity such that the models likely underestimate the estimated price impact of the Transaction.

36. Secondly, in many of their models^{53,54,55} the Parties do not include important segments of the coffee sector such as N-capsules France. The models distinguish between the modelled segments and the non-modelled segments. The modelled segments, for example, the R&G and filter pads markets in France, are those for which the model is able to predict the price increases. The non-modelled segments, for example, the N-capsules in France, include coffee products for which the model does not give price predictions. In the terminology of those types of models, the modelled segments are called the "inside good" and the non-modelled segment the "outside good". The model only needs an assumption on the size of the outside good. According to the logic of the model, if some consumers stop buying a certain coffee product in the inside good segment due to a price increase of that product, some of those consumers will buy another product in the inside good segment. Some of them, however, will rather substitute towards the outside good segment. The products of the outside good segment are treated as non-strategic, that is to say, it is assumed that their prices do not react to the changes in the other segments. However, the Parties often have strong positions in those non-modelled, left-out segments. If the merged entity raises its prices in a segment it will lose some of its customers. Some of those lost customers will switch to another segment that is included in the model. Some of them, however, might instead buy products in the segments not modelled, that is to say the outside goods. For example, if the merged entity raises the price of its filter pad products' price, some of their customers will switch to other filter pad products or to R&G coffee. Some of the switchers might, however, choose other coffee formats for example capsules or instant that are by the models' assumption in the "outside good". It follows that if the merged entity has strong positions in the non-modelled segments, it will recapture some of its lost consumers. This would give it a further incentive to raise prices. In the models of the Parties, however, that effect is not present as they assume that the firms do not take into account the recapture. This leads to smaller predicted post-Transaction price increases compared to a model where the recapture is included. Hence, it was found that the Parties' submissions were likely to underestimate the estimated price impact of the Transaction.
37. Thirdly, the nested logit models impose strong restrictions on the substitution patterns across the different products. In particular, they assume that within a nest the closest substitute of any product is the product with the highest share in the nest. In a two-level nested logit model the same is true within subnests. The implication is that the model, for example, in the French filter pads market assumes that the private label products are the closest competitors of the Senseo or even the Carte Noire brands. Private label products, however, have a lower price positioning than branded products, and are not regarded as close competitors of branded products, especially the premium brands like Carte Noire. As indicated by respondents to the market investigation, private label products exert only a limited competitive constraint on branded products and have been decreasing over the past years⁵⁶. Also, private label products are not uniformly strong across retail channels.

⁵³ Coffee market in France: merger simulation analysis, 8 August 2014, ID00041.

⁵⁴ Additional merger simulation results - France and Spain, 8 September 2014, ID00063.

⁵⁵ Coffee market in France: additional merger simulation results, 17 October 2014, ID00293.

⁵⁶ See Section 7.2 and Section 8.5.1.3 of the Decision.

Some retailers, like the hard discounters, that is to say, retail stores which sell products at lower prices than the typical market value, for example Aldi and Lidl, sell relatively few branded products and focus more on their private label offerings. In other, more mainstream retailers, such as Carrefour, Leclerc and Auchan private label products are less evident. By not taking this into account, the models over-estimate the competitive constraint exerted by private label products on branded goods. Were the model to capture the closer market positioning of the branded products to each other and their relatively weaker link with the private label products, the merger simulations would imply larger incentives to raise prices following a merger of branded products. In previous cases where similar models were used, private label products were less important in terms of market share and, therefore, the modelling issue at hand was less important.⁵⁷ Hence, it was once again found that the Parties' submissions were likely to underestimate the estimated price impact of the Transaction.

38. Remarkably, the Parties' merger simulations predicted non-negligible price increases in many markets, and in particular for the Austrian filter pad market, the French filter pads market (considering potential divestitures of the l'Or and Grand Mere brands) and the Danish R&G and instant coffee markets (and in particular in the R&G market). The Commission also found that, for example, using less elastic aggregate demand assumptions in general tended to increase the predicted price rises. As a result, the Commission found in its Article 6(1)(c) Decision that the First Set of Merger Simulation Models was insufficient to justify the conclusion that the Transaction would not raise serious doubts as to its compatibility with the internal market.

2.3. The Parties' Second Set of Merger Simulation Models

39. During the Phase II investigation the Parties submitted further studies on the merger simulation models^{58,59} (the "Second Set of Merger Simulation Models"). First, the Parties argued that the aggregate elasticity estimates of the academic literature the Commission referred to were not relevant. According to the Parties, those estimates are based on a full coffee segment, that is, one including not only the in-home but also the out-of-home segment. Hence, the Parties argued that those estimates were not the relevant benchmark, as "*is well-known, the more products are included in a putative market, the lower is the aggregated elasticity of demand in that market*"⁶⁰, and hence the relevant aggregate elasticities should be larger in absolute value than those referred to by the Commission. Moreover, the Parties further argued that lowering the aggregate elasticity assumption did not significantly change their original results⁶¹.
40. Second, the Parties argued that including the capsules markets into the models was unnecessary as consumers could not readily switch between capsules and other coffee

⁵⁷ See, for example, Case No COMP/M.5658 – *Unilever/Sara Lee Bodycare*.

⁵⁸ Response to Article 6(1)(c), Annex 5, Response to comments on CL economic submissions in the Article 6(1)(c) Decision, 9 January 2015, ID022431.

⁵⁹ Response to RFI of 21 January 2015, 30 January 2015, ID02988.

⁶⁰ Response to Article 6(1)(c), Annex 5, Response to comments on CL economic submissions in the Article 6(1)(c) Decision, 9 January 2015, page 3, ID022431.

⁶¹ *Ibid*, page 8.

products⁶². Moreover, including the capsules markets into the models would not significantly change the results^{63,64}.

2.4. The Commission's assessment of the Parties' Second Set of Merger Simulation Models

41. The Commission, for the reasons set out in points 42-45, has found that the Second Set of Merger Simulation Models cannot be considered reliable because the models included are likely to underestimate the anti-competitive effect of the Transaction.
42. In the first place the Commission notes that the aggregate elasticity estimates of the academic literature referred to in the Article 6(1)(c) Decision are not necessarily lower than what is relevant for the in-home sales channel. Contrary to what the Parties claim, the aggregate elasticity of demand does not always decrease when more products are included in the aggregate segment. There is a decrease in the aggregate elasticity of demand if the products to be added are substitutes of the products already included. Hence, the relevant question is whether the products of the out-of-home sales channel are a substitute of the in-home channel's products. The out-of-home channel, among others, includes forms of consumption (for example hospitals and prisons) which are not suitable alternatives of the in-home consumption⁶⁵. In fact, the Commission concluded that the in-home and out-of-home channels are part of separate product markets⁶⁶. It follows that inclusion of those out-of-home channels should not necessarily decrease the aggregate elasticity. The aggregate elasticity of two unrelated segments is the weighted average of the two segments' elasticities. In any event, the size of the out-of-home segment is significantly smaller than that of the in-home segment. As a consequence, it still cannot be concluded that the high aggregate elasticity assumption used by the Parties' models is plausible and does not lead to an underestimation of the likely price effects of the Transaction.
43. Secondly, in the Parties' extended models, which include the N-capsules market as well, the price effects are higher despite the fact that the Parties use a simpler model, the so-called one-level nested logit model which might still lead to an underestimation of the price effects. The reason for that underestimation can be a one-level nested logit model which can over-estimate the competitive constraint exercised by private label products on branded products, or Nespresso capsules on Nespresso compatible capsules. In a two- or three-level nested logit framework those relative differences in the strength of competitive constraints can be better taken into account. Even the Parties' simple model specification predicts a price increase higher than [0-5]*% in the French filter pads market when a more realistic aggregate elasticity assumption is used⁶⁷. As that estimated price increase is more likely to be an underestimation of the true price increase, in itself it cannot justify the conclusion that the Transaction would not prevent competition significantly in the French filter pads market. It should be noted that those calculations were made by taking into account the Parties' Commitments of 26 November 2014 which divested the l'Or and Grand Mere brands. In France, those commitments would have eliminated the overlap in

⁶² *Ibid*, pages 9-11.

⁶³ *Ibid*, pages 10-11.

⁶⁴ Response to RFI of 21 January 2015, 30 January 2015, pages 20-21, ID02988.

⁶⁵ Form CO, page 91.

⁶⁶ See Section 7.1 of the Decision.

⁶⁷ *Ibid*, Table 8, page 20.

the R&G coffee market but not in the filter pads market. Hence, the assessment of the modelling results is also an indication as to why the Commitments of 26 November 2014 would not have solved the competition concerns raised by the Transaction.

44. Thirdly, nested logit models use only a very limited number of parameters to describe consumer preferences. Even the more realistic two- and three- level models have only three or four parameters, whereas the Parties mainly rely on one-level models, use two-level models only to a limited extent and do not use three-level models. While that model family can in principle provide some guidance on the overall level of expected effects of a merger, it is less useful when determining the strength of competitive interaction between two segments. In the context of the present case, the interaction between R&G and filter pads at the segment level in the Parties' models, including their preferred one-level nested logit models, remains directly proportional to the relative size of the two segments. That implies that, as the result of the assumed structure of the model, the R&G segment will always exert a relatively strong constraint on the filter pads segment in the Parties' model, regardless of the parameter values simply because the R&G segment has a high volume share. That further implies that the segment level's own-price elasticities of the filter pad segment will be significantly higher than that of the corresponding own price elasticity of the R&G segment regardless of the model parameters. The key question regarding the strength of the constraint on filter pads exercised by R&G is hence not measured or tested by the model. Instead it is driven by the assumptions of the model, the relative size of the segments, and the assumed aggregate elasticity. The reliance on strong assumptions to model the competitive interaction between the key segments of the category raises questions on the reliability of the modelling results. This is particularly the case as there are strong qualitative indications that the substitution from filter pads to R&G is very limited⁶⁸. Those indications together with the other factors set out in points 42 and 43 make it more likely that the models underestimate the price effects stemming from the Transaction.
45. Moreover, the chosen quantification strategy, that is to say, cost calibration, can in itself raise questions and criticisms. For example, the methodology does not allow for statistical hypothesis testing to assess the extent to which the results are driven by the modelling assumptions. Though that in itself does not necessarily render a methodology unreliable, in the present case the models are parameterized using only two or three parameters and even those parameters cannot be uniquely determined by the Parties' calibration. The only data used in the calibrations are market shares and an aggregate margin criterion. The combination of the lack of possibility of statistical testing and the necessarily very strong assumptions needed to complete the model imply that it is likely that the results are primarily driven by the untested assumptions. That casts further doubt on the models' ability to provide sufficiently reliable evidence as to the likely impact of the Transaction.
46. Overall, the Commission finds that the merger simulation results of the Parties cannot be considered reliable as, without the Final Commitments, they are likely to underestimate the anti-competitive effect of the Transaction, . Hence, the Parties' merger simulation models cannot cast any doubt on the Commission's conclusion that, in the absence of the Final Commitments, the Transaction would significantly prevent effective competition.

⁶⁸ See Section 6.7.1 of the Decision.

3. STUDIES OF THE EFFECT OF TASSIMO ON SENSEO

47. During the course of the proceedings, the Commission received several economic studies from Nestlé, which aimed at assessing the closeness of competition between Tassimo and Senseo. For the reasons set out in Sections 3.1 and 3.2, due to severe limitations in the models, the Commission does not consider the results of those economic studies to be reliable.
48. Additionally, Nestlé's studies focus primarily on the competition across different single-serve coffee machines (that is to say, Senseo, Tassimo, Dolce Gusto and Nespresso). As stated in the Commission's analysis in Section 8.2.5.2 of the Decision, even if those studies were able to find a degree of competition between Tassimo and Senseo, due to the peculiar complementarity structure between machines and consumables in the coffee systems, and due to the lack of ability (for DEMB) and incentive (for Mondelez) to increase prices, that finding would still not be enough to assess the likely impact of the Transaction on the price of the components of coffee systems in the present case.

3.1. First Tassimo Study by Nestlé and the Commission's assessment

49. Subsequent to the notification of the Transaction, Nestlé submitted an economic study (the "First Tassimo Study")⁶⁹. In that study, Nestlé argues that Mondelez, with its Tassimo single-serve system, acts as a "maverick" player, that is to say, a firm with an aggressive low price strategy driving competition, among the single-serve systems. Furthermore, the First Tassimo Study indicates that Tassimo machines are Senseo machine's closest competitors, and that Mondelez is DEMB's closest competitor in the filter pads and Nespresso compatible consumables' market⁷⁰. Nestlé therefore argues that the Transaction would eliminate a strong competitive constraint between the Parties, leading to a significant restriction of effective competition.
50. To show the competitive constraints that the Tassimo system exerts on the Senseo system, the First Tassimo Study analyses two events: the entry of Tassimo machines in the Netherlands' in 2014, and the price reductions of Tassimo machines in Germany during 2013. The study argues that in both cases the volumes of Tassimo machines sold increased significantly while the volumes of Senseo machines sold decreased. Hence, the First Tassimo Study concludes that Tassimo exerts a strong competitive constraint on Senseo.
51. In their response to the First Tassimo Study⁷¹ (the "Parties' Response to the First Tassimo Study") the Parties argued that the evidence presented by Nestlé is selective and misleading. In particular, they argued that not only the sales of Senseo machines but also the sales of drip filter machines decreased following the events analysed by Nestlé. Moreover, in the Parties' view Nestlé's analysis is incomplete as it does not investigate the price evolutions around the events, and it does not look at other countries to assess Tassimo's effect on Senseo. The Parties argued that a more complete analysis would have revealed that the relevant substitution happens between Tassimo and either Dolce Gusto or Nespresso, but not Senseo. The Parties further argued that the prices of Tassimo and

⁶⁹ M.7292 – DEMB / Mondelez: The merging parties are each other's closest competitors, 17 November 2014, ID01674.

⁷⁰ Filter pads are the consumables for the Senseo machine.

⁷¹ M.7292 - DEMB / Mondelez / Charger OpCo, Response to complaint of 17 November 2014, 20 November 2014, ID01735.

Dolce Gusto machines as well as the price of their consumables are positioned closer to each other than to the corresponding Senseo prices. In addition, according to the Parties, this similarity between Tassimo and Dolce Gusto would be even stronger if the price data accounted for the coupons offered by the coffee manufacturer upon the purchase of the coffee machines, as the available data in Nestlé's study do not include those coupons. Finally, to assess the closeness of competition in respect of consumables, the Parties added that Mondelez was more closely positioned to Nespresso with regard to N-capsules, and with regard to filter pads Nestlé ignores the effect of private label products.

52. The Commission assessed both the First Tassimo Study and the Parties' Response to the First Tassimo Study in Phase I of the proceeding and found that it was not possible to conclude that Tassimo is Senseo's closest competitor. However, at that stage of the proceeding, it was not possible to conclude that Tassimo and Senseo do not exert a competitive constraint on each other. In fact, an analysis of recent market entries of Tassimo, that is to say, in the Netherlands in 2014 and in Denmark in 2011, suggested that those market entries might have had a negative impact on the Senseo machine prices, as well as on Dolce Gusto machine prices. However, data limitations severely undermined the inferences that can be drawn from those events⁷².

3.2. The Second and Third Tassimo Studies by Nestlé and the Commission's assessment

53. During the course of Phase II of the proceedings, Nestlé submitted two additional economic studies arguing that Tassimo is a closer competitor to Senseo than to other coffee systems (the "Second Tassimo Study" and the "Third Tassimo Study", respectively).^{73,74}
54. The Second Tassimo Study analysed the effect of Tassimo's entry in 14 Member States. The study focused on the effect of Tassimo's entry on the other machines' volume sales, most notably on Senseo and Dolce Gusto. For each country, the study compared the machines' volume sales and volume market shares figures during the year before Tassimo's entry, with the same figures for the year after Tassimo's entry⁷⁵. Based on those comparisons, Nestlé concludes that "*[w]hile the arrival of Tassimo is generally accompanied by a significant increase in total market sales, for Senseo it also corresponds to a loss of sales or a complete halt of its sales growth. In contrast the entry of Tassimo has a lower effect on Nescafé Dolce Gusto's sales, even in markets where Senseo is not present.*"⁷⁶.

⁷² In general, the quantitative technique employed (called "difference-in-differences") may not be strong if the number of "events" analysed (in this case, Tassimo entries) is low and, particularly, if the periods before and after the events are not long enough. The analysis included only two entry events, for which pre-entry and post-entry time periods - respectively in the Danish and Dutch entry cases - are not long enough to deliver a reliable statistical inference

⁷³ M.7292 – DEMB / Mondelez / Charger OpCo: Preliminary assessment of Tassimo's entry in the market of portioned coffee machines, 6 February 2015, ID03083.

⁷⁴ M.7292 – DEMB / Mondelez / Charger OpCo: Econometric analysis of the effect of promotions on sales of single-served coffee machines, 20 February 2015, ID03169.

⁷⁵ Due to data limitation, for some countries it was not possible to compute volume sales and volume market shares figures for a full year before/after Tassimo's entry. In such circumstances, the period of the analysis was reduced to the longest feasible period.

⁷⁶ Preliminary assessment of Tassimo's entry in the market of portioned coffee machines, pp. 3.

55. In the Commission's assessment, a significant problem in the Second Tassimo Study is that it does not take into account the price of the machines. Hence, it disregards price reactions of competitors to Tassimo's entry. The manufacturers of coffee machines compete by setting prices, and the observed movement in the volume sales are the outcome of (among other factors) the machine prices set by the companies. Therefore, the comparison of the volume sales before and after the entry of Tassimo, without taking into account the price reaction of the competitors, cannot fully capture the closeness of competition across coffee machines. Hence, the Commission cannot regard this study as informative on the relative competitive constraint exerted by Tassimo on the other coffee machines.
56. The Third Tassimo Study analysed the effect of promotional activities of different coffee machines on the machines' volume sales. The promotional activities which are of interest in this case are the ones subsidized by the coffee manufacturers, in the form of cash-backs or free consumables. The study employed a regression analysis in first difference where the log volume sales of each coffee machine, that is to say, Nespresso, Dolce Gusto, Tassimo and Senseo, is regressed on the relative size of the promotions of all the coffee machines, and other control variables⁷⁷. The estimated coefficients of the promotions represent the percentage change in the volume sales of the coffee machine should the promotion increase by 1%. For example, the estimated coefficient of the promotions of Tassimo on Senseo's volume sales is -0.01, which means that Senseo's volume sales decrease on average by 1% for each percentage increase in the relative size of Tassimo's promotions. Based on the results of the Third Tassimo Study, Nestlé concluded that "*Senseo and Tassimo exert a significant competitive constraint on each other, and [...] such constraint might be stronger between Senseo and Tassimo than with the two other players*".⁷⁸
57. The Commission notes that there are several shortcomings in the Third Tassimo Study. In particular, the regression model suffers from a severe endogeneity bias, caused by:
- a. *Omitted variable bias*⁷⁹: The model does not account for the variation in the machines' prices that is not caused by promotional activity. For example, the model does not consider instances where the machines manufacturers directly increase or decrease the list prices of the machines. Those changes in list prices have an effect on the machines' volume sales, which the model might erroneously attribute as the effect of the included explanatory variables, which makes the estimated coefficient on those variables biased. That does not mean that *including* the machines' prices as explanatory variables of the regression would be a solution because that inclusion would exacerbate another form of endogeneity bias, the simultaneous causality, referred to in point (c) below.
 - b. *Measurement error*⁸⁰: For all the machines the analysis misses an important element of the promotional activity, the redemption rate. That is to say, the amount

⁷⁷ The relative size of the promotion is the monetary amount of the promotion divided by the list price of the machine.

⁷⁸ Econometric analysis of the effect of promotions on sales of single-served coffee machines, pp. 3.

⁷⁹ Jeffrey M. Wooldridge (2002), *Econometric Analysis of Cross Section and Panel Data*, MIT Press, Cambridge, Massachusetts, pages 50-51 and 61-63.

⁸⁰ *Ibid*, pages 51 and 209-239.

of promotions that have been issued by the coffee manufacturer and redeemed by the final consumer. Instead, the analysis assumes that all the sales of a given machine in a given period are subject to the same promotion⁸¹. That greatly overestimates the magnitude of the promotional activity, and, consequently, introduces a bias in the estimated coefficients.

- c. *Simultaneous causality*⁸²: Although the machines' list price is not fully included in the regression, it is partially included in the relative size of the promotions, that is to say the promotion value or the list price. That gives rise to the endogeneity problem mentioned in paragraph 10: the dependent variable, that is to say volume sales and the explanatory variable, that is to say the price, are simultaneously determined. Additionally, also the promotional activity may itself be endogenous and simultaneously determined with the volume sales. For example, when the sales are low, the coffee manufacturers initiate or increase the promotional activity to stimulate the demand. Simultaneous causality violates the assumption of strict exogeneity of the Ordinary Least Squares ('OLS') estimation model, as the covariate price is correlated with the error term. Hence, it causes a bias in the estimated coefficients.

58. In addition to the endogeneity bias, Nestlé's regression analysis used standard error estimates of the parameters based on Stock Keeping Unit ('SKU')-country-channel level clustering^{83,84}. That clustering choice assumes that the error terms of the regression model are correlated only within a SKU-country-channel. If, however, the error terms are allowed a broader correlation, that is to say at country level or at system-country level, the coefficients estimated by the same regression models become statistically non-significant. That indicates that the regression models' results might not be as precise as Nestlé assumes, and can actually be inconclusive from a statistical point of view.

59. Due to the serious shortcomings examined in this Section, which severely undermine the reliability of the regression analysis' results, the Commission finds the Third Tassimo Study inconclusive for the present case⁸⁵.

⁸¹ Note that the machines in the analysis are at Stock Keeping Unit (SKU, the identifier used by retailers to categorize products) level.

⁸² *Ibid*, pages 51 and 73-76.

⁸³ Channel refers to the sales channel, which is either direct, that is to say Nespresso stores or through retailers.

⁸⁴ In regression analysis "clustering the standard errors" refers to an adjustment applied to the variance of the estimates which relaxes some of the assumptions of the classical regression model.

⁸⁵ In the Annex of "*Econometric analysis of the effect of promotions on sales of single-served coffee machines*" Nestlé performs a dynamic version of its main regression model, although Nestlé notes that the model is incomplete as lacking of the necessary tests to confirm its robustness. The Commission notes that the dynamic model suffers the same limitations of the main regression model; hence, Nestlé's dynamic model is not able to produce reliable results.

CASE M.7292 – DEMB/MONDELEZ/CHARGER OPCO
COMMITMENTS TO THE EUROPEAN COMMISSION

Pursuant to Articles 8(2) and 10(2) of Council Regulation (EC) No 139/2004 (the “*Merger Regulation*”), Acorn and Mondelēz (the “*Notifying Parties*”) hereby enter into the following Commitments (the “*Commitments*”) vis-à-vis the European Commission (the “*Commission*”) with a view to rendering the creation of a full- function joint venture between the business of DEMB, an international coffee and tea company indirectly owned by Acorn, and the coffee business of Mondelēz (th“*Concentration*”) compatible with the internal market and the functioning of the EEA Agreement.

This text shall be interpreted in light of the Commission’s decision pursuant to Article 8(2) of the Merger Regulation to declare the Concentration compatible with the internal market and the functioning of the EEA Agreement (the “*Decision*”), in the general framework of European Union law, in particular in light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the “*Remedies Notice*”).

Section A
Definitions

1. For the purpose of the Commitments, the following terms shall have the following meaning:

Acorn: Acorn Holding B.V, a private limited liability company (*besloten vennootschap met beperkte aansprakelijkheid*) incorporated under the laws of the Netherlands, with its registered office in Amsterdam, the Netherlands, and registered in the Dutch Commercial Register under number 57582041.

Affiliated Undertakings: undertakings controlled by the Parties and/or by the ultimate parents of the Parties, including the joint venture, whereby the notion of control shall be interpreted pursuant to Article 3 of the Merger Regulation and in light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (the “*Consolidated Jurisdictional Notice*”).

Andezeno Beans: as defined at paragraph 7.1(b)(v) of Schedule A

Assets: the assets that contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Business.

Austrian Brand-Related IP Rights: as listed in Annex 2 to Schedule D.

Austrian Closing Date: a date within a period of [...] * from the approval of the Purchaser and the licence terms by the Commission. If the [...] * period would otherwise have expired prior to the closing of the

Concentration, then the date shall be within a period of [...]>* after the closing of the Concentration.

Austrian Divestment Brand: as defined in paragraph 4.1(a) of Schedule D.

Austrian Divestment Business: as defined in paragraph 4.1(a) of Schedule D.

Austrian Transitional Support Period: a period to be agreed between the Notifying Parties and the Purchaser, beginning on the Austrian Closing Date and not to exceed 12 months.

Carte Noire Divestment Brand: as defined in paragraph 5(a);

Carte Noire Divestment Business: as defined in paragraph 5(a).

Carte Noire Divestment Business Personnel: as defined in Schedule A, paragraph 7.1(d).

Carte Noire Divestment Products: means the current range of Carte Noire in-home R&G, Filter Pads, and N-Capsules products sold to customers in the EEA including the current Carte Noire in-home R&G, Filter Pads and N- Capsules pipeline products.

Charger OpCo: Charger OpCo B.V., a private limited liability company (*besloten vennootschap met beperkte aansprakelijkheid*) incorporated under the laws of the Netherlands, with its registered office in Amsterdam, the Netherlands and registered in the Dutch Commercial Register under number 60551720.

Closing: the transfer of the legal title to the Divestment Business to the Purchaser(s). For the avoidance of doubt, Closing of the Carte Noire Divestment Business, and the Danish Divestment Business could occur on different dates.

Closing Period: the period of [...]>* from the approval of the Purchaser and the terms of sale by the Commission.

Confidential Information: any business secrets, know-how, commercial information, or any other information of a proprietary nature that is not in the public domain.

Conflict of Interest: any conflict of interest that impairs the Trustee's objectivity and independence in discharging its duties under the Commitments.

Concentration: as defined in the first recital to these Commitments.

Danish Divestment Brand: as defined in paragraph 6(a).

Danish Divestment Business: as defined in paragraph 6(a).

Danish Personnel: all staff currently employed by, seconded to or to be hired by the Danish Divestment Business, who are dedicated to the Danish Divestment Business as set out in Annex 3 to Schedule C.

DEMB: D.E. Master Blenders 1753 B.V., a private limited liability company (*besloten vennootschap met beperkte aansprakelijkheid*) incorporated under the laws of the Netherlands, with its registered office in Amsterdam, the Netherlands, and registered in the Dutch Commercial Register under number 54760968.

Divestment Business: the Carte Noire Divestment Business, the Danish Divestment Business.

Divestiture Trustee: one or more natural or legal person(s) who is/are approved by the Commission and appointed by the Parties and who has/have received from the Parties the exclusive Trustee Mandate to sell the Divestment Business to a Purchaser at no minimum price.

Effective Date: the date of adoption of the Decision.

First Divestiture Period: the period of [...]* from the Effective Date.

[...]*

French Facility: the Lavérune Facility, as defined in paragraph 5(c), and more fully described in Schedule B.

French Facility Personnel: as defined in Schedule B, paragraph 4.

French Personnel: all staff currently employed by, seconded to or to be hired by the Carte Noire Divestment Business, including the Carte Noire Divestment Business Personnel and the French Facility Personnel, as indicated in the Schedules.

FTE: means full-time equivalent.

Hold Separate Manager: the person or persons appointed by the Parties for the Divestment Business to manage the day-to-day business under the supervision of the Monitoring Trustee.

Instant: means instant or soluble coffee, including instant mixes and microground products.

IP: means rights in and to intellectual property.

Key Personnel: all personnel necessary to maintain the viability and competitiveness of the Divestment Business, as listed in the Schedules, including the Hold Separate Manager.

Merrild Products: means the current range of Merrild in-home coffee products, including R&G, Filter Pads and Instant, as well as the current pipeline products (if any).

Mondelēz: Mondelēz International Inc., incorporated under the laws of the Commonwealth of Virginia and registered under company filing number 0550179 with the Secretary of State of the Commonwealth of Virginia.

Monitoring Trustee: one or more natural or legal person(s) who is/are approved by the Commission and appointed by the Notifying Parties, and

who has/have the duty to monitor the Parties' compliance with the conditions and obligations attached to the Decision.

N-Capsules: means Nespresso-compatible capsules.

OOH: means the out-of-home channel.

Parties: the Notifying Party/Notifying Parties and the undertaking that is the target of the Concentration.

Personnel: the Danish Personnel or the French Personnel (as the case may be).

Philips: Philips Consumer Lifestyle B.V., having its principal office at Piet Heinkade 55, (1019 GM) Amsterdam, The Netherlands, and Koninklijke Philips Electronics N.V., having its principal office at Amstelplein 2, (1096 BC) Amsterdam, The Netherlands.

Philips Agreement: means the agreement between DEMB and Philips entitled Coffee System Agreement on Pod Systems, dated 30 March 2012, which governs their collaboration with respect to the joint commercialisation of Senseo appliances.

Purchaser(s): the entity(ies) approved by the Commission as acquirer(s) of the Divestment Business, or, in the case of the Austrian Divestment Business, as licensee, in accordance with the criteria set out in Section D.

Purchaser Criteria: the criteria laid down in paragraph 20 of these Commitments that the Purchaser(s) must fulfil in order to be approved by the Commission.

R&G: roast and ground coffee products.

Schedules: the schedules to these Commitments describing in more detail the Divestment Business.

Senseo Filter Pads Products: in-home Senseo filter pad products as listed in paragraph 1 of Annex 1 to Schedule D.

Senseo N-Capsules Products: in-home Senseo N-Capsules products as listed in paragraph 2 of Annex 1 to Schedule D.

Shared IP Licence: as defined in paragraph 7.1 of **Annex 2 to Schedule**

A. T-Discs: means Tassimo-compatible discs.

TE Licence: as defined in paragraph 7.1(b)(iii) of Schedule A.

Transitional Support Arrangements: the necessary transitional support services to be agreed between the Notifying Parties and the Purchaser(s) and to be supplied to the Purchaser(s) including, at the option of the Purchaser(s), the manufacture of the Carte Noire Divestment Products that are not currently manufactured in the French Facility or the products manufactured under the Danish Divestment Brand (as the case may be), as more fully described in the Schedules.

Transitional Support Period: a period to be agreed between the Notifying Parties and the Purchaser(s), beginning on Closing and not to exceed (without the Commission's prior approval) 18 months in respect of the Carte Noire Divestment Business and 12 months in respect of the Danish Divestment Business during which Charger OpCo shall supply to the Purchaser(s) the Transitional Support Arrangements.

Trustee(s): the Monitoring Trustee and/or the Divestiture Trustee as the case may be.

Trustee Divestiture Period: the period of [...] from the end of the First Divestiture Period.

[...]*

[...]*

Section B

The commitments to divest and license and the Divestment Business

Commitment to divest

2. In order to maintain effective competition, the Notifying Parties commit to divest, or procure the divestiture of, the Divestment Business by the end of the Trustee Divestiture Period as a going concern to one or more purchasers and on terms of sale approved by the Commission in accordance with the procedure described in paragraph 21 of these Commitments. To carry out the divestiture, the Notifying Parties commit to find a purchaser (or purchasers) and to enter into, or to procure that Charger OpCo or any of their relevant Affiliates enter into, a final binding sale and purchase agreement (or agreements) or, as the case may be, receive an unconditional and binding offer (or put option) under French law, for the sale of the Divestment Business (or the remaining portion of the Divestment Business not already sold to an approved Purchaser) within the First Divestiture Period. If the Notifying Parties, Charger OpCo or any relevant Affiliates have not entered into such an agreement(s), or, as the case may be, have not received an unconditional and binding offer (or put option) under French law, at the end of the First Divestiture Period, the Notifying Parties shall grant, and if necessary shall procure that Charger OpCo and any relevant Affiliates shall grant, the Divestiture Trustee an exclusive mandate to sell the Divestment Business (or the remaining portion thereof) in accordance with the procedure described in paragraph 33 in the Trustee Divestiture Period. For the avoidance of doubt, the Notifying Parties shall be permitted to sell the Carte Noire Divestment Business, the Danish Divestment Business and the Austrian Divestment Business to the same Purchaser or to separate Purchasers.
3. The Notifying Parties shall be deemed to have complied with the commitment in paragraph 2 if:
 - (a) by the end of the Trustee Divestiture Period, the Notifying Parties, Charger OpCo or any relevant Affiliates, or the Divestiture Trustee has entered into a final binding sale and purchase agreement(s) or, as the case may be, have received an

unconditional and binding offer (or put option) under French law for the sale of the Divestment Business to the Purchaser(s) and the Commission approves the proposed Purchaser(s) and the terms of sale as being consistent with the Commitments in accordance with the procedure described in paragraph 21; and

- (b) the Closing(s) of the sale of the Divestment Business to the Purchaser(s) takes(s) place within the Closing Period.
4. In order to maintain the structural effect of the Commitments, the Notifying Parties and Charger OpCo (as the case may be) shall, for a period of 10 years after Closing, not acquire, whether directly or indirectly, the possibility of exercising influence (as defined in paragraph 43 of the Remedies Notice, footnote 3) over the whole or part of the Divestment Business and the Austrian Divestment Business, unless, following the submission of a reasoned request from the Notifying Party or Charger OpCo (as the case may be) showing good cause and accompanied by a report from the Monitoring Trustee (as provided in paragraph 47 of these Commitments), the Commission finds that the structure of the market has changed to such an extent that the absence of influence over the Divestment Business or the relevant part of it or the Austrian Divestment Business is no longer necessary to render the proposed concentration compatible with the internal market.

Structure and definition of the Divestment Business

5. *France*

- (a) Subject to the provisions set out in sub-paragraph (b), the Carte Noire Divestment Business (as defined below), described in more detail in **Schedule A** and **Schedule B**, consists of the Carte Noire brand (including brand-related IP) in the EEA (the “*Carte Noire Divestment Brand*”) and of the R&G, Filter Pad and N-Capsules business of Mondelēz currently operated under the Carte Noire Divestment Brand in the EEA (the “*Carte Noire Divestment Business*”). For the avoidance of doubt the Carte Noire Divestment Business does not include the OOH, Instant and T-Discs business of Mondelēz currently operated under the Carte Noire Divestment Brand in the EEA.
- (b) For the purpose of rebranding certain products that do not raise competition concerns, the Purchaser shall grant the Notifying Parties, Charger OpCo and their Affiliates exclusive, irrevocable, non-renewable, royalty-free licences to use the Carte Noire Divestment Brand in relation to the marketing, manufacture and sale (and any related disposal, offer to dispose, import and warehousing) of Carte Noire branded OOH, Instant and T-Discs products in the EEA for two years and in relation to Velours Noir products in the EEA for a period of one year.

- (c) The Carte Noire Divestment Business will include Mondelēz's Lavérune manufacturing plant (the "**French Facility**"), subject to the reconfiguration arrangements further described in **Schedule B**.
 - (d) For the avoidance of doubt, the Carte Noire Divestment Business will not include any IP that relates to products that are retained by the Parties, including without limitation the Carte Noire products retained by the Parties under Clause 5(a) above. The Parties will grant to the Purchaser the Shared IP Licence further described at paragraph 7.1 of **Annex 2 to Schedule A** in respect of shared IP.
6. **Denmark**
- (a) Subject to the provisions set out in sub-paragraph (b), the Danish Divestment Business (as defined below), described in more detail in **Schedule C**, consists of: the business of DEMB currently operated under the brand name Merrild in the EEA (the "**Danish Divestment Brand**"), with the exception of the Merrild OOH business (the "**Danish Divestment Business**")
 - (b) For the purpose of rebranding certain products that do not raise competition concerns, the Purchaser shall grant DEMB, Charger OpCo and their Affiliates exclusive, irrevocable, non-renewable, royalty-free licences to use the IP of Merrild during a transitional licence period in relation to OOH in the EEA for a period of one year and in relation to Café Noir and Senseo products for a period of one year.
7. The legal and functional structure of the Divestment Business is described in the Schedules. The Divestment Business includes all assets and staff necessary to maintain and run the current operation necessary to ensure the viability and competitiveness of the Divestment Business, in particular:
- (a) all tangible and intangible assets (including through intellectual property rights, transfers and licences) necessary to manufacture and sell the Carte Noire Divestment Products, including, if any, pipeline products (except that no manufacturing facility will be transferred in relation to the Merrild Products and in relation to those SKUs the production of which is currently outsourced to third party manufacturers);
 - (b) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Divestment Business;
 - (c) all leases and commitments of the Divestment Business;
 - (d) the disclosure of all customer, credit and other records and full information about the terms of customer contracts of the Divestment Business; and
 - (e) the French Personnel and the Danish Personnel.
8. In addition, the Divestment Business includes the benefit:

- (a) for a Transitional Support Period and on terms and conditions equivalent to those at present afforded to the Divestment Business and described in more detail in **Schedule A** and **Schedule C**, of all current arrangements under which the Notifying Parties or Charger OpCo (as the case may be) or their Affiliated Undertakings supply products or services to the Divestment Business, constituting the Transitional Support Arrangements and as detailed in **Schedule A** and **Schedule C** unless otherwise agreed with the Purchaser(s);
 - (b) for the Transitional Support Period, on a cost basis to be agreed with the Purchaser and described in more detail in **Schedule A**, of all arrangements under which the Notifying Parties or Charger OpCo (as the case may be) or their Affiliated Undertakings co-manufacture Carte Noire Divestment Products that are not currently manufactured in the French Facility; and
 - (c) for the Transitional Support Period, on a cost basis to be agreed with the Purchaser and described in more detail in **Schedule C**, of all arrangements under which the Notifying Parties or Charger OpCo (as the case may be) or their Affiliated Undertakings co-manufacture products under the Danish Divestment Brand.
9. Strict firewall procedures will be adopted so as to ensure that any competitively sensitive information related to, or arising from the Transitional Support Arrangements will not be shared with, or passed on to, anyone outside the Notifying Parties' retained businesses or Charger OpCo (as the case may be).
10. For the avoidance of doubt, the Danish Divestment Brand business will not include any IP that relates exclusively or predominantly to products that are retained by the Parties, including without limitation the Café Noir products retained by the Parties as further described in Annex 5 **Schedule C** below.

Commitment to license

11. *Austria*

- (a) the Notifying Parties shall procure that Charger OpCo will grant a licence for the use of the Austrian Divestment Brand. The terms of this licence are further described in paragraph 4.1(a) of **Schedule D**;
- (b) the Austrian Divestment Business shall include the benefit, on a cost basis to be agreed with the Purchaser, of co-manufacturing services as further described in paragraph 4.1(c) of **Schedule D**;
- (c) the Austrian Divestment Business shall also include the technical services reasonably required by the Purchaser to enable the Purchaser to transfer the production of Senseo Filter Pad Products, as further described in paragraph 4.1(e) of **Schedule D**; and

- (d) the Notifying Parties shall be deemed to have complied with the commitment in this paragraph 11 if, by the end of the Trustee Divestiture Period, the Notifying Parties, Charger OpCo or any relevant Affiliates, or the Divestiture Trustee has entered into a final binding licence agreement in relation to the Austrian Divestment Brand, and the Commission approves the proposed Purchaser and the terms of licence as being consistent with the Commitments in accordance with the procedure described in paragraph 21.

Section C

Related commitments

Preservation of viability, marketability and competitiveness

12. From the Effective Date until Closing or until the Austrian Closing Date (as the case may be), the Notifying Parties and Charger OpCo (as the case may be) shall preserve or procure the preservation of the economic viability, marketability and competitiveness of the Divestment Business and the Austrian Divestment Business, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Business or the Austrian Divestment Business. In particular the Notifying Parties undertake on their behalf and on behalf of Charger OpCo:
- (a) not to carry out any action that might have a significant adverse impact on the value, management or competitiveness of the Divestment Business or the Austrian Divestment Business or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of the Divestment Business or the Austrian Divestment Business;
 - (b) to make available, or procure to make available, sufficient resources for the development of the Divestment Business and the Austrian Divestment Business, on the basis of the business plan of the Carte Noire Divestment Business, the existing business plans for the Merrild Products and the existing business plan for the Austrian Divestment Business;
 - (c) to take all reasonable steps, or procure that all reasonable steps are being taken, including appropriate incentive schemes (based on industry practice), to encourage all Key Personnel to remain with the Divestment Business, and not to solicit or move any Personnel to the remaining business of the Notifying Parties or Charger OpCo (as the case may be). Where, nevertheless, individual members of the Key Personnel exceptionally leave the Divestment Business, the Notifying Parties or Charger OpCo (as the case may be) shall provide a reasoned proposal to replace the person or persons concerned to the Commission and the Monitoring Trustee(s). The Notifying Parties or Charger OpCo (as the case may be) must be able to demonstrate to the Commission that the replacement is well suited to carry out the functions exercised by those individual members of the Key

Personnel. The replacement shall take place under the supervision of the Monitoring Trustee(s), who shall report to the Commission.

Hold-separate obligations

13. To the extent possible, without impeding the proper functioning of the Divestment Business and/or the business retained by the Notifying Parties, the Notifying Parties or Charger OpCo (as the case may be) commit, from the Effective Date until Closing, to keep the Divestment Business separate from the businesses they are retaining and to ensure that the Key Personnel of the Divestment Business have no involvement in any business retained by the Notifying Parties or Charger OpCo (as the case may be) and do not report to any individual outside the Divestment Business. To the extent possible, without impeding the proper functioning of the Austrian Divestment Business and/or the business retained by the Notifying Parties, the Notifying Parties or Charger OpCo (as the case may be) commit, from the Effective Date until the Austrian Closing Date, to keep the Austrian Divestment Business separate from the businesses they are retaining.
14. Until Closing, the Notifying Parties or Charger OpCo (as the case may be) shall assist the Monitoring Trustee(s) in ensuring, that the Divestment Business is managed as a distinct and saleable entity separate from the businesses which Charger OpCo is retaining. Immediately after the Effective date, the Notifying Parties shall appoint a Hold Separate Manager. The Notifying Parties may either appoint the Hold Separate Manager for the entire Divestment Business and the Austrian Divestment Business or one Hold Separate Manager for each of the Carte Noire Divestment Business, the Danish Divestment Business and the Austrian Divestment Business, or any combination thereof. Each Hold Separate Manager, who shall be part of the Key Personnel (except in the case of the Austrian Divestment Business), shall manage the Divestment Business and the Austrian Divestment Business independently and in the best interest of the business with a view to ensuring its continued economic viability, marketability and competitiveness and its independence from the businesses retained by the Notifying Parties or Charger OpCo (as the case may be). Each Hold Separate Manager shall closely cooperate with and report to the Monitoring Trustee(s) and, if applicable, the Divestiture Trustee. Any replacement of a Hold Separate Manager shall be subject to the procedure laid down in paragraph 12(c) of these Commitments. The Commission may, after having heard the relevant Notifying Party and Charger OpCo, require that Notifying Party or Charger OpCo (as the case may be) to replace the Hold Separate Manager.

Ring-fencing

15. To the extent possible without impeding the proper functioning of the Divestment Business and the Austrian Divestment Business, the Notifying Parties or Charger OpCo (as the case may be) shall implement, or procure to implement, all necessary measures to ensure that they do not, after the Effective Date, obtain any Confidential Information relating to the Divestment Business and the Austrian Divestment Business. In

particular, the Notifying Parties will require appropriate members of the Carte Noire Divestment Business's workforce co-mingled with Mondelēz or appropriate members of the Notifying Parties' retained business's work force to sign non-disclosure agreements relating to Confidential Information, the details of which to be determined in coordination with the Monitoring Trustee. Moreover, the participation of the Divestment Business and the Austrian Divestment Business in any central information technology network shall be severed to the extent possible, without compromising the viability of the Divestment Business or the Austrian Divestment Business. The Notifying Parties or Charger OpCo (as the case may be) may obtain or keep information relating to the Divestment Business and the Austrian Divestment Business which is reasonably necessary for the divestiture of the Divestment Business and the Austrian Divestment Business or the disclosure of which to the Notifying Parties or Charger OpCo (as the case may be) is required by law.

Non-solicitation clause

16. The Parties undertake, subject to customary limitations, not to solicit, and to procure that Affiliated Undertakings do not solicit, the Key Personnel transferred with the Divestment Business for a period of two years after Closing.

Due diligence

17. In order to enable potential purchasers to carry out a reasonable due diligence of the Divestment Business and the Austrian Divestment Business, the Notifying Parties shall, subject to customary confidentiality assurances and dependent on the stage of the divestiture process and to the extent this has not yet been done already:
 - (a) provide to potential purchasers sufficient information as regards the Divestment Business and the Austrian Divestment Business;
 - (b) provide to potential purchasers sufficient information relating to the Personnel and allow them reasonable access to the Personnel.

Reporting

18. The Notifying Parties shall submit written reports in English on potential purchasers of the Divestment Business and the Austrian Divestment Business and developments in the negotiations with such potential purchasers to the Commission and the Monitoring Trustee no later than 10 days after the end of every month following the Effective Date (or otherwise at the Commission's request). The Notifying Parties shall submit a list of all potential purchasers having expressed interest in acquiring the Divestment Business or the Austrian Divestment Business to the Commission at each and every stage of the divestiture process, as well as a copy of all the offers made by potential purchasers within five days of their receipt (or, if received beforehand, within five days of the Effective Date).
19. Subject to the second sentence of this paragraph, the Notifying Parties shall inform the Commission and the Monitoring Trustee(s) on the

preparation of the data room documentation and the due diligence procedure and shall submit a copy of any information memorandum to the Commission and the Monitoring Trustee(s) before sending the memorandum out to potential purchasers. Where any such information memorandum has been sent to potential purchasers prior to the Effective Date, the Notifying Parties shall submit documentation describing the data room and the due diligence procedure and a copy of such information memorandum to the Commission and the Monitoring Trustee(s) no later than five days after the Effective Date (and if the Monitoring Trustee(s) is appointed later than this date, to the Monitoring Trustee(s) no later than five days after its appointment).

Section D

The Purchaser(s)

20. In order to be approved by the Commission, the Purchaser(s) must fulfil the following criteria:
 - (a) The Purchaser(s) shall be independent of and unconnected to the Notifying Parties and their Affiliated Undertakings (this being assessed having regard to the situation following the divestiture).
 - (b) The Purchaser(s) shall have the financial resources, proven expertise and incentive to maintain and develop the Divestment Business or the Austrian Divestment Business (as the case may be) as a viable and active competitive force in competition with the Parties and other competitors;
 - (c) The acquisition of the Divestment Business or the Austrian Divestment Business (as the case may be) by the Purchaser(s) must neither be likely to create, in light of the information available to the Commission, prima facie competition concerns nor give rise to a risk that the implementation of the Commitments will be delayed. In particular, the Purchaser(s) must reasonably be expected to obtain all necessary approvals from the relevant regulatory authorities for the acquisition of the Divestment Business or the Austrian Divestment Business (as the case may be).
21. The final binding sale and purchase agreement(s) (as well as ancillary agreements) or, as the case may be, the unconditional and binding offer (or put option) under French law, relating to the divestment of the Divestment Business, and in case of the Austrian Divestment Business, the licence agreement relating to the Austrian Divestment Brand, shall be conditional on the Commission's approval. When the Notifying Parties or Charger OpCo have reached an agreement(s) with a purchaser(s) or, as the case may be, the purchaser has made an unconditional and binding offer (or given an unconditional or binding put option) under French law, they shall submit a fully documented and reasoned proposal, including a copy of the final agreement(s) or, as the case may be, of the final unconditional binding offer (or put option) under French law, within one week to the Commission and the relevant Monitoring Trustee. The Notifying Parties must be able to demonstrate to

the Commission that (i) the purchaser(s) fulfils the Purchaser Criteria and that the Divestment Business is being sold, (ii) with specific reference to the Carte Noire Divestment Business, [...] has given its consent to grant the Purchaser of the Carte Noire Divestment Business an EEA-wide licence on terms no less favourable than currently enjoyed by Mondelēz, and (iii) the Austrian Divestment Brand is being licensed, in a manner consistent with the Decision and the Commitments. For the approval, the Commission shall verify that the purchaser(s) fulfils the Purchaser Criteria and that the Divestment Business is being sold, and the Austrian Divestment Brand is being licensed, in a manner consistent with the Commitments including their objective to bring about a lasting structural change in the market. At the Notifying Parties' request, the Commission may approve the sale of the Divestment Business without one or more Assets or parts of the Personnel, or by substituting one or more Assets or parts of the Personnel with one or more different assets or different personnel, if this does not affect the viability and competitiveness of the Divestment Business after the sale, taking account of the proposed purchaser(s).

Section E

Trustee

I. Appointment procedure

22. The Notifying Parties shall appoint one or more Monitoring Trustee(s) to carry out the functions specified in these Commitments for a Monitoring Trustee(s). The Notifying Parties commit not to close the Concentration before the appointment of a Monitoring Trustee(s).
23. If the Notifying Parties have not entered into a binding sale and purchase agreement(s) or, as the case may be, have not received an unconditional and binding offer (or put option) under French law, regarding the respective Divestment Business one month before the end of the First Divestiture Period or if the Commission has rejected a purchaser proposed by the Notifying Parties at that time or thereafter, the Notifying Parties shall appoint a Divestiture Trustee(s). The appointment of the Divestiture Trustee(s) shall take effect upon the commencement of the Trustee Divestiture Period.
24. The Trustee(s) shall:
 - (i) at the time of appointment, be independent of the Notifying Parties and their Affiliated Undertakings;
 - (ii) possess the necessary qualifications to carry out its mandate, for example have sufficient relevant experience as an investment banker or consultant or auditor; and
 - (iii) neither have nor become exposed to a Conflict of Interest.
25. The Trustee(s) shall be remunerated by the Notifying Parties in a way that does not impede the independent and effective fulfilment of its mandate. In particular, where the remuneration package of a Divestiture

Trustee(s) includes a success premium linked to the final sale value of the Divestment Business, such success premium may only be earned if the divestiture takes place within the Trustee Divestiture Period.

Proposal by the Notifying Parties

26. No later than two weeks after the Effective Date, the Notifying Parties shall submit the name or names of one or more natural or legal persons whom the Notifying Parties propose to appoint as the Monitoring Trustee(s) to the Commission for approval. No later than one month before the end of the First Divestiture Period or on request by the Commission, the Notifying Parties shall submit a list of one or more persons whom the Notifying Parties propose to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the person or persons proposed as Trustee fulfil the requirements set out in paragraph 24 and shall include:
- (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;
 - (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks;
 - (c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether different trustees are proposed for the two functions.

Approval or rejection by the Commission

27. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, the Notifying Parties shall appoint or cause to be appointed the person or persons concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Notifying Parties shall be free to choose the Trustee(s) to be appointed from among the names approved. The Trustee(s) shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Notifying Parties

28. If all the proposed Trustees are rejected, the Notifying Parties shall submit the names of at least two more natural or legal persons within one week of being informed of the rejection, in accordance with paragraphs 22 and 26 of these Commitments.

Trustee nominated by the Commission

29. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom the Notifying Parties shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

30. The Trustee shall assume its specified duties and obligations in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or the Notifying Parties or Charger OpCo, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee(s)

31. The Monitoring Trustee(s) shall:
- (a) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision;
 - (b) oversee, in close co-operation with the Hold Separate Manager(s), the on-going management of the Divestment Business and the Austrian Divestment Business with a view to ensuring its continued economic viability, marketability and competitiveness and monitor compliance by the Notifying Parties or Charger OpCo (as the case may be) with the conditions and obligations attached to the Decision. To that end the Monitoring Trustee(s) shall:
 - (i) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Business and the Austrian Divestment Business, and the keeping separate of the Divestment Business from the business retained by the Parties, in accordance with paragraphs 9, 10 and 15 of these Commitments;
 - (ii) supervise the management of the Divestment Business and the Austrian Divestment Business as a distinct and saleable entity, in accordance with paragraph 14 of these Commitments;
 - (iii) with respect to Confidential Information:
 - (A) determine and effectively put in place all necessary measures to ensure that the Notifying Parties or ChargerOpCo (as the case may be) does not after the Effective Date obtain any Confidential Information relating to the Divestment Business and the Austrian Divestment Business;
 - (B) in particular strive for the severing of the Divestment Business' participation in a central information technology network to the extent possible, without compromising the viability of the Divestment Business and the Austrian Divestment Business;

- (C) make sure that any Confidential Information relating to the Divestment Business and the Austrian Divestment Business obtained by the Notifying Parties or Charger OpCo (as the case may be) before the Effective Date is eliminated to the extent technically possible and will not be used by the party who has obtained such information;
 - (D) decide whether such information may be disclosed to or kept by the Notifying Parties or Charger OpCo (as the case may be) as the disclosure is reasonably necessary to allow that party to carry out the divestiture or as the disclosure is required by law; and
 - (iv) monitor the splitting of assets and the allocation of Personnel between the Divestment Business and the Notifying Parties or Charger OpCo (as the case may be, and where applicable) or Affiliated Undertakings;
- (c) propose to the Notifying Parties or Charger OpCo (as the case may be) such measures as the Monitoring Trustee considers necessary to ensure that party's compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability or competitiveness of the Divestment Business and the Austrian Divestment Business, the holding separate of the Divestment Business and the Austrian Divestment Business and the nondisclosure of competitively sensitive information;
- (d) review and assess potential purchasers as well as the progress of the divestiture process and verify that, dependent on the stage of the divestiture process:
 - (i) potential purchasers receive sufficient and correct information relating to the Divestment Business and the Austrian Divestment Business and the Personnel in particular by reviewing, if available, the data room documentation, the information memorandum and the due diligence process, and
 - (ii) potential purchasers are granted reasonable access to the Personnel;
- (e) act as a contact point for any requests by third parties, in particular potential purchasers, in relation to the Commitments;
- (f) provide to the Commission, sending the Notifying Parties or Charger OpCo (as the case may be) a non-confidential copy at the same time, a written report within 15 days after the end of every month that shall cover the operation and management of the Divestment Business and the Austrian Divestment Business

as well as the splitting of assets and the allocation of Personnel (where applicable) so that the Commission can assess whether the business is held in a manner consistent with the Commitments and the progress of the divestiture process as well as potential purchasers;

- (g) promptly report in writing to the Commission, sending the Notifying Parties or Charger OpCo (as the case may be) a non-confidential copy at the same time, if it concludes on reasonable grounds that either of the Notifying Parties or Charger OpCo is failing to comply with these Commitments;
- (h) within one week after receipt of the documented proposal referred to in paragraph 21 of these Commitments, submit to the Commission, sending the Notifying Parties or Charger OpCo (as the case may be) a non-confidential copy at the same time, a reasoned opinion as to the suitability and independence of the proposed purchaser and the viability of the Divestment Business and the Austrian Divestment Business after the sale and as to whether the Divestment Business is sold and the Austrian Divestment Business is licensed in a manner consistent with the conditions and obligations attached to the Decision, in particular, if relevant, whether the Sale of the Divestment Business without one or more Assets or not all of the Personnel affects the viability of the Divestment Business after the sale, taking account of the proposed purchaser;
- (i) assume the other functions assigned to the Monitoring Trustee(s) under the conditions and obligations attached to the Decision.

32. If the Monitoring and Divestiture Trustee are not the same legal or natural persons, the Monitoring Trustee and the Divestiture Trustee shall cooperate closely with each other during and for the purpose of the preparation of the Trustee Divestiture Period in order to facilitate each other's tasks.

Duties and obligations of the Divestiture Trustee

33. Within the Trustee Divestiture Period, the Divestiture Trustee shall sell at no minimum price the Divestment Business (or the remaining proportion) to a purchaser, provided that the Commission has approved both the purchaser and the final binding sale and purchase agreement (and ancillary agreements) as in line with the Decision and the Commitments in accordance with paragraphs 20 and 21 of these Commitments. The Divestiture Trustee shall include in the sale and purchase agreement (as well as in any ancillary agreements) such terms and conditions as it considers appropriate for an expedient sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the sale and purchase agreement such customary representations and warranties and indemnities as are reasonably required to effect the sale. The Divestiture Trustee shall protect the legitimate financial interests of the Notifying Parties and Charger OpCo (as the case may be), subject to the Notifying Parties' and Charger OpCo's unconditional obligation to divest

at no minimum price in the Trustee Divestiture Period. These provisions will apply *mutatis mutandis* to the licensing of the Austrian Divestment Brand.

34. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the end of every month with a simultaneous copy to the Monitoring Trustee and a non-confidential copy to the Notifying Parties.

III. Duties and obligations of the Parties

35. The Notifying Parties or Charger OpCo as appropriate shall provide and shall cause its advisors to provide the Trustee(s) with all such cooperation, assistance and information as the Trustee(s) may reasonably require to perform its tasks. The Trustee(s) shall have full and complete access to any of the Notifying Parties', Charger OpCo's or the Divestment Business' and the Austrian Divestment Business' books, records, documents, management or other personnel, facilities, sites and technical information necessary for fulfilling its duties under the Commitments and the Notifying Parties, Charger OpCo and the Divestment Business shall provide the Trustee(s) upon request with copies of any document. The Notifying Parties, Charger OpCo and the Divestment Business shall make available to the Trustee(s) one or more offices on their premises and shall be available for meetings in order to provide the Trustee(s) with all information necessary for the performance of its tasks.
36. The Notifying Parties or Charger OpCo (as appropriate) shall provide the Monitoring Trustee(s) with all managerial and administrative support that it may reasonably request on behalf of the management of the Divestment Business and the Austrian Divestment Business. This shall include all administrative support functions relating to the Divestment Business and the Austrian Divestment Business which are currently carried out at headquarters level. The Notifying Parties or Charger OpCo (as the case may be) shall provide and shall cause its advisors to provide the Monitoring Trustee(s), on request, with the information submitted to potential purchasers, in particular give the Monitoring Trustee(s) access to the data room documentation and all other information granted to potential purchasers in the due diligence procedure. The Notifying Parties or Charger OpCo (as the case may be) shall inform the Monitoring Trustee(s) on possible purchasers, submit lists of potential purchasers at each stage of the selection process, including the offers made by potential purchasers at those stages, and keep the Monitoring Trustee(s) informed of all developments in the divestiture process.
37. The Notifying Parties and Charger OpCo (as appropriate) shall grant or procure Affiliated Undertakings to grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee(s) to effect the sale (including ancillary agreements), the Closing and all actions and

declarations which the Divestiture Trustee(s) considers necessary or appropriate to achieve the sale and the Closing, including the appointment of advisors to assist with the sale process. Upon request of the Divestiture Trustee(s), the Notifying Parties or Charger OpCo (as appropriate) shall cause the documents required for effecting the sale and the Closing to be duly executed.

38. The Notifying Parties or Charger OpCo (as appropriate) shall indemnify the Trustee(s) and its employees and agents (each an “**Indemnified Party**”) and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to the Notifying Parties or Charger OpCo (as the case may be) for, any liabilities arising out of the performance of the Trustee’s duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee(s), its employees, agents or advisors.
39. At the expense of the Notifying Parties or Charger OpCo (as appropriate), the Trustee(s) may appoint advisors (in particular for corporate finance or legal advice), subject to that party’s approval (this approval not to be unreasonably withheld or delayed) if the Trustee(s) considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate, provided that any fees and other expenses incurred by the Trustee(s) are reasonable. Should that party refuse to approve the advisors proposed by the Trustee(s) the Commission may approve the appointment of such advisors instead, after having heard that party. Only the Trustee(s) shall be entitled to issue instructions to the advisors. Paragraph 37 of these Commitments shall apply *mutatis mutandis*. In the Trustee Divestiture Period, the Divestiture Trustee(s) may use advisors who served the Notifying Parties or Charger OpCo (as the case may be) during the First Divestiture Period if the Divestiture Trustee(s) considers this in the best interest of an expedient sale.
40. The Notifying Parties and Charger OpCo (as the case may be) agree that the Commission may share Confidential Information proprietary to that party with the Trustee(s). The Trustee(s) shall not disclose such information and the principles contained in Article 17 (1) and (2) of the Merger Regulation apply *mutatis mutandis*.
41. The Notifying Parties agree that the contact details of the Monitoring Trustee(s) are published on the website of the Commission’s Directorate- General for Competition and they shall inform interested third parties, in particular any potential purchasers, of the identity and the tasks of the Monitoring Trustee(s).
42. For a period of 10 years from the Effective Date the Commission may request all information from the Parties that is reasonably necessary to monitor the effective implementation of these Commitments.

IV. Replacement, discharge and reappointment of the Trustee

43. If the Trustee(s) ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee(s) to a Conflict of Interest:
 - (a) the Commission may, after hearing the Trustee(s) and the Notifying Parties or Charger OpCo (as the case may be), require that party to replace the Trustee(s); or
 - (b) the Notifying Parties or Charger OpCo (as the case may be) may, with the prior approval of the Commission, replace the Trustee(s).
44. If the Trustee(s) is removed according to paragraph 43 of these Commitments, the Trustee(s) may be required to continue in its function until a new Trustee(s) is in place to whom the Trustee(s) has effected a full hand over of all relevant information. The new Trustee(s) shall be appointed in accordance with the procedure referred to in paragraphs 19-26 of these Commitments.
45. Unless removed according to paragraph 43 of these Commitments, the Trustee(s) shall cease to act as Trustee(s) only after the Commission has discharged it from its duties after all the Commitments with which the Trustee(s) has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee(s) if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section F

The review clause

46. The Commission may extend the time periods foreseen in the Commitments in response to a request from the Notifying Parties or, in appropriate cases, on its own initiative. Where a party requests an extension of a time period, it shall submit a reasoned request to the Commission no later than one month before the expiry of that period, showing good cause. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to the Notifying Parties. Only in exceptional circumstances shall that party be entitled to request an extension within the last month of any period.
47. The Commission may further, in response to a reasoned request from the Notifying Parties showing good cause waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to the Notifying Parties. The request shall not have the effect of suspending the application of the undertaking and, in particular, of suspending the expiry of any time period in which the undertaking has to be complied with.

Section G

Entry into force

48. The Commitments shall take effect upon the date of adoption of the Decision.

SCHEDULE A [...]*

SCHEDULE B [...]*

SCHEDULE C [...]*

SCHEDULE D [...]*



EUROPEAN COMMISSION
DG Competition

***CASE M.7555 - STAPLES/OFFICE
DEPOT***

(Only the English text is authentic)

**MERGER PROCEDURE
REGULATION (EC) 139/2004**

Article 8(2) Regulation (EC) 139/2004

Date: 10.2.2016

This text is made available for information purposes only. A summary of this decision is published in all EU languages in the Official Journal of the European Union.

Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets.

EUROPEAN
COMMISSION

Brussels, 10.2.2016
C(2016) 710 final

Public version

COMMISSION DECISION

of 10.2.2016

**declaring a concentration to be compatible with the internal market and the EEA
Agreement**

(Case M.7555 - STAPLES/OFFICE DEPOT)

(Only the English text is authentic)

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COMMISSION DECISION

of 10.2.2016

declaring a concentration to be compatible with the internal market and the EEA Agreement

(Case M.7555 - STAPLES/OFFICE DEPOT)

(Only the English text is authentic)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings¹, and in particular Article 8(2) thereof,

Having regard to the Commission's decision of 25 September 2015 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations²,

Having regard to the final report of the Hearing Officer in this case³,

Whereas:

1. INTRODUCTION

- (1) On 21 August 2015, the Commission received a notification of a proposed concentration pursuant to Article 4 of Regulation (EC) No 139/2004 ("the Merger Regulation") by which the undertaking Staples, Inc. ("Staples" or the "Notifying Party") intends to acquire sole control, within the meaning of Article 3(1)(b) of the Merger Regulation, of the whole of the undertaking Office Depot, Inc. ("Office Depot") by way of purchase of shares ("the transaction"). Staples and Office Depot are collectively referred to as the "Parties", while the company resulting from the transaction is referred to as "the merged entity".
- (2) Staples is a publicly held US-based company, listed on the NASDAQ. It is active as a distributor of office products in North and South America, Europe, Asia, Australia and New Zealand. In the EEA, Staples sells office supplies mainly to business customers (business-to-business, "B2B") through framework contracts, wholesale, catalogues, online sales and brick and mortar retail shops.

¹ OJ L 24, 29.1.2004, p. 1. With effect from 1 December 2009, the Treaty on the Functioning of the European Union ("TFEU") has introduced certain changes, such as the replacement of "Community" by "Union" and "common market" by "internal market". The terminology of the TFEU will be used throughout this Decision.

² OJ C ...,.... 201X., p.

³ OJ C ...,.... 201X., p.

- (3) Office Depot is a publicly held US-based company, listed on the NASDAQ. It is active as a distributor of office products in 57 countries. Like Staples, in the EEA Office Depot focuses on B2B sales of office supplies through framework contracts, wholesale, catalogues, online sales and brick and mortar retail shops.

2. THE OPERATION AND THE CONCENTRATION

- (4) On 4 February 2015, Staples, Office Depot and Staples AMS, a wholly-owned subsidiary of Staples, entered into an Agreement and Plan of Merger pursuant to which Staples AMS shall be merged into Office Depot, with Office Depot surviving the merger as a wholly-owned subsidiary of Staples.
- (5) As a result of the transaction, Staples would acquire sole control of Office Depot. The notified operation therefore constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

3. UNION DIMENSION

- (6) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million (Staples: EUR 17 399 million; Office Depot: EUR 8 462 million). Each of them has a Union-wide turnover in excess of EUR 250 million (Staples: EUR [...]; Office Depot: EUR [...]), but they do not achieve more than two-thirds of their aggregate Union-wide turnover within one and the same Member State.
- (7) The transaction therefore has a Union dimension pursuant to Article 1(2) of the Merger Regulation.

4. THE PROCEDURE AND THE INVESTIGATION

- (8) The Notifying Party notified the transaction on 21 August 2015.
- (9) After a preliminary examination of the notification and based on the Phase I market investigation, the Commission concluded that the transaction raised serious doubts as to its compatibility with the internal market and with the functioning of the EEA agreement as regards the potential markets for the sale of office supplies through international contracts in the EEA and through national contracts in the Netherlands and Sweden and in relation to the potential market for the wholesale of office supplies in Sweden. Therefore, on 25 September 2015 the Commission adopted a decision to initiate proceedings pursuant to Article 6(1)(c) of the Merger Regulation (the "Article 6(1)(c) Decision"). The period up to the adoption of the Article 6(1)(c) Decision will hereafter be referred to as "Phase I". The period from the adoption of the Article 6(1)(c) Decision until the adoption of this Decision will hereafter be referred to as "Phase II".
- (10) On 6 October 2015, the Notifying Party submitted its written comments on the Article 6(1)(c) Decision (the "Response to the Article 6(1)(c) Decision").
- (11) On 8 October 2015 a formal State of Play meeting took place between the Commission and the Parties.
- (12) During the in-depth market investigation in Phase II, the Commission:
- (a) reviewed the submissions of the Parties, sent several requests for information to the Parties and reviewed responses, held several meetings and telephone interviews with the Parties;

- (b) sent several requests for information to third parties (competitors, customers, purchasing groups, the Parties' distributors and suppliers), reviewed responses, and held telephone interviews with third parties;
 - (c) reviewed internal documents submitted by the Parties;
 - (d) conducted a targeted market reconstruction analysis by requesting data from major market participants; and
 - (a) reviewed bidding data gathered by the Parties' themselves, transaction data of the Parties and two customer surveys commissioned by Staples in 2013 (for the purposes of this Decision the following two parts of the 2013 survey will be distinguished: 'the 2013 national survey' and 'the 2013 international survey') and 2015 ('the 2015 international survey').⁴
- (13) A second State of Play meeting took place on 6 November 2015. In that meeting the Parties were informed about the outcome of the Phase II market investigation, the Commission's intention to issue a Statement of Objections and the scope of the Statement of Objections.
- (14) On 11 November 2015 the Phase II proceedings were extended by 15 working days in agreement with the Notifying Party, pursuant to Article 10(3) of the Merger Regulation, in order to allow the Commission to fully assess the arguments advanced by the Parties and to discuss the scope of potential commitments considered by the Parties. On 25 November 2015 and also in agreement with the Notifying Party, the Phase II proceedings were extended by five working days for the same reasons, pursuant to Article 10(3) of the Merger Regulation.
- (15) In order to address the competition concerns identified by the Commission, of which the Parties were informed in the course of the procedure, the latter submitted commitments on 27 November 2015. The Commission launched a market test of those commitments on 30 November 2015. On 10 December 2015 the Parties submitted revised commitments.
- (16) The meeting of the Advisory Committee took place on 27 January 2015.

5. THE OFFICE PRODUCTS MARKET AND THE ACTIVITIES OF THE PARTIES

- (17) The term "office products" is used to describe a wide range of products used in offices by businesses or consumers. Traditionally it includes: (i) stationery (for instance pens, pencils, notebooks, and staplers), (ii) ink & toner and (iii) cut sheet paper. Other categories of office products are office furniture and office equipment (for instance computers, printers, and copying machines).

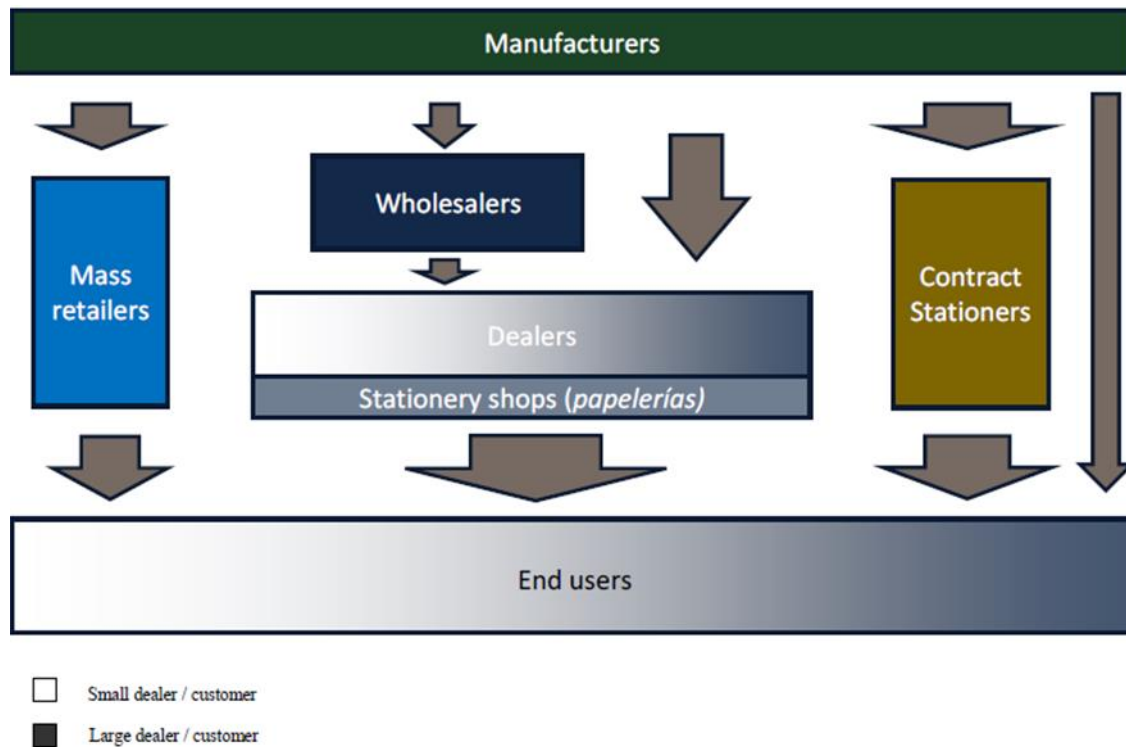
⁴ Staples commissioned one customer survey for national customers in the Netherlands and Sweden and for international customers in 2013 and an additional survey for international customers in 2015. The surveys were conducted over the phone in the form of computer assisted telephone interviews, that is to say the interviewer followed a script provided through a software application. The company [...] was responsible for conducting the survey. The company [...] was the company responsible to collect the data in the field. The respondents were not informed that the survey was commissioned by Staples. It was presented as an independent market study, only [...]s name was mentioned. There was also no contact between the Parties' external counsel and [...], the latter being in contact only with [...]. As regards the selection of the contact details of international customers, Staples was asked to provide a comprehensive list of its customer contact details, those lists were then provided in full to the survey vendor, without any modification. The survey vendor then chose contacts from those lists at random to interview (see email sent by the Parties to the Commission on 3 September 2015).

- (18) According to the Parties,⁵ the European traditional office supplies sector (including the product categories stationery, ink & toner and cut sheet paper) is in decline. Office supplies providers, including the Parties, face a declining demand for traditional office products as a result of the increased digitalisation of the European workplace. Customers are using fewer office supplies as offices become increasingly "paperless" due to an increased usage of PCs, laptops, tablets and smart phones and greater emphasis is placed on environmental considerations. The trend is expected to continue as younger generations enter the workforce. Additionally, in the face of fairly stagnant economic growth in Europe, customers are increasingly cost conscious and businesses have targeted their office supply spending as an area for savings.
- (19) In response to those market trends, existing suppliers, including the Parties, have diversified into the supply of non-traditional products such as cleaning products, washroom supplies and personal protective equipment, presentation and planning supplies, arts and graphics supplies, food and break room supplies (for example coffee, tea, snacks), mail and shipping supplies (boxes for sending packages) and mobile phones.
- (20) On the business customers' side, the trend is towards the centralised procurement of various product categories for as many locations as possible in order to benefit from volume related discounts and to optimise the time and effort spent on the purchasing of input materials of low importance such as office supplies.
- (21) The Parties distribute a full range of office products in all EEA countries where they are active. Both Parties have a direct presence in Austria, Belgium, France, Germany, Ireland, Italy, the Netherlands, Spain, Sweden and the United Kingdom. In addition, there are countries where the Parties have distribution agreements with third Parties giving rise to overlaps between the direct operations of one Party and the operations carried out indirectly through a distributor in that country by the other Party. Those countries are the Czech Republic, Denmark, Finland, Norway, Poland and Slovakia.⁶
- (22) The distribution of office products is made through a multitude of channels as illustrated in Figure 1. The illustration, however, does not show sales through open online systems or physical catalogues ("the direct channel" or "direct sales") which would take a similar position as the "stationery shops" or the "mass retailers" in the illustration in Figure 1:

⁵ Form CO, section 6 A.

⁶ According to the submissions in the Form CO, [...] where Staples has distribution agreements in place for the supply of its international customers.

Figure 1: Distribution channels in the office supply sector⁷



- (23) The Parties' sales are made through contract sales, physical retail outlets (where there is insignificant overlap), direct sales (online or through paper catalogues), and wholesale.
- (24) In previous decisions,⁸ the Commission has provided the following description of the different types of distribution channels:
- (a) Contract distributors supply office products on the basis of framework contracts under which the customers may order supplies whenever the need arises.
 - (b) Retail outlets (stationery shops) are physical shops selling office products primarily to individuals and small enterprises/offices.
 - (c) Wholesalers purchase office products directly from manufacturers in order to sell them to dealers and stationery shops for re-sale (but not to end users).
- (25) As regards catalogue sales, the Parties explained that those are direct sales made through a physical catalogue. These have decreased over time due to the emergence of online sales. Online sales are direct sales made through open online systems on the internet.
- (26) In the Article 6(1)(c) Decision, the Commission raised serious doubts as to the compatibility of the transaction with the internal market in relation to the potential market for the sale of office supplies through international contracts in the EEA and through national contracts in the Netherlands and Sweden, and in relation to the potential market for the wholesale of office supplies in Sweden.

⁷ Case M.6382 – Unipapel/Spicers, recital 27.

⁸ For instance case M.6382 – Unipapel/Spicers, recitals 26 and 28.

- (27) On the basis of the in-depth investigation in Phase II the Commission confirms its preliminary findings as regards the existence of a separate market for the sale of traditional office supplies through international contracts. Moreover, based on the in-depth investigation in Phase II the Commission confirms its preliminary concerns in relation to the following markets: (i) the market for international contracts for the sale of traditional office supplies and stationery, (ii) the market for non-international contracts for the sale of traditional office supplies and stationery to large business customers (250 employees and more) in Sweden and the Netherlands and (iii) the wholesale market for office supplies in Sweden.
- (28) As regards the direct channel (online and catalogue sales) no competition concerns were identified in the 6(1)(c) Decision or the Phase II investigation. Furthermore, the Parties' activities in retail result in very limited overlaps and do not lead to affected markets.⁹ Therefore retail will not be discussed further in this Decision.

6. RELEVANT MARKETS

6.1. Product market definition

- (29) Pursuant to the Commission Notice on Market Definition,¹⁰ the purpose of the definition of the relevant product market is to identify in a systematic way the competitive constraints faced by the undertakings involved in a concentration. A relevant product market comprises all those products and services which are regarded as interchangeable or substitutable by customers. For the definition of the relevant market, demand substitutability and supply substitutability play a role.¹¹
- (30) The Parties distribute a full range of office products to business customers¹² through different distribution channels as shown in Figure 1 and described in recitals (23) to (25). Depending on the various EEA countries where they are present, they act as contract stationers (distribution of office supplies through framework contracts), wholesalers, catalogue and online sellers or brick and mortar retailers.
- (31) The Notifying Party rejects any possible sub-segmentation within the B2B distribution of office products. It argues that the relevant product market is the overall distribution of office products, irrespective of the categories of products supplied or the channels through which those sales are made. Nevertheless, the Notifying Party submits that the product market definitions can be left open in this case.

⁹ Staples is active in the retail distribution of office supplies in Germany, the Netherlands, Norway, Portugal and Sweden; Office Depot has retail shops in France and Sweden. Therefore the only overlap in retail distribution of office supplies arises in Sweden where, according to the Parties, the Parties' combined market share is around [5-10]%. As regards the local level, both Parties sell office supplies through shops in four Swedish cities: Gothenburg, Lund, Stockholm and Uddevalla. However, it is doubtful whether Staples' presence in Gothenburg and Stockholm can be considered as a retail presence. In those two cities, Staples has very small shops which are [...]. In any event Staples' market share would be negligible in those cities at well below [0-5]%. As regards the overlaps in Lund and Uddevalla, the Parties estimate the market shares to be less than [5-10]% for Staples and less than [10-20]% for Office Depot leading to a combined market share of less than [20-30]%.

¹⁰ Commission Notice on the definition of relevant market for the purposes of Community competition law ("Commission Notice on Market Definition"), OJ C 372, 9.12.1997, p. 5-13.

¹¹ Commission Notice on Market Definition, paragraphs 2, 7 and 13 et seq.

¹² The Parties also sell office products to consumers directly (business-to-customer, "B2C") but they estimate their combined shares for B2C as negligible (well below 5%) in all EEA countries irrespective of the sales channel, Form CO, paragraph 88. Therefore, the B2C channel will not be assessed further in this Decision.

- (32) On the basis of the market investigation, the Commission finds that the B2B distribution of office products can be segmented in a number of different ways.
- (33) First, a distinction can be made according to the different distribution channels through which office products are supplied, at least identifying the contract channel, the direct sales channel (including catalogue and online sales) and the wholesale channel as separate markets, since suppliers of those channels cater to the different needs of customers (section 6.1.1).¹³
- (34) Second, the product market can be segmented according to product categories, identifying as separate markets either the market for the supply of traditional office supplies or the market for the supply of each product category, such as stationery, ink & toner and paper (section 6.1.2).
- (35) Third, as regards the contract channel, a distinction can be drawn between international and non-international contracts (section 6.1.3).
- (36) Fourth, as regards non-international contracts, another distinction can be drawn based on the size of the customers (section 6.1.4).

6.1.1. *Segmentation by distribution channel*

- (37) The Notifying Party considers that the relevant product market includes sales made through all distribution channels and that it should not be sub-segmented by channel. It argues that contract customers as a whole are not substantially different from customers who purchase through the direct (online/catalogue) or retail channels. Moreover, according to the Notifying Party, contract suppliers face strong competition from online suppliers such as Amazon, who offer a competitive service and competitive price benchmarking.¹⁴ Therefore, it would be inappropriate, according to the Notifying Party, to focus only on a specific channel and ignore other channels in the competitive assessment.¹⁵
- (38) In a previous decision, the Commission found evidence that the market could be segmented according to different channels: sales from manufacturers, wholesaling, contract sales, retail sales, online and catalogue sales.¹⁶ According to the Commission, different distribution channels correspond to the needs of different customer groups, although certain customer groups may be served through several channels.

6.1.1.1. Contract distribution channel

- (39) With regard to the contract channel in particular, the Commission previously concluded with respect to the Dutch market that there is a separate market for contract stationers within the larger market for the distribution of office supplies. Contract stationers typically conclude framework contracts with customers which are usually awarded on the basis of tenders. Those contracts are generally written agreements, sometimes of several years' duration, which govern prices and other sales conditions, and under which the customer may order supplies whenever the need arises.¹⁷

¹³ Retail is not discussed in this decision for the reasons outlined in footnote 9.

¹⁴ Form CO, paragraph 113.

¹⁵ Form CO, paragraph 75.

¹⁶ Case M.2965 – Staples/Guilbert, recitals 9 and 13.

¹⁷ Case M.2286 – Buhmann/Samas Office Supplies, recitals 19, 20.

- (40) The Commission's conclusion was based on the finding that contract stationers have specific characteristics that particularly match large customers' needs. In particular, contract stationers supply a full range of products (including stationery, paper, ink & toner as well as other product categories), which makes them a one-stop-shop allowing customers to satisfy the bulk of their needs from one preferred supplier. According to the Commission's previous findings, those are distinguishing characteristics which make the contract channel different from other distribution channels.¹⁸
- (41) Those findings were confirmed in *Staples/Guilbert* where the Commission found, following the market investigation, that large firms tend to prefer the contract channel for their office supplies and do not use direct sales or retail stores.¹⁹
- (42) According to the Notifying Party, both Parties operate a separate business division for their contract customers with the main difference being that many contract customers use an active sales network including account managers.²⁰ Furthermore, the Parties consistently analyse the market distinguishing between the contract B2B market on the one hand and non-contract B2B market on the other hand in the ordinary course of business.²¹ Indeed, both Parties' businesses are structured into the following business divisions (i) contract business, (ii) direct/online business and (iii) retail business. More specifically, Staples has different business divisions for "Advantage Europe" (the European contract business), "Online Europe" and "Retail Europe", while Office Depot distinguishes at least between "Contract Europe" and "Direct Europe".²²
- (43) The Parties have submitted internal documents to the Commission which reflect that approach. The slide in Figure 2 illustrates the internal distinction between contract, direct and retail business in one of Staples' internal documents:

Figure 2: Staples internal document entitled "EU Market Shares", March 2014, slide 4, Annex 7.7 of the Form CO

[...]

- (44) Similarly, Office Depot distinguishes between competitors active in the contract channel and the direct channel in its internal analyses of the competitive landscape. For instance, in one of its internal documents submitted with the notification, Office Depot analyses the "EU Contract Competitor Landscape" separately from the "EU Direct Competitor Landscape" and the national "Contract Competitors" separately from national "Direct Competitors".²³

6.1.1.1.1. Demand-side considerations

- (45) From a demand-side perspective, in line with its precedents,²⁴ the Commission finds, on the basis of the results of the investigation, that business customers purchasing their office products under contracts generally do not consider other sales channels,

¹⁸ Case M.2286 – Buhrmann/Samas Office Supplies, recitals 37, 39.

¹⁹ Case M.2965 – Staples/Guilbert, recital 13.

²⁰ Form CO, paragraph 89.

²¹ Form CO, paragraph 78.

²² See the organisational charts of the Parties submitted by Staples on 5 June 2015.

²³ Office Depot internal document entitled "EU OP Market Situational Analysis", March 2015, Annex 8.1 of the Form CO.

²⁴ Case M.2286 – Buhrmann/Samas Office Supplies, recital 20.

including manufacturers, retail shops, open online shops or distance order catalogues, to be viable alternatives.²⁵

- (46) In that respect and on the basis of the results of the market investigation, the Commission considers that purchasing under contracts offers a number of advantages to customers, such as common and consistent services provided by one supplier to several offices, one single agreement to manage, one price list on a dedicated web portal, the optimisation of logistics, the efficient management and control of expenditure in office supplies and the possibility of leveraging a position as a high spending customer to obtain good service levels and competitive pricing.²⁶
- (47) The majority of contract customers that responded to the market investigation in Phase I and Phase II indicated that they would not switch to other providers (such as manufacturers, wholesalers, mass merchandisers and brick-and mortar retailers) should the price of office products sold through contracts increase by 5-10%.²⁷ Although roughly half of the respondents during the Phase I market investigation had initially indicated their willingness to switch to online or catalogue sellers in the event of price increases in the contract channel, customers submitted in subsequent explanations and follow-up phone calls that only suppliers fulfilling the requirements set out in the invitations to tenders for the supply of office products (in particular, distribution of office supplies to business customers and readiness to enter into a framework contract) are taken into account as suitable suppliers.²⁸
- (48) The Notifying Party contends that the fact that roughly half of the respondents to the Phase I market investigation originally indicated their willingness to switch to online or catalogue sellers in the event of price increases is evidence of the fact that customers could equally satisfy their needs for office supplies through other channels.²⁹
- (49) However, on the basis of the investigation in Phase II the Commission considers that, even if other channels are available to business customers, the sourcing of office supplies through framework contracts remains an essential element of their procurement strategy for those products, as more than 75% of customers that purchase through contracts indicated that it is not viable to purchase traditional office supplies without a framework contract in place.³⁰ Moreover, the majority of respondents that replied to the market investigation in Phase II confirmed the existence of a number of indirect cost savings that would compensate for an increase in prices of their purchases of office supplies under contract. The main indirect cost savings indicated by those customers include savings on transaction costs and on management and administration of the contracts, easier supplier management, increase control in expenditure and no minimum purchasing costs.³¹

²⁵ Replies to Phase II questionnaires Q8a-j to customers – Question 11; replies to Phase I Questionnaire Q4 to customers (contract) – Question 7; agreed minutes of the conference calls with customers.

²⁶ Replies to Phase II questionnaires Q8a-j to customers – Question 11; replies to Phase I Questionnaire Q4 to customers (contract) – Question 8.

²⁷ Replies to Phase II questionnaires Q8a-j to customers – Question 20.5; replies to Phase I questionnaires Q4 to customers (contract) and Q5 to customers (international) – Question 9.

²⁸ Replies to Phase I questionnaires Q4 to customers (contract) and Q5 to customers (international) – Question 9.

²⁹ Response to the Article 6(1)(c) Decision.

³⁰ Replies to Phase II questionnaires Q8a-j to customers – Questions 11 and 11.1.

³¹ Replies to Phase II questionnaires Q8a-j to customers – Question 20.5.

- (50) The Notifying Party also argues that customers multi-source office supplies, including the three traditional product categories, from multiple sales channels through leakage in practice. According to the Notifying Party, customers who have awarded a contract to a provider of office suppliers may still opt out of some purchases from the contracts and switch part of their spending to other suppliers, including from suppliers in other sales channels.
- (51) However, the 2013 and 2015 surveys³² [...] for national customers in the Netherlands and Sweden and for international customers suggest that leakage is limited. In the Netherlands, [70-80]% of the respondents mentioned that their organisation sources all requirements for stationery exclusively through contracts,³³ (the corresponding figure for ink & toner is [70-80]%,³⁴ [80-90]% for paper³⁵). In Sweden, the corresponding figures are [70-80]% for stationery, [70-80]% for ink & toner, and [90-100]% for paper.³⁶ In other words, a limited number of customers source the traditional product categories outside the contracts. This is also confirmed by the international surveys conducted in 2013 and 2015. The 2013 international survey shows that leakage concerns only a minor part of the office supplies needs of international customers as only [10-20]% of respondents who indicated they had made purchases outside their international contracts purchased more than [20-30]% of their needs outside the contracts relationship.³⁷ The limited importance of leakage is also confirmed in the 2015 international survey which shows that, among the respondents who use a single supplier for several countries, (i) only [20-30]% mention that some local country units opted out of the central office supplies contracts in the last five years, and (ii) only [10-20]% purchased more than [20-30]% of their needs outside the contracts relationship.³⁸ The multi-sourcing behaviour (of the three traditional product categories) through leakage therefore appears limited.

6.1.1.1.2. Supply-side considerations

- (52) According to the Notifying Party, a further segmentation of the market according to the type of supplier (for instance contract stationers, dealers, mass retailers, other resellers, and manufacturers) is not appropriate because that would not take into account a substantial part of competition. The Notifying Party submits that such segmentation by channel is less relevant than before as there is intense competition

³² See footnote 4.

³³ See Annex B.1, question 19, of the submission "*Staples/Office Depot – competition from specialist suppliers*", RBB Economics, 31 August 2015.

³⁴ See Annex B.1, question 23, of the submission "*Staples/Office Depot – competition from specialist suppliers*", RBB Economics, 31 August 2015.

³⁵ See Annex B.1, question 27, of the submission "*Staples/Office Depot – competition from specialist suppliers*", RBB Economics, 31 August 2015.

³⁶ See Annex B.2, questions 19, 23, and 27, of the submission "*Staples/Office Depot – competition from specialist suppliers*", RBB Economics, 31 August 2015.

³⁷ See Annex A.1 of the submission "*Competitive Assessment - International Customers*", dated 18 May 2015, question 14. [50-60]% of those respondents purchased less than [10-20]% of their needs outside contract relationship, [30-40]% of those respondents purchased between [10-20]% and [20-30]% of their needs outside contract relationship, [5-10]% purchased [20-30]% to [40-50]% of their needs outside the contracts relationship, [0-5]% purchase more than [40-50]% of their needs outside the contract relationship. [5-10]% of respondents replied that they did not know.

³⁸ See question 16 and question 17 of the 2015 International survey, "Project Warrior – survey Questionnaire", dated 11 May 2015. [40-50]% of those respondents purchased less than [10-20]% of their needs outside contract relationship, [30-40]% of those respondents purchased between [10-20]% and [20-30]% of their needs outside contract relationship, [10-20]% purchased [20-30]% to [40-50]% of their needs outside the contracts relationship, [5-10]% purchase more than [40-50]% of their needs outside the contract relationship. [5-10]% of respondents don't know.

between different channels including channels not explicitly referred to by the Commission, such as general wholesale, online dealers, mass merchandisers and specialist suppliers.³⁹

- (53) The Commission considers, on the basis of the market investigation that there is no supply-side substitutability between the contract market and other sales channels, contrary to the Notifying Party's claims, and in line with the findings in previous decisions.⁴⁰ Indeed, according to the results of the market investigation a number of competitors operating in other sales channels would not be capable of offering the customer service, pricing models and logistics required by business customers in the contract channel.⁴¹
- (54) In the words of a competitor, who has previously tried to enter that channel, the tender contract market "*suffers from high barriers to entry. Those barriers are not only related to the size and the capacity needed to serve the customers, but also to endogenous strategies pursued by the incumbents. Special systems are needed in order to be an effective competitor in the tendering market.*"⁴²
- (55) In particular, supply through the contract channel necessitates setting up a dedicated organisation (with account management, dedicated customer service and sales force, efficient logistics and supply chain) and providing a wide-range of services (such as broad product assortment, easy ordering via online and e-procurement solutions as well as efficient logistics solutions) to meet specific customer needs. This has been confirmed by contract suppliers who responded to the market investigation.⁴³ However, supply-side substitutability requires that suppliers would not need to adjust existing tangible and intangible assets, make additional investments, take strategic decisions or incur time delays.⁴⁴
- (56) The relevance of barriers to entry as well as the constraints posed by potential competitors will be addressed further within the competitive assessment.⁴⁵

6.1.1.1.3. Conclusion

- (57) Based on the assessment in recitals (39) to (56), the Commission finds that the supply of office products by contract stationers through the contract channel constitutes a separate product market from other distribution channels such as direct distribution and wholesale distribution.

6.1.1.2. Direct distribution channel

- (58) There are indications in the Commission's precedents pointing to the existence of a separate product market for the direct sales channel which is separate from the product markets for contract sales and for wholesale of office suppliers, although the Commission ultimately left that question open for the direct sales channel.
- (59) In *Buhrmann/Samas Office Supplies*, the Commission distinguished between different types of office supplies distributors, including contract stationers, smaller office supplies dealers and dealer groups, mail order companies, office superstores, electronic office supplies wholesalers selling directly to larger end-user offices and

³⁹ Form CO, paragraph 119.

⁴⁰ Case M.2286 – Buhrmann/Samas Office Supplies, recital 37.

⁴¹ Replies to Phase I Questionnaire Q3 to competitors (direct sales) – Question 9.

⁴² Agreed minutes of a conference call with a competitor of 11 June 2015.

⁴³ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 9.

⁴⁴ Commission Notice on Market Definition, paragraphs 20 and 23.

⁴⁵ Commission Notice on Market Definition, paragraph 23.

other resellers such as electronic office supplies dealers, e-tailers (resellers only selling via the internet and outsourcing stock keeping and delivery to others), hardware dealers and high street retailers.⁴⁶ The suppliers active mostly via the direct channel include mail order companies and e-tailers according to that distinction.

- (60) In *Staples/Guilbert*, the Commission distinguished between the contract channel and distant selling and established that large firms tend not to use distant selling or superstores and prefer contract stationers for their office suppliers. The Commission further found that the number of references between distant selling and superstores was comparable, if not identical, and fairly different from that of high street specialists, department stores and comparison stores and supermarkets. At the same time, it was not clear whether customers would switch from distant selling to superstores in the event of a non-temporary price increase in this channel, or if they would prefer another distribution channel. The Commission ultimately left the market definition open.⁴⁷
- (61) Whereas in previous decisions a distinction was made between mail order companies who issue printed catalogues and electronic retailers, in today's digitised world the suppliers active in the direct sales channel mostly offer their clients the opportunity to purchase office supplies via online catalogues available on the website of the supplier. In a previous decision on catalogue sales in a different distribution industry, the Commission found that home-shopping by catalogue and home-shopping on the internet form part of the same relevant market, since those channels are interchangeable from the customer's point of view and are subject to a similar regulatory framework with regard to the right of return, for example.⁴⁸
- (62) With regard to the relevant customer groups targeted by the direct sales channel, the Notifying Party submits that it does not apply an internal threshold to distinguish between contract and non-contract customers. However, the Notifying Party also explains that it rarely enters into a contract with customers with an annual spend below EUR 5 000.⁴⁹ Those customers use other sales channels than the contract channel, that is to say the retail or the direct sales channel.
- (63) According to the results of the market investigation, suppliers active in direct sales do not have the capabilities to compete with contract stationers and they target smaller B2B customers (mainly customers with less than 50 office workers).⁵⁰
- (64) Based on the assessment in recitals (58) to (63), the Commission finds that the supply of office products through the direct channel constitutes a separate product market from contract sales and the wholesale of office supply. The Commission can, however, leave open whether the relevant product market for direct sales also includes retail sales since the transaction does not lead to a significant impediment to effective competition if only the narrower market for direct sales is considered where the overlap between the Parties' activities is more pronounced.

6.1.1.3. Wholesale distribution channel

- (65) In *Buhrmann/Samas Office Supplies*, the Commission found that wholesalers of traditional office products do not, or at least do not primarily, sell directly to end-

⁴⁶ Case M.2286 – Buhrmann/Samas Office Supplies, recital 13.

⁴⁷ Case M.2965 – Staples/Guilbert, recital 13.

⁴⁸ Case M.5721 – Otto/Primondo Assets, recital 20.

⁴⁹ Form CO, paragraph 89.

⁵⁰ Replies to Phase I Questionnaire Q3 to competitors (direct sales) – Question 16.

users and concentrate on servicing dealer groups, smaller independent dealers and retailers. They offer a wide range of services to dealers, including logistical systems whereby orders are fulfilled directly from the wholesaler's stocks and dispatched directly to the end-user.⁵¹ Similarly, in *Unipapel/Spicers*, the Commission found that wholesalers buy from manufacturers and sell to downstream dealers and stationery shops, but not to end-users.⁵² The Commission furthermore considered that manufacturers do not compete actively with "pure" traditional office wholesalers; however they do exert an important competitive constraint.⁵³ Similarly, buyer groups and specialised office supply chains were also excluded as competitors from the competitive assessment; however the Commission indicated that they also do exert competitive pressure on "pure" traditional office wholesalers.⁵⁴

(66) In this Decision and on the basis of the results of the market investigation, the Commission considers that wholesalers serve a customer base different from the one served by manufacturers and that they are situated on a step of the value chain different from the one where retailers, contract and direct sales stationers operate. In addition, both buyer groups and manufacturers can clearly be distinguished from wholesalers in terms of services offered as only the latter provide to dealers and retailers IT solutions, a large range of products, low requirements in terms of minimal order size and direct delivery service from the wholesaler's warehouse to the end customers, allowing dealers and retailers to operate without the need to run their own warehouses.⁵⁵

(67) Based on the assessment in recitals (65) and (66) and in line with the Commission's precedents, the Commission finds that the wholesale distribution of office supplies constitutes a separate product market from direct distribution to end-users and distribution through contracts.

6.1.2. *Segmentation by product category, all channels*

(68) In the Form CO, the Notifying Party considers both generally and for all distribution channels that segmenting the market by product category⁵⁶ would be artificial, because such an approach would not reflect the commercial reality. The Notifying Party argues that business customers choose interchangeably between purchasing office products jointly and separately (the latter either in separate tender lots or in separate tenders). According to the Notifying Party, many of the Parties' competitors are active across different categories and the different product categories are, as a general rule, sold through the same channels with the same business teams and with the same assets (for instance, warehouses or online ordering systems). In addition, all suppliers can easily and rapidly expand into different product categories. Even when customers choose to purchase products separately, competition from specialist suppliers remains.

⁵¹ Case M.2286 – Buhrmann/Samas Office Supplies, recital 15 and Case M.6382 – Unipapel/Spicers, recital 29.

⁵² Case M.6382 – Unipapel/Spicers, recital 28.

⁵³ Case M.6382 – Unipapel/Spicers, recitals 103-106.

⁵⁴ Case M.6382 – Unipapel/Spicers, recital 37.

⁵⁵ Replies to Phase I Questionnaire Q7 to competitors (wholesale) – Question 4; replies to Phase II Questionnaire Q11 – Question 9.

⁵⁶ The categories are stationery, ink & toner, cut sheet paper, facilities supplies, break room supplies, office furniture, office and printing machines, computer accessories, printing and copying services, packaging material and others.

- (69) Therefore, in the Parties' view the distribution of office supplies encompasses at the very least traditional office supplies (stationery, ink & toner and cut sheet paper), catalogue furniture and small business machines.⁵⁷
- (70) In a previous decision, the Commission indicated that the distribution of complete ranges of office furniture and the distribution of larger business machines and services associated therewith are separate activities from the distribution of office supplies, although there can be some overlaps.⁵⁸ The same reasoning would apply to the distribution of broad ranges of other types of products sold by the Parties such as cleaning products, food and break room supplies (for example coffee, tea, snacks), computers and mobile phones.
- (71) The evidence gathered by the Commission in this Decision, in line with precedents, points to each distribution channel as a relevant market consisting of the distribution of office supplies including traditional categories (stationery, ink & toner and cut sheet paper) and excluding the distribution of complete ranges of office furniture, large business machines and associated services, cleaning products, food, IT and telecommunications equipment. The specific claims made by the Parties and the specific features concerning the contract, direct and the wholesale channels will be further addressed in sections 6.1.2.1 to 6.1.2.3.

6.1.2.1. Distinction by product categories, contract channel

6.1.2.1.1. The views of the Notifying Party

- (72) The Notifying Party argues that there is not a single market encompassing the sale of stationery, ink & toner and cut sheet paper through contracts.⁵⁹
- (73) First, as regards customers' current purchasing patterns, the Notifying Party submits that between [40-50]% and [50-60]% of the Parties' customers buy all three traditional product categories together. This relatively infrequent single-sourcing behaviour would demonstrate, in the Notifying Party's view, that multi-sourcing (that is to say sourcing individual product categories separately from different suppliers) is a viable option for customers and so the cost advantage of single-sourcing (that is to say purchasing the three traditional product categories together) cannot be substantial.⁶⁰
- (74) Second, as regards customers' switching patterns, based on evidence from the Parties' customer database, the Notifying Party contends that many customers switch from using a single supplier to using multiple suppliers, and any preference for single-sourcing the three traditional product categories is transient, with the majority of customers who purchased their full range of traditional office supplies from Staples or Office Depot in 2012 switching at least partially to alternative suppliers in 2014.
- (75) Third, the Notifying Party argues that specialist suppliers exert a competitive constraint on the Parties and should be included in the relevant product market, in particular the manufacturers of ink & toner, including suppliers of Managed Print Services ("MPS"), and manufacturers or specialised distributors of cut sheet paper. Suppliers of MPS sell ink & toner as one element of a broader service contract

⁵⁷ Form CO, paragraphs 81-86.

⁵⁸ Case M.2286 – Buhrmann/Samas Office Supplies, recital 10.

⁵⁹ See submission "*Competition from specialist suppliers*", dated 31 August 2015, RBB Economics.

⁶⁰ See submission "*Staples/Office Depot – competition from specialist suppliers*", dated 31 August 2015, RBB Economics, pages 9-10.

encompassing mainly the supply of printing machines and the provision of services such as maintenance and provision of printing consumables.

- (76) During Phase II, the Notifying Party also expressly submitted that there is no separate business for stationery sales as the Parties do not treat those sales as a separate market in their internal documents; there is no monitoring of stationery sales, and there are no separate business plans or budgets for stationery. Similarly, the Parties do not have stationery-specific sales representatives, and no infrastructure specifically targeted at stationery.⁶¹

6.1.2.1.2. The Commission's assessment

- (77) The existence of a customer focus on a one-stop-shop for purchases of traditional office supplies is confirmed by how the Parties target customers and monitor their sales in the ordinary course of business. For instance, when calculating the target spending to classify customers, such as international customers or "Enterprise" customers, the Parties use turnover thresholds that normally include stationery, paper and ink & toner. Facility products are sometimes included, whereas one of the Parties only exceptionally classifies customers as international also based on spending in furniture.⁶² Similarly, other contract stationers, including the Parties' main competitors, monitor sales by broad categories corresponding to the full-range of supplies of traditional office products.
- (78) Moreover, as will be further explained in recitals (79) to (85), the customers' preference for the one-stop-shop purchase of traditional office supplies has been confirmed by the outcome of the market investigation on current purchasing and switching patterns.

6.1.2.1.2.1. *Current purchasing patterns*

- (79) As regards the Notifying Party's first main argument that the single-sourcing behaviour for the three traditional product categories is relatively infrequent, with [40-50]%-[50-60]% of customers buying all three traditional product categories together, the Commission notes that the figure quoted by the Parties includes all customers, irrespective of their size (small or large business customers) and types (national or international customers). It is therefore of limited relevance in the Commission's assessment for international customers and for large national customers (those segmentations will be discussed in sections 6.1.3 and 6.1.4).
- (80) Against this background, the Commission reviewed Staples' sales data in Belgium and the Netherlands for international and enterprise (namely large private) customers, focusing on customers who made a purchase in at least one of the three traditional office product categories of paper, ink & toner and stationery.⁶³ As shown in Table 1, [60-70]% of Staples' customers that made a purchase in at least one of the traditional office product categories made purchases in all three categories together. Essentially no customer bought only paper or only ink & toner from Staples. Overall, these two products are always bought jointly with stationery products.
- (81) Therefore, the analysis of Staples' sales data for international and large customers in Belgium and the Netherlands suggests that such customers have a strong preference for purchasing the three traditional office product categories of stationery, paper and

⁶¹ See Memo on the Commission's concerns as regards stationery, at points 2, and 5 to 8.

⁶² See Replies to the Commission's request for information of 2 October 2015, Question 1.

⁶³ For example, customers having bought only furniture, or computers and none of the traditional categories were omitted.

ink & toner together. Within those products, stationery is a key element of the traditional product categories, without which paper and ink & toner are rarely sold. Neither paper nor ink & toner is typically purchased without stationery, whereas some customers ([10-20]%) purchased only stationery.

Table 1: Staples customers buying in at least one of the traditional categories, 2014. Staples sales data (BE, NL), IAT and ENTR customers only

Customer buying...	Number of customers	Value [1000 EUR]	% of customers	% of value sold in traditional categories
Stationery only	[...]	[...]	[...]%	[...]%
Paper only	[...]	[...]	[...]%	[...]%
Ink only	[...]	[...]	[...]%	[...]%
Stationery&Ink. no Paper ⁶⁴	[...]	[...]	[...]%	[...]%
Stationery&Paper. no Ink ⁶⁵	[...]	[...]	[...]%	[...]%
Paper&Ink. no Stationery	[...]	[...]	[...]%	[...]%
Stationery&Ink&Paper	[...]	[...]	[...]%	[...]%
Total	[...]	[...]	100%	100%

Source: Staples sales data submitted with the report RBB Economics: "Relevance of bidding data for the competitive assessment", dated 18 May 2015.

- (82) Furthermore, on the basis of the qualitative results of the market investigation, the Commission considers that, contrary to the Notifying Party's claim, a majority of contract customers have a preference for the one-stop-shop supply of office products offered by contract stationers as it offers several cost and convenience advantages which are not available when purchases are split. Indeed, a vast majority of customers replying to the Commission's market investigation purchase most traditional office supplies from the same company. Few respondents purchase each category separately; of the minority that purchases only one category separately from the others, that category predominantly consists of ink & toner, and paper and stationery are almost always purchased together.⁶⁶
- (83) The majority of competitors replying to the Commission's market investigation also confirmed the customers' preference for the one-stop-shop supply of office products. Almost all responding competitors in the Phase II investigation report that most customers typically purchase different categories of office supplies together⁶⁷ and

⁶⁴ The existence of separate contracts for paper seems to be explained by the existence of separate contracts for large volumes of paper purchased in bulk as discussed in recital (88).

⁶⁵ The existence of separate contracts for ink & toner seems to be explained – at least in part – by the existence of a different business model and contractual arrangements for MPS as discussed in recitals (86) and (87). This option is not available to all customers and in particular not for customers requiring ink & toner for desktop printers as opposed to multifunctional printer-copiers.

⁶⁶ Replies to Phase II questionnaires Q8a-j to customers – Questions 4 and 5; replies to Phase I Questionnaire Q4 to customers (contract) – Questions 10 and 10.1.

⁶⁷ Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – Question 6. In Phase I respondents unanimously pointed out that different office products are purchased together either typically or by some customers: replies to Phase I Questionnaire Q1 to competitors (contract) – Question 14, however the Phase I question referred to a wider range of categories than traditional office supplies only.

that this is a particularly clear preference for large customers.⁶⁸ Aside from savings generated by a rationalisation of suppliers,⁶⁹ another reported reason relates to the fact that traditional office supplies consist of a large number of products of a relatively low value.⁷⁰

6.1.2.1.2.2. *Switching patterns*

- (84) As regards the second main argument of the Notifying Party that the preference for single sourcing is transient since the majority of customers purchasing their full range of traditional office supplies from the Parties in 2012 have switched, at least partially, to alternative suppliers in 2014, there is no distinction in the Parties' analysis by the type of customers (international and large national customers vs smaller customers). Therefore, the argument is less relevant for the assessment of the sourcing preference for international and large customers, which is the focus of the Commission's investigation. Moreover, among the customers who purchased their full range of traditional office supplies from the Parties in 2012 and switched to alternative suppliers in 2014 (see recital (74)), a significant proportion of those customers have switched their purchases completely between 2012 and 2014 (around [30-40]%), which is equally consistent with single-sourcing the three traditional product categories from another supplier.⁷¹ Moreover, partial switching is defined as a reduction of sales of 50% or more in any of the traditional product categories.⁷² Therefore, that definition of partial switching does not allow to infer a preference for single sourcing within each product category, in particular stationery.⁷³
- (85) Furthermore, the Commission analysed the sourcing behaviour of the Top 100 employers in each country where the Parties' contract businesses overlap in order to verify whether the Notifying Party's claim would apply to large contract customers

⁶⁸ Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – Question 8, where a majority of competitors indicated that 70% or more of their large customers prefer having a one-stop-shop for their office supplies under one single contract.

⁶⁹ For instance, reply of a competitor to Phase II Questionnaire Q9 to competitors (contract stationers) – question 8: '(...) *Most large corporate customers have a long tail-end of suppliers that they wish to rationalize. More categories from 1 supplier equal optimization of supplier database, cost savings and efficiency in total cost of ownership. Meaning consolidated orders, bigger average order value, less invoices, less reporting and less administrative work at the customer end.*'

⁷⁰ For instance, reply of a competitor to Phase II Questionnaire Q9 to competitors (contract stationers) – question 8: '*Due to the high number of products in combination of the relative low value per item in office supplies, companies / customers prefer to have one supplier to handle all the logistics and knowledge of the product groups*'

⁷¹ See RBB Economics, "*Staples/Office Depot – competition from specialist suppliers*", 31 August 2015, Table 10 and Table 11.

⁷² See RBB Economics, "*Staples/Office Depot – competition from specialist suppliers*", 31 August 2015: partial switching is defined as "*reduction in sales of 50% or more in any of the traditional categories*" between 2012 and 2014.

⁷³ Importantly, this definition of partial switching does not allow distinguishing between moving purchases to another supplier and reducing purchase value with the same supplier, and therefore is likely to overestimate true supplier switching. Reducing purchase value with the same supplier may occur for example due to the rationalisation and reorganisation of purchases. The Parties explain on page 4 in their "Replies to the 25 June 2015 Commission's RFI" that [...]. Such switching from non-core to core products is particularly relevant for stationery, as stationery seems to constitute the bulk of non-core products, as explained in footnote 224.

that buy under contract.⁷⁴ The Commission found that most of the Parties' large customers made purchases in all three product categories, both in 2012 and 2014.⁷⁵

6.1.2.1.2.3. *Role of specialist suppliers*

- (86) As regards the Parties' third main argument that specialist suppliers providing only one or very few categories of traditional office supplies should be included in the relevant product market, the Commission refers to its finding set out in recitals (70) and (71) that the distribution of office machines and associated services such as managed print services (MPS) should be considered a separate activity from the distribution of office supplies, even if there is a certain overlap in the distribution of ink & toner. That overlap in the distribution of ink & toner means that MPS may exert a competitive pressure when the market for distribution of ink & toner is considered individually but not when the market for the full range distribution of traditional office supplies is considered. MPS providers confirmed in the market investigation that they do not compete with the Parties in the provision of office supplies through contracts to final consumers.⁷⁶
- (87) The reason why the ink manufacturers who are active in MPS cannot be considered as a competitive constraint in the broader market for contract supplies of traditional office products is due to the nature of their distribution arrangements. The manufacturers normally sell ink & toner as consumables, and not as part of MPS, via reselling partners such as contract stationers.⁷⁷ Thus, private label manufacturers and Original Equipment Manufacturers ("OEMs"), such as Canon and HP, do not provide ink & toner or other office supplies directly to end consumers outside of MPS contracts. Even when large customers negotiate better prices for large supplies of those consumables directly with OEMs, they do not source directly from OEMs, but via the contract stationer of their choice, which receives ad hoc rebates by the OEM in order to be able to supply the customer at the agreed price.⁷⁸ While the manufacturers may compete with the Parties through MPS as an alternative to contract distribution of ink & toner, they cannot be considered as active within the contract channel itself, nor as potential competitors for full range supplies.
- (88) As for cut sheet paper, it is mostly sold together with stationery products, as set out in recital (81). Specialist paper manufacturers rely on contract stationers to distribute their products. They contract directly with the final customer only in the event of large orders.⁷⁹ While this may exert a competitive pressure when the market for distribution of cut sheet paper is considered individually, the main features of their

⁷⁴ For more details on this type of analysis, see below at recitals (256) et seq.

⁷⁵ In 2014, [70-80]% of customers that made a purchase in any traditional office category from Staples actually bought all three categories together. With Office Depot's customers the same figure is [80-90]%. Purchases in 2012 show essentially the same pattern.

⁷⁶ Reply of an MPS provider to Phase II Questionnaire Q10 to specialists – Question 6.1, where the respondent stated that it is not a competitor, but: "*...only a supplier to Lyreco, Office Depot and Staples.*" Replies to Phase II Questionnaire Q10 to specialists, Questions 3, 5 and 16.

⁷⁷ Agreed minutes of a conference call with a competitor of 22 October 2015: "*In case of large customers, where there is a big deal, certain terms (including the prices) can be negotiated between the customers and the manufacturer directly (...) [competitor], as a distributor, in big deal cases can receive assigned rebates from the manufacturers.*" (...) "*The largest suppliers include HP and Lexmark.*"; reply of an OEM to Phase II Questionnaire Q10 to specialists – question 9.1 "*This may occasionally occur in tenders held by large corporate customers. We may negotiate a maximum sale price. (Distributors are permitted to discount from the agreed maximum resale price and the retailers can negotiate a discount)*".

⁷⁹ Agreed minutes of a conference call with a specialist supplier of 21 October 2015.

supplies, notably the large volumes,, make the specialist paper suppliers unsuited to be considered as competitors in the contract distribution of traditional office supplies. Similar to the ink & toner specialists, while the paper specialists may compete with the Parties as an alternative to contract distribution of cut sheet paper, they cannot be considered as potential competitors for full range contract supplies.

- (89) Despite the fact that some customers buy paper or ink & toner separately from specialist suppliers, the majority of the supplies are thus made by generalist contract stationers such as the Parties and their contract stationer competitors, most notably Lyreco. Contrary to the Notifying Party's submission that ink & toner manufacturers and paper manufacturers could easily expand or enter the stationery segment, the specialist suppliers replying to the Commission's market investigation indicate that they are generally not active in stationery supplies, and deny their ability to expand their business model to encompass stationery.⁸⁰ An explanation for their inability to supply stationery is that distributing stationery and other office product categories would require logistics arrangements which they do not have,⁸¹ or which are more advanced than those they are able to set up.⁸² As discussed in recitals (86) to (88), while they may exert a competitive pressure on contract distribution of ink & toner through MPS or on contract distribution of cut sheet paper through bulk sales, if those categories were analysed separately, they may only exert a very limited pressure when considering the market for stationery contracts or contracts for traditional office supplies including stationery.⁸³ Nevertheless, that competitive pressure will be taken into account in the competitive assessment, for instance when the Commission assesses the closeness of competition between the Parties and their competitors (such as in recitals (351), (417) and (496)).
- (90) Therefore, the Commission finds that the evidence points to the existence of a market for contract distribution of traditional office supplies, which encompasses stationery, ink & toner, and paper. Customers within the relevant market most often purchase those categories together from contract stationers. Manufacturers and distributors of ink & toner and paper have limited sales within the relevant market compared to contract stationers who are capable of offering the full range of products.

6.1.2.1.3. Conclusion

- (91) In the light of the considerations set out in recitals (72) to (90), the Commission concludes that there is in all likelihood a separate product market for the one-stop-shop supply under contracts of the three traditional office supply categories (stationery, paper, ink & toner). However, for the purpose of this Decision, it can be left open whether, alternatively, separate product markets could be defined by individual product categories (defining thus three separate product markets for the supply of stationery, the supply of paper and the supply of ink & toner) because a significant impediment to effective competition arises regardless of whether a market is defined for one-stop-shop contracts for traditional office supplies or whether separate markets by product categories are distinguished, in which case concerns arise for the contract distribution of stationery products. Furthermore, it is not

⁸⁰ Replies to Phase II Questionnaire Q10 to specialists – Question 2.

⁸¹ Reply to Phase II Questionnaire Q10 to specialists – Question 7.

⁸² Agreed minutes from conference call with a specialist paper supplier: *"Logistics is generally a barrier to expansion for this market. In order to compete with the Parties, a company should be able to sell and deliver small quantities of product, and have efficient logistic arrangements in place to achieve this at a low cost. Setting this up can be very difficult"*.

⁸³ Any such pressure will be considered in the competitive assessment.

necessary for the Commission to conclude on the matter, given that the Parties have submitted remedies that would adequately remove any competition concerns identified by the Commission under the alternative product market definitions.

6.1.2.2. Distinction by product category, wholesale channel

- (92) In *Unipapel/Spicers*, the Commission found that the wholesale of traditional office supplies encompasses a number of categories, including: (i) traditional office/stationery products, for example pens, pencils, notepads, filing products, folders, paper; (ii) basic electronic office supplies, such as printer cartridges and data storage, as well as business machines, such as printers and faxes as well as (iii) office furniture, for example chairs and desks.⁸⁴ The Commission analysed those three markets separately but it ultimately left the market definition open.
- (93) In Sweden, the only country where the Parties' wholesale activities overlap to any significant extent, the Parties are active in the wholesale of the whole range of office supplies, including all of the three product categories listed in recital (92). The respondents to the market investigation indicate that the majority of retailers purchasing office supplies at the wholesale level have a preference for one-stop-shop purchasing with regard to the traditional office supplies categories including at least stationery products, ink & toner and paper.⁸⁵ This is due to the fact that a large proportion of customers in Sweden are small online retailers whose business model consists of running an online website where end-users can place orders and the handling and delivery is done directly by the wholesaler. In order to have a competitive offer in their online shops, the retailers require that the wholesaler offers a full range of products which can be then delivered to the end-users by a single supplier, which minimises the delivery costs and allows the online shops to offer competitive prices.⁸⁶
- (94) Based on the assessment in recitals (92) to (93), for the purpose of this Decision, the Commission will assess the effects of the transaction in the wholesale market for office supplies in Sweden, including at least the one-stop-shop supply of the three traditional office supplies categories (paper, ink & toner and stationery).

6.1.2.3. Distinction by product categories, direct channel

- (95) Given that no significant impediment to competition arises in the direct channel under any alternative market definition examined for the contract and the wholesale channel, for the purposes of this Decision, it can be left open whether the conclusions regarding the segmentation by product category for the contract or wholesale channel apply to the direct channel in the same way.

6.1.3. *Contract market: Distinction between international and non-international contracts*

- (96) Within the contract market, there are customers who purchase office supplies in two or more different countries. In order to procure office supplies in different countries, such customers may group their spending for office supplies with a single supplier under a single contract covering more than one country. While the Commission has not drawn a distinction between international and non-international contracts for office supplies in its previous decisions, the results of the Commission's market investigation presented in this Decision provide evidence to suggest that there is a

⁸⁴ Case M.6382 – Unipapel/Spicers, recital 24.

⁸⁵ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 5 and replies to Phase II Questionnaire Q11 to customers (wholesale) – Question 10.

⁸⁶ Agreed minutes of conference calls with retailers of 28 October and 4 November 2015.

separate product market for international contracts of office supplies due to limited demand- and supply-side substitutability between international and non-international contracts.

6.1.3.1. The views of the Notifying Party

- (97) In the Form CO, and particularly in Annex 22, in the Response to the Article 6(1)(c) Decision, as well as in further submissions during Phase II, the Notifying Party has provided a number of factual elements and arguments that would run counter to a sub-segmentation of the contract market between international and national contracts.
- (98) The Notifying Party's main arguments are the following:
- (a) International customers are able to switch all or part of their requirements to different types of suppliers including national suppliers.
 - (b) Customers with spending in multiple countries do not have a strong preference for international contracts because international contracts do not provide customers with a material pricing advantage;
 - (c) Customers would switch to national contracts in the event of a 5 to 10% price increase. In order to come to that conclusion, the Notifying Party relies to a large extent on two customer surveys commissioned by Staples, the 2013 international survey and the 2015 international survey mentioned in recital (12);⁸⁷
 - (d) Tenders for international contracts are made up of different product baskets per each country; since baskets are priced per country, customers can benchmark the prices offered by international suppliers with the prices offered by national suppliers;
 - (e) Margins for international customers are not higher than for non-international customers;
 - (f) Even when customers purchase office supplies in more than one country, since many of the sales under purportedly international contracts are in fact made mainly in one EEA country or in very few EEA countries, international contracts would not be markedly different from national contracts.

6.1.3.2. Internal classification by the Parties

- (99) First, the Parties themselves define a sub-set of international contracts within their respective contract businesses. They define international contracts as those signed with customers (i) purchasing office supplies for at least three countries and (ii) spending a minimum amount per year (Staples: minimum spend of EUR [500 000-1 000 000]; Office Depot: minimum spending of EUR [500 000-1 000 000]). Staples defines such customers as "International Account Team" ('IAT') customers and Office Depot defines them as "International Key Accounts" ('IKA').
- (100) Staples sees the international customers segment as follows: "[...]."⁸⁸
- (101) Second, both Parties have separate departments and employees dealing with customers purchasing under international contracts. Staples European international

⁸⁷ For a description of the methodology of the surveys, see footnote 4.

⁸⁸ Staples internal document entitled "ISR. International Sales Roadmap", February 2012, page 15.

team includes the head of the international team and [...] employees. Office Depot's contract business in Europe includes a "Director International Accounts Europe" and there are a total of [...] dedicated employees under the Director, including dedicated International Business Development Managers and International Business Managers.⁸⁹

- (102) Staples introduced its International Account Team in 2001 and summarises its functions in Figure 3:

Figure 3: Staples internal document entitled "ISR. International Sales Roadmap", February 2012, page 3
[...]

- (103) Therefore, the Parties themselves internally distinguish a separate group of customers who purchase under international contracts which lends weight to the argument that international contracts should be considered as a separate product market.

6.1.3.3. Demand-side considerations

- (104) From a demand-side perspective and in the light of the results of the market investigation, the Commission considers, for the reasons set out in the present section, that international customers do not view purchasing under international and non-international contracts as equal or sufficiently comparable substitutes to include them in the same product market.

- (105) Moreover, according to the results of the market investigation, a significant number of international customers are unable or unwilling to switch between supply under international and non-international contracts and have a preference for being supplied through international contracts.

- (106) That is consistent with what is stated in Office Depot's internal documents "*A typical international customer or prospect is looking for: i) cross border reduction of supplier base; ii) cross border harmonization of assortment; iii) economies of scale: price and cost (TCO); iv) single point of contact; v) 'Glocal' approach; vi) footprint maximization; vii) blueprint for more strategic categories; viii) partner mirroring their own purchasing organization; ix) partner with cross border authority*".⁹⁰

6.1.3.3.1. Trend to move to international contracts

- (107) The international customers' category is expanding. Customers and competitors reported, in the context of the market investigation, that they observe a general trend to move to international contracts.⁹¹ One competitor explains in that context: "*Several years ago multinational companies were much more keen on discussing separately (e.g. country per country) their need in office supplies. There is an evident trend where they tend to cumulate all needs in one single international contract excluding companies that are unable to compete internationally, which are by far the majority*".⁹²

- (108) This trend is the result of an ongoing process aimed at optimising time and effort spent on the purchasing of input materials, and in particular of materials of low

⁸⁹ See Staples' reply to the Commission's request for information of 2 October 2015.

⁹⁰ Office Depot internal document "International Accounts Europe - GAC meeting - Boca Raton, April 30th 2014".

⁹¹ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 27.2; agreed minutes of the calls with customers and competitors.

⁹² Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 27.2.

importance such as office supplies. Indeed, many customers refer to office supplies as "c-parts" which have a low importance in the running of their business and therefore they prefer to keep the purchasing process as simple as possible, also in order to better monitor their spending.⁹³ In line with that general trend, most customers who currently purchase under international contracts and who replied to the Commission's market investigation reported that they had decided to switch to international purchasing in recent years.⁹⁴ Some companies follow that trend by relying on the assistance of service providers specialised in the organisation of multinational procurement strategies.⁹⁵ Other companies confirmed the existence and importance of that trend by highlighting that it has been accompanied by an internal re-organisation which results in the reduction of procurement staff in favour of central contracting and tenders implemented at headquarter level.⁹⁶

- (109) Staples itself appears to acknowledge the growing importance of international contracts for its business in the last ten years: "[...]."⁹⁷
- (110) Staples also identifies a trend towards more international tendering: "[...]."⁹⁸
- (111) The trend is confirmed by the fact that against the backdrop of a market which is shrinking in size, an increasing proportion of the Parties' net contract sales is represented by international contracts.⁹⁹ Although the Commission asked for turnover data for the past ten years (2005-2014), the Parties were only able to provide data for a shorter period. Staples was able to provide data only for the last three years (2012-2014) and for the first months of 2015. Even data for this relatively short period shows, however, that the proportion of international contract sales [increased by 1-3 percentage points between 2012 and the first months of 2015] (for Stationery [the increment was of 1-3 percentage points between 2012 and the first months of 2015]). Office Depot was able to provide data for the last five years in the overlap countries except Sweden. International contract sales as a proportion of contract sales [increased by 2-4 percentage points between 2010 and 2014].

⁹³ Agreed minutes of the call with a customer of 2 September 2015: "*[customer] does not want to invest more procurement resources in the procurement of office supplies which are "C-parts" and as such not important input products for [customer]. More specifically, [customer] would not have the manpower to launch several local tenders and compare all the prices at the local level.*"

⁹⁴ Replies to Phase I Questionnaire Q5 to customers (international contracts) – Question 17.

⁹⁵ Agreed minutes of a conference call with a service provider of 29 September 2015: "*There is a significant and increasing trend towards global tenders for customers: international customers want international contracts.*" (...) "*The customers generally consult [company] in order to get its advice on how to globalize its contracts and not to regionalize them.*"

⁹⁶ In a conference call one of those customers stated that: "*If [customer] were to have 6 different, local contracts, they would need 6 different webshops and payment / invoicing systems. This would create a need of 3 more employees.*" (agreed minutes of conference call with customer of 18 November 2015). Another customer stated that: "*.. decentralisation would add personnel costs as the national business units would have to run the tender processes again. Currently, only two employees within [customer] are managing the contract centrally.*" (agreed minutes of call with a customer of 9 September 2015).

⁹⁷ Staples internal document entitled "ISR. International Sales Roadmap", February 2012, page 3.

⁹⁸ *Ibid*, page 7.

⁹⁹ See reply to RFI of 2 October 2015 on international contracts.

6.1.3.3.2. Advantages of international contracts

(112) The customers replying to the Commission's market investigation explained that international contracts for office supplies have the following advantages compared to multiple national contracts:¹⁰⁰

- (a) Lower prices/international rebates through pooling of purchasing volumes
- (b) Reduced human resources spending on purchasing process
- (c) Uniform quality
- (d) Uniform IT ordering system
- (e) Uniform invoicing system
- (f) Improved cost control
- (g) Central and advanced reporting to identify best practices
- (h) Advanced logistics
- (i) Better service/one key account manager

(113) The following quotes illustrate customers' comments received in the course of the market investigation on the advantages of international contracts:¹⁰¹

"An international contract against several national contracts represents: only one negotiation, only one implementation, only one supplier monitoring, quick and global and detailed view of our spending."

"The advantage of an international framework contract is that [a customer] has more negotiating power (when the whole Group is involved); it also facilitates the deployment of good practice policies, as all the entities can take advantage of the Group power negotiation. Office supplies represent a rather small spending: there is no interest for the Group to generate human resources to tackle local negotiation country by country."

"Lower prices (including volume discounts, centralized monitoring of our international spending, reduction of the number of different products we purchase, simplification of invoicing, payment and deliveries, etc.)"

(114) To quantify such advantages, a distinction should be made between direct cost advantages (through lower purchasing prices), indirect cost advantages (through process cost optimisation) and other advantages in terms of service and quality. When asked during the market investigation how much cheaper it is for them to buy through an international contract, customers' replies ranged from "a few percent" to 40%. Conference calls with some of those customers during Phase I showed that some customers had understood their answer to include only direct cost advantages. The individual (non-confidential) replies were:¹⁰²

¹⁰⁰ Replies to Phase I Questionnaire Q5 to customers (international contracts) – Question 13; agreed minutes of calls with customers; almost all of the customers replying to the Commission's market investigation identified all or some of the advantages listed in recital (112).

¹⁰¹ Replies to Phase I Questionnaire Q5 – Question 13.

¹⁰² Replies to Phase I Questionnaire Q5 – Question 13.1; none of the customers explicitly stated in reply to Question 13.1 that the price levels were the same (although the lack of reply by some customers has to be interpreted with caution); agreed minutes of the conference calls with customers.

Company	Cost Savings	Company	Cost Savings
Respondent 1	10-15%	Respondent 7	5-10%
Respondent 2	10%	Respondent 8	5%
Respondent 3	10-20%	Respondent 9	5-10%
Respondent 4	5-10%	Respondent 10	40%
Respondent 5	"a few%"-40%	Respondent 11	"much cheaper"
Respondent 6	8-15%%	Respondent 12	15%

- (115) More interviews with customers buying under international contracts took place during the market investigation in Phase II. When asked how much cheaper it is for them to buy through an international contract, the respondents gave the following replies, referring either only to direct cost advantages or to both direct and indirect cost advantages.¹⁰³

Company	Cost Savings	Company	Cost Savings
Respondent 1	5-10% [D]	Respondent 7	10 % [I]
Respondent 2	40% [D/I]	Respondent 8	up to 20 %[D]
Respondent 3	10%[D]	Respondent 9	up to 30%[D]
Respondent 4	20%[D]	Respondent 10	5-10%[D]
Respondent 5	12-13% [D]	Respondent 11	20%[D]
Respondent 6	10 %[D]	Respondent 12	10-15% [D/I]

- (116) The Parties argue that international contracts do not provide customers with a material pricing advantage.¹⁰⁴ This is based on question 34 of the 2013 international survey which asked the surveyed customers about the price differential between contracts with national and international vendors.¹⁰⁵ According to the Parties, the responses to that question show that the expected prices from a single international vendor may be either higher or lower than the expected prices from a combination of national vendors. More precisely, the distribution is symmetric across the different options available to the respondents: [10-20]% of respondents mention that international prices are higher by more than [5-10]%; [10-20]% of respondents mention that international prices are higher by less than [5-10]%; [30-40]% of respondents mention that there is no difference between international prices and national prices; [10-20]% of respondents mention that national prices are higher by

¹⁰³ The replies including only direct cost advantages are marked in the table as [D] while only indirect cost advantages are marked as [I] and replies including both are marked [D/I] (agreed minutes of conference calls with customers of 20 November 2015, 23 November 2015, 24 November 2015, 23 November 2015, 24 November 2015, 18 November 2015, 18 November 2015, 12 November 2015, 24 November 2015, 26 November 2015, 26 November 2015, 26 November 2015).

¹⁰⁴ See the submission "*Competitive Assessment – International Customers*", dated 18 May 2015, RBB Economics, page 14.

¹⁰⁵ The 2015 International survey has similar results as the 2013 International survey.

less than [5-10]%; and [10-20]% of respondents mention that national prices are higher by more than [5-10]%.¹⁰⁶

- (117) The Commission, however, considers that the formulation of the question does not allow for such inferences. This question is phrased as: "*assuming no differences in other features, what is your expected price differential between purchasing from a single international vendor vs a group of 2-3 national vendors – if any?*".¹⁰⁷ The Commission considers that the wording "*assuming no differences in other features*" is potentially misleading since it prompts the respondents to assume that potentially important differences between international and national suppliers such as for example the number of countries covered do not exist. Moreover, given the assumption implied by the wording of that question, which is that national suppliers are identical to international suppliers in all other features except prices, it is not surprising that the proportion of customers that mention that international prices are lower than national prices ([30-40]%) is relatively similar to the proportion of customers mentioning that international prices are higher than national prices ([20-30]%).¹⁰⁸
- (118) As part of a broader effort to verify the results of its market investigation against the findings of the 2013 and 2015 surveys submitted by the Parties, the Commission has been able to reach 28 of the 104 respondents to the 2015 international survey. Among the customers that could quantify the savings generated by an international contract, all but two indicated that the savings they obtain from international contracts are 10% or higher. This is in line with the Commission's findings in the market investigation.
- (119) The price advantage of international contracts, moreover, is not exclusively explained by the fact that customers can aggregate the volumes they purchase under a single contract with a supplier, and obtain rebates based on volumes. Internal documents show that rebates may also be granted in correlation with the geographical scope of the contract itself.¹⁰⁹
- (120) As regards the Notifying Party's argument that it would not be relevant to distinguish a different segment for international contracts, because the spending made under such contracts in the EEA is in any case concentrated in one or few EEA countries, the Commission finds that the evidence available to it does not support that conclusion. According to a submission on the geographical coverage for each of the Party's international contracts,¹¹⁰ only one third of the Parties' international contracts cover more than [70-80]% of the customer's demand in one country only. Of the

¹⁰⁶ Question 18 of the 2015 international survey allows to carry out a similar analysis. Excluding the don't know/unsure category, [10-20]% of respondents mention that international prices are higher by more than [5-10]%, [10-20]% of respondents mention that international prices are higher by less than [5-10]%, [20-30]% of respondents mention that there is no difference between international prices and national prices, [10-20]% of respondents mention that national prices are higher by less than [5-10]%, and [20-30]% of respondents mention that national prices are higher by more than [5-10]%.
¹⁰⁷ See the submission "*Competitive Assessment – International Customers*", dated 18 May 2015, RBB Economics, page 14.

¹⁰⁸ In the 2015 international survey, despite the potentially misleading wording, the proportion of respondents mentioning that national prices are higher than international prices increases up to [40-50]%, compared to [30-40]% in the 2013 international survey.

¹⁰⁹ See internal documents showing rebates offered for additional countries added to the contract, irrespective of the quantity thresholds purchased by the customers. For instance, Office Depot internal excel file titled ODP – EU – 00017765.

¹¹⁰ Form CO, Annex 23.

remaining two-thirds of contracts, [70-80]% cover sales of office supplies to more than five countries.¹¹¹

6.1.3.3.3. Customer preference

(121) Based on the results of the 2015 and 2013 International surveys, the Parties argue that international customers do not have a strong preference for international contracts.

(122) Table 2 summarises the replies to the relevant questions in the 2013 and 2015 international surveys asking the surveyed customers about the number of different suppliers they have across different countries.¹¹²

Table 2: Results of the 2013 and 2015 International surveys on sourcing policy for international customers

2015 International survey	Number of observations	%	Cumulative %
A single supplier covering all countries	[...]	[...]%	[...]%
A single supplier covering most of the countries	[...]	[...]%	[...]%
A single supplier covering some of the countries	[...]	[...]%	[...]%
Different suppliers in each country	[...]	[...]%	100%
Total	[...]	100%	

Don't know/unsure: [...] observations

2013 International survey	Number of observations	%	Cumulative %
Single vendor in all countries	[...]	[...]%	[...]%
Single vendor for more than 50% of countries	[...]	[...]%	[...]%
Single vendor for less than 50% of countries	[...]	[...]%	[...]%
Different vendors in each country	[...]	[...]%	100%
Total	[...]	100%	

Don't know/unsure: [...] observations

Source: Commission' calculations based on the 2013 and 2015 International surveys.

(123) In their interpretation of the results concerning the 2015 international survey in Table 2, the Parties aggregated the number of respondents for the following three categories: (i) a single supplier covering most countries, (ii) a single supplier covering some countries, and (iii) a different supplier in each country. This allows them to claim that [60-70]% of the customers responding to the 2015 international survey use multiple vendors across countries ([60-70]% in the 2013 international survey).¹¹³

(124) The Commission notes however that the survey results may also lead to different interpretations. In particular, it is also possible to aggregate the number of respondents having indicated that they have (i) a single supplier covering all countries; (ii) a single supplier covering most countries, in which case the Parties' surveys could be read as indicating that [60-70]% ([70-80]% in the 2013

¹¹¹ Form CO, Annex 23.

¹¹² Question 8 of the 2013 International survey (see Annex A.1 of the submission "*Competitive Assessment - International Customers*", dated 18 May 2015, RBB Economics), and Question 8 of the 2015 International survey (see "*Project Warrior – survey Questionnaire*", dated 11 May 2015, RBB Economics).

¹¹³ See "*Competitive Assessment – International Customers*", submission of 18 May 2015, RBB Economics.

international survey) of the respondents use a single supplier for all or most of the countries.

- (125) The important gap in the percentages between the categories "single supplier covering most of the countries" ([30-40]% of respondents in the 2015 international survey, [30-40]% of respondents in the 2013 international survey) and "single supplier covering some of the countries" ([10-20]% of respondents in the 2015 international survey, [5-10]% of respondents in the 2013 international survey) suggests that the strength of the preference for single sourcing is different between those two categories of respondents. Therefore, the Commission disagrees with the Parties' approach to pool the respondents that use a single supplier for most countries with the respondents that use a single supplier for some countries or a different supplier in each country.
- (126) The results of the Commission's market investigation on the advantages of international contracts also point to a marked preference of multinational customers for contracting office supplies under an international contract (see recitals (112) to (120)).
- (127) Furthermore, to address the Parties' claim presented in recital (121) and to better understand large customers' preference for sourcing office supplies internationally from a single supplier, the Commission reviewed sales data provided by the Parties on Staples' and Office Depot's international customers.¹¹⁴ That data includes purchases from the Parties by customer and country. The Commission could identify 55 firms that appear as customers with both Parties in at least one EEA country. While those firms do indeed purchase from both Parties across various countries (and possibly within the same country as well), the Commission found that they typically make the overwhelming share of purchase value from only one of the Parties. Analysing the value split of purchases made from the Parties by subsidiaries of those customers located in various countries showed that typically more than [90-100]% of the total sales value of customers across all subsidiaries were completed with one of the Parties, leaving less than [0-10]% for the other Party. This behaviour is consistent with a strong preference for single sourcing office supplies internationally.

6.1.3.3.4. Switch to national contracts in reaction to a SSNIP

- (128) In the Phase I investigation, a majority of respondents among international customers (13 out of 20 respondents who took a clear position on the matter¹¹⁵) indicated that they would not switch to sourcing separately per country if they could get a better price from national suppliers. Those customers confirmed in their reply that they had a set preference to source office supplies from one international supplier.¹¹⁶ However, when asked about a hypothetical small but significant and non-transitory increase in price ("SSNIP") of 5 to 10% in international contracts, a clear majority of customers (14-15¹¹⁷ out of 21 respondents) indicated that they would switch to non-international contracts.¹¹⁸ Out of the 20 respondents who took a clear position on the

¹¹⁴ Form CO, Annex 23.

¹¹⁵ That counting of replies is based on the confidential and non-confidential replies. In total, seven respondents indicated that they would switch to sourcing separately per country, 13 indicated that they would not and four respondents indicated "Other".

¹¹⁶ Replies to Phase I Questionnaire Q5 – Question 14.

¹¹⁷ One of the customers who had indicated that it would switch to national contracts in reaction to a SSNIP in international contracts explained its reply by stating "*If there are no other international substitutions available*" so it is not clear whether its reply can be counted as a yes or no.

¹¹⁸ Replies to Phase I Questionnaire Q5 – Question 15.

first question, 18 also replied to the second question. Out of these, eight respondents provided seemingly contradictory replies by replying no to the first switching question and yes to the second switching question.

- (129) To investigate those potential inconsistencies in the customers' replies, the Commission conducted follow-up calls with the eight customers whose answers appeared to be contradictory. The Commission also spoke to the other respondents who had indicated their readiness to switch to national contracts in the event of a SSNIP in international contracts and to respondents who had indicated that they would not switch.
- (130) While the 15 customers who had indicated that they would switch to national contracts in the event of a SSNIP in international contracts generally clarified that it is very difficult to reply to a hypothetical question of that kind, nine of them replied that they would not switch in light of a price increase of 5 to 10%, and the remaining six said that a price increase of 5 to 10% would not by itself be sufficient to persuade them to revise their procurement strategy, and they would probably continue sourcing under an international contract.¹¹⁹ The Commission thus found that virtually all of those respondents had overstated their actual switching behaviour when replying to the written Commission questions in the Phase I investigation. The Commission also contacted customers that indicated they would not switch in the event of a 5 to 10% price increase (even if there was no inconsistency in their reply) but none of those customers suggested that they would switch when clarifying their replies, thus confirming their reply. While there was evidence of overstated switching behaviour in their replies to the SSNIP question, there was no evidence of an understated switching behaviour in reply to the same question. This was also consistent with the indication of savings achieved through international contracts, which generally exceed 10%.¹²⁰
- (131) The Parties, however, reiterated their argument to prove that customers purchasing office supplies under international contracts would switch to non-international contracts in case of a SSNIP in international contracts. The Parties mostly rely on the 2013 and 2015 International surveys. [80-90]% of the respondents in the 2015 international survey replied that they would switch from international suppliers to national suppliers in the event of a price increase of [10-20]% by all international suppliers (the corresponding figure was [80-90]% in the 2013 international survey).¹²¹ The detailed results of the 2015 international survey are presented in Table 3.

¹¹⁹ See minutes of follow-up conference calls with customers.

¹²⁰ See paragraphs (114) and (115).

¹²¹ See email sent by the Notifying Party to the Commission on 3 September 2015.

Table 3: Results of the 2015 international survey on the Question 20 "What is the minimum price increase by the major international suppliers that would cause you to purchase from national players for your office supply needs"

	Incl. don't know			Excl. don't know		
	Number of observations	%	Cumulative %	Number of observations	%	Cumulative %
A price increase of less than [0-5]%	[10-20]	[10-20]%	[10-20]%	[10-20]	[10-20]%	[10-20]%
A price increase of between [0-5]% and [0-5]%	[20-30]	[30-40]%	[40-50]%	[20-30]	[40-50]%	[50-60]%
A price increase of between [5-10]% and [10-20]%	[10-20]	[10-20]%	[60-70]%	[10-20]	[20-30]%	[80-90]%
A price increase above [10-20]%	[10-20]	[10-20]%	[70-80]%	[10-20]	[10-20]%	100%
Don't know/unsure	[10-20]	[20-30]%	100%	NA		
Total	81	100%		64	100%	

Source: Commission's calculations based on the 2015 international survey.

- (132) The follow-up calls with customers who answered positively to the SSNIP question in the Commission's Phase I investigation as described in recital (128) raised the question whether the differing outcomes of the Parties' surveys and of the Commission's market investigation could be explained by a tendency of customers to overstate their switching behaviour in reply to the SSNIP question also in the context of the Parties' surveys.
- (133) In order to assess that hypothesis, the Commission identified the 52 respondents that replied positively to the SSNIP question in the 2015 international survey, that is to say those customers who replied that they would switch to national contracts in the event of a price increase of 10% or less.¹²² The Commission was able to contact more than half (28 out of 52) of those who indicated that they would switch for a price increase of 10% or less.
- (134) Three of the respondents do not, in fact, purchase office supplies under an international framework contract, so for those respondents, the SSNIP question was not applicable. As regards the remaining respondents, the Commission found evidence that they had overstated their switching intentions and that in most cases they had not taken into account the cost of switching when replying to the 2015 survey.¹²³ None of those remaining 25 respondents contacted by the Commission clearly confirmed that they would switch to national contracts in the event of a SSNIP in international contracts. Eight respondents explained that they may consider switching subject to a number of factors (such as prior attempts to negotiate better prices with their existing international suppliers) but that this was not certain. Six respondents indicated that they would rather not switch, and 11 respondents indicated that they would definitely not switch. Generally, the respondents contacted by the Commission indicated that they would not switch from international contract

¹²² Those 52 customers include the 11, 27 and 14 customers listed in Table 3 who replied they would switch in case of a price increase of less than 2%, between 2% and 5% and between 5% and 10% respectively.

¹²³ Minutes of conference calls with respondents to the 2015 survey.

to national contracts because that would entail reversing their company's policy of central sourcing.¹²⁴

- (135) Those results cast significant doubt on the results of the 2013 and 2015 international surveys regarding the switching behaviour of international customers. Even assuming that the eight respondents that were unsure about their potential behaviour would indeed switch for a price increase of up to 10%, this leads to a switching proportion within the sample of 32% for a price increase of up to 10%. While that proportion is based on a relatively small number of respondents (25), it is in stark contrast to the Parties' submission of a figure of 80-90% from the survey evidence. The Commission also notes that its approach is conservative and thus favourable to the Parties, since the 28 respondents contacted were classified as switchers in the 2015 international survey (and thus had made 100% positive replies to the SSNIP question), which should therefore have led to a bias toward a high number of switches.
- (136) Furthermore, some of the survey responses are inconsistent when comparing the question on switching and the question on price differences between international and national suppliers. In the 2015 international survey, among the 38 respondents replying that they would switch in the event of a price increase by international suppliers of less than 5%, eight respondents also replied that national prices are more than 5% higher.
- (137) Those findings were further confirmed by the customers' actual switching behaviour as reported in the market investigation. Only two respondents to the market investigation in Phase II reported that they had actually switched to national suppliers in the past, in response to a lower price offer compared to international suppliers,¹²⁵ while only one respondent in Phase I reported a partial switch to a non-international contract.¹²⁶ All other respondents that switched in the past had switched from national to international contracts and were thus part of a progressive trend to pool the spending in different countries under a single international framework contract.¹²⁷
- (138) The Parties further submitted a sample list of customers of both Parties that allegedly switched from an international contract to a national contract. The Commission verified those submissions, also contacting some of those customers mentioned by the Parties, and found that several of the customers were examples of customers

¹²⁴ Minutes of conference calls with respondents to the 2015 survey.

¹²⁵ Reply of one customer to Phase II Questionnaire Q8f to customers – Questions 34 and 43.1. However, the suppliers of this customer are Staples in the United Kingdom and Lyreco in the remaining countries in which the customer is active, see reply to question 43.1. Further, in Phase I of the market investigation, the same customer stated that: "*3 international suppliers can meet our 'one stop shop' needs: Staples, Lyreco or Office Depot*", Phase I Questionnaire Q4 to customers (contract), question 19.3. For the other customer, the switch happened because the company purchases such low amounts of office supplies that no volume gains can be obtained by having centralised purchasing, (agreed minutes of conference call with a customer of 30 November 2015).

¹²⁶ Agreed minutes of conference call with customer of 2 September 2015.

¹²⁷ For example, one customer explained: "*The global agreement was concluded in 2011.[...] Before 2011 the contracts were mostly national/regional.*" Another customer stated that: "*[...] has had local contracts historically, but 1,5 years ago it started to gradually replace these by moving to international sourcing.*" A customer further explained "*At the beginning of 2013, [...] started preparing its first international tender for office supplies. [...] regarded stationery/office supplies as a product group well-suited for international supply. At the end of 2013, the tender was launched for 6 countries in Europe.*" (agreed minutes of conference calls with customers of 16 October 2015, 24 November 2015 and 12 November 2015).

sourcing a product from a specialist supplier¹²⁸ or customers moving from central sourcing to local sourcing but maintaining the Parties or Lyreco as a supplier. In one instance, a customer reached by the Commission expressly denied having already switched away from the international contract with one of the Parties in reaction to a planned price increase.¹²⁹

6.1.3.3.5. Price setting and benchmarking in international contracts

- (139) The Parties further submit that the prices in international contracts are set at a national level and that customers use national prices as a benchmark to assess the competitiveness of international offers. Calls with competitors and replies from customers to the market investigation confirm that prices in international contracts appear to be set at the national level in many cases.¹³⁰ However, that does not in itself provide evidence on demand-side substitutability since the comparison of prices at the national level can be caused by a number of reasons (including comparison with previous offers made under national tenders, differences in local purchasing power and differences in cost-to-market). Therefore, comparison of national prices does not necessarily imply that national contracts will be considered as adequate substitutes for international contracts.
- (140) Furthermore, the Parties' internal documents indicate that there is a growing trend towards uniform pricing in Europe and that discounts are granted on the basis of overall volumes instead of being granted on a country by country basis. While multinational customers responding to the market investigation largely confirmed that the comparison of offers within international tenders is made on the basis of national baskets, some of them acknowledged that contracting under an international contract allowed them to obtain a uniform price, or that they expected that by contracting internationally they could achieve a uniform price across different countries.¹³¹
- (141) Even in the many cases where a price comparison is made based on national baskets of products and national price lists, benchmarking cannot be fully made against prices set nationally because of rebates. Most international contracts contain volume rebates which are granted across the total spending of the customer so that irrespective of the starting price, customers have to factor in an overall spending rebate when comparing offers.
- (142) As regards price benchmarking, the Commission has also analysed the results of the 2013 survey.¹³² Among the international customers who conducted a price benchmarking in the market place in the last two years before the 2013 survey, [80-90]% included Staples in the price benchmark, [70-80]% of the respondents

¹²⁸ See Reply to Request for information on the reply to the Article 6(1)(c) decision, reply to Question 1 and Annex 1.

¹²⁹ See Minutes of a conference call with a customer, 30 October 2015.

¹³⁰ Replies to Phase I Questionnaire Q5 – Question 20; agreed minutes of conference calls with customers of 26 November 2015, 25 November 2015 and 23 November 2015.

¹³¹ In a conference call one customer said that: *"The prices for the products covered by the contract are set at an international level."* Another customer who recently tendered said that: *"Prices will be negotiated centrally with the new framework contract"*. Another customer said that: *"Generally, [customer] requests to have uniform prices for all countries under its international contact. This is however not always possible, especially in case of products manufactured locally."* (agreed minutes from conference calls with customers of 28 November 2015, 24 November 2015 and 24 November 2015 respectively).

¹³² See Annex A.1 of the submission *"Competitive Assessment - International Customers"*, dated 18 May 2015, RBB Economics, question 20 and question 21. See also footnote 273 for a detailed description of this question in the 2013 International survey.

included Lyreco, and [40-50]% of the respondents included Office Depot. Other alternatives appear significantly less than the three international suppliers: "a combination of local vendors" is mentioned by only [5-10]% of the respondents, Amazon by only [5-10]% of the respondents, Fiducial (which is a national supplier in France and to a lower extent in Belgium) by only [5-10]%, specialised ink & toner vendors by only [0-5]% of the respondents, and Quantore (which is a national supplier in the Netherlands) by only [0-5]% of the respondents. Those results suggest that international customers benchmark prices among the three international suppliers, and that national vendors and specialists suppliers are often not included in the price benchmarking against international suppliers. The Commission also notes that it was not possible to conduct a similar analysis with the 2015 international survey since that question on price benchmarking was not included.

6.1.3.3.6. Conclusion on demand-side substitutability

(143) Based on the assessment in recitals (104) to (142) and the outcome of the market investigation, the Commission considers that there is limited demand-side substitutability between international and non-international contracts.

6.1.3.4. Supply-side considerations

6.1.3.4.1. Capability of national suppliers to supply customers in other countries

(144) From a supply-side perspective, suppliers do not appear to be able to offer international contracts if they do not have operations set up in the relevant countries.¹³³ Such operations would include at the very minimum logistics capabilities and customer service which can be performed either through the supplier's own operations or through an alliance with a local partner. Further requirements would include knowledge of the specific market situation and local product preferences as well as the ability to serve multi-lingual clients in terms of catalogues and customer service.

(145) In the words of a competitor, 'due to the legal structure, the complexity, the geographical scope and various law/jurisdictions, international contracts differ materially from national contracts'.¹³⁴

(146) The results of the market investigation indicate that setting up new contract distribution operations in an EEA country or entering into an international business alliance are options that are not available in the short term without incurring significant costs or risks.¹³⁵ For instance, one of the competitors estimated that the required investments would exceed several million EUR and take several years. However, as already set out in recital (55), supply-side substitutability requires that suppliers would not need to adjust existing tangible and intangible assets, make additional investments, take strategic decisions or incur time delays.¹³⁶

(147) Another competitor¹³⁷ indicated that: '[competitor] is not operating internationally (...). This is a real disadvantage, as large customers want international framework contracts. (...). There are barriers to expansion that generally make it difficult to

¹³³ Further details on the need to have a local presence in the EEA countries will be discussed in the section on the geographic market definition (see section 0).

¹³⁴ Reply of a competitor to Phase II Questionnaire Q9 – Question 32.1.

¹³⁵ Replies to Phase I Questionnaire Q1 – Questions 55.1 and 55.2.

¹³⁶ Commission Notice on Market Definition, paragraphs 20 and 23.

¹³⁷ Agreed minutes of a conference call with a competitor of 16 October 2015.

expand to other countries: those are related to specific local demands, market knowledge, the need to build a local presence and suitable logistics'.

- (148) The inability to supply customers internationally also reduces the ability to participate in international tenders from the outset, particularly when the tender specifications on an international tender expressly require previous experience in supplying customers under international contracts. For example, in an invitation for an international tender, a customer included an eligibility requirement for the supplier to have "*performed at least three contracts within the last five years substantially similar in scope and magnitude.*"¹³⁸ Another customer listed "*experience with international companies with high coverage of footprint in Europe*"¹³⁹ as the "*key attribute*" of the successful supplier. Yet another customer listed the "*supplier's relevant global experience*" as part of the evaluation criteria for the assessment of suppliers' proposals in response to its tender.¹⁴⁰
- (149) Therefore, the Commission finds that national suppliers have little to no capacity to supply customers in other countries under international contracts.

6.1.3.4.2. Participation of national competitors in international tenders

- (150) The results of the market investigation indicate that some customers allow suppliers to only bid for certain countries covered by an international tender.¹⁴¹ However, in most cases, only the Parties and Lyreco participate in international tenders. Of the customers purchasing under international contracts who replied to the market investigation, only a few listed national suppliers as participants in their international tenders.¹⁴²
- (151) Evidence from the market investigation also suggests that, while locally active, companies may be invited in order to have more competitive pressure on international suppliers, they are either unable to bid or do not succeed in securing only part of the customer's tendered spending.¹⁴³ Furthermore, local companies do not appear to be successful in international tenders as the bidding data analysis presented by the Parties shows (see recitals (319) to (325)).
- (152) The 2013 international survey also shows that in most cases, only the Parties and Lyreco compete for international tenders. As discussed in recitals (326) to (330), when respondents were asked about the suppliers participating in tenders, Staples, Office Depot, and Lyreco were by far the most cited participants, both at the initial stage and at the shortlist stage of the tenders. National suppliers and specialists rarely appear as participants for international tenders. In addition, as discussed in recital (142), the Parties and Lyreco are the most cited suppliers included in price benchmarking conducted by the respondents, compared to national suppliers and specialists which cited by very few respondents. As discussed in recitals (335) to

¹³⁸ See internal documents of Office Depot, a document entitled "Invitation for international bidding for [customer] centralised contract for the procurement of office supplies" of 10.07.2015.

¹³⁹ See reply to RFI of 20 November, including Office Depot's internal document entitled "Request for proposal, office supplies [company]" of 17.02.2015.

¹⁴⁰ See reply to RFI of 20 November, including Office Depot's internal document entitled "Request for proposal (RFP), Global Office Consumables Tender" of 03.06.2015.

¹⁴¹ Replies to Phase I Questionnaire Q5 – Question 47 and replies to Phase II questionnaires Q8a-j to customers – Question 8.

¹⁴² Replies to Phase I Questionnaire Q5 – Question 45.

¹⁴³ Agreed minutes from conference calls of 29 September 2015 and 16 October. Replies to Phase II questionnaires Q8a-j to customers – Question 8 for evidence of local suppliers being invited but unable to bid or win the contract.

(338), the 2013 international survey also reveals that international customers consider that national suppliers and specialists are not credible alternatives to the Parties and Lyreco for international contracts. Last, the analysis of bidding data for international tenders suggest that the competition is mainly between the Parties and Lyreco, while national and specialist suppliers do not pose a significant competitive pressure in international tenders (see recitals (319) to (325) for a detailed discussion).

- (153) The evidence thus indicates that despite receiving bids of competitors which can only provide non-international contracts, in practice, the customers do not consider such bids as viable substitutes to international bids.

6.1.3.4.3. Conclusion on supply-side substitutability

- (154) In light of the analysis in recitals (144) to (153), the Commission finds that there is limited supply-side substitutability between international and non-international contracts.

6.1.3.5. Margin levels

- (155) The Parties also argue that margin levels can be used as an indicator to assess whether national and international contracts could fall into separate product markets. According to the Parties, their margins for international contracts¹⁴⁴ are, on average, almost the same as their margins for national contracts. According to the Parties, this justifies not defining separate markets since the purported differences in competitive conditions (in terms of number and strength of competitors) should lead to higher margin levels for international contracts.¹⁴⁵

- (156) However, the margin levels can be influenced by many factors (not considered in the analysis provided by the Notifying Party), including but not limited to the scale of the contracts and the dynamics in the negotiations between customers and suppliers. That issue notwithstanding, the margin analysis alone is insufficient to counter the findings related to demand and supply-side substitutability as established in line with the available evidence and the results of the market investigation.

6.1.3.6. Conclusion on the segmentation of the contract market

- (157) Based on the assessment in recitals (144) to (156), the Commission considers all the evidence available and the outcome of the investigation and takes into account the trend for customers to move toward international contracts, the advantages to customers provided by international contracts and their potential and actual switching behaviour and the inability of national suppliers to compete for international contracts. In light of that evidence, the Commission concludes that international contracts of office supplies constitute a separate product market from non-international contracts of office supplies.

6.1.4. *Non-international contract market: Segmentation by customer size*

6.1.4.1. The views of the Notifying Party

- (158) With regard to national contracts, the Parties consider that a further distinction among national contracts according to customer sizes (for example based on a specific number of office workers) is not warranted. According to the Notifying Party, given the arbitrary nature of a cut-off point which would separate large and small customers, distributors are not in a position to price discriminate between

¹⁴⁴ Following the Parties' internal classification, see recital (99).

¹⁴⁵ Form CO, Annex 22, page 15.

customers; no matter how large or small the customer, suppliers will provide the same service and product range offering.

6.1.4.2. The Commission's assessment

- (159) As regards the contracts for different customer sizes, the Commission previously concluded in *Buhrmann/Samas Office Supplies*¹⁴⁶ that it was necessary to distinguish between, on the one hand, small customers and, on the other hand, medium-sized to large customers (which would generally include at least customers with 200 office workers or more but the category would be extendable to customers with 100 offices workers or more). The latter source traditional office supplies nationwide and have specific requirements in terms of one-stop-shop ordering and account management, specific ordering and delivery facilities adapted to their own systems and processes and logistics. That approach is broadly confirmed by the results of the market investigation in this Decision.¹⁴⁷
- (160) That distinction is in line with the Parties' own internal segmentation of different customers, which they classify in different categories depending on their target spending in office supplies.
- (161) According to Staples' internal classification, a customer with less than [200-300] employees is classified as a 'Mid-Market account', while above that level it is classified as an 'Enterprise account' (with the exception of International IAT accounts as defined in recital (99)).
- (162) Similarly, Office Depot's customer classification relies on the potential spending of those customers. The main categories are 'Inside Sales Accounts' (Spending under EUR [5 000-10 000] per year), 'Regional Accounts' (EUR [5 000-10 000] to [25 000-30 000] per year), 'Mid-Market Accounts' (EUR [25 000-30 000] to [100 000-110 000]), and Major Accounts (more than EUR [100 000-110 000] per year), excluding the International IKA category as defined in recital (99).
- (163) When providing data on their customers spending, the Parties submitted that while they have no means to monitor sales to customers with 100-200 office workers, they are able to provide data on customers with more than 250 total employees, which could be used as a proxy for the previous office-worker level established in the Commission's precedent.
- (164) Internal documents of the Parties confirm the Commission's previous findings that when supplying large business customers, suppliers need to meet specific requirements, concerning logistics, service, invoicing, and specific e-platforms.¹⁴⁸ Below that threshold, the contract market has less distinctive features and may be subject to competition from other channels. In this regard, the Notifying Party itself acknowledges that from a demand-side perspective, Enterprise customers (that is to say customers with [200-300] or more employees) typically have procurement departments and follow more formal procurement processes (for example, they engage in more in-depth negotiations and there is more involvement from the Parties'

¹⁴⁶ See case M.2286 – *Buhrmann/Samas Office Supplies*, recital 18.

¹⁴⁷ Replies to Phase I Questionnaire Q1 – Questions 16 to 18.

¹⁴⁸ See reply to the Commission's request for information of 20 November, including for example Office Depot's internal document entitled "Tender Information, Request for Quotation(RFQ) – Gating Document –" of 3 June 2014, page 13. See also Staples' internal document entitled "[...] Request For Proposal event" of 31 July 2015.

account managers), as opposed to midmarket customers (that is to say customers with less than [200-300] employees).¹⁴⁹

- (165) Moreover, the Notifying Party indicated in a submission during the Phase II investigation that *“The level of threshold of contract sales is very low and contracts are relatively subjective concept (...). Indeed, negotiated contracts that follow negotiations basically only exist for very large customers with more than [200-300] employees. As such, the hypothetical market for 250+ customers is arguably the best proxy of the hypothetical contract market”*.¹⁵⁰
- (166) Therefore, based on the findings in its precedents, the Parties’ internal segmentation of customers and customers’ specific requirements which can only be met by a subset of suppliers, the Commission considers that there is a separate product market for contracts with customers with more than 100-200 office workers or 250 employees.
- (167) Moreover, according to the results of the market investigation in Phase I and as set out in the Article 6(1)(c) Decision, the Commission initially saw indications that there could be a further sub-segmentation of the market for non-international contracts pertaining to the uppermost part of the market, that is to say very large contracts. Thus, the Commission investigated also whether in addition to a separate market of contracts with customers with more than 250 employees there could be a separate market with customers larger than that, for instance with more than 1 000 employees or with a very large spending per year, including the largest customers who spend more than EUR 1 million per year.
- (168) During the market investigation in Phase II, however, the Commission found that several of those large customers purchase office supplies under international and not national contracts. Furthermore, while the national competitors selling to customers with more than 250 employees confirmed their inability to supply office products to customers spending in more than one country, they did not generally indicate any specific barriers to supplying such very large contracts across the different national markets. Therefore, the Commission’s initial hypothesis concerning the existence of a potential market for very large contracts was not confirmed in the course of the Phase II investigation.

6.1.4.3. Conclusion on the non-international contract market

- (169) Based on the arguments in recitals (160) to (168) and in line with its precedents, the Commission concludes that the market for non-international contracts can be split into (i) the market for non-international contracts with large customers with more than 100-200 office workers or 250 total employees; and (ii) the market for non-international contracts with customers with less than 100-200 office workers or 250 employees.

¹⁴⁹ See "Note on the reduction in the number of key suppliers for stationery", submitted on 23 October 2015, paragraph 7.

¹⁵⁰ Form CO, Annex 26, 'Market shares of full range contract suppliers'.

6.1.5. Conclusion on the product market definition

(170) In the light of the analysis set out in sections 6.1.1 to 6.1.4, the Commission concludes that for the purposes of the product market definition in this case, the following separate product markets can be identified:

- (a) As regards the channels for distribution of office products: (i) contract channel, (ii) direct channel and (iii) wholesale channel constitute separate product markets;
- (b) Within the contract channel, international and non-international contracts constitute separate product markets. The non-international contract market can be further segmented into (i) the market for large business customers with more than 250 employees (or 100-200 office workers) and (ii) the market for business customers with less than 250 employees (or 100-200 office workers);
- (c) As regards the categorisation by product, there is a separate product market for the one-stop-shop supply of traditional office supplies categories. The question whether there exists a further segmentation by individual category of traditional office products can be left open.

6.2. Geographic market definition

6.2.1. International contracts

(171) The Notifying Party contests that there is a separate market for international contracts and has therefore not submitted specific arguments on the geographic scope of that market.

(172) According to the results of the Commission's investigation, multinational customers that purchase under international contracts require supplies at different locations in several EEA countries. The Parties are not themselves active in all European countries but when they supply an international customer in countries where they are not active, they rely on partnerships with third parties.¹⁵¹

(173) The Parties' business model seems to be structured in such a way as to allow for them to have their own direct local presence in countries where international customers have the highest spending or where several international customers have operations.

(174) Table 4 summarises the geographic presence of the Parties in the EEA.¹⁵²

Table 4: The Parties' geographic presence in the EEA

Country	Staples	Office Depot
Austria	Active	Active
Belgium	Active	Active
Bulgaria	Third party distribution	
Croatia		Third Party distribution
Cyprus		

¹⁵¹ Office Depot has partnerships in place in the following countries: Denmark (with Paperlinx Scandinavia), Finland (with Paperipalvelu Koskimo ja Rannali), Norway (with Wittusen & Jensen), Poland (with Ofix) and Croatia (with Gornji Grad). Further, [...]. Staples has partnerships in place in the following countries: Czech Republic (with Activa), Slovakia (with Activa), Bulgaria (with OPlus) and Romania (with Dacris). See Form CO, Annex 27.

¹⁵² Form CO, paragraph 145.

Country	Staples	Office Depot
Czech Republic	Third party distribution	Active
Denmark	Active	Third party distribution
Estonia		
Finland	Staples	Third party distribution
France	Active	Active
Germany	Active	Active
Greece		
Hungary	Active (through Austria)	
Iceland		
Ireland	Active	Active
Italy	Active	Active
Latvia		
Liechtenstein		
Lithuania		
Luxembourg	Active (through BE)	Active (through NL)
Malta		
Netherlands	Active	Active
Norway	Active	Third party distribution
Poland	Active	Third party distribution
Portugal	Active	
Romania	Third party distribution	
Slovakia	Third party distribution	Active
Slovenia	Third party distribution	
Spain	Active	Active
Sweden	Active	Active
United Kingdom	Active	Active

- (175) Similar to the Parties, Lyreco – the Parties' main competitor in international contracts in the EEA – has presence in a large number of EEA countries.¹⁵³
- (176) The Parties submitted information about the country split of their international customers in the EEA.¹⁵⁴ Both Parties generate the highest proportion of their sales from international contracts in the EEA in Germany, the United Kingdom and France. The geographic coverage of their contracts with customers labelled as international is much wider however. [80-90]% of Staples international-labelled customers (IAT) have at least 25% of their EEA spending in two or more countries. [60-70]% of Office Depot international-labelled customers (IKA) have at least 25% of their EEA spending in two or more countries.
- (177) While many international contracts thus involve significant spending in at least the larger western European economies (such as Germany, France, the United Kingdom and Benelux), the EEA countries where international customers purchase under

¹⁵³ See footnote 247 for a list of countries where Lyreco is active.

¹⁵⁴ Form CO, Annex 23.

international contracts varies and is customer specific, as it depends on the locations where they are present. To be competitive in international contracts, suppliers thus need to be able to cover a significant number of EEA countries.

- (178) The purchasing needs of customers across the EEA, as well as the direct and indirect presence of the Parties and of their main competitor Lyreco in most EEA countries, indicate that the market is EEA-wide in scope.
- (179) Nevertheless, several of the Parties' customers buy under international contracts of a dimension wider than the EEA, including mainly purchases in the United States, which may indicate a geographic market wider than the EEA. However, the Commission found that a global dimension of this market seems to be excluded by the qualitative and quantitative findings set out in recitals (180) to (184).
- (180) From a demand-side perspective, within the market investigation, customers with a presence wider than the EEA generally expressed a preference for global contracts.¹⁵⁵ However, they also indicated that sourcing at regional level (for instance separately in the EEA and in North America) is an alternative option to joint sourcing because contracts at regional level are of such a significant size as to allow for the typical benefits of international contracts to be reaped.¹⁵⁶
- (181) A quantitative analysis of the countries included in the Parties' international contracts confirms those findings. As regards Staples, more than [60-70]% of the international-labelled customers (IAT) with spending in the EEA have no spending on office supplies outside of the EEA. As regards Office Depot, while a large majority of its customers with spending in the EEA also have some spending outside of the EEA under international contracts, EEA sales represent approximately [60-70]% of sales to those international customers.¹⁵⁷
- (182) Moreover, even if some EEA customers have also purchased for office supplies outside of the EEA, a large majority of those customers purchase under a European or regional contract as opposed to a global contract. Information from the Parties on their contracts with international customers shows that less than [30-40]% of their international customers have a global contract. Even adopting a conservative approach which excludes customers from which it was not possible to obtain information, the percentage would be below [30-40]% for Office Depot, and below [40-50]% for Staples. In value terms, less than [30-40]% of the value from international contracts at Office Depot and less than [40-50]% of the value from international contracts at Staples is generated from global contracts.¹⁵⁸
- (183) From a supply-side perspective, the observed competitive dynamics are homogeneous at EEA level. Tenders for international contracts covering the EEA where the Parties submit bids typically see also Lyreco, a supplier active at EEA level, as a participant to the tender and often as a successful bidder.

¹⁵⁵ Agreed minutes from a conference call with a customer of 26 November 2015: "*The reason why only invited Staples and Office Depot to this tender is because they are the only suppliers which are able to offer their products on a global basis*".

¹⁵⁶ Agreed minutes from a conference call with a customer of 24 November 2015: "*Although a global contract covering the EU and other regions is theoretically possible, this is not something [customer] is currently seeking. This is because at the moment [customer]'s strategies are driven on a regional basis.*"

¹⁵⁷ See reply to RFI of 13 November 2015, question 1.

¹⁵⁸ See reply to RFI of 20 November 2015.

(184) The Commission thus finds that the market for international contracts has an EEA-wide geographic dimension.

6.2.2. *Non-international contracts with large business customers (250+)*

(185) The Notifying Party submits that the plausible markets it identified, that is to say the distribution of office supplies irrespective of the distribution channel, are national in scope, and 'not narrower than national' for B2B customers.¹⁵⁹

(186) In *Buhrmann/Samas Office Supplies*, the Commission found that the geographic scope of the distribution of office supplies in the Netherlands was national, and thus concluded that the geographic scope of the market for contract stationing for the distribution of office supplies to larger end-users is national in scope.¹⁶⁰

(187) Those findings are broadly confirmed by the results of the Commission's investigation in this Decision.¹⁶¹ Non-international contracts with large business customers are generally entered into at national level; there are different national preferences which result in different product catalogues and assortments across countries,¹⁶² as well as different pricing and rebate systems at the national level in different countries. From a supply-side perspective, only domestic contract stationers bid for contracts within a country, as they have to avail themselves of an existing logistical framework to service such contracts.

(188) As regards the competitive dynamics, the competitors differ from country to country (with the exception of the Parties and Lyreco), and in their monitoring of competition in a given country, as is reported in internal documents,¹⁶³ the Parties themselves compare their position to that of other competitors established in the same country.

(189) Therefore, the Commission finds that the market for non-international contracts with large business customers has a national dimension.

6.2.3. *Non-international contracts with business customers (250-)*

(190) Contracts with business customers employing less than 250 employees fulfil all the criteria as described in section 6.2.2. While some participants indicated an even more local dimension of contracts with smaller business customers, as many customers with less than 250 employees have one or a limited number of locations and do not need deliveries to multiple nationwide offices,¹⁶⁴ the majority of participants in the market investigation confirmed the national dimension of contracts with business customers employing less than 250 employees.¹⁶⁵

(191) Therefore, the Commission finds that the market for non-international contracts with less than 250 employees has at most a national dimension.

¹⁵⁹ Form CO, paragraph 135.

¹⁶⁰ Case M.2286 – Buhrmann / Samas Office Supplies, recitals 49 and 54 – 55.

¹⁶¹ Replies to Phase I Questionnaire Q4 to customers (contract) – Questions 13 to 17.

¹⁶² Agreed minutes of a conference call with a competitor of 22 October 2015: 'Each local market [has] different private label assortment, as some products characteristics or the popularity of brands differ from one local market to another'.

¹⁶³ See for instance Office Depot Internal Document "Office Depot - Competitor Intelligence, European Markets", April 2015.

¹⁶⁴ Agreed minutes of a conference call with a competitor of 9 September 2015.

¹⁶⁵ Replies to Phase I Questionnaire Q4 – Questions 13 to 17.

6.2.4. Wholesale distribution channel

- (192) In Unipapel/Spicers, the Commission found that the wholesale of traditional office supplies was to a large extent national in scope, because the marketing and sale activities are organised on a national basis and each country has particular features when it comes to demand for the traditional office supply products.¹⁶⁶ This was also confirmed for the wholesale of IT products and printing consumables.¹⁶⁷ The Commission ultimately left the geographic market definition open however.
- (193) In this Decision, the results of the market investigation for the Swedish wholesale market – the only wholesale market where the activities of the Parties overlap to a significant extent – indicate that the market is national in scope. The respondents to the market investigation indicated that they do not purchase from wholesalers located outside Sweden and that a wholesale supplier needs a local presence in order to be able to cater to the requirements of the customers.¹⁶⁸
- (194) Therefore, the Commission finds that the market for the wholesale of office supplies in Sweden has a national dimension.

6.2.5. Direct distribution channel

- (195) As indicated in recital (185), the Notifying Party submits that the plausible markets it identified, that is to say the distribution of office supplies irrespective of the distribution channel, are national in scope, and '*not narrower than national*' for B2B customers.¹⁶⁹
- (196) In previous decisions, the Commission assessed the geographic market for the distance selling of office supplies and home-shopping.
- (197) In *Staples/Guilbert*, the Commission found that the distance selling of office supplies may be national in scope, among other things due to language and cultural differences for catalogues, to the close proximity to customer base required for efficient delivery costs and to the fact that the same references are usually available within the national market. The market definition was however left open.¹⁷⁰
- (198) In a case related to home-shopping in a different distribution industry, the Commission confirmed that the market is national, due to language differences and costs and delays associated with placing international orders and the international distribution of individual packages.¹⁷¹
- (199) The results of the market investigation were mixed in this respect. A number of competitors indicated that local presence is necessary in order to sell office supplies through the direct sales channel in a given country, however other competitors pointed to the contrary and indicated that it is possible to supply many locations from a single country.¹⁷² The results of the market investigation also pointed to the existence of companies whose activities encompass more than one country being served from a single location.¹⁷³ The customers participating to the market

¹⁶⁶ Case M.6382 – Unipapel/Spicers, recital 58.

¹⁶⁷ Case M.6382 – Unipapel/Spicers, recitals 60-67.

¹⁶⁸ Replies to Phase I Questionnaire Q7 – Questions 6 and 7.

¹⁶⁹ Form CO, paragraph 135.

¹⁷⁰ Case M.2965 – Staples/Guilbert, recital 15.

¹⁷¹ See case M.5721 – Otto/Primondo Assets, recitals 31 and 32.

¹⁷² Replies to Phase I Questionnaire Q3 – Question 22.

¹⁷³ Replies to Phase I Questionnaire Q3 – Question 23.

investigation also indicated their readiness to purchase office supplies from providers not present in their country.¹⁷⁴

- (200) Amazon, who is one of the largest competitors in the direct channel, does not have a national presence in all of the countries where it delivers its products, but nevertheless offers deliveries to multiple European countries (in a number of countries and cases without additional shipment fees). Therefore both arguments used by the Commission in the *Otto / Primondo Assets* case do not apply in this Decision, as (i) in certain cases there are no additional costs for placing international orders with Amazon and (ii) the linguistic argument is not valid for certain cases, such as Amazon UK servicing customers in Ireland, Amazon DE servicing customers in Austria and Amazon FR servicing customers in Belgium.
- (201) The Commission therefore finds that the market for the direct distribution of office supplies is national or wider. However, for the purposes of this decision, the precise market definition can be left open since the transaction would not lead to a significant impediment to effective competition if only the narrower national markets are considered where the overlap between the Parties' activities is more pronounced.

6.3. Conclusion on the relevant markets

- (202) On the basis of its analysis laid down in sections 6.1 and 6.2, the Commission concludes that the relevant markets to assess in this Decision are:
- (a) The markets for contracts for the distribution of traditional office supplies and for the distribution of stationery (to be assessed in section 7.2), namely:
- The EEA-wide market for international contracts;
 - The national markets for non-international contracts with business customers with more than 100-200 office workers or 250 employees;
 - The national markets for non-international contracts with business customers with less than 100-200 office workers or 250 employees;
- (b) The national markets for the wholesale supply of traditional office supplies (to be assessed in section 7.3);
- (c) The national or wider markets for the direct distribution of office supplies (to be assessed in section 7.4).

7. COMPETITIVE ASSESSMENT

7.1. Legal and analytical framework for the assessment

- (203) Pursuant to Article 2(2) and (3) of the Merger Regulation, the Commission must assess whether a proposed concentration would significantly impede effective competition in the internal market or in a substantial part of it, in particular through the creation or strengthening of a dominant position.
- (204) In accordance with the Horizontal Merger Guidelines¹⁷⁵, in order to evaluate whether mergers between actual or potential competitors on the same relevant market may significantly impede effective competition, the Commission conducts its analysis by

¹⁷⁴ Replies to Phase I Questionnaire Q6 – Question 13.

¹⁷⁵ Commission guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (the "Horizontal Merger Guidelines"), OJ C31, 5.2.2004, p. 5-18.

"compar[ing] the competitive conditions that would result from the notified merger with the conditions that would have prevailed without the merger".

(205) The Horizontal Merger Guidelines distinguish between two main ways in which mergers between actual or potential competitors on the same relevant market may significantly impede effective competition, namely non-coordinated and coordinated effects. The assessment in this Decision will focus exclusively on non-coordinated effects.

(206) The Horizontal Merger Guidelines describe horizontal non-coordinated effects as follows:

"A merger may significantly impede effective competition in a market by removing important competitive constraints on one or more sellers who consequently have increased market power. The most direct effect of the merger will be the loss of competition between the merging firms. For example, if prior to the merger one of the merging firms had raised its price, it would have lost some sales to the other merging firm. The merger removes this particular constraint. Non-merging firms in the same market can also benefit from the reduction of competitive pressure that results from the merger, since the merging firms' price increase may switch some demand to the rival firms, which, in turn, may find it profitable to increase their prices. The reduction in those competitive constraints could lead to significant price increases in the relevant market."

(207) Generally, a merger giving rise to such non-coordinated effects would significantly impede effective competition by creating or strengthening the dominant position of a single firm, one which, typically, would have an appreciably larger market share than the next competitor after the transaction. Nevertheless, mergers that do not lead to the creation or the strengthening the dominant position of a single firm may also give rise to competition concerns. In particular, mergers in oligopolistic markets involving the elimination of important competitive constraints that the Parties previously exerted upon each other with a reduction of competitive pressure on the remaining competitors may, independently of the likelihood of coordination between the members of the oligopoly, also result in a significant impediment to competition.

(208) The Horizontal Merger Guidelines list a number of factors which may influence whether or not significant non-coordinated effects are likely to result from a merger, such as the large market shares of the merging firms, the fact that the merging firms are close competitors, the limited possibilities for customers to switch suppliers, or the fact that the merger would eliminate an important competitive force. That list of factors applies equally regardless of whether a merger would create or strengthen a dominant position, or would otherwise significantly impede effective competition due to non-coordinated effects. Furthermore, not all of those factors need to be present to make significant non-coordinated effects likely and it is not an exhaustive list.

7.2. Competitive assessment of sales made through the contract channel

(209) The activities of the Parties in the contract channel overlap in (i) international contracts with business customers, (ii) non-international contracts with business customers with more than 100-200 office workers or 250 employees and (iii) non-international national contracts with business customers with less than 100-200 office workers or 250 employees.

(210) The Commission's assessment of the distribution of office supplies through the contract channel in this Decision will focus on the markets for international

customers and non-international customers with more than 100-200 office workers or 250 total employees. The evidence available to the Commission shows that the distribution of office supplies through non-international contracts to customers with less than 100-200 office workers or 250 total employees is highly unlikely to be affected by the transaction in any significant way.

- (211) Based on the market investigations, the Commission considers that there are a wide number of competitors able to cater for the needs of smaller contract customers. The majority of competitors replying in the course of the market investigation indicated that they are targeting customers belonging in the range of 0-200 office workers. Fewer competitors indicated their ability to win contracts for and supply customers with 200 and more office workers. This was further confirmed by a qualitative analysis where some competitors indicated that the smaller customers are easier to supply because they usually require less complicated logistics due to one or few locations, they pay less attention to prices per product but appreciate more the customer service, good long-lasting relationship with their local supplier and other aspects offered by small suppliers.¹⁷⁶
- (212) The Notifying Party indicated that depending on the methodology applied, the affected markets in the segment for below 250 employees would be Sweden and the Netherlands. However, the overall data gathered by the Commission during the market investigation points to sufficient competition in the B2B contract segment for the supply of office products to companies with less than 250 employees.
- (213) According to the results of the market investigation a number of competitors are active and competitive in the contract channel for smaller customers in Sweden, including 24 individual distributors belonging to the RKV dealer group, as well as Ocay and Wulff Supplies.¹⁷⁷ In the Netherlands, there are around 450 smaller suppliers belonging to the Quantore purchasing cooperative who supply the needs of small and medium sized customers and compete on the market for smaller customers who do not require a formal tender procedure.¹⁷⁸ Overall, no competition concerns were raised by the participants to the market investigation with regard to the customers below 250 employees.
- (214) Therefore the distribution of office supplies through contracts to customers with less than 100-200 office workers or 250 total employees will not be discussed further in this Decision.
- (215) The remainder of section 7.2 will first discuss three general points applicable to the analysis of the contract markets, namely the calculation of market shares (section 7.2.1), the analysis of margins (section 7.2.1.2) as well as the level of differentiation in the markets (section 7.2.1.3).
- (216) This will be followed by an assessment of the markets for the distribution of office supplies through international contracts (sections 7.2.2 and 7.2.3) and through non-international contracts in Sweden and the Netherlands (sections 7.2.4 to 7.2.7) where competition concerns arise, followed by an analysis of the markets for non-international contracts in Austria, Belgium, France, Germany, Ireland, Italy, Spain and the United Kingdom where no competition concerns arise (sections 7.2.8 to

¹⁷⁶ Agreed minutes with a competitor of 9 September 2015.

¹⁷⁷ Agreed minutes of a phone call with competitors of 9 September 2015, 9 September 2015 and 28 July 2015.

¹⁷⁸ Agreed minutes of a phone call with a competitor of 11 June 2015.

7.2.23). Finally, the Commission will also assess the overlaps which arise in the contract distribution of office supplies due to partnership agreements (section 7.2.24).

- (217) For each of those markets, the Commission left open the question whether the relevant market consists in the contract distribution to large business customers of the three traditional office supplies categories or of each of those product categories separately. The Notifying Party submitted, and the Commission acknowledges, that there exist specialist suppliers only active in the contract distribution of paper or ink & toner, that is to say there are manufacturers and specialised distributors of paper, such as Antalis or Papyrus, and specialised manufacturers and distributors of ink & toner, such as HP, Canon or 123inkt.
- (218) While those specialist suppliers may face limitations in terms of distribution logistics as set out in recital (89), they have specialised knowledge and may offer competitive prices and were therefore considered as viable suppliers in those two individual product categories by a number of customers in the market investigation.¹⁷⁹ Moreover, the specialist suppliers also appear to exert pressure on the Parties' margins in the distribution of paper and ink & toner which are lower than the margins in the distribution of stationery products, as will be set out in section 7.2.1.2. The overall evidence collected by the Commission in the Phase I and Phase II market investigations thus suggests that there are a sufficient number of strong suppliers if the product categories of ink & toner and cut sheet paper are considered separately. It also suggests that the specialist suppliers are able to exert competitive pressure on the Parties for those customers who choose to purchase ink & toner or paper separately from stationery.
- (219) In the event of a separate product market definition according to product category, the presence of those specialist suppliers thus makes it unlikely that the transaction would result in a significant impediment to effective competition on the markets for contract distribution of ink & toner and contract distribution of paper to large business customers, where they are active. Consequently, for each of the markets listed in recital (216), the Commission assessed the two alternative scenarios of a relevant product market encompassing the contract distribution of traditional office supplies to large business customers, and the contract distribution of stationery products to large business customers.

7.2.1. Common issues

7.2.1.1. Calculation of market shares

- (220) In this section the Commission analyses the different submissions of the Notifying Party on market shares. The Commission considers that the market shares provided by the Parties are subject to significant uncertainty and are highly sensitive to the assumptions used. The significant uncertainty on market shares provided is also recognised in the own Notifying Party's submission, mentioning that those approaches are "*subject to significant uncertainties and require a number of assumptions*" (see Annex 21, page 1). This is a consequence of the absence of contemporaneous independent third party estimates of the market size of the contract channel for large national customers and international customers. The Commission has therefore examined alternative ways to assess the Parties' competitive position in its assessment of the contract channel in this section.

¹⁷⁹ Replies to Phase I Questionnaire Q4 – Question 22.

7.2.1.1.1. Market shares at the country level

7.2.1.1.1.1. *The Notifying Party's estimates*

- (221) The Notifying Party argues that the market shares of the merged entity would be small in candidate national markets for B2B contracts overall and in a potential sub-segment of large customers with more than 250 employees (corresponding roughly to 100-200 office workers) in all overlapping countries. This would be the case regardless of whether one considers all office supplies, core office supplies (consisting in stationery, ink & toner, and paper), or stationery, ink & toner and paper separately.
- (222) As the total market size of each candidate market or sub-segment is unknown, the market shares provided by the Parties rely on estimates of the total size of the market that are based on a series of assumptions. The different approaches are described in recitals (223) to (238).
- (223) In the first approach referred to as "top-down" (see Annex 21 of the Form CO), the Notifying Party multiplied an estimate of the number of office workers in both the private and public sector by an estimate of the annual spending on office supplies per office worker. The Commission understands that the annual spending includes all office supplies and is not limited to the spending on traditional office supplies (that is to say stationery, ink & toner, paper). The Notifying Party then calculated the total annual spending on office supplies (that is to say the market size) per country with a distinction between smaller (below 250 employees) and larger (above 250 employees) companies. This information was then used to calculate the Parties' market shares based on their actual sales in a given country.
- (224) In order to estimate the number of office workers per country, the Notifying Party uses Eurostat and OECD statistical data on the total number of employees in each country, coupled with statistical data on the sizes of enterprises, employees in the public sector and the proportion of office workers versus non-office workers. In order to allocate the public employees to large organisation above 250 workers, the Notifying Party assumes that in each country 90% of the public workers are working in organisations with at least 250 employees. In this first approach, the annual spending per office worker is assumed to be EUR 300.
- (225) With this first approach, the combined market share of the Parties for organisations with more than 250 employees would be below 20% in all overlapping countries, except in Sweden with a [30-40]% market share.¹⁸⁰
- (226) The Parties also provide additional market shares by using a EUR 200 and EUR 400 annual spending per office worker to show how sensitive the combined market share is to the applied assumption on annual spending. With EUR 200 annual spending per office worker, the combined market share of the Parties as regards the large organisations would only be above 20% in Sweden ([50-60]%).¹⁸¹ Similarly, with a EUR 400 annual spending per office worker, the combined market share of the Parties would only be above 20% in Sweden for large organisations.¹⁸²

¹⁸⁰ Form CO, Annex 21, Table 5.

¹⁸¹ Form CO, Annex 21, Table 14 and 15.

¹⁸² Form CO, Annex 21, Table 17 and 18.

- (227) The second approach proposed by the Notifying Party uses MPA¹⁸³ data to estimate the total sizes of the market for office supplies. The MPA total figures include both the traditional office supplies (stationery, ink & toner, and paper) and other product categories such as IT equipment and office furniture. The MPA figures include both the retail sales to customers (B2C) as well as sales to corporate customers (B2B sales). The Notifying Party considers that the MPA figures should be reduced by 20% to remove the B2C sales. In other words, the Notifying Party considers that 80% of the MPA figures are relevant to calculate the market size for office supplies for B2B customers. Moreover, since MPA stopped reporting on the office supplies market in 2008, the Parties used the data from 2006 to 2008 with some adjustments based on employment change between 2008 and 2012-2014.¹⁸⁴
- (228) In this second approach, the Parties also calculated those market shares with a distinction between smaller (below 250 office workers) and larger (above 250 office workers) customers. As regards organisations with more than 250 employees, the Parties use their previous estimates of the total number of office workers in large organisations (including private business above 250 employees and including 90% of the public sector employees) and compute its share over the total office workers.¹⁸⁵ The proportion obtained is then applied to the MPA market figures in order to obtain the market size for large organisations with more than 250 employees (see Tables 11 and 12 of Annex 21 of the Form CO).
- (229) As regards the organisations with more than 250 employees, the combined market share of the Parties would be below 20% in all overlapping countries, except in Sweden with a market share of [20-30]%.¹⁸⁶
- (230) The third approach proposed by the Notifying Party estimates directly the market size of each product category from different sources in order to calculate market shares by product category.^{187 188} As discussed in recital (227), each market size is reduced by 20% to remove the B2C sales (in other words, 80% of the figure obtained is assumed to be related to B2B customers). As regards large organisations with more than 250 employees, the market sizes of each product are reduced by the same proportions as used to adjust the MPA data as described in recital (227).
- (231) With this third approach, as regards the overall B2B market, the combined market share of the Parties would be above 20% for Stationery in Sweden (with [60-70]%),¹⁸⁹ above 20% for paper in Ireland ([40-50]%), the Netherlands ([20-30]%), and Sweden ([30-40]%),¹⁹⁰ and slightly above 20% for ink & toner in the Netherlands ([20-30]%).¹⁹¹ As regards the large organisations, the combined market share of the Parties would be above 20% for Stationery in Sweden (with

¹⁸³ MPA International is a research organisation which reports on the office supplies industry (see Form CO, Annex 21, page 13).

¹⁸⁴ Form CO, Annex 21, Table 9.

¹⁸⁵ Form CO, Annex 21, Table 11.

¹⁸⁶ Form CO, Annex 21, Table 12.

¹⁸⁷ Form CO, Annex 29, where the Parties uses this data to argue that the average annual spend per office workers should be in the range of EUR 1 000 to 2 000. Based on his data, the Parties' share exceeds 20% only in Sweden for the organisations with more than 250 employees.

¹⁸⁸ Form CO, Annex 30: description of the different public sources for data on stationery, ink & toner, paper, facilities products, furniture, office technology, and other.

¹⁸⁹ Form CO, Annex 21, Table 20.

¹⁹⁰ Form CO, Annex 21, Table 23.

¹⁹¹ Form CO, Annex 21, Table 26.

[70-80]%),¹⁹² above 20% for paper in Ireland ([30-40]%) and Sweden ([30-40]%),¹⁹³ and below 20% for ink & toner in all overlapping countries.¹⁹⁴

- (232) As regards stationery in particular, in a memo submitted by the Notifying Party on 23 October 2015, "*Memo on the Commission's concerns as regards stationery*", the market share in Sweden is [20-30]% (instead of [60-70]% in Annex 1 of the Form CO) for the overall B2B market and [20-30]% (instead of [70-80]% in Annex 21 of the Form CO) for large organisations. The Notifying Party considers that the market size used for Sweden was understated since it implies a "*far lower*" per-office worker annual spending in office suppliers than the average of the 10 overlapping countries.¹⁹⁵ Assuming that the spending per office worker was the same as the average of the 10 overlapping countries, the market share of the merged entity for stationery in Sweden would decrease to [20-30]% for the overall B2B market and [20-30]% for large organisations (see paragraph 12 and Table 29 of Annex 29 of the Form CO). The Notifying Party makes a similar observation for the market size of paper in Ireland, which seems under-stated based on public data. After correction, the market share of the merged entity for paper in Ireland would decrease from [40-50]% to [20-30]% for the overall B2B market and from [30-40]% to [20-30]% for large organisations (see paragraph 12 and Table 29 of Annex 29 of the Form CO).
- (233) In addition, the Notifying Party provided market shares for the combination of stationery, ink & toner, and paper together. The combined share of the Parties for the B2B market of stationery, ink & toner and paper would be below 20% in all overlapping countries, except for the Netherlands with a market share slightly above 20% ([20-30]%) and Sweden ([30-40]%).¹⁹⁶ As regards the large organisations, the combined share of the Parties would only be above 30% in Sweden ([30-40]%).¹⁹⁷
- (234) In a fourth approach (see Annex 26 of the Form CO), called the bottom-up approach, the Notifying Party estimates the revenues of the main competitors for the full range of traditional categories. The total size of this hypothetical market is given by the sum of the revenue of the rivals concerned. With this approach, the combined market share of the Parties is above 20% in France, Ireland, the Netherlands, Sweden, and the United Kingdom.¹⁹⁸
- (235) Last, in a fifth approach, in Annex 24 of the Form CO, the Notifying Party provides market shares for the contract distribution channel for all categories of office supplies. The total B2B market size is estimated using a EUR 400 and a EUR 1 000 spending per office worker. The Notifying Party mentions that this is a conservative approach since Staples estimates that in countries in which it is active the average spending per office worker across all categories ranged from EUR 1 000 to EUR 2 000 (see paragraph 13 of Annex 24 of the Form CO, see also Table 2 of Annex 29 of the Form CO). The total market size obtained is then reduced to include only contract sales (see Table 1 of Annex 24). This data was then used to calculate the Parties' market shares based on their actual contract sales in a given country.

¹⁹² Form CO, Annex 21, Table 21.

¹⁹³ Form CO, Annex 21, Table 24.

¹⁹⁴ Form CO, Annex 21, Table 27.

¹⁹⁵ See Memo on the Commission's concerns as regards stationery, paragraph 38, and Annex 29 to the Form CO, paragraph 12.

¹⁹⁶ Form CO, Annex 29, Table 4.

¹⁹⁷ Form CO, Annex 29, Table 5.

¹⁹⁸ Form CO, Annex 26, Table 3.

- (236) Using EUR 400 of annual spending per office worker, the combined share of the merged entity for the contract distribution channel for all categories would be below 20% in all overlapping countries, except in the Netherlands with a market share slightly above 20% (a [20-30]% market share) and Sweden with a [30-40]% market share.¹⁹⁹ Using EUR 1 000 of annual spending per office worker, the combined share of the merged entity for the contract distribution channel for all categories would be below 20% in all overlapping countries.²⁰⁰
- (237) The Notifying Party also submit market shares for the traditional categories by assuming using EUR 300 annual spending per office worker (see also paragraph 8 of Annex 29 of the Form CO). In that case, the combined share of the merged entity for the contract channel for the traditional categories would be slightly below 20% in the Netherlands ([10-20]%) and [30-40]% in Sweden.²⁰¹
- (238) In Annex 26 (section V) of the Form CO, the Notifying Party submits additional estimates of the market share for the contract channel. The approach is similar to the one described in recital (235), but with an additional step that excludes the estimated percentage of the contract segment accounted for by specialist suppliers for all categories of office supplies. The Notifying Party only uses EUR 1 000 of annual spending per office worker. In this case, the combined share of the merged entity for the contract channel for the all categories would be slightly below 20% in all overlapping countries, except in Sweden with a [20-30]% market share.²⁰² In addition, the Notifying Party uses EUR 300 of annual spending per office worker to estimate the market size for the traditional product categories (stationery, ink & toner, and paper). Under this scenario, the combined share of the Parties is below 20% in all overlapping countries, except in France ([20-30]%), Netherlands ([20-30]%), and Sweden ([40-50]%).

7.2.1.1.1.2. *The Commission's assessment*

- (239) The Commission considers that, while the different approaches proposed by the Notifying Party are not unreasonable in general, in the context of this Decision, a significant number of assumptions have to be combined to obtain those estimates, each of which is subject to significant uncertainty. Moreover, the accuracy of those assumptions was either impossible to verify for the Commission or was not verified by the results of the market investigation and other evidence (for instance tender data to assess the credibility of alternatives suppliers). The assessment of the different approaches proposed by the Notifying Party is discussed in recitals (240) to (258).
- (240) As regards assessing the first approach, the Commission considers that it relies on at least two critical assumptions (see recitals (223)-(224)):²⁰³
- (a) The estimate of EUR 300 of annual spending per office worker;
 - (b) The assumption that 90% of the public workers work in organisations with at least 250 employees.

¹⁹⁹ Form CO, Annex 24, Table 2.

²⁰⁰ Form CO, Annex 24, Table 5.

²⁰¹ Form CO, Annex 24, Table 7.

²⁰² Form CO, Annex 26, Table 4.

²⁰³ See recitals (223) - (226). As regards the proportion of workforce comprised of office workers, the Notifying Party combined employment data provided by Eurostat and occupational data provided the International Labor Office to determine the proportion of office workers in each country (see Annex 30 of the Form CO, section 3). The Commission considers that the estimated proportion of office worker for each country is reliable since it does not rely on any particular assumption.

- (241) As regards the first assumption, the results of the market investigation indicated a significantly lower annual spending per office worker with an average spending of EUR 188 and a median spending of EUR 119 based on 50 responses²⁰⁴. Due to the importance of the heterogeneity in the annual spending in office supplies (from EUR 50 for the first quartile to EUR 230 for the third quartile, with a minimum spending of EUR 7 and a maximum spending of EUR 1 200), the Commission considers that the median spend is more appropriate since it is less sensitive to outliers than the average spend. Using an annual spending of EUR 119 instead of EUR 300, the combined market shares of the Parties would be multiplied by a factor of almost three.
- (242) As regards the second assumption, when providing the market shares for large organisations with more than 250 employees, the Notifying Party assumes that 90% of the public workers are working in organisations with at least 250 employees. This is based on statements from the Office of National Statistics in the United Kingdom and the Irish 2009 and 2010 National Employment surveys that more than 90% of workers in the public sector are working in large organisations.²⁰⁵
- (243) This is an important assumption since it results in an equivalent or larger estimated employment in large public organisation than in large private organisations.²⁰⁶ In other words, the assumption that 90% of the public workers are working in organisations with at least 250 employees implies that more than half of the employees in large organisations are from the public sector. The Commission was not in a position to verify the validity of this implication.
- (244) The Commission also considers that the lack of detailed data on the size of the different public employers per country (namely how many public employers have more than 250 employees) is an important shortcoming and source of uncertainty. For example, assuming instead that 50% of public workers are working in organisations with more than 250 employees reduces significantly the estimate of the market size, for example from EUR 408 million to EUR 284 million in Belgium (-30%), from EUR 3743 million to EUR 2 767 million in Germany (-26%), from EUR 791 million to EUR 560 million in the Netherlands (-29%), from EUR 424 million to EUR 310 million in Sweden (-27%).
- (245) Moreover, the Commission examined data obtained from the Notifying Party about the 100 largest employers by country. On those lists, in the United Kingdom and Ireland, at most 23 and 33 firms are public entities respectively. This suggests that public sector employees are likely less than half of the workforce in large organisations, which illustrates the uncertainty surrounding the market shares estimates provided by the Notifying Party.²⁰⁷
- (246) In addition, public sector entities account for only [...] of Staples' sales to large organisations (including international customers, large private organisations, and

²⁰⁴ Agreed minutes of calls with customers; replies to Phase I Questionnaire Q4 to customers (contract) – Question 18 and replies to Phase I Questionnaire Q5 to customers (international contracts) – Question 23.

²⁰⁵ Form CO, Annex 30, page 9.

²⁰⁶ Form CO, Annex 21, Table 4.

²⁰⁷ As discussed in recital (243), the assumption that 90% of public workers are working in large organisations implies that in each overlapping country approximately more than 50% of the employees in large organisations are from the public sector.

large public entities),²⁰⁸ which is significantly lower than 50% as implied by the underlying assumptions of the Notifying Party.²⁰⁹ While Staples' distribution of sales within large customers is not necessarily representative of the overall distribution, this casts further doubt on the market shares estimates provided by the Notifying Party.

- (247) Finally, the analysis of employment data from the UK Office for National Statistics also illustrates the uncertainty about the Notifying Party's assumption that 90% of public employees are working in large organisations, and therefore the uncertainty surrounding the market shares estimates provided by the Notifying Party. Table 5 shows the number of public firms per employment size ranges. Assuming that average employment in public organisations below 250 employees is in the middle of the respective size class and using the figure of 9 million employees in the public sector in the UK provided by the Notifying Party,²¹⁰ the resulting share of public employees in large organisations is merely 60%.²¹¹ Furthermore, data on public employment statistics in the UK show that in Q1 2015, total public sector employment was 5.36 million, instead of 9 million used by the Notifying Party.²¹² Using the figure of 5.36 million employees in the public sector in the UK would lead to a proportion of 31% of public employees working in large organisations, instead of the 90% proportion used by the Notifying Party.

Table 5: Number of enterprises/local units by Employment size band, Legal status – UK 2013

Legal status	Employee size class							Total
	0-4	5-9	10-19	20-49	50-99	100-249	250+	
Public Corp. / Nationalised Body	1,165	1,485	1,035	600	245	220	220	4,970
Central Government	5,265	3,680	4,455	6,770	4,390	4,635	2,200	31,395
Local Authority	24,210	8,070	9,785	16,245	8,505	3,700	1,500	72,015

Source: UK Office for National Statistics dataset ID "UKBAE", title: "Enterprise/local units by Employment size band, Legal status and Region".

- (248) As regards the second approach proposed by the Notifying Party (see recitals (227)-(229)), the MPA data used refers to the market situation eight to six years ago and the market has undergone serious changes in the meantime. The Parties submitted that in the recent years, due to digitisation of the workspace there is

²⁰⁸ See Excel file "Retrieval EMG (annex 7)_v4_local.xlsx", provided in the response to the Request For Information dated 02/09/2015. The four categories are: international customers, large private organisations, large public entities, and smaller entities. The analysis of Staples' sales data in 2014 shows that public entities accounts for [...] of the total sales, large private organisations account for [...], international customers accounts for [...], and smaller entities account for [...]. Once the [...] of sales to smaller entities are excluded, public entities represent [...] of the sales to large organisations (including international customers, large private organisations, and large public entities).

²⁰⁹ If the assumption of the Notifying Party that 90% of public workers are working in large organisations were correct, which drives the Parties' estimate according to which more than half of the employees in large organisations are from the public sector, one would expect to see that public entities represent a large proportion of Staples' sales to large private organisations and public entities, around 50%.

²¹⁰ According to the Notifying Party, the total public sector employment in the UK is assumed to be 9,081,332 employees (see Form CO, Annex 21, Table 1).

²¹¹ For example, for size class 5-9 employees this corresponds to assuming 7 employees on average, in size class 15-19 employees it corresponds to assuming 17 employees on average.

²¹² Office for National Statistics - "Public sector employment, Q2 2015" accessible at http://www.ons.gov.uk/ons/dcp171778_416567.pdf.

a strong trend to reduce the use of stationery and increase the use of electronic equipment (for instance PCs and tablets) (see recital (18)). Therefore, the Commission considers that the use of old sets of data might not therefore be accurate to represent the current situation on the European market for office supplies.

- (249) In the second approach, in order to consider only the B2B ("Business to Business") sales, the Notifying Party also reduces by 20% the MPA figures to remove the B2C ("Business to Customers") sales. In other words, the Notifying Party considers that 80% of the MPA figures are related to B2B customers. However, the Commission's investigation focuses on B2B contract sales. Based on Staples' sales data, [...] of sales in Europe are related to contract customers.²¹³ Applying a [...] proportion instead of 80% would multiply by a factor of [...] the combined market share provided by the Notifying Party. The Commission also notes that a [...] proportion is also consistent with Table 1 of Annex 24 of the Form CO, where the proportion of contracts sales for the ten overlapping countries is estimated in the range of 32%-53%, depending on the country considered. While Staples' distribution of sales across the different channels may not be necessarily representative of the overall distribution of sales across the different channels among all industry participants, this casts further doubt on the market shares estimates provided by the Notifying Party.
- (250) The third approach (see recitals (230)-(233)) proposed by the Notifying Party also relies on assumptions subject to a significant uncertainty: (i) a reduction of the market size figures by 20% to remove the B2C sales, and (ii) as regards large organisations, the market size for each product is reduced by the estimated proportion of office workers in large organisations (which relied on the assumption that 90% of public workers are working in large organisations). As discussed in recital (249), the proportion of B2B contract sales in Europe is [...] in Staples' sales data, which implies that the market size should be reduced by [...] instead of 20%. This would increase the combined market share by a factor of [...]. Moreover, as discussed in recitals (243)-(247), the assumption that 90% of public workers are working in large organisation is also subject to uncertainty.
- (251) As regards the fourth approach proposed by the Notifying Party, the Commission considers that the estimates of competitors' sales values provided by the Notifying Party are also subject to uncertainty, where the resulting market shares are sensitive to errors in the estimates, which the Commission considers to be possibly large. In particular, during the market investigation the Commission has collected sales data from some competitors to verify figures provided by the Notifying Party.
- (252) For Germany (see Table 4 of Annex 26 of the Form CO), the Notifying Party has overestimated the sales data for two cooperatives (MGW and Soennecken). The sales of those two cooperatives are significantly below the sales data provided by the Notifying Party. Moreover, as regards Buromix, Kaut Bullinger, and Plate, their turnovers are also significantly overestimated by the Notifying Party. Last, the turnover of Lyreco was also overestimated.
- (253) The Commission also asked several market participants to estimate the revenue of their main competitors in various member States.²¹⁴ A comparison of estimated

²¹³ See Excel file "Retrieval EMG (annex 7)_v4_local.xlsx", provided in the response to the Request For Information dated 02/09/2015. Staples' advantage, which is the division of Staples responsible for contract sales, represents [...] of Staples' sales in 2014 in Europe.

²¹⁴ Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – question 9 asking "To the best of your knowledge, which are the firms offering the full range of traditional office supplies

revenues of competitors by different firms in the market illustrates a large degree of uncertainty in the estimates. Indeed, the resulting estimates show very large variation, with a gap between the highest and lowest estimate for the estimated revenues of the same firm often exceeding 200%. The Commission also compared those estimated sales values of competitors to those provided in the Parties' submission,²¹⁵ and found that the respondents' estimates for the sales value of competitors in various countries differ very significantly from those indicated in the Parties' submission in both directions, with up to nearly fourfold deviations between the estimated sales values of the respondents and the Parties.²¹⁶

- (254) Therefore, the Commission considers that the fourth approach proposed by the Notifying Party to reconstruct market shares relying on estimating competitors' revenues is not sufficiently reliable.
- (255) As regards the fifth approach, the Notifying Party uses an annual spending of EUR 400 per office worker. As discussed in recital (235), this figure was not supported by the results of the market investigation, with a median of annual spending per office worker around EUR 119. Using EUR 119 instead of EUR 400 would multiply the combined market share of the Parties by a factor of almost four. Moreover, using EUR 300 of annual spending for traditional supplies seems even more subject to uncertainty given the results of the market investigation (see recital (241)).
- (256) Finally, in order to assess the importance of the Parties in supplying large contract customers, the Commission collected data from the Parties about their sales of traditional office supplies to the top 100 employers in the ten overlapping countries.
- (257) Table 6 shows that the merged entity would be an important supplier to the largest employers in seven of the 10 overlapping countries for stationery, supplying for example [50-60]% of the top 100 employers in France, [50-60]% in Germany, [60-70]% in the Netherlands, [80-90]% in Sweden, [40-50]% in the UK. The proportion of the top 100 employers supplied by the Parties is lower in Belgium ([20-30]%), Italy ([10-20]%), and Spain ([30-40]%). As regards paper, the Parties supply more than 50% of the top 100 employers in France ([50-60]%), Germany ([50-60]%), Netherlands ([50-60]%), and Sweden ([70-80]%). As regards ink & toner, the Parties supply more than 50% of the top 100 employers also in France ([50-60]%), Germany ([50-60]%), Netherlands ([50-60]%), and Sweden ([70-80]%).

(Stationery, Paper, Ink & Toner) in the EEA and in the other selected countries indicated in the sub-questions? Please also provide estimates for their annual sales of such products and / or their estimated market shares. Please provide country specific information only if your company is active in such country (or countries)".

²¹⁵

Table 2 in the Parties' note on "*Market shares of full range contract suppliers*".

²¹⁶

Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – Questions 9.1-9.4.

Table 6: Number of top 100 employers that are customers with the Parties, by country - 2014

	Stationery			Paper			Toner/ink		
	Customer of...								
	Staples	Office Depot	Either (or both) Parties	Staples	Office Depot	Either (or both) Parties	Staples	Office Depot	Either (or both) of the Parties
AT	[30-40]	[10-20]	[40-50]	[30-40]	[10-20]	[40-50]	[30-40]	[10-20]	[40-50]
BE	[10-20]	[5-10]	[20-30]	[10-20]	[5-10]	[20-30]	[10-20]	[5-10]	[20-30]
FR	[10-20]	[50-60]	[50-60]	[5-10]	[50-60]	[50-60]	[5-10]	[40-50]	[50-60]
DE	[40-50]	[30-40]	[50-60]	[30-40]	[20-30]	[50-60]	[30-40]	[20-30]	[50-60]
IE	[10-20]	[30-40]	[40-50]	[10-20]	[30-40]	[40-50]	[10-20]	[20-30]	[30-40]
IT	[5-10]	[5-10]	[10-20]	[5-10]	[5-10]	[10-20]	[5-10]	[0-5]	[10-20]
NL	[40-50]	[30-40]	[60-70]	[30-40]	[20-30]	[50-60]	[30-40]	[20-30]	[50-60]
ES	[0-5]	[30-40]	[30-40]	[0-5]	[20-30]	[20-30]	[0-5]	[20-30]	[30-40]
SE	[30-40]	[70-80]	[80-90]	[30-40]	[70-80]	[70-80]	[30-40]	[60-70]	[70-80]
UK	[20-30]	[20-30]	[40-50]	[10-20]	[20-30]	[40-50]	[20-30]	[20-30]	[40-50]

Source: data provided by the Parties'. A firm was assumed to be customer with the Parties in 2014 in a particular product category if the annual sales value of the Party to that firm was positive in 2014.

(258) The top 100 customers list for each country includes international customers. As the Parties have a stronger position with international customers than with national customers, those lists are likely to overstate the Parties' market position as regards non-international contracts in some instances. The Commission took this into account when assessing the top 100 customer lists in the respective sections of the competitive assessment. That issue notwithstanding, the analysis of the top 100 customer lists indicates stronger market positions of the Parties than the low combined market shares figures provided by the Notifying Party, casting further doubt on the reliability of those market share estimates.

7.2.1.1.1.3. Conclusion

(259) The Commission concludes that the market shares provided by the Notifying Party are subject to significant uncertainty due to the assumptions used in the different approaches. In particular, based on the market investigation, the Commission could not confirm the estimated combined market shares of the Parties. Moreover, the results of the market investigation indicate that the estimates provided by the Notifying Party are not sufficiently reliable and that they are likely to significantly understate the combined market shares of the Parties.

(260) The Commission considers that the nature of the industry makes it impossible to engage in a complete and reliable market reconstruction due to the large number of individual products included in each product category, the large and disperse customer base and the large number of suppliers which, according to the Notifying Party, make significant sales. Even if all of those firms and customers could be contacted, different recording practices make it difficult to obtain precise estimates for sub-segments such as large customers. In addition, the absence of contemporaneous independent third party estimates of the market size on the contract channel for large national customers is an important obstacle to obtain reliable market shares.

(261) The Commission has therefore examined alternative ways to assess the competitive positions of the Parties and the credibility of alternative suppliers, in particular for large contract B2B customers. The Commission presents its assessment of the bidding data and the qualitative evidence gathered during the market investigation in the framework of the competitive assessment, suggesting that the Parties are close competitors for international contracts and for domestic contracts in Sweden and the Netherlands.

7.2.1.1.2. Market shares at the international level

7.2.1.1.2.1. *The Notifying Party's estimates*

- (262) The Notifying Party also provided market shares for customers who purchased office supplies via contract in multiple EEA countries. The Notifying Party presents four methodologies, mentioning that each of them is subject to a large degree of uncertainty.²¹⁷
- (263) The first approach proposed by the Notifying Party is based on bidding data. The Parties calculate the relative importance of Lyreco and Office Depot in the international tenders lost by Staples and the relative importance of Lyreco and Staples in the international tenders lost by Office Depot (see also section 7.2.2 for the analysis of bidding data). This is used to calculate the relative size of those three suppliers in the hypothetical international customers market, to which an estimate of the importance of other (local/specialist) suppliers from the tender analysis is applied in order to calculate overall market shares. With this approach, the combined share of the Parties is [50-60]% (Staples: [20-30]%; Office Depot: [20-30]%), Lyreco has a [30-40]% market share, and local and specialist suppliers have a market share of 11%.
- (264) The second approach proposed by the Notifying Party is largely based on national market shares discussed above in recitals (239)-(261). From a database of Staples' international customers, the Parties calculate the proportion of customers with centrally managed and with locally managed purchasing— [30-40]% and [70-80]% respectively. First, the Parties assume that all centrally managed customers are served by either Staples, Office Depot or Lyreco and apply their relative importance weights from the international tender analysis to find combined centrally managed market shares. Second, the Parties assume that the Parties' shares for locally managed international customers will reflect the Parties' weighted average national market shares for customers with 250+ employees. The "centrally managed" shares and the "locally managed" shares are then weighted by the respective proportions of customers to arrive at the final market shares for the Parties. This approach does not allow for any competitor's market shares to be estimated. With this approach, the combined market share of the Parties is [20-30]% (Staples: [10-20]%; Office Depot: [10-20]%).
- (265) The third approach proposed by the Notifying Party uses the 2013 international survey. This approach is based on the responses to the following question of the 2013 international survey, which covers Staples and [...] customers: "*Did a single vendor win the tender across all the product categories? If yes, who?*" According to the Notifying Party, the drawback of this methodology is that it is likely to favour Staples and [...], given that the sample of the 2013 international survey covers mainly Staples and [...] customers (as well as some prospective customers).

²¹⁷ See the submission "Competitive Assessment – International Customers", dated 18 May 2015.

Conversely, this is also likely to underestimate Office Depot's market share. With this approach, the combined market share of the Parties is [40-50]% (Staples: [30-40]%; Office Depot: [10-20]%), Lyreco has a market share of [30-40]%, and local and specialists suppliers have a market share of 17%.

- (266) The fourth approach is based on data provided by the Parties to their external economic advisors showing the identity of the main provider(s) of office suppliers for the top 100 European companies. The Parties claim that given those customers' size, it is likely that most of them source office supplies internationally. In order to determine the combined international market share, the number of customers which are served by both Parties separately was added to the number of clients served by both Parties. This, in turn, was divided by the number of customers in the sample. With this approach, the combined market share of the Parties is [30-40]%.

7.2.1.1.2.2. *The Commission's assessment*

- (267) The Commission agrees with the claim of the Notifying Party that the various approaches used to establish market shares are subject to a degree of uncertainty.²¹⁸ This is the case because the office supply industry is characterised by a large and disperse customer base, the absence of contemporaneous independent third party estimates of the market size for international contracts, as well as large ranges of individual products in each product category. However the Commission considers that some of the approaches proposed by the Notifying Party are not as uncertain.
- (268) In particular, the Commission considers that the first approach relying on bidding data is subject to a lower degree of uncertainty. Data on tender values, participants and winners stem from the competitive interactions between the Parties and other firms, and therefore provide useful information on the competitive constraints faced by each of the Parties.²¹⁹ The analysis of bidding data is further discussed in sections 7.2.2 and 7.2.3. Bidding data analysis is particularly useful to assess the competitive strength of the various suppliers when competing against the Parties. The market share calculations based on bidding data (yielding a combined market share of [50-60]% for the Parties) therefore also captures the competitive strengths of the different suppliers. Moreover, contrary to market shares provided on a national basis (see recitals (239)-(261)), that approach does not rely on any assumption on the size of the market which is not possible for the Commission to verify.
- (269) The Parties argue that this first approach would underestimate the importance of local suppliers as national tenders by international customers are excluded, and that this analysis is unlikely to capture fully the use of specialist suppliers. The Commission disagrees with the Parties for the following reasons. First, national contracts are not part of the relevant market, which concerns international contracts. Second, if specialist suppliers were able to win an important number of tenders against Staples or Office Depot, the approach used by the Notifying Party would lead to a high market share for the specialist suppliers. The low market share of specialist suppliers is just the reflection that they did not win a high number of tenders against each of the Parties.

²¹⁸ See the submission "Competitive Assessment – International Customers", dated 18 May 2015, RBB Economics, page 7.

²¹⁹ Such data may involve some subjective elements. While the Parties may not know with certainty the participants and the winner in some tenders, the bidding data provided by the Parties is based on their competitive intelligence and perception on who participated and won in tenders, and therefore still provides useful information on the competitive constraints faced.

- (270) The Commission therefore considers that this first approach is less uncertain than market shares provided at national level.
- (271) As regards the second approach proposed by the Notifying Party, the Commission notes that it relies mainly on market shares provided at national level. In particular, for [70-80]% of the international customers with locally managed purchasing, the Parties have used the Parties' weighted average national market shares for customers with more than 250 employees. As discussed in recitals (239)-(261), the Commission considers those market shares to be subject to an important degree of uncertainty. Therefore, the Commission considers this approach as not being sufficiently reliable.
- (272) As regards the third approach based on the 2013 international survey, the Commission found slightly higher market shares for the Parties, compared to ones provided by the Parties.²²⁰ The Commission finds that the Parties have a combined market share of [50-60]% (Staples: [30-40]%; Office Depot: [10-20]%) and Lyreco has a market share of [30-40]%. Other alternatives, like local suppliers and specialists, have a lower market share of [10-20]% (Bruneau: [0-5]%; Fiducial: [0-5]%; Wulff Supplies: [5-10]%). The Commission notes that it was not possible to carry out a similar analysis with the 2015 international survey since the relevant question was not asked to the respondents.
- (273) The Commission notes that market shares calculated on the basis of the 2013 international survey are very similar to the market shares calculated on the basis of bidding data. Moreover, if local or specialist suppliers were winning a significant number of tenders, one would have expected to see a higher market shares for the category "others", which is not the case. Moreover, contrary to market shares submitted on a national basis, the market shares from the 2013 international survey do not rely on any assumption on the market size. The Commission therefore considers that this third approach is subject to a lower uncertainty than market shares provided at a national level.
- (274) As regards the fourth approach proposed by the Notifying Party, and described at recital (266), the Commission notes that the combined market shares of the Parties is close to [40-50]%.

7.2.1.1.2.3. *Conclusion*

- (275) The Commission concludes that while the market shares provided by the Notifying Party are subject to some uncertainty, the level of uncertainty is lower for the market shares relying on bidding data and on the 2013 international survey compared to market shares provided in relation to the Parties' position on a national level. The Commission also considers the market shares provided under the fourth approach. Overall, the combined market share of the Parties for international contract would be in the range of [40-50]% to [50-60]%.
- (276) The Commission has also examined alternative ways to assess the competitive positions of the Parties and the credibility of alternative suppliers. The Commission presents its assessment of the bidding data and the qualitative evidence gathered during the market investigation within the competitive assessment.

²²⁰ See Annex A.1 of the submission "Competitive Assessment - International Customers", dated 18 May 2015, question 24.

7.2.1.2. Margin analysis

7.2.1.2.1. The views of the Notifying Party

- (277) The Commission received data from the Parties on product margins submitted on 3 September 2015. The submitted data states that in the contract channel margins on stationery (Staples: [...] in Europe, Office Depot: [...] in Europe) are higher than on the other traditional office supply product categories of paper (Staples: [...] in Europe, Office depot: [...]) and ink & toner (Staples: [...] in Europe, Office depot: [...] in Europe) for both Parties. This holds in all EEA countries as well as in the EEA as a whole.
- (278) The Parties argued that data on product margins does not include distribution costs which are variable in nature and therefore affect economically relevant margins. The Parties further argued that distribution costs are a more important cost factor for stationery than for paper and ink & toner. Therefore, ignoring distribution costs in the margin calculation overestimates margins on stationery vis-à-vis those on other product categories.²²¹ However, the Parties consider that due to some variable costs being common to products of all types, it is not possible to attribute distribution costs specifically to a single product category.²²² The Commission followed up with the Parties with multiple information requests to clarify the information on margins and distribution costs.²²³

7.2.1.2.2. The Commission's assessment

- (279) On 12 October 2015 the Commission followed up with questions to the Parties and asked them to provide information about the magnitude of distribution costs, as well as to estimate the avoidable distribution costs if their sales across the three traditional products categories (that is to say stationery, ink & toner, paper) were hypothetically reduced by 5% and 10%, while the sales of other products remained unchanged.
- (280) Based on the responses received, the Commission revised the initial margins calculation by adding estimated distribution costs, and allocated those costs to various product categories by two methods: first, by allocating all costs to product categories proportionately to sales value and second, by allocating distribution costs using the obtained information on avoidable distribution costs by product category.
- (281) Taking distribution costs into account reduced the margins significantly compared to the product margins excluding those costs. However, regardless of the method chosen to allocate distribution costs to various product categories, margins on stationery (Staples: around [...] in Europe, Office Depot: around [...] in Europe) remained significantly higher than those on ink & toner (Staples: around [...] in Europe, Office Depot: around [...] in Europe) as well as paper (Staples: around [...] in Europe, Office Depot: around [...] in Europe).
- (282) In correspondence with the Parties, the Commission learned that in addition to distribution costs, certain revenues were also excluded from the product margins that are of variable nature and should therefore be included in the margins calculation. On 20 and 23 October 2015 the Commission requested further information on

²²¹ See the submission "Staples/Office Depot, Margin Analysis", RBB Economics, dated 10 December 2015, slide 10: "[...]".

²²² Among other occasions this was raised in the meetings with RBB Economics on 8 October 2015, 28 October 2015 and 18 November 2015.

²²³ This included information requests sent on 12, 16, 20 and 23 October 2015 as well as on the 20th of November 2015.

various variable costs and revenues that were not taken into account in the initially submitted product margins. In particular, the Commission found that the underlying data for margin calculations presented earlier exclude variable revenues such as cash discounts, which are relatively large in magnitude. The resulting margins are presented in Table 7 and Table 8. Omitted variable revenues such as cash discounts are also taken into account in the calculation of margins essentially entirely offsets the downward effect of distribution costs. The resulting margins in Table 7 and Table 8 are very close to the product margins when distribution costs were ignored in recitals (277) and (278).

Table 7: Staples 2014 margins in the contract channel including all variable costs/revenues. Distribution costs were allocated to product categories according to avoidable costs, other variable costs and revenues allocated according to the product category's sales share

Staples	EU	AT	BE	DK	FI	FR	DE	IE	IT	NL	PT	ES	SE	UK
Ink & toner	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %
Paper	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %
Stationery	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %

Source: Commission's calculations based on the response to the Request for Information of 20 November 2015.

Table 8: Office Depot 2014 margins in the contract channel including all variable costs/revenues. Distribution costs were allocated to product categories according to avoidable costs, other variable costs and revenues allocated according to the product category's sales share

Office Depot	EU	AT	BE	DK	FI	FR	DE	IE	IT	NL	PT	ES	SE	UK
Ink & toner	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %
Paper	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %
Stationery	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %	[...] %

Source: Commission's calculations based on the response to the Request for Information of 20 November 2015.

7.2.1.2.3. Conclusion

(283) In conclusion, the analysis of data concerning margins suggests that the margins for stationery are relatively higher than margins for other traditional product categories, namely paper and ink & toner. The fact that stationery margins are higher than those for paper and toner/ink holds regardless of whether distribution costs were taken into account or not, and which method the Commission applied to allocate costs and revenues to product categories.²²⁴ Those findings may support the qualitative

²²⁴ The Parties conducted further analysis on margins across various product categories, the results and the underlying data of which has been provided to the Commission in the submission "Staples/Office Depot, Margin Analysis", RBB Economics, dated 10 December 2015. In this submission the Parties argue that [...].

evidence available to the Commission for the competitive assessment, indicating that specialist suppliers may exert some competitive pressure on the Parties' pricing of the product categories also sold by specialists (paper, ink & toner), but significantly less for stationery.

7.2.1.3. Office supplies contract markets as differentiated product markets

7.2.1.3.1. The views of the Notifying Party

- (284) According to the Notifying Party, the factors affecting the customers' choice of supplier mainly include price, service and product range but that none of those factors differentiate the suppliers in the market to any significant extent.
- (285) First, according to the Notifying Party, office supplies are homogeneous, unsophisticated and commoditised products with limited scope for products differentiation, which allows customers to force prices down to competitive levels. The Notifying Party argues that the products are simple and commoditised, making prices on the market very competitive.
- (286) Second, the Notifying Party submits that although certain suppliers are specialised in a particular product, for instance paper or ink & toner, the services provided by those specialist suppliers are the same as the corresponding services provided by other suppliers including the Parties.²²⁵ Furthermore, according to the Notifying Party, the service demanded by customers includes an efficient delivery system and low transaction costs which can be easily outsourced to third parties.
- (287) Third, the Notifying Party contends that most customers do not utilise or require one-stop shopping and hence a wide range of products and that most suppliers offer a wide range of products or can simply adjust the range of products offered to meet the customers' demands.²²⁶
- (288) Finally, the Notifying Party claims that there are a number of competitors in the market which are able to meet all the specific requirements of large contract customers.²²⁷

7.2.1.3.2. The Commission's assessment

- (289) The Commission agrees with the Notifying Party that office supplies as such are rather homogeneous and most suppliers on the market offer a number of similar individual products of the same brands sourced from the same manufacturers or wholesalers.²²⁸
- (290) However, the Horizontal Merger Guidelines set out that products may be differentiated in various ways.²²⁹ In particular, the Commission's assessment in this Decision does not concern the overall market for all B2B sales of office supplies (which according to the Notifying Party is the correct market definition)²³⁰ but focuses on the specific market for distribution of traditional office supplies through contracts to large customers. This particular market presents certain specificities and a differentiation of the suppliers in terms of the product range and services offered as

²²⁵ Form CO, paragraphs 200-201.

²²⁶ Form CO, paragraph 203.

²²⁷ "Note on customer requirements and competitor capabilities", submitted by the Notifying Party on 25 October 2015.

²²⁸ Agreed minutes of a call with a competitor of 28 July 2015.

²²⁹ Horizontal Merger Guidelines, footnote 32.

²³⁰ Form CO, paragraph 154.

well as in terms of the pricing strategies used. Those factors differentiate the suppliers from one another and may make the Parties particularly close competitors of one another in some of the relevant markets. For this reason, contrary to the Notifying Party's claim, it is necessary to assess how closely the Parties and other competitors compete in each of those assessed markets.

- (291) With regard to the product range, in *Buhrmann/Samas Office Supplies* the Commission found that small dealers are at a disadvantage when competing with larger suppliers because "*[s]mall dealers cannot match the large contract stationers in terms of ability to supply a full range of products (such a range can include some 8000 product types) from their own stock*".²³¹ Customers do not only compare individual products offered by different suppliers, which may be the same from supplier to supplier, but they compare the range of products available. A large proportion of customers confirmed the significant value attached to a supplier's wide product range and indicated in the market investigation that one of their main requirements when selecting a supplier is a wide range of products.²³²
- (292) The Parties have the advantage of being able to offer a wide overall range of traditional office supply products which offers customers one-stop-shop sourcing and a wide range of specific private label products which are not offered in the same breadth by some of their competitors.
- (293) One-stop-shop supply based on a wide available range of products is an important factor when selecting a supplier for many customers: "*When a European company buys office supplies, it often thinks that by pooling its purchases together, it will get the best price. This is not always true, however, as specialized suppliers can sometimes offer better prices on individual products. Nevertheless, it is very difficult for large companies to split the contract, and it may eventually not lead to savings as large suppliers can offer better prices across the whole range of products, thus offsetting any better price offered by single-product suppliers on certain products (for instance companies supplying paper)*".²³³
- (294) As regards the private label products, Office Depot offers on average [2000-2500] private label stock keeping units ("SKUs") per country and Staples offers on average [1500-2000] private label SKUs per country.²³⁴ While a number of competitors do not have their own private label products at all, out of the competitors replying to the market investigation who have a private label offer, only one has a comparable range of private label products, three competitors have around 1200-1300 SKUs and the remaining competitors offer below 1000 SKUs.²³⁵ A competitor explained in this context: "*The Parties have their own private label sourced in large part from Asia. This gives them a strong advantage when it comes to prices, which smaller suppliers cannot match, as they have to depend on traditional brands of office supplies.*" Similarly, a customer underlined the importance of private label products: "*[...] has a preference for private label*

²³¹ See Case M.2286 – Buhrman/Samas Office Supplies, recital 33.

²³² Replies to Phase I Questionnaire Q4 to customers (contract) – Question 12.

²³³ Agreed minutes of a phone call with a customer of 29 September 2015.

²³⁴ See reply to the Commission's request for information submitted on 19 October 2015. Office Depot offers between [1000-1500] and [3000-3500] private label SKUs and Staples between [500-1000] and [2500-3000] SKUs, depending on the country.

²³⁵ Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – questions 26.

products as they are equivalent at lesser pricing. [...] It is important that a supplier can offer a range of private label products."²³⁶

- (295) Contrary to the Notifying Party's arguments on the simplicity of expanding the product range,²³⁷ the competitors indicate that in general, it is possible to expand a limited range of products within an already existing product category. Expanding the existing range by a substantial number of items could be very cost intensive, however, as it requires additional warehouse storage, more advanced logistic solutions, marketing activities and additional trainings for sales people. Expanding the product range to new categories requires research, start-up investment and additional personnel and is difficult to carry out.²³⁸ Further details on expansion and entry will be discussed in the assessment of the problematic markets in sections 7.2.2 to 7.2.7 .
- (296) As regards the service levels in the market, the argument of the Notifying Party that the service expected by the customers only includes efficient delivery and low transaction costs was not supported by the results of the market investigation. The customers participating in the market investigation list a very broad list of services they require from their suppliers, including: desktop delivery, stock control and replenishment of office supplies cupboards, unpacking upon delivery, standard and customised reporting, dedicated or designated customer support, regular business reviews/meetings, shipping cost management, a formal return process, technical support, development for customisations of interfacing with the customer's systems, emergency deliveries, Key Account Managers dedicated to the company, a progress plan for the future allowing for cuts in cost, management information and product quality evaluations.²³⁹
- (297) The customers indicate that only the largest distributors present on the market have the necessary tools and scale to provide those specific services: "*Price and quality of the products and services are the main critical factors in selecting a supplier. Furthermore, large customers require the suppliers to be able to offer specific reporting on the consumption broken down by year, product categories and company divisions. They also require delivery of the products to many locations. Only the larger suppliers have the logistics to serve a significant number of locations and the IT capabilities to provide comprehensive statistics on invoices and consumption.*"²⁴⁰
- (298) Some customers explicitly indicate that they do not pay for the product as such, but for the additional tailored services offered by the suppliers. A customer explained: "*Stationery as such is a dying industry, what is important are not the products and prices as such, but the distribution model. The products are secondary, what mainly counts are the logistic capabilities and IT systems of the suppliers.*"²⁴¹
- (299) The results of the market investigation further indicated that there are considerable differences in pricing strategies between the suppliers. One former competitor explained that it had to step out of business as it was impossible to match the pricing

²³⁶ Agreed minutes of a phone call with a customer of 16 October 2015.

²³⁷ See also the Horizontal Merger Guidelines, paragraph 30.

²³⁸ Replies to Phase II questionnaires Q8a-j to customers – Question 23.

²³⁹ Replies to Phase II questionnaires Q8a-j to customers – Question 23.

²⁴⁰ Agreed minutes of a phone call with a customer of 15 July 2015.

²⁴¹ Agreed minutes of a phone call with a customer of 23 November 2015.

strategy of the Parties²⁴². Another one stated: "*it is very difficult / impossible [...] to win the largest public tenders, due to very low prices offered by the Parties*".²⁴³

- (300) Furthermore, the Parties are able to use sophisticated pricing models allowing them to analyse the individual customer's preferences and to tailor their pricing individually across the range of products offered. More specifically, when the customer starts the tender, the customer will provide a list of specific SKUs and ask suppliers to prepare a price for that list of items. That list is known as "the core list", or "the basket". As the Parties review the basket provided by the customer, an opinion is formed about how much of the customer's total purchase potential is represented by the basket. Generally, the pricing and margins on the items in the basket are lower than the pricing and margins on "non-core" items. With the overall goal of winning new customers and achieving a certain level of overall profitability, the supplier can decide how aggressive to be on the price of the core items, based on an assumption of how many non-core purchases will also be made by the customer. The assumption formed about the non-core business potential of a customer is based on market knowledge, past experience with similar customers, and any other knowledge about that specific customer. The results of the market investigation indicated that certain smaller suppliers may be less capable of using such strategies due to inferior market knowledge or inferior risk-taking abilities.
- (301) Against that background of differentiating factors, when requested to list the closest competitor of Staples, 67% of the customers named Office Depot, 22% named Lyreco and 10% named a different supplier.²⁴⁴ Similarly, when requested to list the closest competitor of Office Depot, 60% of the respondents indicated Staples, 24% pointed to Lyreco and 16% named a different supplier.²⁴⁵ The criteria that the customers took into account when assessing the closeness of competition included prices, distribution networks, product range, customer supports and IT tools (especially the IT ordering system which is compatible with the customer's own platform as well as advanced reporting).²⁴⁶ Further details on the closeness of competition and the availability of strong competitors will be discussed in the assessment of the individual markets in sections 7.2.2 to 7.2.24.
- (302) In conclusion, the market for the supply through contracts of at least the traditional office supplies categories is a differentiated market. Determining whether the Parties are close competitors is relevant to the assessment of the transaction, contrary to the Parties' opinion. The Parties compete closely with each other and with Lyreco. The remaining suppliers active on the market may be more distant competitors depending on the national market under consideration. In particular, smaller or more specialised competitors are not able to compete closely with the Parties in terms of product range, services and pricing strategies. The specificities will be discussed in the individual sections 7.2.2 to 7.2.24.

7.2.2. *International contracts - Traditional office supplies*

7.2.2.1. Market structure

- (303) The market for international contracts is characterised by customers with a demand for office supplies in different countries in the EEA. Such customers tender their

²⁴² Agreed minutes of a phone call with a competitor of 11 June 2015.

²⁴³ Agreed minutes of a phone call with a competitor of 9 September 2015.

²⁴⁴ Replies to Phase I Questionnaire Q4 to customers (contract) – Question 29.

²⁴⁵ Replies to Phase I Questionnaire Q4 to customers (contract) – Question 30.

²⁴⁶ Replies to Phase I Questionnaire Q4 to customers (contract) – Questions 29 and 30.

supply needs for some or all of those countries together in order to cover them under a single contract. This generates benefits for international customers, and in particular the benefits stemming from direct savings (due to volume rebates) as well as indirect savings which reduce the total cost of ownership of the supply contract (for instance the need to manage one single contract for supplies in different countries, single invoicing system, and uniform purchasing platform).

- (304) The Parties both sell office supplies under framework contracts which cover deliveries in more than one country in the EEA. Staples' sales under international contracts in the EEA amounted to EUR [...] in 2014, while Office Depot's sales amounted to EUR [...] (joint sales of EUR [...]). The Parties are capable of supplying customers in almost all EEA countries thanks to their wide geographic footprint, which is complemented by partnership agreements and third party distribution in those countries where they are not themselves present, but where the customer may require supplies (see Table 4 above).
- (305) A similar model is run by Lyreco, a French-based contract stationer which has operations in several EEA countries.²⁴⁷ Lyreco is capable of entering into international contracts for the provision of traditional office supplies to large business customers in the EEA.
- (306) As discussed in section 7.2.1.1, the Notifying Party submitted²⁴⁸ market shares based on different approaches. Based on those findings, the Commission concluded²⁴⁹ that market shares based on the 2013 international survey and on bidding data present a lower level of uncertainty than market shares provided for the position of the Parties at national level. Market shares estimate according to those two methodologies are presented in Table 9.

Table 9: Market share data submitted by the Parties according to international tenders data and the 2013 international survey

Company	International tenders	Customer survey
Staples	[20-30]%	[30-40]%
Office Depot	[20-30]%	[10-20]%
Combined	[50-60]%	[40-50]%
Lyreco	[30-40]%	[30-40]%
Local/specialist suppliers	11%	17%

- (307) According to the data in Table 9Table 9: Market share data submitted by the Parties according to international tenders data and the 2013 international survey, the transaction would result in the combination of two of the three main competitors in the market for international contracts for traditional office supplies to large business customers in the EEA. By merging the second leading and third leading suppliers on that market, the transaction would result in the creation of a market leader with

²⁴⁷ Lyreco offers office supplies to business customers in Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Hungary, Ireland, Italy, Luxembourg, Netherlands, Norway, Poland, Portugal, Slovakia, Spain, Sweden and the UK; reply to Phase I Questionnaire Q1 – Question 5.

²⁴⁸ Most of the Parties' arguments are spelled out in a submission made by RBB Economics for the Parties on 18 May 2015, and attached as Annex 22 to the Form CO.

²⁴⁹ See recitals (267) to (276).

market shares near to, or exceeding, [50-60]%, with only one comparable competitor left.

- (308) In the course of the market investigation in Phase II, the Commission gathered data on the revenues of those companies from international contracts for the provision of traditional office supplies. The revenue data confirm the relative position of the Parties and Lyreco. Lyreco is the largest supplier by turnover in the EEA international contracts market, followed by the Parties. In its market investigation, the Commission has not identified any other supplier which has comparable operations or turnover in this market.

7.2.2.2. Competitive constraints faced by the Parties and closeness of competition

7.2.2.2.1. The views of the Notifying Party

- (309) The Notifying Party submits that other suppliers active in the supply of traditional office products, or specialist suppliers, exert a competitive constraint on the Parties. In particular,²⁵⁰ it argues that the Parties face competition not only from Lyreco, but also from national suppliers and specialist suppliers, to whom international customers would also be able to switch following the transaction.

7.2.2.2.2. The Commission's assessment

- (310) The Commission assessed the effective constraints faced by the Parties on the relevant market based on qualitative evidence from the market investigation, on the bidding data submitted by the Parties, and the basis of the surveys submitted by the Parties. The findings resulting from each of those sources, also examining the closeness of competition, will be presented in the present section.
- (311) The likelihood of customers' switching behaviour as regards national contracts has already been assessed for the purposes of the definition of the relevant market. In its competitive assessment of the transaction, however, the Commission also verified whether national suppliers do exert competitive pressure on the Parties within the relevant market by participating in international tenders.
- (312) Similarly, while the possibility of switching between full range contracts and special products contract has been discussed within the definition of the relevant market, the Commission also assessed whether specialist suppliers exert a competitive constraint on the Parties within the relevant market.

7.2.2.2.2.1. *Qualitative evidence from the market investigation*

- (313) On the basis of the market investigation the Commission confirms that the international contract market is very concentrated, as the Parties and Lyreco are the only competitors capable of supplying customers through international contracts, with specialist suppliers and other suppliers having a very limited presence on this market.
- (314) Customers labelled as international by the Parties provided information on bidders in their last tenders for traditional office supplies. Within the replies received to the market investigation, it was possible to identify 45 tenders by international customers where information about bidders and winners was available.²⁵¹

²⁵⁰ Form CO, Annex 22, section 4.

²⁵¹ Replies of international customers to Phase II questionnaires Q8a-j to customers – Question 8.

Table 10: Bidding information by customers on tender participants

Only Lyreco, Staples, Office Depot	29
All three participated	17
Only both Parties	3
One Party and Lyreco	5
Only One Party	3
Only Lyreco	1
At least one other competitor	16

- (315) In almost two-thirds of instances, the Parties and Lyreco were the only participants to tenders by international customers. Only in one-third of cases did a different supplier other than the Parties and Lyreco submit a bid. Those resulted in only four wins or partial wins for other suppliers.
- (316) The bidding information submitted by the Parties is in line with the qualitative feedback from customers regarding the market participants that they consider as viable suppliers for their office supplies need.²⁵² Customers were asked to indicate the actual or potential suppliers that could satisfy a number of criteria relating to their sourcing of traditional office supplies, including portfolio size, ability to supply the full range of products, quality of the products, logistics capability, IT ordering system, account management. For all those criteria, almost 90% of customers indicated the Parties and Lyreco as the only actual or potential suppliers capable of satisfying them.
- (317) Information received from customers is in line with the replies of competitors to the market investigation in Phase II. Among responding competitors,²⁵³ a large majority replied that they only target national contracts, and occasionally contracts for two countries. Only two competitors replied they target also contracts for three or more countries. Among all of those suppliers, only Lyreco offers specific services or account management support to international contract customers that are not typically offered to national customers, in a similar way to the Parties.
- (318) The evidence gathered by the Commission thus confirms that the Parties and Lyreco are the only viable suppliers of traditional office products to large business customers through international contracts in the EEA. The Parties and Lyreco are also seen by market participants as closest competitors with regard to any parameter assessed.

7.2.2.2.2. Analysis of bidding data in tenders with international customers

- (319) The Parties provided tender data for Staples and Office Depot on tenders involving international customers.²⁵⁴ The data on tenders confirm the findings of the Commission during the market investigation, and in particular indicate that in tenders involving international contracts, only the Parties and Lyreco compete with each

²⁵² Replies of international customers to Phase II questionnaires Q8a-j to customers – Question 10.

²⁵³ Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – Questions 28 and 29.

²⁵⁴ See the annexes of the submission "*Competitive Assessment – International Customers*", RBB Economics, dated 18 May 2015.

other effectively. Other suppliers do not exert a significant competitive pressure on the Parties. This is also in line with the analysis submitted by the Notifying Party.²⁵⁵

- (320) As regards the tenders where Staples participates, it loses mainly to Lyreco which accounts for [40-50]% of Staples' losses ([50-60]% in terms of value) and to Office Depot which accounts for [30-40]% of Staples' losses ([40-50]% in terms of value) (see Table 11 below). The Notifying Party acknowledges that '*when Staples loses international tenders, Lyreco is the most frequent winner, followed by office Depot*'. As regards the tenders where Office Depot participates, it loses mainly to Lyreco which accounts for [50-60]% of Office Depot's losses and to Staples which accounts for [40-50]% of Office Depot's losses (see Table 12). This is also recognised by the Notifying Party, which acknowledges that '*Office Depot loses the majority of its international tenders for which the winner is known to Lyreco, followed by Staples. Only a small number of tenders are won by other competitors*'.²⁵⁶
- (321) The findings are the same, regardless of whether one focuses on tenders with known winners only or includes those with unknown winners. In particular, the Parties found that in tenders which Office Depot loses, the winner is Lyreco and Staples in respectively [30-40]% and [20-30]% of cases respectively. The winner is unknown in [30-40]% of tenders. Other firms very rarely win, with "various", Office Max, Wulff, SCA and Office Express emerging as winner in a total of [10-20]% of tenders Office Depot loses (see Table 12).²⁵⁷

Table 11: International tenders lost by Staples

[...]

Source: Table 3 of submission "*Competitive Assessment – International Customers*" dated 18 May 2015, RBB Economics.

Table 12: International tenders lost by Office Depot

[...]

Source: Table 4 of submission "*Competitive Assessment – International Customers*", dated 18 May 2015, RBB Economics.

- (322) The international bidding data of Staples also contained information on the identity of the previous suppliers (or "incumbents"). The Commission therefore assessed from which incumbent Staples won international tenders, and found that in most cases the incumbents were Lyreco and Office Depot.²⁵⁸ In particular, out of

²⁵⁵ See the submission "*Competitive Assessment – International Customers*", RBB Economics, dated 18 May 2015, section 3.2.

²⁵⁶ See "*Competitive Assessment – International Customers*", dated 2015 May 18, RBB Economics, pages 9-10.

²⁵⁷ Looking at values instead of number of tenders leads to similar findings. In terms of value share of tenders lost by Office Depot, Staples and Lyreco captured respectively [20-30]% and [20-30]%. Unknown winners received [40-50]% of the value of tenders Office Depot lost, and a handful of other winners (such as "various", Office Max, Wulff, SCA and Office Express) captured in total less than [5-10]% of the value of tenders lost by Office Depot.

²⁵⁸ Tenders may have multiple winners in different product categories. Furthermore, the same tender may have multiple winners within each product category. Throughout this Decision, in its analysis of tender data the Commission regards tenders with multiple winners in the same product category or across different product categories as distinct observations. These are counted and reported separately. The same applies to the analysis of bidders in tenders. For example, if a single tender had two winners in any product categories, those are reported and referred to as two tenders won. In case a tender had

[...] tenders where Staples won and where the incumbent is known, the incumbent was Lyreco and Office Depot in [...] and [...] tenders respectively. Other suppliers appear significantly behind: the incumbent was "local" in [...] tenders, "Other" appeared as incumbent in [...] tenders, and Fiducial, Gullberg and JM Bruneau were incumbents in [...] each.²⁵⁹ In terms of value, the gap between Office Depot/Lyreco and other suppliers is even more important: the tenders where Office Depot (respectively Lyreco) was the incumbent represent [40-50]% of the value (respectively [30-40]%) of the tenders won by Staples where the incumbent is known, while the tenders where the incumbent is coded as "local" represent only [5-10]% in value.

- (323) The Commission also looked at participants and winners of tenders in which the Parties participated. In the bidding data submitted by Office Depot, which concerns all tenders where Office Depot participated, no firm other than Staples and Lyreco could be identified as a significant participant against Office Depot.²⁶⁰ Among the [...] international tenders where Office Depot participated, Staples participated in [...] and Lyreco in [...] tenders. The next firm is coded as "various", with only [...] participations.^{261 262}
- (324) Looking at winners of international tenders, an analysis of Office Depot's bidding data shows that out of [...] tenders where data on the winner was available, Office Depot, Lyreco and Staples won [...], [...] and [...] tenders respectively.²⁶³ Other winners appear only occasionally, namely "various" ([...] wins), Office Max ([...] wins), Office Express, SCA and Wullf ([...] each).²⁶⁴ In Staples' international bidding data, the winners could be identified in [...] tenders.²⁶⁵ Out of those, Staples won [...] tenders, followed by Lyreco and Office Depot, with [...] and [...] wins respectively. Other winners appear significantly behind, with "other" and "local" winning in respectively [...] and [...] tenders, while Office Discount, Abraham and Errebian/Felian each won in [...] each.
- (325) To conclude, the analysis of the bidding data confirms that the Parties are close competitors and exert a significant competitive pressure on each other for the following reasons: (i) they participate against each other in an important number of international tenders, (ii) Staples loses a significant number of tenders against Office Depot and vice-versa, and (iii) Office Depot was an incumbent in a significant number of tenders won by Staples. Moreover, the analysis of bidding data also suggests that other firms, except Lyreco, do not exert a significant competitive pressure on the Parties in international tenders (due to few participations and few wins). Overall, on the basis of the analysis of the bidding data, the Commission considers that there are three credible and close competitors for international tenders, namely the Parties and Lyreco.

multiple winners in a particular category, the Commission followed RBB Economics in its assumption to split the value won equally among winners.

²⁵⁹ In [...] tenders Staples won, the incumbent was "unknown."

²⁶⁰ The data provided by the Parties on international tenders do not allow for separating tenders by product categories.

²⁶¹ In [...] tenders, the bidder that participated against Office Depot is coded as "unknown".

²⁶² Staples' data on international tenders did not contain usable information on the identity of participants other than winners. Therefore, this analysis cannot be carried out with bidding data provided by Staples.

²⁶³ In the calculations for tenders with multiple winners, the Commission followed RBB's approach and treated these as one win for each winner.

²⁶⁴ The winner was unknown in [...] tenders.

²⁶⁵ The winner is unknown in [...] tenders.

7.2.2.2.3. *Analysis of the survey evidence on participants and shortlisted bidders in international tenders and on price benchmarking*

- (326) The data from the 2013 international survey also contain information on participants and shortlisted bidders in international tenders launched in the last two years. This corresponds to [...] tenders (that is [...] respondents from a sample of [...] respondents in total).²⁶⁶ Among those [...] tenders, Staples, Office Depot and Lyreco are the suppliers that participated the most often, with [...], [...], and [...] participations respectively. The other suppliers appear significantly behind: a combination of local vendors with [...] participations, Fiducial with [...] participations, Wulff Supplies with [...] participations, and specialised ink & toner vendors with [...] participations.²⁶⁷ Those findings suggest that suppliers other than the Parties and Lyreco do not exert a significant competitive pressure in international tenders and that there are essentially three competitors in international tenders, namely the Parties and Lyreco.
- (327) Among the [...] tenders where Staples participated, the other two main participants are Office Depot (with [...] participations) and Lyreco (with [...] participations). Other suppliers appear significantly less frequently: a combination of local vendors with [...] participations, Wulff Supplies with [...] participations, Fiducial and specialised ink & toner vendors with [...] participations, and specialised paper vendor with [...] participations.²⁶⁸ Those findings suggest that the Office Depot is a close competitor to Staples, as is Lyreco, while other suppliers are more distant competitors.²⁶⁹
- (328) Among the [...] tenders where Office Depot participated, the other two main participants are Staples (with [...] participations) and Lyreco (with [...] participations). The other suppliers appear significantly less frequently: a combination of local vendors with [...] participations, Fiducial with [...] participations, specialised ink & toner vendors with [...] participations, and specialised paper vendor with [...] participations.²⁷⁰ Those findings suggest that Staples is a close competitor to Office Depot, in addition to Lyreco, while other suppliers are more distant competitors.
- (329) The 2013 international survey also contains information on shortlisted suppliers in tenders. Staples, Office Depot and Lyreco are the suppliers who are the most often shortlisted: Staples with [...] shortlists, Office Depot with [...] shortlists and Lyreco with [...] shortlists. The other suppliers appear significantly less frequently: a

²⁶⁶ See question 19 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015.

²⁶⁷ See question 23 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015.

²⁶⁸ Commission's calculations based on question 23 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015.

²⁶⁹ This analysis was carried out based on the raw data of the 2013 survey. The Notifying Party provided the raw data on 16/11/2015 (see Excel file "*2013 survey (national and international customer - final raw data in rows.xlsx)*"). However, the raw data was requested on 02/09/2015, but in response only tables of descriptive statistics were provided ("*M.7555 – Annex 2 - 2013 survey (national and international customers) - final raw data.xlsx*", response from the Notifying Party on 03/09/2015). Another Request for Information, dated 02/10/2015 (question 32), was sent to the Notifying Party asking to provide the raw data for the 2013 survey. The Parties replied on 09/10/2015 that "*Nothing in addition to the file submitted on 3 September is available – results were provided in the form of the frequency tables submitted*".

²⁷⁰ Commission's calculations based on question 23 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015.

combination of local vendors with [...] shortlists, Wulff Supplies with [...] shortlists, Fiducial with [...] shortlists.²⁷¹ Those findings confirm that suppliers other than the Parties and Lyreco do not exert a significant competitive pressure in international tenders and that there are essentially three competitors in international tenders, namely the Parties and Lyreco.

- (330) The analysis of the 2013 international survey data also shows that the Parties are often shortlisted against each other in international tenders. Among the [...] tenders where Staples is shortlisted, Office Depot and Lyreco are shortlisted in [...] and [...] tenders respectively, while other suppliers appear significantly behind. Among the [...] tenders where Office Depot is shortlisted, Staples and Lyreco are shortlisted in [...] and [...] tenders respectively, while other suppliers appear significantly less frequently.²⁷² Those findings confirm that the Parties are close competitors.
- (331) The 2013 international survey also contains information on the suppliers included in the price benchmarking done by customers in international tenders.²⁷³ The question on price benchmarking was designed for the respondents that did not launch a tender in the last two years. Therefore it provides additional information on the competitive landscape for international contracts by considering those customers who were not included in the previous analysis of participation data in recitals (327)-(328).
- (332) Among the 56 respondents, 34 indicated that they conducted a price benchmarking exercise in the last couple of years. Staples, Office Depot, and Lyreco were the main firms included in the price benchmarking exercise: Staples was mentioned by [80-90]% of those respondents, Office Depot by [40-50]%, and Lyreco by [70-80]%. In contrast, other suppliers appear significantly behind: a combination of local vendors is mentioned by only [5-10]% of those respondents, Amazon by only [5-10]%, Fiducial by only [5-10]%, specialised paper vendor by only [5-10]%, and specialised ink & toner vendors by only [0-5]%.²⁷⁴
- (333) Those findings confirm that there are essentially three close competitors in international tenders, namely the Parties and Lyreco, and that other competitors appear more distant and less credible.
- (334) The Commission notes that it was not possible to carry out the same analysis of participants, shortlisted bidders and price benchmarking in international tenders using the 2015 international survey [...]. This is because the relevant questions were not included in the survey.

7.2.2.2.2.4. *Analysis of survey evidence on the credibility of the different alternatives*

- (335) The 2013 international survey also contains information on the credibility of the different suppliers. In particular, a list of suppliers was provided to the respondents and the respondents were asked to indicate how likely they would switch to each of this vendor on a scale from 1 (very unlikely) to 5 (very likely).²⁷⁴

²⁷¹ See question 25 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015.

²⁷² Commission's calculations based on question 25 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015.

²⁷³ See question 20 and question 21 of Annex A.1 of the submission "*Competitive Assessment - International Customers*", RBB Economics, dated 18 May 2015. The questions were: "Did you conduct a price benchmarking in the marketplace in the last couple of years?" and "Which of the following companies did you include in your price benchmark?".

²⁷⁴ The scale used is the following: 1 = very unlikely, 2 = unlikely, 3 = neutral, 4 = likely, 5 = very likely. Question 33 of Annex A.1 of the submission "*Competitive Assessment - International Customers*",

- (336) For Staples, Office Depot, and Lyreco, the Commission calculated the proportion of respondents selecting options "4" (likely) or "5" (very likely). This leads to the following proportions: [30-40%] for Office Depot, [30-40%] for Lyreco, and [30-40%] for Staples. In order to assess the credibility of other suppliers in international tenders, the Commission compares the lowest of those three proportions, which is [30-40%], with the corresponding proportions for each of the alternative suppliers. If the proportion for an alternative supplier is close to (respectively distant from) [30-40%], this supplier can be considered as being as credible as (respectively less credible than) the Parties and Lyreco.
- (337) The corresponding proportions for the alternative suppliers are the following:²⁷⁵
- (a) For many suppliers, no or very few respondents answered the question. This concerns for example many national suppliers such as AB Supplies, Alter Buro, Fiducial, Hedera, Kontorab, Lekolar, Nyblogruppen, Papyrus, Procurator, Quantore, RKV, Wulff Suppliers.
 - (b) Other alternatives have proportions which are at least significantly lower than the benchmark of [30-40%]: a combination of local vendors has a proportion of [10-20]%, specialised ink & toner vendor has also a proportion of [10-20]%, specialised paper vendor has a proportion of [20-30]%, Amazon [5-10]%, all online
 - (c) retailers (not Amazon) [10-20]%, Mass market retailer (who sell office supplies) [10-20]%
- (338) The significant gap between the three international suppliers (that is to say Staples, Office Depot and Lyreco) and other alternatives - such as national suppliers, a combination of local vendors, specialist suppliers and Amazon -, suggest that those alternatives are significantly less credible for international tenders.²⁷⁶ The 2013 international survey data thus confirms the above findings on market structure and the closeness of competition in the international contract market.
- (339) The Commission also notes that it was not possible to carry out the same analysis of participants, shortlisted bidders and credible alternatives in international tenders using the 2015 international survey [...]. This is because the relevant questions were not included.

7.2.2.2.3. Conclusion

- (340) On the basis of the feedback from market participants within the market investigation, bidding data from international tenders submitted by the Parties, and the data collected in the framework of the 2013 international survey, the Commission considers that there are only three suppliers active on the traditional office supplies market through international contracts with large business customers, that is to say the Parties and Lyreco. Those three suppliers are the closest competitors to each

dated 18 May 2015: "*For each of the alternatives vendors below, considering all features that important to you, please indicate how likely (on a scale from 1 = very unlikely to 5 = very likely) you would be to switch to this vendor*".

²⁷⁵ See Excel file "M.7555 - Annex 2 - 2013 survey (national and international customers) - final raw data".

²⁷⁶ In the submission "*Staples/Office Depot – economists' meeting*", RBB Economics, slide 13, the Notifying Party essentially argues that the proportions used for benchmarking should also include the respondents that are "neutral" (see footnote (276)). Taking this comment into account (which is equivalent to use the proportion of respondents replying "unlikely" and "very unlikely") leads to similar findings.

other, and account for almost all sales on the relevant market. The remaining suppliers account for fewer participations in the international contracts market, have marginal sales and do not exert a significant constraint on the Parties.

7.2.2.3. Competitive conditions following the transaction

7.2.2.3.1. The views of the Notifying Party

(341) The Notifying Party submits that the merged entity would be constrained by other suppliers and would not have the ability to raise prices. In particular, the Notifying Party submits that customers will have the ability to switch all or part of their requirements of traditional office supplies:

- (a) to national suppliers;²⁷⁷
- (b) to Lyreco;²⁷⁸
- (c) to specialist suppliers.²⁷⁹

(342) The Notifying Party also submits that there would be no significant barriers to expansion of existing suppliers, and that other suppliers, such as Amazon, are about to or could potentially enter the market to supply B2B customers of any size and exert a competitive constraint on the Parties, particularly because of its wide existing online and physical presence in the EEA.²⁸⁰

7.2.2.3.2. The Commission's assessment

7.2.2.3.2.1. *Framework of the analysis*

(343) As regards the likelihood that the transaction would lead to higher prices, economic models of oligopolistic competition predict that in mergers between firms producing differentiated products the merged entity would have an incentive to increase prices after the transaction. This incentive arises from the ability of the merged entity to recapture, through the sales of the merger partner's products, some of the sales that would otherwise be lost as a result of such price increase. This effect is stronger if the transaction brings together close competitors and if the concentration on the market is already high (that is if there will be few remaining rivals).²⁸¹ In practice, the degree of substitutability (or the degree of closeness) between the products of the Parties can be evaluated through the diversion ratio.²⁸² As discussed in the present

²⁷⁷ Form CO, Annex 22, section 4.1.

²⁷⁸ Form CO, Annex 22, section 4.2.

²⁷⁹ Form CO, Annex 22, section 4.3.

²⁸⁰ Form CO, paragraphs 52-60, and 'Note on Amazon' submitted by the Notifying Party on 20 October 2015.

²⁸¹ This conclusion does not hold in the very specific context of so-called Bertrand models which predict perfectly competitive outcomes with prices at marginal cost even with only two firms operating in the market. This outcome depends on rather extreme assumptions, such as the firms being identical, selling homogeneous products at identical marginal cost and facing no capacity constraints. Relaxing any of these extreme assumptions changes the prediction that perfectly competitive prices can arise with just two competitors. Even in markets where prices are set through bidding-like processes, it is only under very specific conditions that significant further concentration through a merger may have limited impact on prices, such as firms having perfect information on the offers made by rivals and on how the customer values these offers (see also footnote 284). This is also mentioned in the Horizontal Merger Guidelines, paragraphs 24-25, paragraph 27, and paragraph 31.

²⁸² The diversion ratio from product A to product B measures the proportion of the sales of product A lost due to a price increase of A that are captured by product B. See Horizontal Merger Guidelines, paragraph 29.

section, this reasoning extends to markets where prices are determined through bilateral negotiations/bidding-like processes.²⁸³

- (344) In tenders, firms typically compete against each other by proposing a bid which is unknown to other firms ("sealed"). Auctions are best characterised as sealed-bid environments where firms are paid according to their bid (if they are ultimately selected as the winner) and when they face uncertainty on the conditions offered by competing bidders, for example on the quality of competing products or the prices at which they are offered, or on how the buyer will evaluate different characteristics of each bid.²⁸⁴
- (345) With uncertainty on what is required to submit a winning bid, each firm will face a trade-off between the probability of winning the tender and the margin earned in the event of winning the tender. A higher bid will reduce the probability of winning the tender but will increase the margin if the bid is successful. This trade-off is equivalent to the standard trade-off between quantity sold and price in an ordinary differentiated goods market, with the difference being that in the case of a tender it is the expected quantity sold (that is to say the probability of winning the auction) rather than actual quantity sold which enters the trade-off.
- (346) The primary difference between the tender environment and an ordinary differentiated product market is that in the former, the diversion of sales between competing firms should be understood in terms of the expected sales (that is to say the probability of winning the tender) rather than actual sales. In a tender environment prior to the merger, if one of the merging firms (Firm A) raised its price, the other merging firm's probability (Firm B) of winning would have increased, in particular if Firm B was a close competitor of Firm A. This induced Firm A to bid more aggressively pre-merger, in order to increase its chances of winning a tender. A merger between firms A and B would remove this direct competitive constraint between the Parties, resulting in both firms bidding less aggressively, for example by submitting higher prices or lower quality offers. This effect is stronger the closer the two Parties are to each other.²⁸⁵

²⁸³ See case M.7278 – General Electric/Alstom (Thermal Power – Renewable Power & Grid Business), recitals 252-263, and Annex 1 for a detailed discussion of the competitive effects for mergers in bidding markets. See also case M.6950 – UPS/TNT Express, Recital 722.

²⁸⁴ See Annex 1 of the decision in case M.7278 – General Electric/Alstom (Thermal Power – Renewable Power & Grid Business) for a detailed discussion on competitive effects in bidding market. The other leading alternative auction process is called a second-price auction. In a procurement procedure, a second-price auction can be approximated by a descending auction, where the price is lowered by rivals until only one competitor remains. In this framework, the price paid by the winner is the lowest price that any other competitor was willing to offer before dropping out of the tender. This auction format provides a good description of how a tender actually operates under fairly strict assumptions, namely that each bidder can fully observe the characteristics and customer valuation of offers made by rival bidders before submitting its own final offer. In that framework, the only determinant of the winning price is indeed the price proposed by the number 2 ranked bidder (that is to say the runner-up bidder). The Parties did not put forward this auction framework. Moreover, the uncertainty in this industry with respect to the identity of competitors as illustrated by the large number of missing information relative to the incumbents, rivals and winners in bidding databases suggests that a sealed bid auction framework is more appropriate (for example, see recital (618), and footnotes 259, 261, 264, 265).

²⁸⁵ In a tender environment, the diversion ratio between Firm A and Firm B is therefore determined by the fraction of the reduction in Firm A's winning probability that is captured by Firm B, and vice versa for the diversion ratio from Firm B to Firm A. A merger between Firm A and Firm B will induce each firm to bid less aggressively, since a higher bid by Firm A will increase the probability of Firm B winning, and thus increase its profits (in proportion to its pre-merger margin). Similarly, less aggressive bidding by Firm B will make it more likely that Firm A will win the tender, and thus increase its profit. The

- (347) The effects of mergers in tenders with imperfect information are likely to affect a relatively broad class of buyers, rather than being targeted on customers for whom the Parties are the two preferred bidders. This follows from the fact that bidding incentives will change for all tenders where the Parties consider that the winning probability of one of the merging firms would be affected by the bid of the other merging firm (and vice versa). This also includes tenders in which the two merging firms are not the two best-placed firms, if firms cannot identify those tenders *ex ante*, and adapt their bidding behaviour only for those tenders.²⁸⁶ In practice, all bids where the Parties would have met absent the merger (which can be proxied by bids where the parties have actually met in the recent past) are apt to be affected by merger effects.
- (348) Similar to ordinary markets with differentiated products, the non-merging firms can also benefit from the reduction of competitive pressure resulting from the merger. In other words, incentives to increase prices are likely to also apply to non-Parties, since the merged entity would be less aggressive in its bidding behaviour. The Commission's Horizontal Merger Guidelines specify that "*mergers in oligopolistic markets involving the elimination of important competitive constraints that the Parties previously exerted upon each other together with a reduction of competitive pressure on the remaining competitors may, even where there is little likelihood of coordination between the members of the oligopoly, also result in a significant impediment to competition*".²⁸⁷ In this case, non-merging firms, in particular Lyreco, can also benefit from the reduction of competitive pressure that results from the merger, since the merged firms' price increase may switch some demand to the rival firms, which in turn may find it profitable to increase their prices.²⁸⁸

7.2.2.3.2.2. *Effects of the transaction*

- (349) Based on the results of the market investigation the Commission finds that Staples, Office Depot, and Lyreco are the main suppliers active on the relevant market for international contracts.
- (350) The Notifying Party's claim that customers could be supplied by national suppliers found no support in the available evidence. While national suppliers are more successful in securing national contracts, they are almost not present on the market for international contracts. Even if they do participate in a few international tenders, they cannot typically satisfy the supply needs of international customers through international contracts. The Parties and Lyreco, different from those other suppliers, can avail themselves of a network of national operations through which they can supply and offer services directly or through partnerships in a wide number of EEA countries. For several customers tendering internationally for several locations, this means that the Parties and Lyreco are effectively the only available choice, as testified by the large number of tenders where only those three suppliers, or even only one or two of them, submit bids for international contracts.
- (351) Also the potential switch to specialist suppliers is not supported by the results of the investigation, nor is it decisive in order to evaluate the effects of the transaction. In particular, very few international tenders were partly allocated to specialist suppliers

incentives to increase prices are thus determined by the level of diversion between the merging firms (evaluated in terms of winning probabilities) and by the level of pre-merger margins.

²⁸⁶ See also Case M.6950 – UPS/TNT Express, recital 722.

²⁸⁷ See Horizontal Merger Guidelines, paragraph 25.

²⁸⁸ See Horizontal Merger Guidelines, paragraph 24.

for the specific category of office supplies they can provide. The existing barriers for specialist suppliers to establish themselves as full range suppliers, including stationery, and which will be further discussed in section 7.2.2.4, exclude them from the range of competitors that could constrain the merged entity after the transaction.

- (352) Therefore, following the transaction, the only alternative to the merged entity in the supply of traditional office supplies to large business customers would be Lyreco, thus reducing the range of potential suppliers from three to two.
- (353) The transaction would thus lead to a reduction in the already limited number of alternatives available to customers. In this specific market, this is also in line with the expectation of customers as regards the minimum number of bidders that would ensure a competitive outcome for the tenders. In the framework of the market investigation in Phase II, most responding customers indicated that three or more bidders is the minimum number normally invited to submit an offer in order to have a sufficient competition.²⁸⁹ It is also of particular significance that, in the context of tenders reported by those respondents, when they obtained bids from more than two companies, in the majority of cases these were bids by Office Depot, Staples and Lyreco. As underlined by one customer, *'There are only three companies than can respond to our need. This merger will reduce this number to two. (...) Prices could increase and the level of service could decrease.'*²⁹⁰
- (354) In this context, the only remaining constraint exerted by Lyreco would not be sufficient to constrain the merged entity's incentive and ability to raise prices after the transaction and avoid a significant impediment to effective competition. The removal of Office Depot would remove a close competitor of Staples. As discussed in recital (348), on top of the difficulty for customers of the Parties to switch because of the absence of a sufficient number of alternative suppliers, the only remaining competitor, Lyreco, may itself become less aggressive in its bidding behaviour as it benefits from the reduction of competitive pressure resulting from the transaction.
- (355) This assessment is in line with the perception of a large number of customers who purchase under international contracts²⁹¹ who indicated that the transaction would impact on the possibility of having a sufficient number of potential bidders and potentially result in price increases. As summarised by one customer: *'The transaction will create one very large player; therefore it will be difficult to have strong competition when running a tender. Currently, the main companies (e.g. Lyreco, Office Depot and Staples) bid against each other allowing customers to reach the best purchasing price, it is questionable what will be the situation after the merger. (...).'*²⁹²

7.2.2.4. Barriers to entry and potential competition

7.2.2.4.1. The views of the Notifying Party

- (356) The Notifying Party submits that the market for the B2B distribution of office supplies is highly contestable irrespective of the exact market definition. In the

²⁸⁹ Replies of international customers to Phase II questionnaires Q8a-j to customers – Question 10.3.

²⁹⁰ Non-confidential reply of one customer to Phase I Questionnaire Q5 – Question 56.1.

²⁹¹ Replies of international customers to Phase II questionnaires Q8a-j to customers – Question 10.4 and 53.1, and replies to Phase I Questionnaire Q5 – Questions 55, 56 and 56.1.

²⁹² Reply of a customer to Phase I Questionnaire Q5 – Question 55.

Notifying Party's view there are no significant barriers between different customer segments, distribution channels or product categories.²⁹³

- (357) The Notifying Party puts forward three main arguments to support its claim regarding the absence of barriers to entry.
- (358) First, it submits that suppliers who do not yet offer contracts can easily do so, such as Amazon who already has penetrated the B2B segment, as this only requires a limited investment in personnel.²⁹⁴ According to the Notifying Party, the term "*contract*" is very misleading. In the view of the Notifying Party, those agreements are essentially framework agreements without any detailed contractual provisions. The main parameter that is covered in those agreements is the price including any discounts. Contracts very rarely include customised offerings or other customer-specific services that cannot be provided by online suppliers. Therefore, the fact that online suppliers do not offer "contracts" does not mean that they cannot, or do not compete against the Parties. Online competitors can easily set up individualised e-catalogues allowing them to customise their offerings for specific customers (and offer volume rebates and other special offers to specific customers).²⁹⁵
- (359) Concerning in particular the ability to serve contracts with large customers, the Notifying Party submits that there are no significant expansion or entry barriers for existing stationery suppliers, such as online suppliers, that would prevent them from becoming even more active in the segment for the largest customers, either through direct sales or contract sales.²⁹⁶ Moreover, the Notifying Party submits that there are no insurmountable barriers that would prevent even a relatively small supplier from serving large customers, as it requires only minimal investments.²⁹⁷
- (360) Second, according to the Notifying Party, specialist suppliers can easily extend their product range into traditional office supplies, as is evidenced by various examples, including for example, Manutan, which has recently expanded its offer from office furniture to stationery, paper, ink & toner and office machines. As regards stationery more particularly, the Notifying Party submits that suppliers which are active in neighbouring markets face low barriers to entry into stationery and can easily add stationery to their existing product portfolio.²⁹⁸
- (361) Third, in the Notifying Party's view, in a market that is characterised by relatively homogeneous products with limited scope for differentiation, a key issue is whether suppliers can easily increase output in response to price increases. It is self-evident that there are no significant constraints that prevent suppliers from increasing their sales swiftly against minimal cost.²⁹⁹ In this regard, the Notifying Party claims that any supplier that already wins a small number of large tenders for the supply of stationery can exert a competitive constraint on large suppliers since they would only

²⁹³ Form CO, paragraph 237.

²⁹⁴ *Ibid.*

²⁹⁵ Note on the reduction in the number of key suppliers for stationery, submitted on 23 October 2015, paragraph 22.

²⁹⁶ Note on the reduction in the number of key suppliers for stationery, submitted on 23 October 2015, paragraphs 14-21.

²⁹⁷ Note on customer requirements and competitor capabilities, submitted on 25 October 2015, paragraph 7.

²⁹⁸ Note on the reduction in the number of key suppliers for stationery", submitted on 23 October 2015, paragraphs 14-21.

²⁹⁹ Form CO, paragraph 238.

need to increase their levels of purchases of office supplies in order to increase output.³⁰⁰

- (362) As regards potential entry, the Notifying Party submits that the Parties clearly view online suppliers such as Amazon as a significant threat, as is evidenced by numerous internal documents. In the Notifying Party's view, the important question for the competitive assessment is whether the Parties' competitive behaviour would be influenced by the threat of such expansion or entry.
- (363) In this regard, the Notifying Party repeatedly mentions Amazon as a supplier capable of posing a significant competitive threat to the traditional office supplies companies.³⁰¹ The Notifying Party submits that "Amazon Business", which was launched in the United States in April 2015, is set to become a viable competitor in the European contract business. According to the Parties, Amazon Business is currently operating in B2B office supplies in the United States and there are no significant barriers to entry in the EEA. The development of Amazon Business from the simpler predecessor system AmazonSupply is seen by the Parties as an initiative to capture the contract business.³⁰²
- (364) The Notifying Party further submits that Amazon has always been very aggressive in expanding into the B2B office supply business and that with its recent launch of Amazon Business it intends to capture business office supplies accounts.³⁰³ According to the Notifying Party, Amazon already targeted large customers with the launch of AmazonSupply in 2012,³⁰⁴ and is currently aggressively expanding to compete for this customer category with "Amazon Business"³⁰⁵. The Notifying Party further supports this argument by referring to a number of job vacancies for Amazon Business positions in the US that Amazon is advertising publicly and some B2B positions in the EEA, in particular in Germany and in France.³⁰⁶
- (365) As regards the contract market particularly, the Notifying Party also claims that Amazon is threatening to disrupt the entire contract business model, by offering customers the possibility to quickly and easily set up free Amazon Business accounts. According to the Notifying Party, this would allow Amazon to put itself in a similar position to a traditional office supplies dealer that has gone through the tendering process and has won a contract with a business customer.³⁰⁷ Moreover, the Notifying Party indicates that there are no barriers to entry that would prevent a supplier like Amazon who do not yet offers contracts to easily do so, since it has already penetrated the B2B segment and expansion into contracts only requires a limited investment in personnel.³⁰⁸

7.2.2.4.2. The Commission's assessment

7.2.2.4.2.1. *Barriers to entry*

- (366) Regarding the argument that entry into the contract market is very easy, the Commission considers on the basis of the market investigation that, contrary to the

³⁰⁰ *Ibid.*

³⁰¹ Form CO, paragraphs 53, 59 and submission on Amazon of 20 October 2015.

³⁰² Form CO, paragraphs 53-60.

³⁰³ Note on Amazon, submitted by the Notifying Party on 20 October 2015, paragraph 16.

³⁰⁴ Note on Amazon, submitted by the Notifying Party on 20 October 2015, paragraphs 18-20.

³⁰⁵ Note on Amazon, submitted by the Notifying Party on 20 October 2015, paragraphs 21-27.

³⁰⁶ Note on Amazon, submitted by the Notifying Party on 20 October 2015, paragraphs 23-27.

³⁰⁷ Note on Amazon, submitted by the Notifying Party on 20 October 2015, paragraphs 46-49.

³⁰⁸ Note on Amazon, submitted by the Notifying Party on 20 October 2015, paragraph 51.

Notifying Party's claims, the tender contract market suffers from high barriers to entry.

- (367) According to a Dutch supplier that tried to (unsuccessfully) enter this market "these barriers are not only related to the size and the capacity needed to serve the customers, but also to endogenous strategies pursued by the incumbents. Moreover, special systems are needed in order to be an effective competitor in the tendering market. Despite the fact that Quantore satisfies the technical features to serve big customers, it does not have the business knowledge and intelligence to bid against the incumbents".³⁰⁹
- (368) Moreover, the Notifying Party attempts to compare the infrastructure and the full-range of services provided by contract stationers such as the Parties and Lyreco with the capabilities that online suppliers may offer (individualised e-catalogues allowing them to customise their offerings for specific customers and to offer volume rebates and other special offers to specific customers). The results of the market investigation allow the Commission to conclude otherwise:³¹⁰ large contract customers need very specific requirements which suppliers that are not active in this channel cannot offer.
- (369) Finally, since any new supplier in the contract market would have to compete with the prices offered by the merged entity, which is one of the most important criteria for customers, new potential entrants to this market would face substantial barriers to entry. According to the results of the market investigation a new supplier cannot easily enter this market, mainly because of a lack of access to products at competitive prices, in conjunction with the low margins that the declining sector of office products has to offer.³¹¹
- (370) Second, as regards the Notifying Party's arguments on the ease of expanding the product range offered, the majority of competitors indicate that in general it is possible to expand a limited range of products within an already existing product category. Expanding the existing range by a substantial number of items could be very cost intensive, however, as it requires additional warehouse storage, more advanced logistic solutions, more marketing activities and additional trainings for sales people. Expanding the product range to new categories requires research, start-up investment and additional personnel and is difficult to carry out.³¹² Based on the results of the market investigation, it seems that smaller or more specialised competitors would not be able to compete with the Parties in terms of the products range.
- (371) More specifically on the international contracts market, as discussed in recital (144) and following, the results of the market investigation indicate that setting up contract distribution operations in a new EEA country or entering into an international business alliance are options that are not available in the short term to national suppliers without incurring significant costs or risks. The investment required would exceed several million EUR and take several years. The specific difficulties for national suppliers to expanding to new countries are related to factors such as local demand, market knowledge, the need to build a local presence and setting up suitable logistic operations.

³⁰⁹ Non-confidential minutes of the conference call with Quantore of 11.06.2015, paragraph 8.

³¹⁰ See recitals (164) and following.

³¹¹ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Questions 58 and 59.

³¹² Replies to Phase I Questionnaire Q1 Questionnaire to Competitors (Contract) – Question 52.

7.2.2.4.2.2. *Potential competition*

- (372) According to the results of the market investigation Amazon Business in the US targets only small and medium-sized businesses. Large businesses use Amazon Business for occasional purchases at most and not for their regular requirements of office supplies, because, as Amazon itself indicated, Amazon Business is not yet able to fulfil large customers' requirements.³¹³ The results of the market investigation confirmed that the vast majority of Amazon Business' customers are individual employees at companies who have created their own Amazon accounts or small business owners that use individual credit cards. In Amazon's own words "purchasing in the Amazon Business marketplace involves an experience similar to purchasing through Amazon retail site".³¹⁴
- (373) Amazon is currently not active in the contract channel and there is no business plan in place to expand into this segment and to participate in tenders in the EEA. Hence, contrary to the Notifying Party's view, Amazon is not in a position to start competing in the near future with the Parties for long-term contracts with customers, either for international contracts or at national level.³¹⁵ Contrary to the Notifying Party's claim that expansion into the contract channel is very easy as it only requires a limited investment in personnel, the results of the market investigation reveal that there are a number of gaps (in terms of requirements and capabilities needed to be active in the contract market) that prevent Amazon (or any other supplier not active already in the contract market) from being able to serve large customers under contract in the near future.
- (374) Finally, as regards the Notifying Party's argument that Amazon's postings for B2B positions in some countries in Europe reveal its clear intentions to compete for the large customers in the EEA, it became apparent during the market investigation that all those postings are for business unrelated to Amazon Business, namely Amazon Web Services and Amazon Payment Europe. As regards the potential entry of Amazon on the international contract market, in light of its geographical spread and its online and physical assets, the results of the market investigation showed that this entry is not planned nor likely in the immediate future. Thus, the Commission finds that Amazon cannot be considered as an immediate constraint on the merged entity's ability and incentive to raise prices.

7.2.2.5. Conclusion on international contracts for the supply of traditional office products to large business customers in the EEA

- (375) The Commission concludes that the transaction would lead to a significant impediment to effective competition on the market for international contracts for the supply of traditional office products to large business customers in the EEA in light of: (i) the elimination of an important competitive force from the market and a close competitor; (ii) the absence of significant alternative suppliers in addition to Lyreco; and (iii) the existence of high barriers for national suppliers to enter the international market.
- (376) In particular, the Commission finds that by reducing the range of credible potential suppliers for international contracts from three to two, the transaction would result in

³¹³ Non-confidential minutes of the call with a competitor.

³¹⁴ Amazon's reply to the Commission's request for information, submitted on 26 November 2015.

³¹⁵ Non-confidential minutes of the call with a competitor; competitor's reply of 26.11.2015 to Commission's request for information.

the removal of an important competitive force from the market and a close competitor. The reduction to two credible bidders for international contracts would be such as to significantly reduce competition for those contracts, providing the merged entity as well as the remaining competitors with the incentive and ability to raise prices in international contracts concluded with large business customers for the supply of traditional office products. This is corroborated by the majority of international customers responding to the market investigation, which indicate a critical reduction of competition and a risk of price increases as a result of the transaction.

7.2.3. *International contracts - Stationery only*

7.2.3.1. The Notifying Party's arguments

- (377) The Notifying Party submits³¹⁶ that there is little scope for differentiation among suppliers of stationery, and that any supplier could thus be deemed as equally close as a competitor to any other supplier. All suppliers offer private label products and this should not be seen as a differentiating factor.
- (378) As regards service, the Notifying Party indicates that other suppliers can provide the same service as the Parties, and have a track-record of winning large tenders involving stationery.
- (379) Finally, the Notifying Party submits that no significant barriers exist to expanding existing stationery supplies because of the lack of product differentiation and capacity constraints. In particular, competitors who are already successful in securing wins on stationery tenders, could also win other large national or even multinational tenders. This would be true not only for existing stationery suppliers, but also for suppliers in neighbouring markets, which could expand into stationery. The Notifying Party provided a list of examples of specialist suppliers or competitors active in neighbouring markets and who expanded into stationery.³¹⁷

7.2.3.2. The Commission's assessment

- (380) The structure of the market for full range supplies of traditional office products through international contracts is not materially different when assessing the market for supply of stationery products only. The Parties and Lyreco are the only suppliers of such products with a wide international reach. Therefore, in principle, the same findings apply as regards the competitive assessment of such a market.
- (381) The transaction would lead to the creation of the market leader in the supply of stationery through international contracts, with only one credible alternative competitor available post-transaction. The loss of a close competitor in such a concentrated market would lead to a significant loss of competition and critically affect the capability of customers to obtain a sufficient number of bids to run competitive tenders for the supply of stationery. Moreover, the removal of such a constraint would also reduce the competitive pressure on the only remaining competitor, Lyreco.
- (382) The Notifying Party could not provide the Commission with a breakdown of data for international tenders by product category. The Commission could thus not analyse the bidding and survey data separately for stationery.

³¹⁶ Form CO and 'Memo on the Commission's concerns as regards stationery' ('Memo on Stationery') submitted on 23 October 2015.

³¹⁷ See Memo on Stationery, paragraphs 31 and following.

- (383) However, other findings from the market investigation support the general findings on the market for traditional office supplies also more specifically as regards stationery. If a limited competitive pressure may exist on certain product categories (particularly ink & toner and paper) because of the possibility of obtaining those supplies from specialists, such a possibility does not exist for stationery, so that the competition concerns could only be aggravated for this specific product category. These findings are corroborated by the analysis of the margin data provided by the Parties, as further described in section 7.2.1.2.
- (384) The Parties and Lyreco are the only suppliers of stationery with a strong international presence enabling them to offer stationery through international contracts in the EEA. The scale of their operations in the EEA is such that the stock of products, including private label products that those companies can provide across the EEA is not matched by any competitor. Contrary to what the Notifying Party argues, it is not the abstract capability of stocking and offering private label products but the very wide numbers of products offered as well as the capability of doing so in several countries that is crucial for the assessment of the closeness of competition. The Parties and Lyreco can thus be regarded as close competitors even when considering the supply of stationery products alone.
- (385) The Notifying Party's suggestion that suppliers active at national level and that won large contracts for stationery could be able to supply also customers through international contracts cannot be confirmed on the basis of the market investigation. The same consideration on geographical presence and market knowledge which have been detailed for full range contracts for traditional office supplies³¹⁸ apply also in this respect.
- (386) An additional finding concerns the effective possibility of companies active in neighbouring market, as well as specialist suppliers, to expand to stationery. When responding to the market investigation, such companies stressed the difficulties of expanding their business to stationery. This is mainly due to the different focus of their activity, and to the fact that the delivery of paper and provision of MPS services require different logistics arrangements than stationery distribution.³¹⁹ As regards suppliers active in neighbouring markets, while some of them may have some stationery sales, they indicated that those are add-ons to orders for other items on which they specialise, and that they would not be capable to service large and complex stationery contracts, particularly at the international level. This is also the case for companies specifically indicated by the Parties as examples of entry into the stationery market. Some of them clarified that they purchase some stationery products from the Parties to complement their offer to customers.³²⁰

³¹⁸ See recital (366) and following.

³¹⁹ See for instance agreed minutes of a conference call with a specialist supplier, 21 October 2015: '*The supply of other traditional office products such as stationery is a mature market which requires big scale and significant investment (...) Logistics is generally a barrier to expansion for this market. (...) In order to compete with the Parties, a company should be able to sell and deliver small quantities of product, and have efficient logistic arrangements in place to achieve this at a low cost. Setting this up can be very difficult*'. Replies to Phase II Questionnaire Q10 – Questions 15 to 15.2.

³²⁰ See agreed minutes of a conference call with a competitor, 5 November 2015, '[competitor] does not see itself to be a competitor of Staples and Office Depot. [it] sells some of the products they offer, but it channels sales in a different way. (...) Staples and Office Depot could be considered [competitor name]'s partners, as [competitor] buys and sells some of their products. (...) If the customers only need office supplies they would generally go directly to Staples and Office Depot.

7.2.3.3. Conclusion on international contracts - Stationery only

(387) In light of the arguments set out in recitals (380) to (386) and also for the reasons set out in recitals (375) and (376), the Commission concludes that the transaction would lead to a significant impediment to effective competition on the market for international contracts for the supply of stationery to large business customers in the EEA.

7.2.4. Sweden - Traditional office supplies

7.2.4.1. Market structure

7.2.4.1.1. The views of the Notifying Party

(388) According to the Notifying Party, a number of suppliers of office products are present in the Swedish market, providing supplies to large corporate customers. Those include Lyreco Sweden, Nyblomgruppen, Ocaj, Papyrus, Procurator, RKV, Tingstad Papper and Wulff Supplies.³²¹ In addition, the Parties allege that MPS providers exert intense competitive pressure on the Parties in Sweden. Finally, in relation to large contracts for public sector institutions, the Notifying Party makes reference to the strict regulation to which tendering is subject; this, according to the Notifying Party prevents the discrimination of tender participants based on smaller size and geographical coverage, providing this way even smaller local suppliers rivals with extensive scope for competing in the market.³²²

(389) In the Response to the 6(1)(c) Decision, the Notifying Party alleges that specialist suppliers such as Atea are frequently outperforming the Parties in the individual categories of ink & toner and paper.³²³ Furthermore, the Notifying Party infers from the bidding data that smaller suppliers such as Ocaj, UTEC, Papyrus, Antalis, Konotrsspecial, Kontorab (members of RKV) and Wulff have won tenders with values above EUR 100 000 lost by the Parties.³²⁴ Finally, the Notifying Party states that half of Staples' and Office Depot's largest customers are neutral or positive about the transaction.³²⁵ The Notifying Party in its note on customer requirements and competitor capabilities,³²⁶ restated that Ocaj, RKV, Nyblomgruppen, Wulff and Procurator all have the capabilities required to supply large customers.³²⁷

7.2.4.1.2. The Commission's assessment

(390) The Commission conducted an extensive market investigation in Sweden, both in Phase I and Phase II. According to the results of the market investigation, some of the suppliers named by the Parties as competitors are in fact not active in the market for contract sales of office supplies to customers of more than 100-200 office workers or 250 employees.

7.2.4.1.2.1. Suppliers identified by the Parties which are not active in the relevant market

(391) Some of the suppliers mentioned by the Parties are not contract stationers offering at least the traditional office supplies categories (stationery, paper, ink & toner). Some

³²¹ Form CO, paragraph 283; Response to the 6(1)(c) Decision, paragraph 26.

³²² Form CO, paragraph 283.

³²³ Response to the 6(1)(c) Decision, paragraph 25.

³²⁴ Response to the 6(1)(c) Decision, paragraph 26.

³²⁵ Response to the 6(1)(c) Decision, paragraph 27.

³²⁶ Note on customer requirements and competitor capabilities, submitted by the Notifying Party on 25 October 2015.

³²⁷ Note on customer requirements and competitor capabilities, submitted by the Notifying Party on 25 October 2015, table 12 and paragraph 58.

others which qualify as contract stationers for the provision of traditional office supplies are not in a position to serve large customers of more than 100-200 office workers or 250 employees. In some instances both circumstances concur.

- (392) More precisely, Procurator is a company mainly dedicated to industrial supplies, offering work clothing, and work protective equipment, cleaning and hygiene products, catering and packaging products. In supplying traditional office supplies to large size corporate contract customers, Procurator appears constrained because of lack of sufficient assortment.³²⁸ Its sales of stationery are marginal.³²⁹ Procurator admits that larger business customers (with more than 100-200 office workers) in the contract business have special requirements, in that they require significant rebates, a broader range of office supplies, as well as significant effort in running tenders.³³⁰ For this reason, unlike the Parties, Procurator targets only small to medium size customers, from those with less than 50 office workers, to those with up to 100-200 office workers.³³¹ Furthermore, Procurator does not sell customised office products (own-brand).³³² On that basis, the Commission takes the view that Procurator is not active in the market for contract sales of office supplies to customers with more than 100-200 office workers.
- (393) ATEA Sverige AB sells “printer-supplies and IT-accessories”³³³. Although ATEA Sverige AB states that it targets all sizes of business customers, (from those with less than 50 office workers to those with more than 1000 office workers),³³⁴ and all types of business customers (from those with a local – smaller than national – presence, to those with a multinational presence), ATEA Sverige AB does not supply stationery,³³⁵ and does not intend to do so in the near future.³³⁶ More specifically, ATEA Sverige AB focuses “on Printer-supplies, Printer-hardware, Scanning and Printer-accessories, [n]ot traditional office products such as paper, pens and stationery”.³³⁷ ATEA Sverige AB does not sell customised office products (own-brand). On that basis, the Commission takes the view that ATEA Sverige AB is not active in the market for contract sales of traditional office supplies to customers with more than 100-200 office workers.
- (394) Papyrus does not supply stationery or ink & toner,³³⁸ but rather focuses on “Office and Graphical paper”.³³⁹ Papyrus supplies some smaller suppliers, such as RKV with paper.³⁴⁰ On that basis, the Commission takes the view that Papyrus is not active in the market for contract sales of office supplies to customers with more than 100-200 office workers.

³²⁸ Replies to Phase II Questionnaire Q9 – Questionnaire to Competitors (Contract Stationers) – Question 15.

³²⁹ Replies to Phase II Questionnaire Q9 – Questionnaire to Competitors (Contract Stationers) – Question 2.

³³⁰ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 19.1.

³³¹ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 17.

³³² Replies to Phase II Questionnaire Q9 – Questionnaire to Competitors (Contract Stationers) – Question 26.

³³³ Replies to Phase II Questionnaire Q10 – Questionnaire to Specialists – Question 2.1.

³³⁴ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 17.

³³⁵ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 2 ; replies to Questionnaire Q10 – Questionnaire to Specialists – Question 2.

³³⁶ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 51.

³³⁷ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 52.1.

³³⁸ Replies to Phase II Questionnaire Q10 – Questionnaire to Specialists – Question 2.

³³⁹ Replies to Phase II Questionnaire Q10 – Questionnaire to Specialists – Question 3.

³⁴⁰ Replies to Phase II Questionnaire Q10 – Questionnaire to Specialists – Questions 16.1 and 16.2.

- (395) Antalis is a paper and packaging supplier. It distributes paper products, including printing paper to printing companies (60% of activities) and office paper (accounting for approximately 20% of its business). Antalis appreciates that the main problem that all paper suppliers (including Antalis) encounter is associated with selling only one product category, namely paper, and not more product categories within the range of office supplies. According to Antalis, customers are more likely to place an order with Office Depot than with an ordinary paper supplier, as Office Depot can offer special services, such as cupboard delivery, floor delivery, and desktop delivery. This is one of the competitive disadvantages for Antalis when competing with the large suppliers of office products. In addition, large suppliers selling more product categories of office supplies, often sacrifice margins in paper in order to win customers. On that basis, the Commission takes the view that Antalis is not active in the market for contract sales of office supplies to customers with more than 100-200 office workers.³⁴¹
- (396) Tingstad Papper AB does not consider itself a competitor of either Staples or Office Depot. Tingstad Papper AB supplies restaurants with napkins, food packaging, paper cups and plastic cutlery, and shops with plastic and paper bags. Tingstad Papper AB also supplies its customers with a limited range of office supplies (approximately 1000 stock keeping units ("SKUs") to be able to serve as a one-stop-shop. Those products are included in the cash and carry part of the business, and Tingstad Papper AB does not have any customers who only purchase office products. Furthermore, Tingstad Papper AB does not participate in any tenders in the office supplies sector, and office products represent only 2.7% of its annual turnover. The company has no plans to expand its business in relation to office supplies. Finally, Tingstad Papper AB does not conclude any contracts for office supplies.³⁴² On that basis, the Commission takes the view that Tingstad Papper AB is not active in the market for contract sales of office supplies to customers with more than 100-200 office workers.
- (397) Other suppliers mentioned by the Parties but not offering a full range of products including at least the three categories of traditional office supplies are UTEC, Dustin, Ricoh, Despec Despec/Büngers, InkClub and Isolda.

7.2.4.1.2.2. Suppliers identified by the Parties which are active in the relevant market but have limited capacity to supply large customers

- (398) Nyblomgruppen is a contract stationer active in the B2B distribution of traditional office supplies through contracts in Sweden. Although it might occasionally participate in tenders for contracts with customers with more than 250 employees, the results of the market investigation indicate that either they are not known or not perceived as suitable suppliers by the larger customers.³⁴³
- (399) RKV is a dealer group operating in Sweden. The organisation consists of 25 members that are small and medium sized independent suppliers, often family owned. The main role of RKV is to negotiate purchasing agreements with suppliers based on the combined volume and purchasing power of RKV as a group. RKV's members operate in the market with their own names, each of them organising warehousing, transportation and logistics independently. RKV's members are not able to participate in large private tenders, because they are not able to service such

³⁴¹ Agreed minutes of a phone call with a specialist supplier, 21 October 2015.

³⁴² Email exchange with Tingstad Papper of 3 September 2015; minutes of a conference call with Tingstad Papper AB.

³⁴³ Replies to Questionnaire Q9 – Questionnaire to Competitors (Contract Stationers) – Question 9.2.

large accounts.³⁴⁴ RKV members, including Kontorsspecial and Kontorab are therefore mostly focused on small business customers,³⁴⁵ with a local (smaller than national) presence³⁴⁶ (90% of its members' contracts are local – smaller than national – in scope)³⁴⁷, of 50-100 office workers,³⁴⁸ without having separate business divisions dealing with customers of different sizes.³⁴⁹ The reason for this in the words of RKV is that “[their] members are local, family owned businesses with a strong focus on the local customers”.³⁵⁰ Neither RKV nor its individual members can therefore be considered as credible competitors in the relevant market.

7.2.4.1.2.3. *Competitive Landscape*

- (400) On the basis of the market investigations the Commission is able to confirm that apart from the Parties, only Lyreco, Ocaj and Wulff Supplies offer the full range of traditional office supplies (stationery, paper, ink & toner) in Sweden in the market for non-international contracts with customers with more than 250 employees.³⁵¹ However Ocaj and Wulff Supplies are much smaller suppliers than the Parties and Lyreco.
- (401) Ocaj states that its competitive advantage is an overall flexible customer service, resulting in proximity to customers and decentralised business acumen. Those qualities are targeted at small and medium customers, rather than large corporations. Ocaj's capability of supplying traditional office supplies to large-size corporate contract customers appears constrained.³⁵² In addition, Ocaj states that the pricing of the Parties is very aggressive and sometimes Staples, for instance, is able to offer prices 30-40 % cheaper than Ocaj. Therefore Ocaj is a distant competitor to the Parties. This is also confirmed by the analysis of the bidding data in section 7.2.4.2.
- (402) Wulff Supplies is a Swedish company with a product portfolio including at least the three traditional office supplies categories. However, its focus is on small and medium-sized customers and only rarely manages to win larger tenders because it cannot compete on prices with the Parties.³⁵³ Wulff targets small and medium as well as large-size corporate customers. However, it has only a handful of contracts with large customers. Purchasing prices is a key constraint for Wulff Supplies in order to be able to serve large-size customers.³⁵⁴
- (403) Based on data submitted by the Notifying Party, Staples' sales under non-international contracts in Sweden amounted to approximately EUR [...] in 2014 while Office Depot's sales amounted to approximately EUR [...]. For large

³⁴⁴ Agreed minutes of a phone call with a competitor, 9 September 2015.

³⁴⁵ Agreed minutes of a phone call with a competitor, 28 July 2015.

³⁴⁶ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 20.

³⁴⁷ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 27.

³⁴⁸ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 17.

³⁴⁹ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 18.

³⁵⁰ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Question 20.1.

³⁵¹ Replies to Phase II Questionnaire Q9 – Questionnaire to Competitors (Contract Stationers) – Question 9.2 (Ahsell named also Kontorab, however, in paragraph (399) the Commission took the view that RKV, as well as its members individually (including Kontorsspecial and Kontorab) are not active in the market for contract sales of office supplies to customers of more than 100-200 office workers or 250 employees).

³⁵² Replies to Questionnaire Q9 – Questionnaire to Competitors (Contract Stationers) – Question 15.

³⁵³ Agreed minutes of a phone call with a competitor, 28 July 2015.

³⁵⁴ Agreed minutes of a phone call with a competitor, 11 December 2015.

customers, Staples' sales of traditional office supplies in 2014 amounted to approximately EUR [...] and Office Depot's sales in 2014 amounted to EUR [...].³⁵⁵

Table 13: Parties' sales of traditional office supplies through contracts in Sweden, EUR 000s

Category	Party	All customers	Large customers
<i>Traditional office supplies</i>	<i>Staples</i>	[...]	[...]
Stationery	Staples	[...]	[...]
Ink & toner	Staples	[...]	[...]
Paper	Staples	[...]	[...]
<i>Traditional office supplies</i>	<i>Office Depot</i>	[...]	[...]
Stationery	Office Depot	[...]	[...]
Ink & toner	Office Depot	[...]	[...]
Paper	Office Depot	[...]	[...]

Source: Parties' replies of 22 December 2015 and 7 January 2016 to requests for information on contract sales data.

- (404) Staples is currently the leading supplier followed by Lyreco, Office Depot is the third supplier and Ocaj comes fourth with approximately half the sales of Staples. Wulff Supplies less than half of Ocaj's sales and it is the fifth supplier, although very small.
- (405) The transaction would combine the leading and third leading suppliers in terms of revenues. It would reinforce Staples' current position as market leader. In particular, the merged entity would be more than three times larger than each of Lyreco and Ocaj in terms of sales of traditional office products through contracts. Lyreco and in particular Ocaj and Wulff Supplies will be lagging far behind with significantly lower turnover.
- (406) A similar picture arises when considering the number of the top largest employers in Sweden (both public and private) to whom the Parties and their competitors supply to. Following an assessment of how many of those top 100 employers are purely national entities and therefore only have non-international contracts in place for office supplies (in order not to overestimate the Parties market power for non-international contracts in Sweden), the Commission concludes that 65 of those entities are purely national customers.³⁵⁶ Out of those 65 entities, [70-80]% currently have contracts in place with Office Depot and [20-30]% with Staples.³⁵⁷ Lyreco,

³⁵⁵ See the Parties' replies of 22 December 2015 and 7 January 2016 to requests for information on contract sales data.

³⁵⁶ The Commission assessed how many of the top 100 largest employers in Sweden currently have international contracts in place with the three suppliers that are currently able to offer international contracts: Staples, Office Depot and Lyreco. The source of this information is the document provided by the Notifying Party as Annex 23 to the Form CO and the information provided by Lyreco in its reply of 29.10.2015 to the Commission's request for information on the top 100 customers.

³⁵⁷ Top 100 companies in terms of numbers of employees.

which is the second supplier in terms of revenues, has contracts with only [10-20]% of the top 65 purely national employers in Sweden, some of which overlap with the Parties. Ocaj serves only [...] out of the top 65 national employers in Sweden, some of which overlap with those supplied by the Parties. In terms of the value of the contracts that those suppliers have with the customers from the top employers list, Staples is the clear leader, followed by Office Depot.

- (407) Furthermore, according to Office Depot's bidding data analysis on national tenders for office supplies³⁵⁸, in the tenders lost by Office Depot, the main winners were Staples and Lyreco, and to a lesser extent Ocaj. Data from Staples on tenders to which it participates show a similar pattern, especially when restricting attention to the largest customers. The vast majority of tenders in which Staples participated were won by the Parties, as well as Lyreco. Ocaj and Wulff Supplies won on a handful of occasions, tenders of a smaller total value than the Parties.

7.2.4.1.3. Conclusion

- (408) On the basis of the above, the Commission considers that only Staples, Office Depot, Lyreco, Ocaj and Wulff Supplies are active competitors in the Swedish market for distribution of office supplies to customers of more than 100-200 office workers or 250 employees. The transaction would reinforce Staples' leading position, increase the distance between the leading and the second leading suppliers and would reduce the market to two large suppliers, the Parties and Lyreco, with another two of them, Ocaj and Wulff Supplies lagging far behind.

7.2.4.2. Competitive constraints exerted by the Parties on each other

7.2.4.2.1. The views of the Notifying Party

- (409) According to the Notifying Party, office supplies are highly commoditised products with limited scope for product differentiation, both Parties selling often the same products. The Notifying Party claims that the limited scope for product differentiation allows customers to force prices down to competitive levels even with only a limited number of suppliers in the market.³⁵⁹ The Notifying Party further claims that since products are relatively homogeneous, the closeness of competition is of less importance.³⁶⁰
- (410) Furthermore, the Notifying Party claims that according to an analysis of the Parties' bidding data in Sweden, assessing which suppliers win the tenders they lose, the strength of the competitors is demonstrated, and therefore all rivals need to be taken into account when assessing the competitive constraints that the Parties face.³⁶¹

7.2.4.2.2. The Commission's assessment

- (411) As explained in section 7.2.1.3, although the products sold by the Parties are generally homogeneous products, the contract market is a market differentiated in terms of customer service and scope of the product range Staples, Office Depot and Lyreco are close competitors. Ocaj and Wulf are more distant competitors.

³⁵⁸ Annexes to the submission by RBB Economics, "Relevance of bidding data for the competitive assessment", dated 18 May 2015. For the review, for Staples the Commission used raw data submitted by the Parties on 28 September 2015 ("RE: M.7555 – STAPLES/OFFICE DEPOT - RFI concerning RBB papers "Relevance of bidding data" and "Competitive assessment-International customers") including updates and additional information compared to the RBB Bidding data analysis.

³⁵⁹ Form CO, paragraph 366.

³⁶⁰ Form CO, paragraph 368.

³⁶¹ Form CO, paragraph 370.

- (412) This is clearly reflected in Staples' internal documents of the Parties. A few examples are described below:
- (a) Staples monitors core and non-core/tail prices of Office Depot and Lyreco. More specifically, Staples has price comparison on [...] items on Office Depot and [...] items on Lyreco. Staples calculates [...], and concludes that Staples is very competitive vis-à-vis Office Depot and Lyreco.³⁶²
 - (b) In a presentation setting forth Staples' pricing strategy for the period 2013-2017, Staples Advantage, Lyreco and Office Depot are [...] together in the Swedish pricing landscape, the rest of suppliers being far away. In the same presentation, Staples sets out the base prices today, and in the future. In relation to base prices today, and more specifically as far as the Advantage channel (Contracts) is concerned, Staples characterises its business as [...], comparing to Lyreco and Office Depot only.³⁶³ The latter slide entitled "Staples Sweden - Pricing" features in various presentations of Staples.³⁶⁴
 - (c) In an email exchange initiated by the Tender Manager for Staples Sweden and Denmark, Staples is shaping its tender strategy in relation to four large tenders that [...]. The email discusses the approach that Office Depot and Lyreco are likely to adopt: [...].³⁶⁵ This suggests that, according to Staples, there are no other competitors able to win those tenders in the Swedish market and that Ocaj is a less close competitor to the Parties than Lyreco.³⁶⁶
 - (d) In a presentation for a Staples management meeting, entitled Staples Sweden/Denmark and dated 18 March 2014, Staples discusses its pricing and (product) extended range. Among other action points, Staples specifically refers to price comparison between Staples on the one hand and Office Depot and Lyreco on the other hand. The presentation reads: [...].³⁶⁷
- (413) On the basis of the results of the market investigation, the Commission considers that the Parties are close competitors. All eight customers that responded to the market

³⁶² Staples internal document entitled "VB: Core & Non-Core/Tail Prices Sweden vs Competition", 24 March 2015.

³⁶³ Staples internal document entitled "Staples Sweden Pricing strategy 2013-2017", page 2.

³⁶⁴ See for instance Staples internal document entitled "Staples Sweden/Denmark, [...], Visit Boras/Sweden", 23 October [2012], page 13; Staples internal document entitled "Transformation of Staples, [...]", 30 September 2013, page 11; Staples internal documents entitled "Transformation of Staples, [...]", 15 August [2013].

³⁶⁵ Staples internal document entitled "VB: Stockholm Office+Paper and Borås+4 Facility - Tender approval - [...] if you agree", 15 November 2014. Staples also refers to OneMed, however in the email exchange it is implied that OneMed sources office supplies from Lyreco.

³⁶⁶ Additionally, in a weekly report of Staples Sweden Advantage (Contract channel) prepared by [...] for [...] on 18 November 2013, Staples underlines the fact that Lyreco and Office Max (Office Depot) won a very large customer that Staples lost. The report reads: [...] (Staples internal document entitled "Staples Sweden Advantage, To: Weekly report - [...]" 18 November 2013). Also, in an email exchange between [...] and [...] discussing Staples Enterprise Q1 review, [...] wishes to obtain open prices from Office Depot and Lyreco, in order to compare Staples' position against theirs. The email reads: [...] (Staples internal document entitled "VB: Bi-weekly - Background to our call of today", 7 May 2014). Also, a [...] presentation for Staples Sweden, Staples Denmark, Staples Norway and Staples Finland, addressed to [...], Staples advertises that only two competitors exist in the Nordic market for office supplies, namely Lyreco and Office Depot. The [...] presentation reads: [...] (Staples internal document entitled "[...]" 12 September 2014).

³⁶⁷ Staples internal document entitled "Staples Sweden/Denmark, Ledningsmöte", 18 March 2014. The presentation originally reads in the Swedish language: [...].

investigation indicated Office Depot as Staples' closest competitor. The majority of customers also referred to Office Depot's as Staples' closest competitor.

- (414) The analysis of the bidding data submitted by the Parties on national tenders for office supplies in Sweden³⁶⁸ confirms that Staples, Office Depot and Lyreco are close competitors. Ocaj and Wulff Supplies are active competitors, but exert a weak competitive pressure on the Parties. This view also emerges from the results presented in the Parties submission on bidding data for Sweden.³⁶⁹
- (415) The Commission assessed Staples' tenders focusing on Enterprise customers. That assessment omitted tenders where the customer was classified by Staples as midmarket (namely small customers) or international (IAT).
- (416) Staples' tender data showed that taking all traditional product categories together,³⁷⁰ Office Depot is the major bidder in tenders where Staples participates, followed closely by Lyreco, as well as Ocaj and bidders classified as local and unknown. In Staples tenders for enterprise customers [...] bids were identified across the three traditional office supplies product categories. Out of those, Office Depot and Lyreco essentially participated along Staples in [...] tenders. Ocaj and local bidders submitted [...] and [...] bids respectively. Other firms have only little participation in those tenders, for example: Antalis ([...] participations), Atea ([...] participations), Kabucco ([...]), Kontorab ([...] participations), Kontorspecial ([...] participations), Papyrus ([...] participations), Wulff ([...] participations), Xerox ([...] participations).
- (417) Among the tenders lost by Staples involving enterprise customers, Office Depot and Lyreco are the main winners. Office Depot is the winner in [30-40]% of those tenders, corresponding to [20-30]% in value. Lyreco won in [20-30]% of those tenders, corresponding to [30-40]% in value. Although Ocaj frequently bids along with the Parties for enterprise customers in Sweden, its share of tenders won among those that are lost by Staples in all traditional office supply categories is merely [5-10]%, corresponding to only [0-5]% of value. Specialist suppliers Atea and Xerox won only occasionally large tenders with total estimated value of above EUR 1 million. Moreover, those tenders involved sales in a single product category only: Xerox won tenders for enterprise customers in paper only, while Atea won [...] large tenders for enterprise customers in the category ink & toner. Onemed won [...] tender covering all traditional office supply categories, but [...] involved a single and rather special customer providing care and health care services, where Onemed appears to be well positioned with its focus on health services that the Parties do not have.
- (418) The Commission also received tender data from Office Depot for national customers in Sweden. This data however does not allow to clearly distinguish different product categories in tenders. In particular, over [...] tenders only [...] tenders seem to have involved sales in the three traditional product categories ([...] tenders with two

³⁶⁸ Annexes to the submission by RBB Economics, "Relevance of bidding data for the competitive assessment", dated 18 May 2015. In its assessment, the Commission used for Staples the raw data submitted by the Parties on 28 September 2015 ("RE: M.7555 – STAPLES/OFFICE DEPOT - RFI concerning RBB papers "Relevance of bidding data" and "Competitive assessment-International customers") including updates and additional information compared to the bidding data analysis included in the submission "Competitive assessment-International customers".

³⁶⁹ See "Relevance of bidding data for the competitive assessment", dated 18 May 2015, RBB Economics, section 4.7.

³⁷⁰ This involves summing up bids submitted in the categories of stationery, ink & toner and paper. See footnote 258.

product categories, [...] tenders with three product categories). Staples participates in [...] of those tenders, Lyreco and Ocaj in respectively [...] and [...]. Other suppliers essentially do not appear, with only Lekolar and RKV participating in [...].

- (419) Office Depot's tender data contain information mainly on stationery products. The analysis of Office Depot's bidding data for stationery tenders shows that Staples and Lyreco constitute the main competitive constraint on Office Depot, and that Ocaj is a more distant competitor exerting a significantly lower competitive pressure on Office Depot than Staples and Lyreco (see section 7.2.5.2 for further details).
- (420) To conclude, those findings suggest that that Office Depot and Lyreco are the main competitive constraints on Staples in Sweden in tenders involving large national customers. Ocaj is another competitor, but it seems more distant, exerting a significantly lower competitive pressure on Staples than Office Depot and Lyreco. As regards Office Depot's tender data for the traditional office supplies, while the small sample size limits the analysis, it is worth noting that only the Parties, Lyreco, and Ocaj participate in those tenders.

7.2.4.2.3. Conclusion

- (421) On that basis, the Commission concludes that the Parties are close competitors in the market for distribution of office supplies to customers of more than 100-200 office workers or 250 employees in Sweden, and therefore the proposed merger would lead to a significant loss of competition.

7.2.4.3. Competitive conditions following the transaction

7.2.4.3.1. The views of the Notifying Party

- (422) The Notifying Party claims that the transaction will not give rise to competition concerns in Sweden, mainly for two reasons. First, the Notifying Party claims that in Sweden the merged entity will continue to face a range of strong competitors, such as Lyreco Sweden, Nyblomgruppen, Ocaj, Papyrus, Procurator, RKV, Tingstad Papper and Wulff Supplies, as well as from providers of MPS, computer supplies, medical supplies and paper (including Dustin, Atea, Ricoh, Despec/Büngers, InkClub and Isoldaare competing with vendors including HP, Canon, Sharp, and Lexmark).³⁷¹
- (423) Second, according to the Notifying Party, given that products and services provided by the various firms active in the market are highly comparable, customers can switch to alternative suppliers and can threaten to switch all or part of their requirements to negotiate competitive terms.
- (424) According to the Notifying Party, customers are able to secure competitive outcomes by splitting their requirements between different distributors, or threatening to do so. Splitting requirements among different suppliers is a very common sourcing pattern in the Swedish market. The Notifying Party further submits that out of its 25 largest customers in Sweden, only [one-five] rely exclusively on Staples, and all others multisource their office supplies requirements from both general and specialist suppliers.³⁷²

³⁷¹ Form CO, paragraphs 286-287.

³⁷² Form CO, paragraphs 288-289.

(425) Finally, the Notifying Party referred to recent examples of both significant (geographical) entry and expansion including several suppliers who have expanded their product offering.³⁷³

7.2.4.3.2. The Commission's assessment

7.2.4.3.2.1. *Structure of the market following the transaction*

(426) In light of the market structure analysis conducted during the market investigation, and presented in section 7.2.4.1, only Staples, Office Depot, Lyreco, Ocasey, and Wulff Supplies are active competitors in the Swedish market for distribution of office supplies to customers of more than 100-200 office workers or 250 employees.

(427) Contrary to the Notifying Party's argument that the merged entity would continue to face strong competition from specialist suppliers after the transaction (see recital (422) above), the results of the market investigation provide indications leading the Commission to consider that specialists exert a limited competitive constraint on providers of the full range of traditional office supplies, and usually they do not participate in tenders.³⁷⁴

7.2.4.3.2.2. *Likely reaction of actual competitors following the transaction*

(428) The transaction would thus lead to a reduction of the already limited number of alternatives available to customers in Sweden. The remaining main constraint exerted by Lyreco is likely to be insufficient to constrain the merged entity's incentive and ability to raise prices after the transaction and avoid a significant impediment to effective competition. The removal of Office Depot would remove a close competitor to Staples. As discussed in recital (348), in addition to the difficulty for the Parties' customers to switch because of the absence of a sufficient number of alternative suppliers, the main remaining competitor, Lyreco, may itself become less aggressive in its bidding behaviour, as it benefits from the reduction of competitive pressure resulting from the merger. A similar reasoning may apply to the incentives of Ocasey or Wulff Supplies to compete aggressively after the transaction although they are already significantly more distant competitors to the Parties than Lyreco.

(429) Furthermore, the smaller competitors may find it difficult to compete with the merged entity. Pre-transaction, on the basis of the qualitative and quantitative evidence set out above, the Commission considers that Staples/Office Depot/Lyreco on the one hand and other smaller suppliers (like Ocasey and Wulff Supplies) on the other hand are not close competitors. Ocasey is targeting small and medium customers rather than large corporations and its capability to supply traditional office supplies to large-size corporate contract customers appears constrained.³⁷⁵ Ocasey is significantly smaller than each of the Parties, representing, pre-merger, approximately half the sales of Staples, and Wulff Supplies representing less than half of Ocasey's sales.³⁷⁶ Ocasey also achieves relatively low win rates pre-merger against each of the Parties, suggesting that Ocasey faced significant impediments to be successful in tenders where the Parties participate, for example because it may not be able to meet the tender's requirements or suffer from a perceived lack of product or

³⁷³ Form CO, paragraph 285.

³⁷⁴ See agreed minutes of a phone call with a competitor, 28 July 2015, paragraph 10.

³⁷⁵ See recital (401).

³⁷⁶ See recital (404).

commercial fit.^{377 378} Those findings are in line with the important price difference of around 30-40% between Ocay's and the Parties' products.³⁷⁹ Therefore, the Commission considers that, post-merger, smaller suppliers like Ocay and Wulff Supplies would likely remain a weak competitive constraint to the merged entity.

- (430) This lack of competitiveness of smaller suppliers is also confirmed by Ocay and Wulff Supplies themselves.^{380 381} That finding is also supported by RKV – which does not compete in the Swedish market for distribution of office supplies to customers of more than 250 employees. According to RKV, the purchasing power that Staples has, mainly because of its large and diverse customer portfolio, enables Staples to adopt sophisticated commercial strategies, taking risks that smaller suppliers cannot afford to take, given that office supplies contracts are non-exclusive.³⁸²
- (431) That purported gap in competitiveness in winning contracts with customers of more than 250 employees in Sweden, as expressed by the national competitors and summarised in recitals (429) and (430), has been confirmed by the Commission's analysis of the turnover data, top 100 customers and tender data set out in recitals (404)-(405), (406) and (414)-(420) respectively. The smaller competitors are much less successful in winning contracts with customers of more than 250 employees. That evidence, coupled with the evidence on their disadvantages in terms of commercial strategies, suggests that the remaining competition exerted by the smaller Swedish suppliers would be unlikely to offset the loss in competition arising from the transaction.

7.2.4.3.2.3. *Likely reaction of potential competitors following the transaction*

- (432) At first sight, entry in the market of traditional office supplies to large business customers through (framework) contracts appears easy. As the Notifying Party claims, low product differentiation, low-cost switching for customers, and low sunk cost, could in theory accommodate new market entry. However, since a new supplier would have to compete with the merged entity on price, one of the most important criteria for customers, new entrants to the market of office products to large business customers through (framework) contracts will face substantial barriers to entry.
- (433) According to Procurator, a new supplier could not easily enter that market, mainly because of lack of access to products at competitive prices in conjunction with the low margins that the declining sector of office products has to offer. For those reasons Procurator does not expect any market entry in the next two to three years.³⁸³
- (434) In addition, Lyreco sees capital expenditure and workforce with expertise on large customers business as blocking factors.

³⁷⁷ Ocay achieves a relatively low win rates against Staples pre-merger (see recital (417)), suggesting that Ocay has a lower probability than Office Depot to be successful against Staples.

³⁷⁸ Ocay also achieves a relatively low win rates against Office Depot pre-merger (see recitals (418) and (450)), suggesting that Ocay has a lower probability than Staples to be successful against Office Depot.

³⁷⁹ See recital (401)

³⁸⁰ See agreed minutes of a phone call with a competitor, 9 September 2015, paragraph 11.

³⁸¹ See agreed minutes of a phone call with a competitor, 28 July 2015, paragraph 11.

³⁸² See agreed minutes of a phone call with a competitor, 28 July 2015, paragraph 10.

³⁸³ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Questions 58 and 59.

- (435) Finally, none of the Swedish respondents to the market investigation expects any new market entry into the supply of office products to large business customers through (framework) contracts in the next two to three years.³⁸⁴
- (436) In addition, customers are not aware of any new supplier that entered the office supplies market in Sweden during the last five years. Six out of eight customers answered in the negative, and the remaining two did not provide any new supplier or commented on whether such supplier constitutes a viable supply option for their office supplies requirements.³⁸⁵
- (437) On the basis of recitals (432) to (437), potential competitors would find it fairly difficult to enter the market, and are unlikely to pose a competitive constraint to the merged entity after the transaction.

7.2.4.3.2.4. *Likely reaction of customers following the transaction*

- (438) Large businesses that purchase traditional office supplies through (framework) contracts may face difficulties switching to other suppliers after the transaction because there are few alternative suppliers that can cover their requirements.³⁸⁶ As seen in section 7.2.4.1 above, the merged entity and Lyreco would be the only available options for large customers after the transaction and, to a lesser extent, Ocaj and Wulff. Those two suppliers have difficulties at present in competing with the Parties because of the different scale and pricing. Such difficulties will increase after the transaction, hence their capacity to constrain the Parties will be limited. Therefore, Lyreco would be the only supplier in a position to constraint the Parties.
- (439) The reduced options available will limit customer's bargaining power in the context of the bidding process making customers' switching threats less credible.
- (440) In addition, in light of the large number of customers and the limited value of the individual contracts (even the largest ones)³⁸⁷, compared with the Parties' turnover in Sweden, and the low strategic value of office supplies, customers are not in a position to sponsor new entry and thus their buyer power is, if at all limited.

7.2.4.3.3. Conclusion

- (441) In conclusion, the Commission finds that the transaction would result in the removal of an important competitive force from the market and of a close competitor of Staples. The reduction from three to two large credible bidders for non-international contract with large customers in Sweden would be such as to significantly reduce competition for those contracts, providing the merged entity as well as the remaining competitors with the incentive and ability to raise prices. This is corroborated by the majority of customers responding to the market investigation. More specifically, out of the 43 contract customers who purchase office supplies in Sweden, 25 (58%) expressed concerns that the merger would lead to less competition, price increases and reduced bargaining power.

³⁸⁴ Replies to Phase I Questionnaire Q1 – Questionnaire to Competitors (Contract) – Questions 58 and 59.

³⁸⁵ Replies to Phase I Questionnaire Q4 – Questionnaire to Customers (Contract) – Questions 43 and 43.1.

³⁸⁶ Horizontal Merger Guidelines, paragraph 31.

³⁸⁷ The individual value of Office Depot's top five contracts for traditional office supplies in Sweden ranges between EUR [...] and EUR [...]; as regards Staples, its five largest contracts for traditional office supplies in Sweden have a value between EUR [...] and EUR [...] approximately, accounting for a very small percentage of their total sales in the relevant market.

7.2.4.4. Conclusion on Sweden – Traditional office supplies

(442) On the basis of the arguments set out in section 7.2.4, the Commission concludes that the transaction would significantly impede effective competition on the market for distribution of traditional office supplies to customers of more than 100-200 office workers or 250 employees through contracts in Sweden.

7.2.5. *Sweden - Stationery only*

7.2.5.1. Structure of the market

(443) The structure of the market as described in the previous section 7.2.4 is not materially different when assessing the market for the supply of stationery products only. Therefore, the same findings apply as regards the competitive assessment of such a market.

7.2.5.2. Competitive constraints exerted by the Parties on each other

(444) The analysis of tender data of the Parties for stationery only confirms that Staples, Office Depot and Lyreco are close competitors.³⁸⁸ Ocaj is another competitor, but the competitive pressure it exerts on the Parties is weaker.

(445) Using the tender data provided by Staples, the Commission assessed separately tenders for stationery that involve enterprise customers.³⁸⁹ In tenders where Staples participated, Office Depot, Lyreco and Ocaj, as well as suppliers coded as "local", typically bid along each other for stationery tenders.³⁹⁰ Other suppliers rarely appear: for example Kontorab and Wulff participate in only [...] tenders each.

(446) However, those suppliers differ significantly in their winning patterns. In particular, out of a total of [...] stationery tenders involving enterprise customers (with a total value of EUR [...]), Staples emerged as winner in [50-60]% of those tenders, capturing [60-70]% of stationery value won. Office Depot and Lyreco followed with a share of tenders won respectively of [10-20]% and [10-20]%, and of the value won respectively of [10-20]% and [10-20]%. While Ocaj seems to often participate in tenders along with Staples, Ocaj won in merely [0-5]% of stationery tenders that involve enterprise customers, with a value share of [0-5]% only. Kontorab and Onemed won a handful of larger stationery tenders, but not exceeding [0-5]% of the total stationery value in tenders where Staples participated and involving enterprise customers. No other supplier won more than 1% of stationery value in those tenders.

(447) Focusing on stationery tenders lost by Staples for enterprise customers ([...] tenders), the Commission assessed who emerges as the winner in those tenders. This analysis shows that Office Depot and Lyreco are the main winners in those tenders, with Ocaj and other suppliers lagging significantly behind. In particular, out of the [...] tenders where a stationery lot for an enterprise customer was not won by Staples, the winner was Office Depot and Lyreco in respectively [...] and [...] cases, corresponding to a value share of respectively [30-40]% and [40-50]%. Ocaj won in only [...] of those tenders with a value share of [0-5]%. Other suppliers won even less tenders than Ocaj.³⁹¹

³⁸⁸ See footnote 258 for assumptions underlying the analysis presented in this section.

³⁸⁹ This omits tenders for international and midmarket customers.

³⁹⁰ See Footnote 258.

³⁹¹ Kontorab won in [...] instances, with a value share of [5-10]%, lagging significantly behind that of Office Depot and Lyreco.

- (448) The data provided by Office Depot for Sweden shows a very similar pattern and confirms that in Sweden, for stationery, Staples, Office Depot and Lyreco are the closest competitors, with Ocaj and other suppliers lagging significantly behind.
- (449) In particular, among the [...] tenders involving stationery where Office Depot participated, Staples, Lyreco and Ocaj participates in respectively [...], [...] and [...] tenders. Other bidders appeared only occasionally, such as Kontorab ([...] participations) and Wulff ([...] participations). In addition, among those [...] tenders, only Staples, Office Depot and Lyreco won a significant number of tenders, while other suppliers (including Ocaj) achieved very few wins. In particular, Office Depot, Lyreco, Staples and Ocaj won in respectively [...], [...], [...] and [...] tenders. The only other firms appearing as winners in the data of Office Depot were Kontorab and Kontorspecial with [...] each.
- (450) Looking at stationery tenders lost by Office Depot, Staples appears to be the main competitive constraint, winning [50-60]% of the value in those tenders ([40-50]% of tenders). Lyreco follows by winning [30-40]% of the value of those tenders ([30-40]% of tenders). Ocaj, the third largest winner of stationery tenders lost by Office Depot, captured only [5-10]% of the value in those tenders ([10-20]% of tenders). Other suppliers represent a very small share (less than 3% in value) of stationery tenders lost by Office Depot.
- (451) To conclude, on the basis of the bidding data provided by the Parties the Commission considers that: (i) there are essentially 4 credible suppliers in Sweden, the Parties, Lyreco, and Ocaj, (ii) the Parties and Lyreco are close competitors, (iii) Office Depot (respectively Staples) exerts a significant competitive constraint on Staples (respectively Office Depot) and, (iii) Ocaj is a distant competitor to the Parties and exerts a low competitive constraint on the Parties.

7.2.5.3. Competitive conditions following the transaction

- (452) The merger would reinforce Staples' position as market leader in the supply of stationery through contracts, with only one credible alternative competitor available after the transaction. The loss of a significant supplier competing closely with Staples in such a concentrated market would critically affect the capability of customers to obtain a sufficient number of bids to run competitive tenders for the supply of stationery. Moreover, the removal of such a constraint would reduce the competitive pressure also on the remaining competitors (Lyreco, Ocaj and Wulff).
- (453) The results of the market investigation support the Commission's general findings on the market for traditional office supplies also more specifically as regards stationery. If a limited competitive pressure exists on certain product categories (particularly ink & toner and paper) because of the possibility to obtain those supplies from specialists, such possibility does not exist for stationery, so that the competition concerns could only be aggravated if stationery is assessed separately.
- (454) An additional finding concerns the effective possibility of companies active in neighbouring markets, as well as specialist suppliers, to expand to stationery. When responding to the market investigation, paper and MPS specialists stressed that they have a different business focus and no interest in expanding into the distribution of stationery. They also mentioned as a barrier to expansion the specificities of the logistics arrangements required to distribute stationery products. Other suppliers active in neighbouring markets such as cleaning companies, IT suppliers, etc. may have some stationery sales. However, those are add-ons to orders for other items on which they specialise.

7.2.5.4. Conclusion on Sweden – Stationery only

(455) The Commission concludes that the transaction would lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Sweden.

7.2.6. Netherlands - Traditional office supplies

7.2.6.1. Structure of the market

7.2.6.1.1. The views of the Notifying Party

(456) According to the Notifying Party, the Dutch market for office supplies is very competitive, with Dutch customers being very price conscious.³⁹² The Notifying Party indicates that the overall Dutch market for office supplies is characterised by the existence of a number of strong rivals to the Parties, including Lyreco and several other local suppliers that provide office supplies to large corporate customers. These include Quantore, paper suppliers (such as Canon, Papyrus and Buhrmann Ubbens), providers of MPS (such as Canon, HP, Ricoh, Xerox, Lexmark and Samsung), providers of ink such as 123inkt.nl, online catalogue retailers such as Manutan and providers of facility services (such as Bunzl, King, Sligro, Makro, CWS and Initial)³⁹³.

(457) The Notifying Party further indicates Lyreco, Quantore Europe BV ("Quantore"), Manutan, Bunzl Outsourcing BV ("Bunzl") and Hedera as the Parties' top five competitors in the contract market in the Netherlands.³⁹⁴

(458) The Notifying Party submits that Lyreco has a very strong position in the Netherlands with a focus on major accounts. According to the Notifying Party, Lyreco competes aggressively for new business in the Netherlands and has expanded its sales force to this effect.³⁹⁵

(459) Moreover, the Notifying Party claims that several suppliers in the Netherlands apart from the Parties are able to win large tenders involving stationery. For example, King, which is a provider of facility services, won a contract for the value of EUR [...] in a tender involving stationery for an institution within [...] and Hedera (member of the cooperative Quantore) won a contract for [...] for a value of EUR [...]³⁹⁶.

(460) Finally, according to the Notifying Party, companies which are active in neighbouring markets have recently easily and successfully expanded into stationery and should therefore be considered as an alternative credible competitor to the Parties in the Dutch market.³⁹⁷ One example would be Manutan, which has not only expanded its geographic scope, but also incorporated stationery to its main product category (office furniture).³⁹⁸ According to the Notifying Party, Manutan is a very

³⁹² Form CO, paragraph 269.

³⁹³ Form CO, paragraph 271. See further references to Manutan and 123inkt.nl in particular in Response to the 6(1)(c)Decision.

³⁹⁴ Contact details provided in response to the request for information of 5 October 2015 – National contracts (part 2) and to the request of information of on 8 October 2015.

³⁹⁵ Form CO, paragraph 271.

³⁹⁶ Note on the reduction in the number of key suppliers for stationery", submitted on 23 October 2015, paragraphs 12 and 13.

³⁹⁷ Note on the reduction in the number of key suppliers for stationery", submitted on 23 October 2015, paragraphs 31-33.

³⁹⁸ *Ibid.*

rapidly growing supplier that has been identified by [10-20]% of customers as a “likely” or “very likely” alternative for Stationery in the 2015 National survey (compared to [10-20]% for Office Depot and [10-20]% for Lyreco).

7.2.6.1.2. The Commission’s assessment

- (461) The Commission conducted an extensive market investigation, both in Phase I and Phase II, to identify the suppliers that are currently active in the contract market and which supply the full range of traditional office supplies in the Netherlands to customers with more than 100-200 office workers.
- (462) On the basis of the results of the market investigation, the Commission considers that of the five suppliers identified by the Notifying Party as the Parties' top competitors in the contract market in the Netherlands, two (Quantore and Bunzl) are not even active in the contract channel. Only Lyreco, Hedera and Manutan are active in the contract market for traditional office supplies but only Lyreco is capable of exerting a credible competitive constraint on the Parties in this market.

7.2.6.1.2.1. Suppliers identified by the Parties which are not active in the relevant market

- (463) As regards Quantore, the Commission preliminarily concluded in the Article 6(1)(c) Decision that it does not constitute a sufficient alternative to the Parties and Lyreco as regards large contracts in the Netherlands. Quantore is a Dutch purchasing cooperative and logistic company operating in the Netherlands (95% of its business) and in Belgium (5% of its business). It has 450 members that are small and medium sized suppliers to end consumers of office products, computer products and technical equipment. Quantore does not sell its products directly to final consumer but acts at wholesale level only providing logistic services to its members delivering products to their warehouses and to the final consumers on behalf of its members³⁹⁹.
- (464) Quantore is mainly active in the B2B retail market and targets small and medium sized businesses.⁴⁰⁰ Despite having tried to (unsuccessfully) enter the contract market between 2011 and 2014, Quantore does not sell office supplies through contracts anymore.⁴⁰¹ During that period, Quantore contracted with medium and large customers, but decided to discontinue those activities in 2015, due to the dominance of the three main suppliers in the Dutch market, Staples, Office Depot and Lyreco.⁴⁰² According to Quantore, the tender contract market suffers from high barriers to entry, which are not only related to the size and the capacity needed to serve the customers, but also to endogenous strategies pursued by the incumbents. Moreover, special systems are needed in order to be an effective competitor in the tendering market. Although Quantore satisfies the technical features to serve large customers, it does not have the business knowledge and intelligence to bid against the incumbents".⁴⁰³
- (465) On the basis of the market investigation the Commission is able to confirm the limited role and the weak perception of Quantore by customers as a supplier for large contracts. One large customer explained during the Phase I investigation that "*However, Quantore was in the last tender (2011) not adequate to (this customer)'s*

³⁹⁹ Agreed minutes of a phone call with Quantore, paragraph 1.

⁴⁰⁰ Quantore's reply of 21.10.2015 to Commission's request for information on the top 100 customers.

⁴⁰¹ *Ibid*, paragraph 8.

⁴⁰² Quantore's reply to Phase I Questionnaire Q1 to competitors – Question 1.

⁴⁰³ Agreed minutes of a phone call with Quantore, paragraph 8.

needs".⁴⁰⁴ Another large customer, when describing the participants in tenders in the Dutch market indicated that "*Quantore cannot be compared to Staples, Office Depot or Lyreco since it is a group of smaller suppliers*".⁴⁰⁵ The results of the investigation in Phase II supported the findings that Quantore plays a limited role in the contract market in the Netherlands. Only two customers (out of a total of 17 Dutch respondents) indicated Quantore as an alternative supplier to the Parties⁴⁰⁶ and only one respondent indicated that it had invited Quantore for a bid that was held in 2011 (therefore when Quantore was still active in the contract market).⁴⁰⁷

- (466) The Notifying Party also indicated Bunzl as a competitor to the Parties in the market for national contracts, although this company is mostly active in the facilities category. Bunzl supplies a diverse customer base with a broad range of internationally sourced products in a variety of market sectors: food services, grocery, cleaning & hygiene, retail, safety, healthcare and other.⁴⁰⁸
- (467) On the basis of the market investigation in Phase II the Commission considers, however, that Bunzl is not active as a contract stationer in the Netherlands for the distribution of full range traditional office supplies. First, Bunzl does not consider itself as a competitor of the Parties since its activities in the distribution of office supplies are very small and cannot in any case be compared to the activities of the Parties. Second, Bunzl's limited sales of office supplies in the Dutch market result from the distribution of a very limited amount (below EUR 250 000) of stationery materials and paper for hotel conference rooms, which represent an insignificant fraction (below 1%) of its Dutch revenues.⁴⁰⁹ Therefore, even if it may supply some stationery and other office products on an ad hoc basis, in addition to the main services it provides, it is evident from the results of the market investigation that the focus and business strategy of this company is different from the one followed by the Parties.

7.2.6.1.2.2. *Suppliers identified by the Parties which are active in the relevant market but have a limited presence*

- (468) The remaining suppliers identified by the Notifying Party as actual competitors of the Parties in the contract market in the Netherlands are Lyreco, Manutan and Hedera. Those three suppliers are active in the contract channel for traditional office supplies. However, Manutan and Hedera supply very few contracts of a limited value. On the basis of the market investigation the Commission considers that these two suppliers exert very limited competitive constraints on the Parties, as will be explained in section 7.2.6.3.
- (469) The Notifying Party repeatedly refers to Manutan as a primarily online supplier which has expanded its product range into traditional office supplies and which is capable of exerting significant competitive pressure over the Parties.⁴¹⁰ According to the results of the market investigation around [30-40]% of Manutan's turnover is

⁴⁰⁴ Agreed minutes of the phone call with a customer.

⁴⁰⁵ Agreed minutes of the phone call with a customer.

⁴⁰⁶ Reply to Phase II Questionnaire Q8i to customers – Question 10.

⁴⁰⁷ Reply to Phase II Questionnaire Q8i to customers – Question 8.

⁴⁰⁸ See Bunzl's Annual Report 2014: <http://www.bunzl.com/~media/Files/B/Bunzl-PLC/reports-and-presentations/ar-2014.pdf>.

⁴⁰⁹ Emails sent by Bunzl on 14 and 15 October 2015 in reply to Phase II Questionnaire – Q9 to competitors (contract stationers).

⁴¹⁰ Response to the 6(1)(c)Decision, paragraph 26; Note on the reduction in the number of key suppliers for stationery", submitted on 23 October 2015, paragraph 25.

generated through sales online and [70-80]% offline via catalogue.⁴¹¹ Manutan only achieves a small percentage of its total revenues through the contract channel (around [10-20]-[30-40]%).

- (470) Manutan operates in 18 countries in Europe where it sells a very large range of products, with a particular focus on office furniture, including office supplies and stationery.⁴¹² even if some of its contracts with large customers may include some traditional office supplies, Manutan's turnover is primarily generated by the sale of office furniture (namely containers and storage equipment), while the revenues achieved by the sale of traditional office supplies products account for an insignificant percentage (around [5-10]-[10-20]%) of its total contract revenues.⁴¹³
- (471) Finally, Hedera is an independent company, member of the cooperative Quantore, which is active in the supply of office supplies, office furniture, printing supplies (traditional & MPS) and Apple products. However, as will be assessed in recitals (477) and (478) below, the results of the market investigation in Phase II revealed that, while it is active in the Dutch contract market for traditional office supplies, it is a very far fourth supplier in this market for a number of reasons.
- (472) Finally, the Notifying Party mentions a number of specialist companies such as paper suppliers (Canon, Papyrus and Buhrmann Ubbens), providers of MPS (such as Canon, HP, Ricoh, Xerox, Lexmark, and Samsung), and providers of ink such as 123inkt.nl, which would be strong rivals of the Parties in the Dutch market for office supplies. However, for the reasons explained in recitals (86) to (90), those suppliers cannot be considered to be active in the market for full range contracts for traditional office supplies, as defined in section 6.1.2.1.
- (473) Therefore, large customers in the Netherlands have very limited alternatives when looking for suppliers which are able to supply traditional office products through contracts.

7.2.6.1.2.3. *Position of the Parties and their competitors active in the contract market for traditional office supplies*

- (474) Both Parties sell traditional office supplies to large customers under framework contracts in the Netherlands.
- (475) Based on the data submitted by the Notifying Party, Staples is currently the market leader in the Dutch contract market for traditional office supplies with sales of approximately EUR [...] in 2014 and EUR [...] for sales of traditional office supplies to large customers. Lyreco is the second largest supplier in terms of contract sales, whereas Office Depot is the third supplier in the contract market with sales of approximately EUR [...] and EUR [...] for sales of traditional office supplies to large customers.⁴¹⁴ Following the transaction, the merged entity would be the clear market leader in the market for non-international contract sales of traditional office supplies with a combined turnover of approximately EUR [...].

⁴¹¹ Agreed minutes of the conference call with Manutan, paragraph 2.

⁴¹² Agreed minutes of the conference call with Manutan, paragraph 1.

⁴¹³ Agreed minutes of the conference call with Manutan, paragraph 4.

⁴¹⁴ See the Parties' replies of 22 December 2015 and 7 January 2016 to requests for information on contract sales data.

Table 14: Parties' sales of traditional office supplies through contracts in the Netherlands, EUR 000s

Category	Party	All customers	Large customers
<i>Traditional office supplies</i>	<i>Staples</i>	[...]	[...]
Stationery	Staples	[...]	[...]
Ink & toner	Staples	[...]	[...]
Paper	Staples	[...]	[...]
<i>Traditional office supplies</i>	<i>Office Depot</i>	[...]	[...]
Stationery	Office Depot	[...]	[...]
Ink & toner	Office Depot	[...]	[...]
Paper	Office Depot	[...]	[...]

Source: Source: Parties' replies of 22 December 2015 and 7 January 2016 to requests for information on contract sales data.

- (476) Apart from the Parties and Lyreco, the Notifying Party indicated Quantore, Manutan, Bunzl and Hedera as competitors active in the contract market in the Netherlands.⁴¹⁵ As explained in recitals (463) to (467), Quantore and Bunzl are not even active in the distribution of traditional office supplies through contracts.
- (477) As regards Hedera, while it is active in the Dutch contract market for traditional office supplies, it positions itself as a very far fourth supplier in the Dutch market. In terms of revenues, its total sales of traditional office supplies in 2014 (of which only half were achieved through contracts) represent a very small percentage of the merged entity's sales,⁴¹⁶ As Hedera pointed out during the market investigation: "*Staples, Office Depot and Lyreco are the biggest and Hedera would be number four. However, it is important to note that there is a big gap between the three large ones and Hedera in terms of revenues generated*".⁴¹⁷
- (478) Moreover, the value of Hedera's ten largest contracts with business customers in 2014 was below EUR [...],⁴¹⁸ therefore lagging far behind the value of the Parties' top 10 contracts in the Netherlands, which range between approximately EUR [...] for Staples and EUR [...] for Office Depot. Therefore, the starting point of Office Depot's top 10 contracts would be the same as value of Hedera's largest contract. Hedera rarely appears in the bidding data provided by the Parties (see section 7.2.6.2) and it does not supply any of the largest 100 companies and entities (both public and private) in terms of number of employees in the Netherlands.⁴¹⁹ Finally, on the basis of the market investigation in Phase II the Commission confirms Hedera's weak position as a contract stationer in the Netherlands. Only one customer

⁴¹⁵ Contact details provided in response to the request for information of 5 October 2015 – National contracts (part 2) and to the request of information of on 8 October 2015.

⁴¹⁶ Hedera's reply to Phase II Questionnaire Q9 to competitors (contract stationers) – question 2.

⁴¹⁷ Agreed minutes of the phone call with Hedera, paragraph 2.

⁴¹⁸ Hedera's reply to Phase II Questionnaire Q9 – question 5.

⁴¹⁹ Top 100 companies in terms of numbers of employees.

(out of a total of 17 Dutch respondents) mentioned Hedera as an alternative supplier to the Parties (fourth supplier)⁴²⁰. This respondent [...] had invited Hedera to submit bids during the last tender, which was held in 2015.⁴²¹

- (479) On the basis of the results of the market investigation in Phase II the Commission confirms that Manutan plays a very limited role in the contract market for traditional office supplies in the Netherlands. Manutan is only mentioned by four customers (out of 17 Dutch respondents) as an alternative supplier to the Parties.⁴²² However, one of those customers confirmed the distance between the Parties or Lyreco and Manutan by indicating that "*as I mentioned the main companies are now Lyreco, Office Depot and Staples. Shaefer and Manutan are at this very moment not the main competitors. I will be difficult to get 4 or 5 competitive suppliers for a new tender*".⁴²³ Of the other three suppliers, one of them indicated that it had not organised any tender for the procurement of office supplies in recent years, and another one did not invite Manutan to bid in its last tender (despite having identified this supplier as an alternative to the Parties).⁴²⁴
- (480) Moreover, Manutan confirmed the wide distance between the Parties' position as large contract stationers in the Netherlands and its own position and business model, which focuses on offering a wide range of products: *Customers that switch from Manutan do not do so to go for Staples and Office Depot instead. Staples and Office Depot specialise in office supplies, which is only one category and a minor part of Manutan's business.*⁴²⁵
- (481) While Manutan makes some ancillary sales through contracts with some of the top 100 companies and entities (both public and private) in the Netherlands, the value of its largest contract with one of those companies represents an insignificant fraction (below 5%) of the value of the contracts that Office Depot has with the same customer, which reinforces Manutan's role as a supplier offering bundles.
- (482) The assessment of the bidding data provided by the Parties demonstrates that apart from Lyreco, the alternative suppliers mentioned by the Parties rarely participate in tenders together with the Parties, especially in those involving larger customers, and even if they do participate, they hardly win any of those tenders. Although there are several competitors for all tenders, when attention is limited to the largest customers, Staples, Lyreco and Office Depot emerge as the main stationery suppliers (see section 7.2.6.2 for a more detailed analysis of the bidding data).

7.2.6.1.3. Conclusion

- (483) In light of recitals (463) to (482), the Commission concludes that only the Parties, Lyreco, Hedera and Manutan are active in the Dutch market for the distribution of full range traditional office supplies through contracts and that the Parties and Lyreco are the clear market leaders, whereas the other suppliers remain smaller suppliers with limited presence in this market.

⁴²⁰ Reply to Phase II Questionnaire Q8i to customers – Question 48.

⁴²¹ Reply to Phase II Questionnaire Q8i to customers – Question 8.

⁴²² Reply to Phase II Questionnaire Q8i to customers – Question 48.

⁴²³ Reply to Phase II Questionnaire Q8i to customers – Question 10.4.

⁴²⁴ Reply to Phase II Questionnaire Q8i to customers – Question 8.

⁴²⁵ Agreed minutes of the phone call with Manutan, paragraph 28.

7.2.6.2. Competitive constraints exerted by the Parties on each other

7.2.6.2.1. The views of the Notifying Party

- (484) According to the Notifying Party, the Dutch office supplies market is very competitive and there are a number of suppliers with a strong presence in the Netherlands which are able to exert significant competitive pressure over the Merged Entity. Moreover, competitors, including local and regional suppliers have increased product ranges and added services to retain large corporate customers.⁴²⁶
- (485) The Notifying Party considers that customers in the Netherlands can use the existence of specialist suppliers to ensure competitive pricing in the market by explicitly and implicitly threatening to split their requirements.⁴²⁷
- (486) Finally, the Notifying Party submits the results of their analysis of the Parties' bidding data in the Netherlands. According to the Notifying Party, that analysis shows that smaller local suppliers win the majority of tenders lost by Staples in the Netherlands ([40-50]% of the tenders were won by "others"). Lyreco is the individual competitor which wins most tenders that Staples loses both in absolute terms and in terms of value.⁴²⁸ As regards, the tenders that Office Depot loses, most of them are lost to Lyreco ([40-50]%), [30-40]% to Staples and [10-20]% of them to "others".⁴²⁹

7.2.6.2.2. The Commission's assessment

- (487) The results of the market investigation in Phase II has confirmed the Commission's preliminary findings that the Parties are close competitors in the market for the distribution of traditional office supplies through contracts in the Netherlands. Moreover, together with Lyreco, the Parties are *de facto* the only suppliers capable of winning tenders with large customers.
- (488) First, the results of the market investigation in Phase II show that the Parties consistently appear, together with Lyreco, as the preferred suppliers invited to bid in tenders and as winners of the tender. Out of 17 Dutch customers that replied to the questionnaire in Phase II, approximately half (8) indicated that the Parties were invited to submit bids in their last tender (of the remaining 9 suppliers, 2 indicated that no tender was organised in relation to the last framework contract, and 5 indicated that such information was not available).⁴³⁰ In all 8 cases, the Parties appear together with Lyreco as bidders in the tender (in one case together with Hedera and in another instance with Quantore).⁴³¹
- (489) The fact that the Parties are two close competitors in the Netherlands, in particular as regards large customers, is further evidenced by the number of the top largest employers (both public and private)⁴³² that the Parties supply to in the Netherlands. Following an assessment of how many of the top 100 employers are purely national entities (namely those which only operate in the Netherlands) and therefore only have non-international contracts in place for office supplies (in order not to over-estimate the Parties market power for non-international contracts in the Netherlands),

⁴²⁶ Form CO, paragraph 269.

⁴²⁷ Form CO, paragraph 273.

⁴²⁸ Form CO, paragraph 278.

⁴²⁹ *Ibid.*

⁴³⁰ Reply to Phase II Questionnaire Q8i to customers – Question 8.

⁴³¹ *Ibid.*

⁴³² In terms of number of employees.

the Commission concludes that 82 of those entities are purely national customers.⁴³³ Out of those 82 entities, [60-70%] ([40-50]) are currently customers of Staples ([30-40]), Office Depot ([20-30]) or both ([5-10]) for either the full range of traditional office supplies or some categories. Lyreco, which is the second supplier in the Dutch contract market in terms of revenues, has contracts with 36 of the top 82 purely national employers in the Netherlands, some of which overlap with the Parties.⁴³⁴

- (490) As regards Manutan, the results of the market investigation revealed that it has contracts in place with [...] of those top 82 national customers⁴³⁵. However, the value of its largest contract with one of those companies represents an insignificant fraction (below 5%) of the value of the Parties' largest contracts with customers from this list, which confirms the ancillary nature of the purchases of office supplies that customers make with this supplier. Finally, Hedera does not have contracts in place for office supplies with any of those top 82 customers. Their activities with the top Dutch employers are limited to the supply of office furniture to only one of the companies included in the list.⁴³⁶
- (491) In an email exchange between Staples representatives in the Netherlands and other regions, including the Regional Managing Director of Staples Advantage Nordic, it is clearly confirmed that competition for large accounts in the Netherlands is limited to the Parties and Lyreco: [...].⁴³⁷
- (492) The current proximity between the main three suppliers in the Netherlands is further evidenced by the fact that Staples monitors [...] of Office Depot and Lyreco particularly closely: [...].⁴³⁸
- (493) Moreover, the internal documents provided by the Parties show that Staples monitors Office Depot's [...] particularly closely, as opposed to other local suppliers: [...].⁴³⁹
- (494) Finally, the Commission reviewed data submitted by the Parties on national tenders for office supplies in the Netherlands.⁴⁴⁰ That assessment focused on large national customers (Enterprise customers) and therefore tenders where the customer was classified by Staples as midmarket or international (IAT) were omitted. The tender data submitted by the Parties for the Netherlands does not allow for the separation of various product categories and therefore involves all traditional office supplies. The main finding, which emerges from both the Parties' submission on tender data as well as the Commission's analysis, is that in the Netherlands Staples, Office Depot and

⁴³³ The Commission assessed how many of the top 100 Dutch employers currently have international contracts in place with the three suppliers that are able to offer international contracts: Staples, Office Depot and Lyreco. The source of this information is the document provided by the Notifying Party as Annex 23 to the Form CO and the information provided by Lyreco in its reply of 29.10.2015 to the Commission's request for information on the top 100 customers.

⁴³⁴ Lyreco's reply to the Commission's request for information on the top 100 customers.

⁴³⁵ Manutan's reply to the Commission's request for information on the top 100 customers.

⁴³⁶ Hedera's reply to the Commission's request for information on the top 100 customers.

⁴³⁷ Staples' internal document entitled "RE: INFORMATION NEEDED - competitive analysis", 7 March 2013.

⁴³⁸ Staples' internal document entitled "Pricing & Margin Staples NL", 13 June 2013.

⁴³⁹ Staples' internal document entitled "[...]", 9 May 2014.

⁴⁴⁰ See footnote 255 for assumptions underlying the analysis presented in this section.

Lyreco are close competitors. Other suppliers appear more distant and exert a limited competitive pressure on the Parties.⁴⁴¹

- (495) Staples' tender data shows that in tenders for enterprise customers, Office Depot and Lyreco are the major bidders along with Staples. Staples participated in [...] tenders for traditional office supplies involving Enterprise customers. Among those [...] tenders, Office Depot and Lyreco appeared to have participated respectively in [...] and [...] tenders. Quantore submitted [...] bids in those tenders, and other suppliers had an even lower number of bids.
- (496) Among the tenders involving Enterprise customers where Staples participated and lost, Office Depot (in addition to Lyreco) is one of the main winners in those tenders. In particular, out of [...] tenders where Staples lost with enterprise customers, Lyreco won [...], followed by Office Depot with [...] wins. King, Canon and Papyrus each won only [...] lost by Staples, but [...] involved large amounts. However, as explained in section 7.2.7 the Commission found that among the tenders lost by Staples that King, Papyrus and Canon won, those suppliers actually did not sell the full range of office supplies, but only paper or ink & toner.
- (497) The Commission concludes from Staples' tender data on Enterprise customers for the Netherlands that Office Depot is a close competitor (after Lyreco) to Staples in traditional office supplies.
- (498) The data submitted by Office Depot for the Netherlands also confirms that competition is mainly between the Parties and Lyreco. In particular, in Office Depot's bidding data, Lyreco and the Parties emerge as winners in respectively [...], [...] and [...] tenders. No further market participant shows more than one win. Focusing on those tenders that are lost by Office Depot, the main winners are Staples and Lyreco with value shares of [40-50]% each. No other market participant captured a significant number or value of tenders that were lost by Office Depot (the next participants captures a value share of less than 4%).
- (499) On the basis of the analysis of bidding data for the full range of the three traditional office supplies, the Commission considers that: (i) Staples, Office Depot, and Lyreco are close competitors, with the Parties exerting a significant competitive pressure on each other, and (ii) no other suppliers appear as credible alternatives to the Parties and Lyreco.
- (500) The results of the Commission's assessment of the bidding data are further supported and illustrated by internal documents from the Parties. The following graph, extracted from Staples' internal documents, shows the strong prominence of the Parties (notably Staples) and Lyreco as the leading suppliers in the market for office supplies (in particular, stationery) and the limited role that Hedera and Quantore play in tenders:

⁴⁴¹ See "Relevance of bidding data for the competitive assessment", dated 18 May 2015, RBB Economics, section 4.6.

Figure: Competitive insights NL

[...]

[...]

Source: Staples' internal document entitled "Staples Advantage Netherlands, FY14 Commercial Budget Review", November 2013, 8 November 2013, page 4.

(501) The fact that the Parties are close competitors capable of winning tenders and supplying large contracts with large customers is explained by the fact that supplier selection appears to be mostly based on prices and on the ability to meet the specific requirements of large contract customers. As regards their ability to price particularly low, Hedera indicated that it cannot compete with the Parties "*due to the aggressive pricing strategy that the Parties engage in (essentially selling below cost)*".⁴⁴²

7.2.6.2.3. Conclusion

(502) On the basis of the above, the Commission concludes that the Parties are close competitors in the market for distribution of office supplies to customers of more than 100-200 office workers or 250 employees in the Netherlands, and therefore the proposed merger would lead to a significant loss of competition.

7.2.6.3. Competitive conditions following the transaction

7.2.6.3.1. The views of the Notifying Party

(503) The Notifying Party submits that the Parties will not be able to increase prices in the Netherlands, where the available evidence from, among other sources, internal documents, the Commission's own market feedback and the 2015 National survey, demonstrate that there will remain intense competition from both traditional suppliers and specialist suppliers.⁴⁴³

(504) According to the Notifying Party, the Commission does not acknowledge the steep revenue decline in ink & toner where competition is exercised not just by MPS suppliers but also by online suppliers such as 123inkt⁴⁴⁴ or Amazon.⁴⁴⁵ The Notifying Party repeatedly mentions that online suppliers such as Amazon are capable of posing a significant competitive threat to the traditional office supplies suppliers.⁴⁴⁶

(505) Moreover, the Notifying Party submits that customers can threaten to issue separate tenders for stationery, paper and printing facilities, which, according to the Notifying Party is a powerful threat because providers of office supplies know that their chances of being successful in tenders for particular products categories (for instance paper only, ink-only) are often low.⁴⁴⁷ In this regard, the Notifying Party submits that in order to find competition concerns in the contract market for office supplies, the Commission would need to dismiss the indirect constraint exerted by specialist suppliers which are not active in the full range of traditional office supplies but offer some product categories. The Notifying Party claims that the Commission would

⁴⁴² Hedera's reply to Phase II Questionnaire Q9 to competitors (contract stationers) – question 15; agreed minutes of the conference call with Hedera, paragraph 6.

⁴⁴³ Response to the 6(1)(c) Decision, paragraphs 7 and 25-26.

⁴⁴⁴ Response to the 6(1)(c) Decision, paragraph 25.

⁴⁴⁵ Form CO, paragraphs 53, 59 and submission on Amazon of 20 October 2015.

⁴⁴⁶ Form CO, paragraphs 53, 59 and submission on Amazon of 20 October 2015.

⁴⁴⁷ Form CO, paragraph 273.

need to set aside the ability of the largest customers to achieve competitive prices for stationery by threatening to switch other categories, often accounting for the bulk of a customer's requirements to specialist suppliers.⁴⁴⁸

- (506) Finally, the Notifying Party repeatedly indicates that it is very easy to enter into the contract segment. Moreover, the fact that online suppliers do not offer "contracts" does not mean that they cannot, or do not compete against the Parties. Online competitors can easily set up individualised e-catalogues allowing them to customise their offerings for specific customers (and offer volume rebates and other special offers to specific customers).⁴⁴⁹
- (507) Finally, according to the Notifying Party, the Commission would have to dismiss the fact that suppliers in other product categories have certain scope to start supplying stationery.⁴⁵⁰

7.2.6.3.2. The Commission's assessment

7.2.6.3.2.1. *Structure of the market following the transaction*

- (508) In section 7.2.6.1, the Commission carried out a detailed assessment of the current competitive landscape in the contract market for traditional office supplies in the Netherlands. The result of such analysis revealed that only the Parties, Lyreco, Hedera and Manutan are active competitors in the Dutch market for the distribution of full range traditional office supplies. However, for the reasons explained in recitals (479) to (481) Manutan plays a very limited role in the contract market for traditional office supplies in the Netherlands, and therefore its role in the market will not be assessed further.
- (509) Following the transaction, the merged entity would be the clear market leader in the market for non-international contract sales of traditional office supplies in the Netherlands with a combined turnover of EUR [...]. The Merged Entity would be followed by Lyreco, which is currently the second largest supplier in terms of sales in the contract market. The Merged Entity and Lyreco would be followed by Hedera, which lags far behind in terms on sales and numbers of contracts with large customers in the Netherlands. In particular, the Merged Entity would be around 20 times larger than Hedera in terms of revenues generated through contract sales.
- (510) Therefore, the transaction, as initially notified, would lead to a 3-to-2 scenario: it would reinforce Staples' number one position in the contract market for traditional office supplies in the Netherlands, it would remove the significant constraint coming from Office Depot, it would increase the distance between the number 1 and number 2 suppliers and would reduce the market to three suppliers, the third lagging far behind.

7.2.6.3.2.2. *Likely reaction of actual competitors following the transaction*

- (511) The Commission considers that, pre-transaction, the Parties and Lyreco are close competitors, and they are the only players capable of exerting a credible competitive constraint on each other, as evidenced in the analysis of internal documents, bidding data and market investigation results (see section 7.2.6.2).

⁴⁴⁸ Note on the reduction in the number of key suppliers for stationery, paragraph 52.

⁴⁴⁹ Note on the reduction in the number of key suppliers for stationery, paragraph 22.

⁴⁵⁰ Note on the reduction in the number of key suppliers for stationery, paragraph 52.

- (512) Indeed, the competitive constraints that the remaining competitor in the contract market (Hedera) may exert on the Parties as regards large customers are, at most, limited.
- (513) Hedera's overall turnover in the contract market represents a very small fraction of the Parties' individual sales in this market, therefore being a significantly smaller player pre-transaction. Moreover, Hedera rarely appears in the bidding data provided by the Parties (see section 7.2.6.2) and it does not supply any of the largest 100 companies and entities (both public and private) in terms of number of employees in the Netherlands.
- (514) This lack of competitiveness was confirmed by Hedera itself in the course of the market investigation. During the market investigation, Hedera indicated that the main competitive advantage that the Parties have over all the other providers of traditional office supplies in the Netherlands is the ability to have aggressive commercial strategies. More specifically, when asked whether they encounter any particular constraints in dealing with large size corporate contract customers, Hedera indicated that they do not face any limitations in their capacity to serve contracts with large customers, but the reality is that they do not win large contracts in tenders with the top employers in the Netherlands (as evidenced by the fact that they do not have contracts in place with any of the top Dutch employers and the fact that they almost never appear in the bidding data provided by the Parties) due to the aggressive commercial strategy that the Parties engage in (essentially selling below cost). Indeed, the prices of the Parties can go 30-40% below Hedera's prices.⁴⁵¹
- (515) The fact that Hedera cannot compete commercially with the Parties, due to its much smaller size, together with the fact that the name of this supplier almost never appears in the replies from Dutch customers to the market investigation and its limited role in tenders, is indicative that this supplier would likely remain a weak competitive constraint to the merged entity post-transaction.

7.2.6.3.2.3. *Likely reaction of potential competitors*

- (516) The Notifying Party specifically refers to online suppliers active in the Netherlands, such as 123inkt, as an important competitive constraint on the Parties, although they are not active in the contract channel.
- (517) According to the results of the market investigation in Phase II 123inkt is a purely online reseller of computer supplies (ink & toner), stationery and printers, which is not active in the contract segment and which only targets small and medium sized enterprises and end-consumers.⁴⁵² While the Commission does not deny that online suppliers may steal some revenues from the Parties in the segment in which both companies are active (that is to say in online sales targeting SMEs and end consumers) and even though some employees of large business contract customers may source some office supplies from online suppliers, this does not support the Notifying Party's argument that the Parties will face strong competition from local online suppliers in the contract market for traditional office supplies after the transaction, when those suppliers are not even active in contracts and do not target large customers.

⁴⁵¹ Response to Questionnaire Q9 to competitors, question 15; Non-confidential minutes of the conference call with a competitor, 16 November 2015, paragraph 6.

⁴⁵² Reply to Phase II Questionnaire Q10 to specialists – Question 5.

- (518) In addition to specific online suppliers active in the Netherlands, the Notifying Party repeatedly mentions Amazon as an online supplier capable of posing a significant competitive threat to the Parties in the EEA, including the Netherlands.⁴⁵³ However, the results of the market investigation revealed that Amazon is currently not active in the contract channel and that there is no business plan in place to expand into this segment in order to compete with the Parties for long-term contracts with customers.⁴⁵⁴ Contrary to the Notifying Party's claims, the market investigation revealed that there are a number of gaps that Amazon or any other supplier not active already in the contract market (that is to say online suppliers).
- (519) Moreover, the Notifying Party considers that specialist suppliers and OEMs which are not active in the full range of traditional office supplies (but only in some product categories) exert (and will continue to do so) an indirect constraint on the Parties, which the Commission cannot ignore. According to the Notifying Party, the largest customers have the ability to achieve competitive prices for stationery by threatening to switch other categories to specialists, often accounting for the bulk of customers' requirements.
- (520) However, according to the results of the market investigation the specialist companies and OEMs that the Notifying Party repeatedly refers to are in fact partners of the Parties for the sale of their products, for instance for the sale of ink and toner as consumables. Moreover, although this part of the market is still not very significant, it was confirmed that there is a growing trend towards MPS, which constitute a separate market, as indicated in recital (83). Finally, customers may use specialists prices as a benchmark and to negotiate better prices with their current supplier.

7.2.6.3.2.4. *Likely reaction of customers*

- (521) Large corporate customers (both private and public entities) that purchase traditional office supplies through contracts may face difficulties switching to other suppliers after the transaction because there are few alternative suppliers that can cover their requirements.⁴⁵⁵
- (522) Some Dutch respondents to the market investigation that expressed concerns about the transaction indicated that it will be difficult to have strong competition when running a tender, since Staples, Office Depot and Lyreco currently bid against each other allowing customers to pay the best purchasing price. As regards the lack of alternative suppliers in the market, one customer indicated that "*they cannot foresee if any other company can get up to speed with the Parties in the future. If not, there will only be 2 alternatives which is not sufficiently competitive*".⁴⁵⁶ Other customers indicated that the transaction would have an impact in their current procurement of office supplies, "*as we only have one real competitor left (Lyreco)*".⁴⁵⁷
- (523) One customer indicates as a potential advantage the increase of the buyer power of the Merged Entity, but questions that this will ultimately benefit the customer:

⁴⁵³ Form CO, paragraphs 53, 59 and submission on Amazon of 20 October 2015.

⁴⁵⁴ Agreed minutes of the call with Amazon; Amazon's reply to the Commission's request for information.

⁴⁵⁵ Horizontal Merger Guidelines, paragraph 31.

⁴⁵⁶ Reply to Phase II Questionnaire Q8i to customers – Question 10.4.

⁴⁵⁷ Reply to Phase II Questionnaire Q8i to customers – Question 10.4.

*because of the lack of competition it is questionable whether the end-user will profit from this advantage.*⁴⁵⁸

- (524) From the customer's side, the Notifying Party claims that large customers of office supplies purchasing under framework contracts are large sophisticated companies and therefore have significant buyer power.⁴⁵⁹ However, in light of the large number of customers that the Parties have in the Netherlands and the limited value of the individual contracts,⁴⁶⁰ compared with the Parties' turnover in the Netherlands, and the low strategic value of office supplies, customers are not in a position to sponsor new entries and thus their buyer power is, if at all, limited.

7.2.6.3.3. Conclusion

- (525) In conclusion, the Commission considers that the transaction would result in the removal of an important competitive force from the market and a close competitor of Staples. The reduction of the number of credible bidders for non-international contracts with large customers in the Netherlands from three to two would be such as to significantly reduce competition for those contracts, providing the merged entity as well as the remaining competitors, with the incentive and ability to raise prices.
- (526) The merger will therefore bring together two close competitors in the Netherlands, reinforcing Staples' leading position and widening the gap between the merged entity on one hand, and Lyreco and Hedera on the other hand who would lag far behind.

7.2.6.4. Conclusion on Netherlands – Traditional office supplies

- (527) On the basis of the arguments set out in this section, the Commission concludes that the transaction would significantly impede effective competition on the market for distribution of traditional office supplies to customers of more than 100-200 office workers or 250 employees through contracts in the Netherlands.

7.2.7. *Netherlands - Stationery only*

7.2.7.1. Structure of the market

- (528) The structure of the market as described in section 7.2.6 is not materially different when assessing the market for supply of stationery products only. Therefore, the same findings apply as regards the competitive assessment of such a market.
- (529) The tender data received from the Parties for the Netherlands does not allow for distinguishing different product categories in tenders. However, narrowing the analysis to stationery products would further strengthen the competitive constraint the Parties exert on each other compared to what has been presented in section 7.2.6. This is because specialist suppliers are only present in paper and ink & toner. In particular, specialists like Canon, Papyrus and King win very specific tenders.
- (530) As for Canon, it captured individually the largest value share of tenders lost by Staples, but this value was generated by [...] large tenders. In particular, Canon won [...] valuing EUR [...] in 2014, for a public administration customer. Based on information in TenderNed and the name of the customer, the Commission understands that this tender did not involve stationery, but printing and copy

⁴⁵⁸ Reply to Phase II Questionnaire Q8i to customers – Question 10.4.

⁴⁵⁹ See Note on buyer power, submitted by the Notifying Party on 25 October 2015.

⁴⁶⁰ The individual value of Office Depot's top five contracts in the Netherlands ranges between EUR [...] and EUR [...]; as regards Staples, its five largest contracts range between EUR [...] and EUR [...].

paper.⁴⁶¹ Canon also won [...] together with Papyrus in 2014, with the customer being a public body, worth EUR [...]. This is the largest tender in Staples' bidding dataset. However, the Commission understands that in the latter tender Canon did not offer stationery.⁴⁶²

- (531) As for Papyrus, the Parties argue that its value share on the tenders lost by Staples is, with [10-20]%, close to that of Office Depot ([10-20]%).⁴⁶³ A review of the submitted tender data revealed however that Papyrus won [...] involving Enterprise customers, namely [...], together with Canon in 2014, with the public body as customer, worth EUR [...]. However, similar to Canon, Papyrus is not selling stationery, as it is selling Office paper, tissue, hygiene products and standard packaging products in the contract, online and wholesale channels.⁴⁶⁴
- (532) The same applies to King, which won [...] in 2013, that covered [5-10]% of the value of all tenders Staples lost in the Netherlands. This tender had a value of EUR [...] with a public organisation as customer. The Commission however understands that this tender involved primarily cleaning tools and products, hygiene and personal care items.⁴⁶⁵
- (533) This leaves Office Depot and Lyreco as the major competitors to Staples for large customers in the Netherlands for stationery. In particular, Manutan and Misco, claimed by the Parties to be key competitors in the Netherlands did not win any tender from those lost by Staples involving large customers, nor did they participate in such tenders along with Staples.⁴⁶⁶ The bidding data of the Parties confirm that in stationery, the main competitors in the Netherlands are Staples, Office Depot and Lyreco.

7.2.7.2. Competitive conditions following the transaction

- (534) The transaction will therefore bring together two close competitors in the supply of stationery through non-international contracts with large customers in the Netherlands, reinforcing Staples' leading position and widening the gap between the Merged Entity on one hand, and Lyreco and Hedera (which is lagging far behind) on the other hand.
- (535) The loss of a close competitor in such a concentrated market would critically affect the capability of customers to obtain a sufficient number of bids to run competitive tenders for the supply of stationery. Moreover, the removal of such a constraint would also reduce the competitive pressure on the remaining competitors (Lyreco, Hedera).
- (536) The bidding data described in the previous section and the market investigation support the general findings on the market for traditional office supplies also more

⁴⁶¹ Based on the name of customer, the Commission tracked that tender and found that it is described under <http://aanbestedingskalender.nl/aankondigingen/detail/download-document/484831/pdf>, retrieved on 09 November 2015.

⁴⁶² Canon indicated that it does not sell stationery products in its reply to Phase I Questionnaire Q1 to competitors (contract) – Question 2.

⁴⁶³ RBB Economics, "Relevance of bidding data for the competitive assessment", dated 18 May 2015, Table 16.

⁴⁶⁴ Papyrus' reply to Phase II Questionnaire Q10 to Specialists – Question 2.

⁴⁶⁵ <http://www.wijgelderland.nl/nieuws-overzicht/king-nederland-uit-tiel-wint-opdracht-defensie-materieel-organisatie/>, retrieved on 9 November 2015.

⁴⁶⁶ See for example slide 9 of the presentation of the Parties in "Case COMP/M.7555 – Staples/Office Depot State of Play Meeting, 06 November 2015."

specifically as regards stationery. If a limited competitive pressure may exist on certain product categories (particularly ink & toner and paper) because of the possibility to obtain those supplies from specialists, such possibility does not exist for stationery, so that the competition concerns could only be aggravated for this product category separately. Indeed, the specialist suppliers participating in tenders in the Netherlands (for instance Canon, Papyrus, King) do not offer stationery products.

- (537) An additional finding concerns the effective possibility of companies active in neighbouring markets, as well as specialist suppliers, to expand to stationery. When responding to the market investigation, paper and MPS specialists stressed that they have a different business focus and no interest in expanding into the distribution of stationery. They also mentioned as a barrier to expansion the specificities of the logistics arrangements required to distribute stationery products. Other suppliers active in neighbouring markets such as cleaning companies, IT suppliers, etc. may have some stationery sales. However, those are add-ons to orders for other items on which they specialise.

7.2.7.3. Conclusion on Netherlands – Stationery only

- (538) On the basis of the above, the Commission concludes that the transaction would lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in the Netherlands.

7.2.8. Austria - Traditional office supplies

7.2.8.1. Market structure

7.2.8.1.1. The views of the Notifying Party

- (539) According to the Notifying Party, the transaction will not give rise to competition issues in the Austrian market. The Notifying Party submits that the contract market in Austria is very competitive with several strong rivals to the Parties, including Lyreco and local suppliers.
- (540) According to the Notifying Party, the top five competitors to the Parties in the contract market in Austria are Büro Handel, Lyreco, Tekaef, Pagro (former e-Plus) and Bürobedarf Strein.⁴⁶⁷ Other suppliers mentioned as important competitors are A. Reinhart and Schäfer Shop.⁴⁶⁸ The Notifying Party claims that several of those competitors have the same capabilities as the Parties, including a full range of supplies.⁴⁶⁹ Further, Pagro, Horn, Kaut Bullinger and Tekaef have all won tenders with a value above EUR 100 000 that were lost by Staples.⁴⁷⁰
- (541) The Notifying Party submits that Office Depot has negligible activities in the contract business in Austria with 2014 revenues of only EUR [...]. Staples' contract revenues were EUR [...] while, according to the Parties' estimates, the Austrian

⁴⁶⁷ Contact details provided in response to the request for information of 5 October 2015 – National contracts (part 2) and to the request of information of on 8 October 2015..

⁴⁶⁸ See for example slide 6 of the presentation of the Parties in "Case COMP/M.7555 – Staples/Office Depot State of Play Meeting, 08 October 2015".

⁴⁶⁹ See the Parties' note on Customer Requirements and Competitor Capabilities, table 4.

⁴⁷⁰ Response to the Article 6(1)(c) Decision, footnote 13.

revenues of Büro Handel and Lyreco are EUR [...] million and EUR [...] million respectively.⁴⁷¹

7.2.8.1.2. The Commission's assessment

- (542) Based on the results of the market investigation, the Commission considers that there are indeed several suppliers active on the contract market in Austria.
- (543) As stated by the Notifying Party, Büro Handel is the market leader in Austria and has a total turnover of more than EUR [...] million in the contract business in Austria.⁴⁷² Although its turnover for only traditional office supplies is lower than that, Büro Handel is the clear market leader in Austria also in the traditional office supplies category.
- (544) Following an assessment of the sales data provided by the Parties, Staples appears to be the second largest supplier in the contract market in Austria with a total turnover of EUR [...] for the national customers. Office Depot's total turnover in Austria for the national customers is very low compared to the two largest suppliers with less than EUR [...].⁴⁷³ Consequently, the combined total turnover of the Parties achieved through contract sales to national customers in Austria is less than EUR [...], reaching not even half of Büro Handel's turnover. The results of the market investigation showed further that the Parties' turnover estimate for Lyreco was exaggerated.
- (545) Thus, the market seems to be characterised by the presence of the two strong suppliers Büro Handel and Staples (of which Büro Handel is the clear market leader) and a number of smaller suppliers (including Office Depot, Lyreco and a number of local suppliers).

7.2.8.2. Competitive constraints exerted by the Parties on each other

- (546) The market structure outlined in section 7.2.8.1 indicates that Office Depot may not compete closely with Staples in the Austrian market for contracts. This is supported by the bidding data submitted by Staples as shown in Table 15.

Table 15: Tenders lost by Staples in Austria

[...]

Source: Bidding data from the report RBB Economics: "Relevance of bidding data for the competitive assessment", dated 18 May 2015.

- (547) The large number of unknown winners makes it difficult to draw firm conclusions from Staples' bidding data. Nevertheless, the majority of tenders lost by Staples which were not won by unknown suppliers were won by Lyreco and Büro Handel, indicating that they are closer competitors to Staples than Office Depot.
- (548) Büro Handel's strong position on the Austrian market is supported by Lyreco's reply to the Commission's questionnaire in which Büro Handel was listed as the closest

⁴⁷¹ Form CO, paragraph 187.

⁴⁷² Turnover information available on the website of Büro Handel, <http://www.buerohandel.net/BHAT/firmeninfo/zahlen-fakten>, (last accessed on December 15, 2015). See also agreed minutes of the conference call with Büro Handel, 8 September 2015.

⁴⁷³ See the Parties' reply of 22 December 2015 to requests for information on contract sales data.

competitor to Staples. Takaef, Pagro, Office Depot and Lyreco are mentioned as other important competitors.⁴⁷⁴

- (549) Büro Handel has confirmed that it is indeed the market leader in Austria. Its business focuses on sales to customers with more than 100 office workers and its contract portfolio includes contracts with annual sales of more than EUR [...] million. Its strong position on the Austrian market is explained by advantages in terms of service and flexibility.⁴⁷⁵ Customers of the Parties generally confirm Büro Handel's strong position, mentioning it as a viable alternative to their current supplier.⁴⁷⁶
- (550) In addition to the competition from Büro Handel, the Parties also compete with Lyreco and smaller regional suppliers in Austria which were listed by some customers and competitors in their replies to the Commission's market investigation.⁴⁷⁷ One of those customers stated that: "*.. there are enough suppliers in the Austrian market, including Buerohandel GmbH, A. Reihard, Schaefer Shop, Tekae and E-Plus.*"⁴⁷⁸

7.2.8.3. Competitive conditions following the transaction

- (551) The Parties will continue to compete with the market leader Büro Handel as well as with Lyreco and smaller suppliers in Austria following the transaction.
- (552) The competitors on the Austrian market do not express particular concerns about the transaction.⁴⁷⁹ One competitor highlighted the fact that the transaction would create a new supplier with more market power than before but also states that it cannot foresee whether the transaction will lead to positive or negative effects on its business.⁴⁸⁰ Similarly, the vast majority of customers did not express any concerns about the transaction for non-international contracts in Austria.⁴⁸¹

7.2.8.4. Conclusion on Austria

- (553) In the light of the above, the Commission concludes that the transaction does not lead to a significant impediment to effective competition in the market for the distribution of office supplies through contracts to large business customers in Austria.

7.2.9. Austria - Stationery only

- (554) The structure of the market and the effects of the transaction as described in section 7.2.8 are not materially different when assessing the market for supply of stationery products only.
- (555) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility of obtaining those supplies

⁴⁷⁴ Lyreco's replies to Phase I Questionnaire Q1 to competitors (contract), Questions 38 and 39.

⁴⁷⁵ Agreed minutes from conference call with Büro Handel.

⁴⁷⁶ Replies to Phase I Questionnaire Q4 to customers (contract) – Questions 29 and 30; replies to Phase II Questionnaire Q8a to Customers (Austria) – Question 48. See further e-mail from a customer of 1 September 2015 and agreed minutes of conference calls with a customer of 15 July 2015.

⁴⁷⁷ Replies to Phase I Questionnaire Q4 to customers (contract) – Questions 29 and 30; replies to Phase II Questionnaire Q8a to customers (Austria) – Question 48. See further e-mail from a customer of 1 September 2015 and agreed minutes of conference calls with a customer of 15 July 2015.

⁴⁷⁸ Agreed minutes of conference call with a customer of 15 July 2015.

⁴⁷⁹ Agreed minutes of conference call with a competitor of 8 September 2015; replies to Phase I Questionnaire Q1 to competitors (contract) – Questions 62-63.1.

⁴⁸⁰ Agreed minutes of conference call with a competitor of 8 September 2015.

⁴⁸¹ Replies to Phase I Questionnaire Q4 to customers (contract) – Questions 51-52 and to Phase II Questionnaire Q8a to Customers (Austria) – Questions 52-53.1.

from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.

- (556) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Austria.

7.2.10. *Belgium - Traditional office supplies*

7.2.10.1. Market structure

7.2.10.1.1. The views of the Notifying Party

- (557) According to the Notifying Party, the Parties are small suppliers in Belgium with 2014 contract revenues of only EUR [...] and EUR [...] respectively. Lyreco is by far the market leader in Belgium with estimated revenues of EUR [...], while there are other suppliers present in the market such as Manutan, AB Supplies and Fiducial with estimated revenues of EUR [...], EUR [...] and EUR [...], respectively. In addition, the Parties argue that there are a large number of smaller local suppliers, like Otto Office, Interoffice, Pandava and Deroanne, who can equally exert competitive constraints over the Parties.⁴⁸²

- (558) The Notifying Party, in its Response to the Article 6(1)(c) Decision underlined Lyreco's leading position as well as the existence of other local suppliers who are able to win large contracts including Deroanne and AB Supplies. The Notifying Party in its note on customer requirements and competitor capabilities⁴⁸³ restated that Fiducial, Manutan, AB Supplies and Deroanne all have the capabilities required to supply large customers.⁴⁸⁴

7.2.10.1.2. The Commission's assessment

- (559) According to the results of the Commission's market investigation some of the suppliers named by the Parties as competitors are in fact not active in the market for contract sales of office supplies to customers of more than 100-200 office workers or 250 employees.

7.2.10.1.2.1. *Suppliers not active in the relevant market*

- (560) Manutan is present in 18 EEA countries, including Belgium. Manutan's business model is based on offering a wide range of product categories, aiming at providing all the products its clients need, and is focused on equipment and consumables to industrial clients. Although Manutan sells the entire range of office supplies (stationery, paper, ink & toner) through contracts, it offers much fewer SKUs, office supplies representing only 5% of Manutan's overall turnover generated through the contract distribution channel. Manutan claims that it does not consider itself to be a competitor of the Parties, because of their different approach and business strategy. Whereas the Parties specialise in office supplies, Manutan's competitive advantage is

⁴⁸² Form CO, paragraph 187.

⁴⁸³ Note on customer requirements and competitor capabilities, submitted by the Notifying Party on 25 October 2015.

⁴⁸⁴ Note on customer requirements and competitor capabilities, submitted by the Notifying Party on 25 October 2015, table 12 and paragraph 43.

the width of its product categories range, without being specialised in any product category in particular. According to Manutan, customers that switch from Manutan do not go to Staples or Office Depot. Manutan's direct competitors are Raja, Kaiser and Kraft and JM Bruno. The Parties could be considered Manutan's partners, as Manutan buys and sells some of their products. For example, Manutan sources certain products (such as office furniture) from Staples, which it then sells to its customers. In short, Manutan offers its customers all they need (not just the office supplies), and therefore it targets a different customer group. If the customers only need office supplies they would generally go directly to the Parties.⁴⁸⁵

- (561) Other suppliers like Otto Office, Interoffice, Pandava, and AB Supplies which specialises in consumables informatics for companies' IT needs, are not considered to be active in the market for non-international contracts with customers with more than 250 employees. Deroanne stated that AB Supplies can be considered as a competitor only in relation to ink & toner, but not in relation to stationery and cut sheet paper.

7.2.10.1.2.2. *Competitive Landscape*

- (562) According to the results of the market investigation, apart from the Parties, Lyreco, Deroanne and Fiducial offer the full range of traditional office supplies (stationery, paper, ink & toner) in Belgium in the market for non-international contracts with customers with more than 250 employees. However Deroanne and Fiducial are lagging behind compared to the Parties and Lyreco.
- (563) Deroanne, as the Parties claim, is a small local supplier in Belgium. Deroanne provides the full range of office supplies (stationery, paper, ink & toner) through contracts.⁴⁸⁶ However, Deroanne states that large business customers (with more than 100-200 office workers) in the contract business have special requirements in comparison with smaller business customers, namely they demand significant rebates, they require national coverage, they require uniform national pricing, and their tenders are more complex and place a high administrative burden on participating.⁴⁸⁷ For this reason Deroanne targets customers that have less than 50 office workers, customers with 50-100 office workers, and customers with 100-200 office workers.⁴⁸⁸ Deroanne has a nationwide presence in Belgium⁴⁸⁹ and according to Deroanne, 30% of its contracts have national coverage.⁴⁹⁰ Deroanne also claims that it is able to compete with its three largest competitors in office supply tenders in terms of pricing only to a certain extent.⁴⁹¹ Finally, Deroanne won three tenders with large customers in 2014.⁴⁹² Deroanne therefore is active in the market for non-international contracts with customers with more than 250 employees, but it is a very small supplier compared to the Parties and Lyreco.
- (564) Fiducial is a large French supplier that recently entered the Belgian market - an exception that is not observed in other markets. Fiducial has a nationwide presence.⁴⁹³ It targets large-size corporate customers, of more than 1000 office workers, and it is capable of supplying those customers with contracts of an annual

⁴⁸⁵ Non-confidential minutes of a conference call with a competitor, 5 November 2015.

⁴⁸⁶ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 2.

⁴⁸⁷ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 19.1.

⁴⁸⁸ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 17.

⁴⁸⁹ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 29.

⁴⁹⁰ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 27.

⁴⁹¹ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 36.

⁴⁹² Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 37.2.

⁴⁹³ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 29.

spending of more than EUR 1 million per annum.⁴⁹⁴ Fiducial is smaller than Lyreco and the Parties but still a significant competitor.

- (565) Based on data submitted by the Notifying Party, Staples' sales under contract in Belgium amounted to approximately EUR [...] in 2014 while Office Depot's sales amounted to approximately EUR [...]. For large customers, Staples' sales in 2014 amounted to EUR [...] and Office Depot's sales in 2014 amounted to EUR [...] respectively.⁴⁹⁵

Table 16: Parties' sales of traditional office supplies through contracts in Belgium, EUR 000s

Category	Party	All customers	Large customers
<i>Traditional office supplies</i>	<i>Staples</i>	[...]	[...]
Stationery	Staples	[...]	[...]
Ink & toner	Staples	[...]	[...]
Paper	Staples	[...]	[...]
<i>Traditional office supplies</i>	<i>Office Depot</i>	[...]	[...]
Stationery	Office Depot	[...]	[...]
Ink & toner	Office Depot	[...]	[...]
Paper	Office Depot	[...]	[...]

Source: Parties' replies of 22 December 2015 and 7 January 2016 to requests for information on contract sales data.

- (566) Lyreco is currently the leading supplier in Belgium followed by the Parties. Fiducial comes next followed by Deroanne.
- (567) The transaction would thus combine the second and third largest suppliers in terms of revenues in the Belgian contract market. It would reinforce Staples' current position as the second largest supplier followed by Fiducial and Deroanne at a significant distance.

7.2.10.1.3. Conclusion

- (568) On the basis of the above, only Staples, Office Depot, Lyreco, Fiducial and Deroanne are active competitors in the Belgian market for the distribution of office supplies through contracts to customers of more than 100-200 office workers or 250 employees. The transaction would bring together the second and third largest suppliers in a concentrated market with only five competitors of which Fiducial and Deroanne are weaker than the Parties.

7.2.10.2. Competitive constraints exerted by the Parties on each other

- (569) According to the results of the market investigation Staples and the market leader, Lyreco, are close competitors. Customers of the Parties who responded in the market

⁴⁹⁴ Replies to Phase I Questionnaire Q1 to competitors (contract) – Question 17.
⁴⁹⁵ RFI of 22/12/2015 and RFI 07/01/2016.

investigation all stated that Lyreco always participated in their tender, submitting a bid, or won part of the contract.⁴⁹⁶

- (570) The Commission reviewed data submitted by the Parties on tenders for office supplies for 2012-2014, focusing on Enterprise customers only, as well as the Parties' bidding data analysis which included all customer types. It emerges from both the Parties' submission on tender data as well as the Commission's analysis focusing only on Enterprise customers only that in Belgium Lyreco and Staples are the main competitors in traditional office supplies, with Office Depot being a small third competitor.
- (571) Tables 15 and 16 are reproduced from the Parties' submission "Relevance of bidding data for the competitive assessment", dated 18 May 2015 (see Tables 9 and 10 in that submission), including tenders involving all customers. Fiducial and Deroanne show as winners only occasionally.

Table 17: Tenders lost by Staples in Belgium, all customers

[...]

Table 18: Tenders lost by Office Depot in Belgium, all customers

[...]

- (572) Given the importance of Staples in Belgium and the smaller importance of Office Depot (see recital (557)), Staples' bidding data are the most important for the competitive assessment. This allows for an assessment of the competitive constraint that Office Depot exerts on Staples.
- (573) The bidding data confirms Lyreco's strong position in Belgium. As regards the tenders where Staples participated and lost, Lyreco is the main winner, representing [90-100]% of the tender value lost by Staples. Focusing on Staples' lost tenders involving Enterprise customers only conveys a similar picture. Out of [...] such tenders, Lyreco won [...], corresponding to [90-100]% of value. Office Depot won only [...] tenders from those Staples lost, amounting to [0-5]% in terms of value.
- (574) Therefore, the Commission considers that competition in Belgium for contracts with large customers mainly exists between Staples and Lyreco, with Office Depot exerting more limited competitive pressure on Staples followed by Fiducial and Deroanne.

7.2.10.3. Competitive conditions following the transaction

- (575) The Parties will continue to compete with the market leader Lyreco, the new entrant Fiducial and to a lesser extent Deroanne. Due to limited turnover of Office Depot and its limited importance as a competitive constraint to Staples, the transaction would not result in significant changes to the competitive landscape in Belgium.

7.2.10.4. Conclusion on Belgium

- (576) In the light of the above, the Commission concludes that, while the market for the distribution of office supplies through contracts to large business customers in Belgium is concentrated, the transaction would not lead to a significant impediment to effective competition because of Office Depot's limited market position and the new entrant Fiducial.

⁴⁹⁶

Replies to Phase II Questionnaire Q8b to customers (Belgium) – Question 8.

7.2.11. *Belgium - Stationery only*

- (577) The structure of the market and the effects of the transaction as described in the previous section 7.2.10 are not materially different when assessing the market for supply of stationery products only.
- (578) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.
- (579) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Belgium.

7.2.12. *France - Traditional office supplies*

7.2.12.1. Market structure

7.2.12.1.1. The views of the Notifying Party

- (580) According to the Notifying Party, Office Depot is one of the leading suppliers in France (with overall contract revenues of EUR [...]) alongside Lyreco and Fiducial, while Staples is by far the smallest of the four with overall contract revenues of [...].⁴⁹⁷ Staples has reduced its contract business in France notably over the recent years due to declining sales of almost [...] between 2011 and 2014.⁴⁹⁸ The Notifying Party claims that it is unable to exert a competitive constraint on the three leading suppliers and that [...]. The Notifying Party further notes that it is not even shortlisted for the majority of held tenders in France.⁴⁹⁹
- (581) According to the Notifying Party, the strongest competitors for traditional office supplies to the Parties in the contract market in France are Lyreco and Fiducial to which Office Depot lost several tenders in 2013 and 2014 with a value above EUR 1 million. Other important competitors are Dactyl Buro Office, Manutan, Raja, Inapa, Osilog, Alter Bureau, BURO+, Majuscule and Officexpress. The Notifying Party claims that several of those competitors have the same capabilities as the Parties, including a full range of supplies.⁵⁰⁰ Further, Majuscules, Osilog, Officexpress and Buro+ have all won tenders with a value above EUR 100 000 that were lost by Staples.⁵⁰¹ According to the Notifying Party, Raja, who is currently the European leader in mail, shipping and packing supplies, is also active in traditional office supplies and plans to expand the segment in the near future.⁵⁰²
- (582) As a result, the Notifying Party submits that the transaction will not give rise to any competition issues in the French market.

⁴⁹⁷ Form CO, paragraph 187.

⁴⁹⁸ Form CO paragraph 45 and footnote 4.

⁴⁹⁹ Form CO, paragraph 187.

⁵⁰⁰ See Form CO, paragraph 301. See further the Parties' note on Customer Requirements and Competitor Capabilities, table 6.

⁵⁰¹ Response to the Article 6(1)(c) Decision, footnote 15.

⁵⁰² Form CO, paragraph 301.

7.2.12.1.2. The Commission's assessment

- (583) The Commission's assessment, based on the results of the market investigation, showed that there are indeed several suppliers active on the contract market in France.⁵⁰³
- (584) As stated by the Notifying Party, the results of the market investigation showed that Lyreco is the clear market leader in France. Office Depot appears to be the second largest supplier in contract sales in France with a total turnover of approximately EUR [...] for the national customers.⁵⁰⁴ Fiducial, who is also a large supplier in the French contract market, appears to be a strong number three. Based on data submitted by the Parties, Staples' total turnover in France for the national customers is very low compared to the three largest suppliers at less than EUR [...].⁵⁰⁵
- (585) The French market appears to be characterised by the presence of the three strong suppliers Lyreco, Office Depot and Fiducial along with a number of smaller suppliers (Staples and others).

7.2.12.2. Competitive constraints exerted by the Parties on each other

- (586) The market structure outlined in section 7.2.12.1 indicates that Staples may not compete closely with Office Depot in the French market for contracts. This is supported by the bidding data submitted by Staples as shown in Table 19. Given the importance of Office Depot in France and the significantly smaller importance of Staples (see recital (585)), Office Depot's bidding data are the most important for the competitive assessment. This allows for an assessment of the competitive constraint that Staples exerts on Office Depot.

Table 19: Tenders lost by Office Depot in France

[...]

- (587) The bidding data from Office Depot shows that the vast majority of tenders lost by Office Depot are won by Lyreco or Fiducial, indicating that they are closer competitors to Office Depot than Staples. Staples only won a small number of tenders from Office Depot alongside national suppliers like Majuscule and Officexpress.
- (588) The strong market position of the three largest suppliers in France is supported by Lyreco's and Fiducial's replies to the Commission's questionnaire in which they both list each other as Office Depot's closest competitors.⁵⁰⁶
- (589) Fiducial confirms that it is a strong competitor in the French market. Its business targets customers of all sizes, even those with more than 1000 office workers, and wins a large number of the tenders for those large customers. This is supported by the fact that Fiducial has at least [...] contracts with a value above EUR 1 million.⁵⁰⁷ In addition, Fiducial has aspirations of expanding its business beyond the countries in which it is currently present (France, Belgium and Luxembourg).⁵⁰⁸

⁵⁰³ Lyreco's and Fiducial's replies to Phase I Questionnaire Q1 to competitors (contract) – Question 38.

⁵⁰⁴ See the Parties' reply of 22 December 2015 to requests for information on contract sales data.

⁵⁰⁵ *Idem.*

⁵⁰⁶ Lyreco's and Fiducial's replies to Phase I Questionnaire Q1 to competitors (contract) – Question 40. See further agreed minutes of conference call with Lyreco of 22 October 2015.

⁵⁰⁷ Fiducial's replies to Phase I Questionnaire Q1 to competitors (contract) – Questions 17, 37.1 and 40 and replies to Phase II Questionnaire 9 to competitors (contract stationers) – Question 5.

⁵⁰⁸ Agreed minutes from conference call with a competitor of 16 October 2015.

(590) In addition to the competition from Lyreco and Fiducial, the Parties also compete with smaller suppliers in France which were listed by some customers and competitors in their replies to the Commission's market investigation.⁵⁰⁹

7.2.12.3. Competitive conditions following the transaction

(591) The Parties will continue to compete with the market leader Lyreco and with Fiducial as well as the smaller suppliers in France following the transaction. Due to limited turnover of Staples, the transaction would not result in significant changes to the competitive landscape in France.

(592) One competitor stated that the transaction could lead to lowered prices and lowered service levels.⁵¹⁰ As regards the first point, the Commission does not perceive lower prices in the French market for office supplies as a negative impact in itself. As regards the second point, the Commission finds that the impact of any potential degradation of the service of the Parties would be offset by the customers' option to change to one of the two strong competitors in France. None of the French, non-international customers who participated in the Commission's market investigation expressed any concerns about the transaction.⁵¹¹

7.2.12.4. Conclusion on France

(593) In the light of the above, the Commission concludes that the transaction would not lead to a significant impediment to effective competition in the market for the distribution of office supplies through contracts to large business customers in France.

7.2.13. France - Stationery only

(594) The structure of the market and the effects of the transaction as described in the previous section 7.2.12 are not materially different when assessing the market for supply of stationery products only.

(595) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery is neutral to the assessment.

(596) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in France.

⁵⁰⁹ Replies to Phase I Questionnaire Q4 to customers (contract), Questions 29 and 30; replies to Phase II Questionnaire Q8e to Customers (France) – Question 48. Lyreco's and Fiducial's replies to Phase I Questionnaire Q1 to competitors (contract) – Questions 38, 39 and 40 and to Phase II Questionnaire 9 to competitors (contract stationers) – Question 9.6.

⁵¹⁰ Replies to Phase I Questionnaire Q1 to competitors (contract) – Questions 62-63.1.

⁵¹¹ Replies to Phase I Questionnaire Q4 to customers (contract) – Questions 50-51.1 and to Phase II Questionnaire Q8e to Customers (France) – Questions 52-53.1. See further agreed minutes of a conference call with a customer of 25 November 2015.

7.2.14. Germany - Traditional office supplies

7.2.14.1. Structure of the market

7.2.14.1.1. The views of the Notifying Party

- (597) The Notifying Party submits that the German market is characterised by a large number of competitors active in the supply of traditional office products through contracts to large business customers.
- (598) The Notifying Party indicates that⁵¹² aside from Lyreco, the Parties face competition from several companies, the most significant of which are Kabuco (Kaut Bullinger), Plate, Soennecken, MGW (Marketing Gruppe West), Bechtle, Horm and MUP.
- (599) In a further submission relating more specifically to full range contract suppliers,⁵¹³ the Notifying Party lists competitors in Germany by order of estimated turnover in the contract supply of full range office products. According to those estimates, the main competitors in order of estimated turnover would be Soennecken, Lyreco, MGW, Plate, Büro Mix, Kaut Bullinger, Buerohandel, Brüggershemke & Reinkemeier, Buerobedarf Haensel.

7.2.14.1.2. The Commission's assessment

- (600) The results of the Commission's market investigation confirmed the existence of a number of suppliers offering traditional office products through the contract channel in Germany. However, their presence and activity on the relevant market may have been overestimated by the Parties.
- (601) First, because of the general methodological approach discussed in section 7.2.1.1, the total size of the German market, as estimated by the Parties appears to overstate contract sales of traditional office supplies. The estimate of a full range contract market exceeding EUR 2.5 billion led the Parties to attribute a very significant part of such revenues (almost two thirds, equivalent to 1.6 billion) to other suppliers than the ones for which they were able to estimate a turnover.
- (602) Second, the Commission was able to obtain actual turnover figures for the sales of several of the Parties' competitors in the relevant market in Germany. Those figures are provided in an aggregated non-confidential version in the Table 20.

Table 20 Turnover of the Parties and their competitors in the relevant market in Germany

Company Name	Turnover	Turnover
	(Notifying Party's estimate)	(Data from Phase II investigation)
	In million EUR	In million EUR
Staples	[...]	[...]
Office Depot	[...]	[...]
Combined	[...]	[...]
Soennecken	[...]	
Lyreco	[...]	

⁵¹² Form CO, paragraph 187.

⁵¹³ Notifying Party's submission: 'Market shares of full range contract suppliers'. Table 4.

Company Name	Turnover (Notifying Party's estimate) In million EUR	Turnover (Data from Phase II investigation) In million EUR
MGW	[...]	
Plate	[...]	
Büro Mix	[...]	
Kaut Bullinger	[...]	
Total 6 largest competitors	870	201 - 350
Buerohandel	[...]	n.a.
Brüggershemke & Reinkemeier	[...]	n.a.
Buerobedarf Haensel	[...]	n.a.
Others	1,600	n.a.

- (603) The range provided in the table is based on possible alternative interpretations of the data received. In particular, some competitors provided both a figure for total contract sales as well as a figure for contract sales to large customers. In view of the difficulty to obtain specific information about the definition of what some of the competitors identified as 'large' contract customers, the upper range, which is the more favourable to the Parties, is calculated by adding total contract sales as reconstructed by the Commission. The upper estimate also takes into account of estimates of total sales for the cooperatives when those are higher than the sum of reconstructed sales of their members. Even in this hypothesis, the Parties appear to have largely overestimated contract sales of their competitors.
- (604) Aside from an overestimation of the sales⁵¹⁴ (or of the contract portion of competitors' sales) the Commission found that the turnover of cooperatives as reconstructed by the Parties may have included turnover of members of those cooperatives, which was also attributed to members themselves. For instance, among the six largest competitors indicated by the Parties, Büro Mix is a member of MGW, while Plate and Kaut Bullinger are members of Soennecken.
- (605) During Phase II the Commission obtained a breakdown of the Parties' sales enabling it to calculate the sales made by the Parties within the relevant market, as detailed in Table 21.

⁵¹⁴ The size of the market is also inflated by the fact that the Parties' own sales include sales to international customers, and so do the sales data attributed to the other competitor active internationally, i.e. Lyreco. In particular, when calculating sales on the basis of a break-down provided by the Parties which distinguishes national and international sales, and only reports sales to large customers (see Reply to RFI of 6 January 2016), aggregated national sales of traditional office supplies would amount to approximately EUR [...] for Staples, and EUR [...] for Office Depot.

Table 21: Parties' sales of traditional office supplies through contracts in Germany, EUR 000s

Category	Party	All customers	Large customers
<i>Traditional office supplies</i>	<i>Staples</i>	[...]	[...]
Stationery	Staples	[...]	[...]
Ink & toner	Staples	[...]	[...]
Paper	Staples	[...]	[...]
<i>Traditional office supplies</i>	<i>Office Depot</i>	[...]	[...]
Stationery	Office Depot	[...]	[...]
Ink & toner	Office Depot	[...]	[...]
Paper	Office Depot	[...]	[...]

Source: Source: Parties' replies of 22 December 2015 and 7 January 2016 to requests for information on contract sales data.

7.2.14.1.3. Conclusion

(606) In conclusion, the Parties and Lyreco are the three most significant competitors on the traditional office supplies market through non-international contracts to large business customers in Germany. The Commission's assessment, based on the results of the market investigation, confirmed that a number of competitors are active within the contract supply of traditional office products to large business customers in Germany. However, their significance has largely been overestimated by the Notifying Party. However, there are up to six smaller contract stationers active on the German market whose sales have been verified with significant market presence.

7.2.14.2. Competitive constraints exerted by the Parties on each other

7.2.14.2.1. Qualitative evidence from the market investigation

(607) Within the market investigation, customers provided data on the bids they received for their most recent tender on traditional office supplies. The competitors most frequently submitting bids, according to customers' replies, were Lyreco and the Parties.⁵¹⁵ Customers reported in much fewer instances of other contract stationers or specialist suppliers. This is partly in line with the result of the bids which will be further analysed in section 7.2.14.2.2.

(608) Customers also provided feedback on the main criteria they assess when selecting their contract suppliers, and on which available suppliers can satisfy those criteria. Replies almost exclusively indicated Staples, Lyreco and Office Depot as suppliers capable of satisfying customer expectations on criteria such as size of portfolio, ability to provide all traditional office products and logistic capabilities.⁵¹⁶ Other

⁵¹⁵ Replies to Phase II Questionnaire Q8c – and replies from German customers to Phase II questionnaires Q8a, Q8b, Q8d, Q8e, Q8f, Q8g, Q8h, Q8i, Q8j – Question 8.

⁵¹⁶ Replies to Phase II Questionnaire Q8c – and replies from German customers to Phase II questionnaires Q8a, Q8b, Q8d, Q8e, Q8f, Q8g, Q8h, Q8i, Q8j – Question 10.

competitors such as Soennecken, Kaut Bullinger, MGW, Schwendy were only mentioned in single instances.

- (609) The findings of recitals (607) and (608) do not materially change when focussing only on purely national customers, that is customers that the Parties do not supply through an international contract or that they do not target as potential international contract customers.
- (610) In order to obtain a proxy for the Parties' strength on the market for non-international contracts with large business customers in Germany, the Commission asked the parties to provide information on the number of firms within Germany's TOP 100 employers that are supplied by the Parties. The information was verified with similar information provided by six of the competitors identified by the Parties.
- (611) Together, the Parties would supply all the three categories of traditional office supplies to more than [50-60] of the top 100 German employers ([50-60] for Stationery, [50-60] for Paper, and [50-60] for Ink & Toner). [80-90]% of those customers buy all three categories of traditional office supplies together from either of the Parties. Moreover, around [80-90]% of those customers do not buy any traditional office product from any other of the competitors which submitted information.
- (612) When excluding international customers from the assessment,⁵¹⁷ the position of the Parties is not materially different. Of the 60 national customers in the data, the Parties supply approximately [50-60]% (i.e. [30-40]); Lyreco indicated that it supplies [...] of the 60 national customers identified, whereas data from the remaining 6 competitors indicate they supply only 10% of those customers (i.e. [...]).⁵¹⁸ However, an important part of the sample (approximately 30%) is not covered by any of the competitors replying within the Top 100 employers exercise. This may indicate that other suppliers that did not reply, even if smaller, are active within the relevant market.
- (613) The strength of the Parties and Lyreco within the market for non-international contracts with large business customers in Germany can be explained by a number of factors.
- (614) First, some of the competitors replying to the market investigation indicated that they do not target or have few customers among large German companies (above 250 employees). One of the competitors identified among the largest competitors by turnover by the Parties expressly indicated that "[competitor] is particularly strong in business with customers with up to 20-100 office employees."⁵¹⁹ Another of those competitors clarified that the majority of its customers have less than 250 employees.⁵²⁰

⁵¹⁷ The Commission excluded those of the top 100 German employers which currently have international contracts in place with the three suppliers that are currently able to offer international contracts: Staples, Office Depot and Lyreco, or that are targeted as potential international customers by the Parties. The source of this information is the document provided by the Notifying Party as Annex 23 to the Form CO and the information provided by Lyreco in its reply of 29.10.2015 to the Commission's request for information on the top 100 customers.

⁵¹⁸ The gross total of entries by competitor is higher than 60 as there are overlap, i.e. certain customers which purchase from more than one supplier.

⁵¹⁹ Agreed minutes of a call with a competitor of 9 September 2015 '[company] ist besonders stark im Geschäft mit Kunden mit bis zu 20 oder bis zu 100 Büromitarbeitern'.

⁵²⁰ Agreed minutes of a call with a competitor of 6 November 2015.

- (615) Second, even those competitors who have large non-international contract customers in Germany point at a competitive advantage of the Parties and Lyreco because they can source significant volumes and thus offer prices that cannot be matched by smaller competitors. For instance, one of the competitors identified by the Parties among their main competitors indicated that largest competitors reported that *'when it comes to price, then Staples, Office Depot and Lyreco can offer lower prices and are therewith very hard to beat. This is because of the high volumes purchased by those companies from the manufacturers. This equally holds irrespective of the customers' purchasing strategy (national vs. international).'*⁵²¹
- (616) Third, because of their size, the range of traditional office supplies on offer and the geographic coverage, the Parties and Lyreco closely compete with each other, as opposed to smaller national or local suppliers in Germany.

7.2.14.2.2. Bidding Data

- (617) The Commission assessed tender data provided by Staples for traditional office supply products in Germany. Office Depot did not provide bidding data for Germany. While the analysis of Staples' tender data is broadly in line with the results of the market investigation, the Commission considers that bidding data provided for Germany should be interpreted cautiously for the following reasons.
- (618) First, tenders with unknown winners constitute a very large proportion of tenders in the data. In stationery, [...] of wins (corresponding to [...] of the total value won) are labelled as "unknown". Second, the assumption proposed by the Notifying Party to split the value won equally between winners in tenders involving multiple winners can affect the value shares won by the Parties and Lyreco.⁵²² In the bidding data for Germany, this assumption frequently allocates a significant values won to unknown bidders.
- (619) During its investigation, the Commission contacted customers in tenders where the winner was indicated as unknown. This resulted in replies from seven customers, and revealed that in four high-value tenders where the data showed Office Depot to have won together with an unknown winner, Office Depot was in fact the only winner. For the remaining three tenders, customers clarified that Office Depot was not the winner. There is hence significant uncertainty stemming from the allocation of wins and associated values, in particularly where the winner is claimed to be unknown.
- (620) From Staples' tender data, it emerges that Office Depot and Lyreco appear to participate most frequently against Staples. Staples participated in [...] tenders involving Enterprise customers and covering at least one of three traditional office supplies, and won [...] of these. Lyreco participated in [...] and Office Depot in [...] of these [...] tenders. The next supplier is significantly behind Office Depot with only [...] participations. The Commission notes that [...] tenders include another participant coded as "unknown".
- (621) Looking at the tenders in which Staples participated but lost, Lyreco wins [...] of the tenders lost by Staples, corresponding to [...] in value. In contrast, Office Depot is significantly behind, by winning [...] of the tenders lost by Staples, corresponding to [...] in value. The winner is unknown in [...] of tenders, corresponding to [...] of

⁵²¹ Agreed minutes of a call with a competitor of 28 October 2015.

⁵²² As explained in Footnote 258, a single procurement process can have multiple winners and cover several product categories. The term "tender" refers to the number of supply contracts awarded in each product category.

value. The remaining tenders were won by more than [...] suppliers, none of which individually comes close to Office Depot in terms of number of tenders or value won. Allocating values won to these firms is furthermore made difficult by the fact that on occasions larger tenders were won jointly by multiple firms, where a precise split of value won was not possible (see footnote 257).

- (622) Ignoring tenders with unknown winners, the share of Lyreco and Office Depot on tender value lost by Staples was respectively [...] and [...], and in terms of tenders won respectively [...] and [...].
- (623) After Office Depot and Lyreco, the next supplier in terms of value stands out as having won large value tenders of EUR [...] across all product categories against Staples. However, nearly all of the value won by this supplier comes from a single large tender involving a public institution as customer, with another supplier as a co-winner. Overall the instances in which firms other than the Lyreco and Office Depot win large value tenders when bidding against Staples are relatively few.
- (624) To conclude, the analysis of Staples' tender data suggests that competition takes place primarily between Staples and Lyreco for Enterprise customers in Germany. Office Depot, while participating frequently in tenders against Staples, achieves a more limited win rate against Staples, suggesting that it exerts a more limited competitive constraint on Staples than Lyreco. Office Depot is nevertheless ahead of a number of smaller competitors who have won a significant number of tenders by Enterprise customers (in full or in part) when bidding against Staples. It also appears that such alternative competitors win large value tenders against Staples only in isolated cases. Moreover, as discussed in recitals (618) and (621), in light of the uncertainty surrounding the bidding data in Germany, and in particular the very large share of unknown winners in the data, its results should be interpreted with caution.

7.2.14.2.3. Conclusion on the competitive constraints exerted by the Parties on each other

- (625) In conclusion, the Commission considers on the basis of the market investigation that Staples and Lyreco are the strongest suppliers, followed by Office Depot, on the German market for non-international contracts. Because of their size, product-range and coverage, those three companies are close competitors on this market.
- (626) A number of other suppliers are active on the relevant market, but the evidence of the market investigation, as well as the bidding data, indicates that each of them lags far behind the Parties in terms of revenues and tenders won, although their turnover may account, taken together, for approximately one third of the relevant market in Germany. This finding would be in line with the results of the analysis of traditional office supplies' spending of the top 100 German employers, if customers that purchase under an international contract are excluded.

7.2.14.3. Competitive conditions following the transaction

- (627) The acquisition of Office Depot by Staples would remove the third supplier on the German market and an existing competitive constraint on Staples and Lyreco alike. This is suggested both by the closeness analysis carried out by the Commission and some replies to the Phase II questionnaires.
- (628) For instance, one national customer with significant spending highlighted that when considering competitors which constrain Staples' strong presence on the market,

'Lyreco, Office Depot, and Soennecken are the only, all others are too small for our purpose'.⁵²³

- (629) However, a number of other elements indicate that while removing a competitive constraint, the transaction would not be likely to create a significant impediment to effective competition.
- (630) First, although Staples, Lyreco and Office Depot compete closely on the German market, the constraint exerted on Staples by Office Depot is less significant than in the case of Sweden and Netherlands.
- (631) Second, the Commission has been able to identify at least six suppliers with a significant market presence on the market, apart from Lyreco and the Parties, although those suppliers lag far behind the three market leaders. In addition, according to the market investigation, there are a number of additional competitors with a track record of supplies of traditional office products under contract to large business customers, for a value that in some cases exceeds EUR 1 million per year,⁵²⁴ and is confirmed by the results of the analysis of the Top 100 data.
- (632) Third, the results of the market investigation suggest that due to its large size, new entries in the German market are more likely than in smaller markets such as the Netherlands and Sweden.
- (633) Finally, as far as customers are concerned, while a majority of the German respondents are concerned about the transaction, this proportion is less than half when only taking into account the respondents to the market investigation who do not purchase under an international contract.⁵²⁵

7.2.14.4. Conclusion on Germany

- (634) In the light of the above, the Commission concludes that the transaction would not lead to a significant impediment to effective competition in the market for the distribution of office supplies through non-international contracts with large business customers in Germany.

7.2.15. Germany - Stationery only

- (635) The structure of the market and the effects of the transaction as described in section 7.2.14 are not materially different when assessing the market for supply of stationery products only.
- (636) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.

⁵²³ Agreed minutes of the call with a customer of 28 August 2015, '*Lyreco, Office Depot, Soennecken sind die einzigen, alle anderen sind zu klein für unsere Zwecke*'.

⁵²⁴ Replies to Phase II Questionnaire Q9 to competitors (contract stationers) – questions 5 and 12, and minutes of conference calls with competitors.

⁵²⁵ Replies to Phase II Questionnaire Q8c – and replies from German customers to Phase II questionnaires Q8a, Q8b, Q8d, Q8e, Q8f, Q8g, Q8h, Q8i, Q8j.

(637) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Germany.

7.2.16. Ireland - Traditional office supplies

7.2.16.1. Market structure

7.2.16.1.1. The views of the Notifying Party

(638) According to Staples, its business in Ireland has shrunk dramatically following the economic crisis, [...].⁵²⁶

(639) The Notifying Party claims that there are several strong competitors in Ireland,⁵²⁷ listing Lyreco, Codex, Spicers, VOW and Boss Novus as its top five competitors.⁵²⁸ It also submits that its other competitors in Ireland include providers of facility services (such as Bunzl and Bidvest 3663) and traditional retailers (such as Eason),⁵²⁹ Supplies Team/Banner, Sundry Supplies.⁵³⁰ In addition, the Parties list local suppliers that have the capabilities to serve very large business customer, including companies such as Bizquip, B2B, Fieldmaster, Ronnie Moore and Kelly Office Supplies.⁵³¹

(640) The Notifying Party claims that several suppliers in Ireland apart from the Parties are able to win large tenders involving stationery. For example, according to the Notifying Party, Lyreco won the second largest tender lost by Office Depot in 2014, worth EUR [...], for [...], and the largest tender lost by Staples, for [...], worth EUR [...] in 2014. Furthermore, Codex, which is an independently owned supplier of office requirements in Ireland, won [...] tenders from Office Depot worth EUR [...] for [...] and [...], and the second largest lost tender by Staples where the winner was known, worth EUR [...] for [...] in 2014.⁵³²

7.2.16.1.2. The Commission's assessment

(641) The Commission's analysis of the Notifying Party's turnover confirmed Staples' submission that it has reduced its operations in Ireland. The revenues from its contract business, its only line of activity in Ireland, have fallen from EUR [...] in 2010 to just EUR [...] in 2014.⁵³³

(642) The reduction in Staples' operations is also reflected in Office Depot's internal documents as shown in Figure 4:

Figure 4: Office Depot internal document entitled "EU OP Market Situational Analysis", March 2015, Annex 8.1 of the Form CO, excerpt taken from page 89

[...]

(643) According to the results of the market investigation the turnover of Lyreco and Codex is higher than that of the Notifying Party, although lower than that of Office

⁵²⁶ Form CO, paragraph 311.

⁵²⁷ Form CO, paragraph 313.

⁵²⁸ See contact details provided in response to the request for information of 5 October 2015 – National contracts (part 2) and to the request of information of 8 October 2015.

⁵²⁹ Form CO, paragraph 313.

⁵³⁰ See further reference to Supplies Team/Banner and Sundry Supplies in the Note on customer requirements and competitor capabilities, Table 8, page 16.

⁵³¹ Note on customer requirements and competitor capabilities, paragraph 50.

⁵³² Form CO, paragraph 313.

⁵³³ Form CO, paragraph 309.

Depot. Accordingly, Office Depot is the largest supplier of office supplies through contracts in Ireland while Staples plays only a more limited role behind Lyreco and Codex.

- (644) Codex is Ireland's largest independently owned office products company, providing its customers with general office stationery products, office furniture, computer consumables or printed stationery. Codex employs over 50 people in its Glasnevin facility.⁵³⁴

7.2.16.2. Competitive constraints exerted by the Parties on each other

- (645) The Notifying Party submits that it has not been an active supplier in the Irish market in the recent years.⁵³⁵ As discussed in section 7.2.16.1, the Commission's analysis confirmed that the Notifying Party's business in Ireland has shrunk in the recent years.
- (646) Due to Staples' reduction in activities, the Parties do not appear to be closely competing in Ireland. This is supported by the limited bidding data submitted by the Parties as shown in Figure 5:

Figure 5: Tenders lost by Staples in Ireland

[...]

Source: Bidding data from the report RBB Economics: "Relevance of bidding data for the competitive assessment", dated 18 May 2015.

Figure 6: Tenders lost by Office Depot in Ireland

[...]

Source: Bidding data from the report RBB Economics: "Relevance of bidding data for the competitive assessment", dated 18 May 2015.

- (647) The very small sample size for the Parties (less than [...] observations each) makes it difficult to draw firm conclusions. However, of Office Depot's [...] largest tenders in 2014, Staples won only [...]. Similarly, in the [...] stationery tenders lost by Staples, Office Depot emerged as winner in only [...].⁵³⁶
- (648) This is consistent with the Commission's analysis showing that the turnover of Lyreco and Codex, which the Notifying Party listed amongst its top five competitors in the contract in Ireland (see recital (640)), is higher than the turnover of the Notifying Party, although it is in both cases lower than the turnover of Office Depot.
- (649) This evidence suggests that Staples is not exerting a strong competitive pressure on Office Depot in Ireland pre-transaction.

7.2.16.3. Competitive conditions following the transaction

- (650) The Parties submit that the transaction will not give rise to competition concerns in Ireland.⁵³⁷ The Notifying Party specifies that its presence in the Irish market has

⁵³⁴ <http://www.codexltd.com/about-us>.

⁵³⁵ Form CO, paragraph 309.

⁵³⁶ For further reference please see the analysis of RBB Economics in the Relevance of bidding data for the competitive assessment of 18 May 2015.

⁵³⁷ Form CO, paragraph 310.

dramatically decreased in recent years, and that the merged entity will continue to face a range of strong competitors.⁵³⁸

- (651) The Parties' customers have not raised substantiated concerns regarding the effect of the transaction on non-international contracts in Ireland. Although one customer expressed concerns that the transaction could possibly eliminate one of the competitors on the Irish market, that customer also acknowledged that five other competitors apart from Office Depot (namely, Banner, Codex OP, Lyreco, Office 26 and Supplies Team) participated in its last tender in 2014.⁵³⁹
- (652) The Commission has found that the Notifying Party does not exert a strong competitive pressure on Office Depot in Ireland pre-transaction. The Commission also identified that the merged entity will continue to face competition from Lyreco and Codex, who are viable alternative suppliers in the contract market in Ireland.

7.2.16.4. Conclusion on Ireland

- (653) In the light of the above, the Commission concludes that the transaction would not lead to a significant impediment to effective competition in the market for the distribution of office supplies through contracts to large business customers in Ireland.

7.2.17. *Ireland - Stationery only*

- (654) The structure of the market and the effects of the transaction as described in the previous section 7.2.16 are not materially different when assessing the market for supply of stationery products only.
- (655) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.
- (656) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Ireland.

7.2.18. *Italy - Traditional office supplies*

7.2.18.1. Market structure

7.2.18.1.1. The views of the Notifying Party

- (657) According to the Notifying Party, the transaction will not give rise to competition issues in the Italian market. The market is characterised by several suppliers acting as main competitors to the Parties. Those include Errebian, Lyreco, Myo, Misco, Buffetti, Adveo, Systemax, GBR Rossetto, Ingros Carta Giustacchini, Gecal, Ugo Tesi, Polyedra, Karnak and Spicers.⁵⁴⁰ The Notifying Party states that several of

⁵³⁸ *Ibid.*

⁵³⁹ Agreed minutes of the conference call with a customer, paragraphs 3 and 13, 7 July 2015.

⁵⁴⁰ Form CO, paragraph 187. See further Annex 7.7 to the Form CO from March 2014 and reply to RFI of 5 October 2015.

those competitors have the same capabilities as the Parties, including a full range of supplies.⁵⁴¹

- (658) The Notifying Party claims that Staples only has a small contract business in Italy. The Parties have revenues in the contract business market of Italy of EUR [...] and [...] respectively, representing very low market shares. According to the notifying Party, the revenues of Lyreco and Errebian are approximately EUR [...] while Myo's revenues are around EUR [...].⁵⁴²

7.2.18.1.2. The Commission's assessment

- (659) As illustrated in recital (658), Staples' turnover and presence on the Italian market is very low. Further, the Parties will, even in combination, be significantly smaller than the two leading suppliers. Thus, the Italian market seems to be characterised by the presence of two very strong suppliers (Lyreco and Errebian) followed by the Parties and a number of smaller suppliers.

7.2.18.2. Competitive constraints exerted by the Parties on each other

- (660) The findings above indicate that Staples is not competing closely with Office Depot in the Italian market for contracts and that Lyreco and Errebian are stronger than the merged entity.
- (661) The strong position of Errebian on the Italian market is confirmed by its replies to the Commission's questionnaires in Phase I and Phase II of the market investigation. Here, Errebian stated that it does not actively target small customers but focuses on sales to customers with more than 100 office workers. This is further supported by the fact that Errebian has several contracts with a value above EUR 1 million. Moreover, Errebian won more than half of the large number of tenders it participated in during 2014. Alongside Lyreco, Errebian considers itself the closest competitor to Office Depot. GBR Rossetto and MyO are mentioned as other important competitors.⁵⁴³ Lyreco's replies regarding the closest competitors replicate those of Errebian; Alongside Errebian, Lyreco considers itself the closest competitors to Office Depot and it further mentions GBR Rossetto and MyO as other important competitors.⁵⁴⁴

7.2.18.3. Competitive conditions following the transaction

- (662) The Parties will continue to compete with the market leaders Lyreco and Errebian as well as smaller suppliers in Italy following the transaction.
- (663) The majority of competitors on the Italian market do not express any concerns about the impact of the transaction.⁵⁴⁵ Similarly, the customers on the Italian market have not raised any substantiated concerns about the transaction.⁵⁴⁶

⁵⁴¹ See the Parties' note on Customer Requirements and Competitor Capabilities, table 9.

⁵⁴² Form CO, paragraph 187.

⁵⁴³ Replies to Phase I Questionnaire Q1 to competitors (contract) – Questions 17, 37.1 and 40 and to Phase II Questionnaire Q9 to competitors (contract stationers) – Question 5.

⁵⁴⁴ Lyreco's reply to Phase I Questionnaire Q1 to competitors (contract) – Question 40.

⁵⁴⁵ Agreed minutes of conference calls with a competitor of 6 August 2014; replies to Phase I Questionnaire Q1 to competitors (contract) – Questions 62-63.1.

⁵⁴⁶ Agreed minutes of conference calls with customers of 26 November 2015 and 29 July 2015; replies to Questionnaire Q4 to customers (contract) – Questions 51-52 and to Phase II Questionnaire Q8a to customers – Questions 52-53.1.

7.2.18.4. Conclusion on Italy

(664) In the light of the above, the Commission concludes that the transaction would not lead to a significant impediment to effective competition in the market for the distribution of office supplies through contracts to large business customers in Italy.

7.2.19. *Italy - Stationery only*

(665) The structure of the market and the effects of the transaction as described in the previous section 7.2.18 are not materially different when assessing the market for supply of stationery products only.

(666) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.

(667) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Italy.

7.2.20. *Spain - Traditional office supplies*

7.2.20.1. Market structure

7.2.20.1.1. The views of the Notifying Party

(668) The Notifying Party claims that Lyreco's estimated revenues are EUR [...], whereas Office Depot achieved only EUR [...] revenue, and the Notifying Party achieved EUR [...] revenue in 2014. In addition, the Notifying Party claims it is only [...] of the size of PMC, with estimated revenues of around EUR [...].⁵⁴⁷

(669) Moreover, the Notifying Party also listed Alpadisa, Montte and Folder Papelerias SA amongst its top five competitors.⁵⁴⁸

7.2.20.1.2. The Commission's assessment

(670) The results of the market investigation provide indications that Lyreco is the clear leader on the Spanish market, followed by Office Depot and at least two other significant competitors, Montte and PMC. Staples is a smaller competitor with a turnover of only EUR [...].

(671) Post-transaction the merged entity will be only one third the size of the market leader Lyreco and will face competition from at least two large competitors. Office Depot competes more closely with PMC and Montte than with Staples.

7.2.20.2. Conclusion on Spain

(672) In the light of the assessment set out in recitals (668) to (671), the Commission concludes that the transaction would not lead to a significant impediment to effective

⁵⁴⁷ Form CO, paragraph 187.

⁵⁴⁸ Contact details provided in response to the request for information of 5 October 2015 – National contracts (part 2) and to the request of information of on 8 October 2015.

competition in the market for the distribution of traditional office supplies through non-international contracts to large business customers in Spain.

7.2.21. *Spain - Stationery only*

- (673) The structure of the market and the effects of the transaction as described in section 7.2.20 are not materially different when assessing the market for supply of stationery products only.
- (674) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.
- (675) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in Spain.

7.2.22. *United Kingdom - Traditional office supplies*

7.2.22.1. Market structure

- (676) According to the Notifying Party, the UK market is currently characterised by a total of five significant suppliers. Apart from the Parties, those include Lyreco, Vasanta/Office2Office (EVO) and the Spicers-OfficeTeam (SPOT) group.⁵⁴⁹
- (677) The Notifying Party claims that it is a relatively small supplier in the contract segment in the UK market, similar in size to SPOT but smaller than Vasanta/Office2Office.⁵⁵⁰
- (678) The Commission conducted an extensive investigation of the market to identify the suppliers that are currently active in the contract in the UK market. The analysis has shown that there are currently 8 to 10 suppliers that operate in the contract business of office supplies in the UK market.⁵⁵¹
- (679) According to the Commission's analysis, the turnover of Lyreco, mentioned by customers as an alternative supplier,⁵⁵² is higher than that of the Notifying Party, although lower than that of Office Depot. This confirms the Notifying Party's submission that Lyreco is a significant alternative supplier (see recital (676)).
- (680) Based on its market investigation, the Commission considers that Vasanta/Office2Office (EVO) is a credible competitor in contract in the UK market. EVO has 5 warehouses in the UK, and 2 in Ireland.⁵⁵³ In 2014 they achieved more than GBP [...] EEA sales of traditional office supplies.⁵⁵⁴

⁵⁴⁹ Form CO, paragraph 322.

⁵⁵⁰ *Ibid.*

⁵⁵¹ See agreed minutes of a conference call with a competitor, 2 September 2015, paragraph 4.

⁵⁵² Replies to Phase II Questionnaire Q8f to customers – Question 48.

⁵⁵³ Replies to Phase II Questionnaire Q9 competitors (contract stationers) – Question 18.1.

⁵⁵⁴ Replies to Phase II Questionnaire Q9 competitors (contract stationers) – Question 2.

(681) According to the results of the market investigation competitors such as Office Team compete with the Parties for large contracts.⁵⁵⁵

(682) On that basis, the Commission's conclusion is that there are viable alternative suppliers on the UK market other than the Parties, including Lyreco, Vasanta/Office2Office (EVO) and Spicers/Office Team (SPOT).

7.2.22.2. Competitive constraints exerted by the Parties on each other

(683) The Notifying Party submits that following a number of mergers and acquisitions in recent years, the already strong local suppliers in the UK market have further gained in strength (such as Vasanta, created by the merger of various companies including VOW, which is the wholesale business, which then merged with Office2Office, which acts under the trade names Supplies teams and Banner). Moreover, the Notifying Party claims that Office Team is one of the Parties' key rivals in the contract business, and it has recently merged with the leading wholesaler Spicers (SPOT).

(684) The Notifying Party claims that Vasanta, Lyreco and SPOT group operate at significant scale and represent credible bidders, including for very large contracts. In particular, the Notifying Party lost bids for [...] (EUR [...]) and [...] (EUR [...]) to what is now Vasanta/Office2Office. The Notifying Party also lost bids for [...] (EUR [...]), [...] (EUR [...]) and [...] (EUR [...]) to Lyreco. The Notifying Party also lost bids for [...] (EUR [...]), [...] (EUR [...]) and [...] (EUR [...]) to what is now the SPOT group.⁵⁵⁶

(685) Moreover, the Notifying Party claims that following completion of integration of Vasanta/Office2Office and the SPOT group, the competitive threat that those rivals pose can only be expected to further intensify.⁵⁵⁷ In particular, it is submitted that the integration between wholesalers and dealers should be expected to allow those firms to compete even more strongly on price.⁵⁵⁸

(686) The Notifying Party brought to the Commission's attention the analysis provided by the CMA in its decision in *Endless / Office2Office* of the suitability and strength of the various contract stationers including the Notifying Party, and other supplier, such as: Vasanta/Office2Office (Supplies Team), SPOT (Spicers), SPOT (Office Team), Lyreco, Office Depot, Vasanta/Office2Office (Banner).⁵⁵⁹ It is claimed that the analysis shows that all those contract stationers are credible competitors and that ratings given to the Notifying Party and Lyreco do not differ much from ratings given to the various local suppliers, with Supplies Team, Banner, now part of Vasanta/Office2Office coming out particularly strongly.⁵⁶⁰ Moreover, the Notifying Party claims that the CMA recognised that the offerings of those suppliers are highly substitutable.⁵⁶¹

(687) The Commission's analysis above (see recital (684)) shows that there are a number of credible competitors such as Vasanta/Office2Office (Supplies Team), SPOT (Spicers) and SPOT (Office Team) in the UK market which are capable of winning bids, including for very large contracts.

⁵⁵⁵ Agreed minutes of a conference call with a competitor of 2 September 2015, paragraph 4.

⁵⁵⁶ Form CO, paragraph 327.

⁵⁵⁷ Form CO, paragraph 328.

⁵⁵⁸ *Ibid.*

⁵⁵⁹ Form CO, paragraph 329.

⁵⁶⁰ Form CO, paragraph 330.

⁵⁶¹ Form CO, paragraph 331.

(688) Moreover, the Commission's analysis (see recital (680)) demonstrates that based on turnover there is a supplier (EVO) which occupies a stronger competitive position than the Notifying Party in the UK market.

(689) On this basis, the Commission concludes that the Parties face competition from at least three credible suppliers in the UK market, and that the Notifying Party is not competing closely with Office Depot in the UK.

7.2.22.3. Competitive conditions following the transaction

(690) According to the Notifying Party, following the transaction, the UK market will continue to have strong suppliers, and the merged entity will face competitive pressure from a number of specialist providers.⁵⁶²

(691) In particular, the Notifying Party submits that the merged entity would continue to face competitive pressure from the three key suppliers in the UK market, namely: Vasanta/Office2Office, Lyreco and the Spicers-Office Team (SPOT) group.⁵⁶³

(692) According to the results of the market investigation (see 7.2.22.2) there will remain a number of credible competitors able to compete for large contacts in the UK market.

(693) Moreover, the Commission found that Office Team, which is competing with the Parties for large contracts, perceives the transaction as an opportunity to gain market shares,⁵⁶⁴ and that the market would remain very competitive after the merger with plentiful competition remaining in the market.⁵⁶⁵

(694) The Commission concludes there will remain credible competitors on the UK market following the transaction.

7.2.22.4. Conclusion on United Kingdom

(695) In the light of the arguments set out in sections 7.2.22.1 to 7.2.22.3, the Commission concludes that the transaction would not lead to a significant impediment to effective competition in the market for the distribution of office supplies through contracts to large business customers in the UK.

7.2.23. *United Kingdom - Stationery only*

(696) The structure of the market and the effects of the transaction as described in section 7.2.22 are not materially different when assessing the market for supply of stationery products only.

(697) Even if the limited competitive pressure existing on certain product categories (particularly ink & toner and paper) due to the possibility to obtain those supplies from specialists, does not exist for stationery, in the previous section the risk of the transaction giving rise to a significant impediment to effective competition in the market for the distribution of traditional office supplies through non-international contracts with large customers has been excluded without taking into consideration such competitive pressure. Therefore, the lack of competitive pressure on the market for the supply of stationery only is neutral to the assessment.

⁵⁶² Form CO, paragraph 323.

⁵⁶³ Form CO, paragraph 326.

⁵⁶⁴ Agreed minutes of a conference call with a competitor of 2 September, paragraph 7.

⁵⁶⁵ Agreed minutes of a conference call with a competitor of 2 September, paragraph 8.

(698) Therefore, the Commission concludes that the transaction would not lead to a significant impediment to effective competition on the market for non-international contracts for the supply of stationery to large business customers in the UK.

7.2.24. *Overlaps due to partnership agreements*

(699) As listed in recital (174), in addition to their direct presence in a number of EEA countries, the Parties have entered into partnership agreements with third party distributors of office supplies to expand their geographic reach. The following partnerships are relevant in this respect:⁵⁶⁶

Country	Staples	Office Depot
Czech Republic	Third party distribution (international contracts only)	Active
Denmark	Active	Third party distribution
Finland	Active	Third party distribution
Norway	Active	Third party distribution
Poland	Active	Third party distribution
Slovakia	Third party distribution (international contracts only)	Active

(700) Those third party distribution agreements could be considered to lead to additional horizontal overlaps in the listed countries or to vertical links (where entering into distribution agreements for the wholesale supply of office supplies would be considered as the upstream market of the distribution of office supplies in the downstream market). In any event, the Commission has been able to verify that the transaction would not lead to competition concerns in those EEA countries due to the third party distribution agreements.

(701) As regards the Czech Republic and Slovakia, Staples' agreement with its distribution partner Activa relates to sales to customers who have entered into international contracts with Staples, including sales of Staples private label products.⁵⁶⁷ Staples' partner in the Czech Republic achieved a turnover of EUR [...] and EUR [...] with international contracts in the Czech Republic and Slovakia respectively.⁵⁶⁸ The turnover generated with international customers thus accounts for a small proportion of Activa's turnover and Activa is not worried about losing those international customers after the transaction.⁵⁶⁹ Furthermore, the competitive effects of the transaction on the market for international contracts have been assessed in section 7.2.2 and 7.2.3 and thus do not have to be assessed further in this section.

(702) As regards the remaining distribution agreements of Office Depot in Denmark, Finland, Norway and Poland, the agreements allow the third party distributors to act independently on the national markets. In particular, the distributors determine their

⁵⁶⁶ According to the submissions in the Form CO, Office Depot [...] where Staples has distribution agreements in place only for the supply of its international customers. For the same reasons set out in recital (701), [...].

⁵⁶⁷ The distribution agreement refers to [...], Annex 27(4) of the Form CO, page 1.

⁵⁶⁸ Form CO, Annex 27, paragraphs 4 and 10.

⁵⁶⁹ Agreed minutes of the conference call with a third party distributor, paragraph 8.

own business strategies for national customers, including pricing⁵⁷⁰, and act on their own account and risk.

(703) The distribution partners explained that Lyreco and Wulff Suppliers are the main competitors of the Parties' distribution partners in the Nordic region (including, Denmark, Finland and Norway) and that Lyreco and smaller Polish purchasing groups compete with Staples and Office Depot's distribution partner in Poland.

(704) As regards potential foreclosure concerns, one of the third party distributors confirmed that it would be able to stay active in the national market even if the merged entity decided to cancel Office Depot's distribution agreement after the transaction:

"In order to continue serving the [...] customers, [third party distributor] will also need to find other partners in [...]. Even though this might be costly and time consuming, [third party distributor] believes that the transition will be feasible since there are numerous suppliers of office products."⁵⁷¹

(705) In contrast, other third party distributors pointed to potential problems of having competitive access to office supplies after the transaction:

"If after the merger [third party distributor] will not be able to distribute the products of Office Depot any more, it will be hard to compete with other companies, including the merged Staples and Office Depot, as many customers wish to purchase Office Depot's stationery and it is difficult to replace it with other products, which would be as attractive for the customers."⁵⁷²

(706) In any event, as discussed in sections 8.3.2.5 and 8.5, the Final Commitments include the divestment of all of Office Depot's activities in the EEA, including its activities in the Czech Republic and Slovakia and its partnership agreements with third party distributors in Denmark, Finland, Norway and Poland⁵⁷³. Subject to the distributors' agreement – if such agreement is necessary – the partnership contracts will be divested and separated from the business of the merged entity. In the light of the divestment of Office Depot's entire activities in Denmark, Finland, Norway and Poland, it can be left open whether the transaction would lead to an additional significant impediment to effective competition with respect to the markets for the distribution of office supplies to large business customers through contracts in Denmark, Finland, Norway or Poland.

7.3. Competitive assessment of the wholesale channel

(707) The Parties are both active in the wholesale channel in Sweden, where they carry out traditional wholesale activities in the sense of distributing office supplies to smaller dealers and resellers. Staples also runs similar wholesale activities in Finland and Norway, where Office Depot has partnership agreements with local suppliers for the supply of products to the international customers of the company with offices in one of those countries (see section 7.2.24). Although from a formal point of view the supply by Office Depot to its partners in those countries fall into the wholesale channel category, the contracts are exclusive and Office Depot does not serve any

⁵⁷⁰ See the agreements between Office Depot and each of Wittusen & Jensen, OFIX Lewandowski, Papierpalvelu Koskimo ja Rännäli, and Paperlinx Scandinavia A/S, Annexes 27(1), 27(2), 27(3) and 27(5) to the Form CO, paragraph 2.2.2.

⁵⁷¹ Agreed minutes of the conference call with a third party distributor of 26 August 2015.

⁵⁷² Agreed minutes of the conference call with a third party distributor of 27 August 2015.

⁵⁷³ The divestment would also include [...], see footnote 566.

customers apart from the partner in the respective country. Therefore, the analysis in section 7.3 only concerns the wholesale channel in Sweden.

7.3.1. *Market structure*

7.3.1.1. The views of the Notifying Party

- (708) The Parties estimate that the total size of the Swedish wholesale market is approximately EUR 165 million (5% of total market value of EUR 3.3 billion). According to the Notifying Party, Staples (active in wholesale under the brand "EMO") has an estimated market share of [10-20]% with sales of EUR [...] and Office Depot has an estimated market share of [5-10]% with sales of EUR [...].
- (709) The Parties argue that there are a number of competitors present on the market. The largest competitors are Actebis/Also with a market share of [10-20]%, Papyrus with a market share of [5-10]% and Despec/Buengers with a market share of [5-10]%. Other smaller wholesalers include according to the Notifying Party Isolda, TechData, Alpha International and Lyreco.
- (710) The Parties further explain that Staples' wholesale revenues represent [...] of its total sales in Sweden and that Office Depot's wholesale revenues represent [...] of total revenues. Staples primarily sells stationery to distributors, in particular smaller dealers and specialised retail stores such as book stores. According to the Notifying Party, those customers are not dependant on Staples, as they also source stationery from other wholesalers (local and other) or directly from the manufacturers.
- (711) The Parties are both active in the wholesale channel in Sweden, offering a full range of products encompassing the traditional office supplies and many other additional categories. Both Parties offer warehouse handling and delivery either directly to the wholesalers or to their end customer. In addition, Office Depot provides a specialised webshop solution which can be tailor-made for each wholesaler. Staples provides to some of its customers a web platform tailored at front end towards the customer.

7.3.1.2. The Commission's assessment

- (712) According to the results of the market investigation there are two groups of purchasers buying from the Parties:
- (a) resellers which have physical shops and often own warehouses, for instance small retailers and bookshops ;
 - (b) online resellers, who do not own warehouses and their business model consists of running a website which is directly linked to the IT system of the wholesaler. The order is then processed and delivered to the end-customers by the wholesaler and the online reseller charges a commission on every sale it makes.⁵⁷⁴
- (713) Those different customer groups have different requirements with regard to the range of products as well as to the specific services offered by the resellers.
- (714) With regard to the range of products offered, the first group of customers in most cases has some storage capacity and requires that suppliers deliver the goods to their location. Those customers are able to purchase different product groups (namely stationery, paper, ink & toner) separately. The second group of customers identified above however requires the wholesaler to offer a full-range of products, which can

⁵⁷⁴ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Questions 1 and 2; replies to Phase II Questionnaire Q11 to customers (wholesale) – Question 1 and 4.

be then delivered directly to the end-user, as they do not have an own warehouse or storage capacity.⁵⁷⁵ Having multiple deliveries for one order would not be possible, as it would generate too high overall cost for the end-users who would need to pay multiple shipment fees. Secondly, the online resellers underline that having multiple deliveries per order would generate too much burden for their customers and would significantly impair the ability of those resellers to effectively compete and sell goods online.⁵⁷⁶

(715) A customer indicated:

*"Only Staples and Office Depot are able to provide [customer] with the whole range of products it requires (packaging, tech. products, ink and toner, facility products, children toys etc.) as a single supplier. The customers of [customer] require about 8,000 different SKUs and to find an alternative to Office Depot and Staples, [customer] would need about 8 or 9 different suppliers. Having a single supplier is convenient to [customer], as several separate deliveries would raise delivery costs (multiple suppliers mean multiple deliveries). It would be also impossible to have up to 9 separate deliveries for one order, as it would generate unnecessary inconvenience for the customers."*⁵⁷⁷

(716) Regarding the specific IT and logistic solutions, the online resellers indicated that the Parties offer a unique service consisting in offering a dedicated IT system allowing the resellers to directly sell the products of Staples or Office Depot to the final customers, with the Parties taking care of all the logistics and delivery. The business model of many online resellers is fully dependent on this service. The customers belonging to the online reseller group explained:

*"In Sweden the 2 biggest companies working with re-sellers are Staples and Office Depot. They are the obvious 2 options for companies selling online, and are the best option in terms of logistics and warehouse solutions."*⁵⁷⁸

*"Staples and Office Depot are the only two companies capable of offering through the e-platform system a wide range of products that fulfil the needs of [customer]. If they merge, alternatives would be strongly reduced."*⁵⁷⁹

*"At the moment there are no other wholesalers who could offer a similar range of products and delivery arrangements as Office Depot and Staples."*⁵⁸⁰

(717) Whereas in case of the first group of customers, they indeed indicate the ability to source from other suppliers, including wholesalers and manufacturers, the online resellers have specific requirements with regard to the product range and service which to a large extent limits their choice of supplier.⁵⁸¹ Therefore the competitive analysis will concentrate on this second group of customers.

⁵⁷⁵ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 4.1 and to Phase II Questionnaire Q11 to customers (wholesale) – Question 9.2; agreed minutes of the conference calls with customers 1, 2 and 3 on 4 November 2015 and a phone call with a customer, 28 October 2015.

⁵⁷⁶ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 5.2 and to Phase II Questionnaire Q11 to customers (wholesale) – Question 10; agreed minutes of the phone calls with customers 1, 2 and 3 on 4 November 2015.

⁵⁷⁷ Agreed minutes of the phone call with customer 1 – 4 November 2015.

⁵⁷⁸ Agreed minutes of the phone call with customer 3 – 4 November 2015.

⁵⁷⁹ Agreed minutes of the phone call with a customer on 28 October 2015.

⁵⁸⁰ Agreed minutes of the phone call with customer 2 – 4 November 2015.

⁵⁸¹ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 4 and to Phase II Questionnaire Q11 to customers (wholesale) – Question 9.

- (718) The qualitative and quantitative data collected during the market investigation indicates that whereas in the separate sub-segments (stationery, paper, ink & toner and other) there would be still some competition remaining after the merger, the Parties would be dominant in the one-stop-shop segment, or at least stationery, paper and ink & toner supplied together. Furthermore, when the specific IT and logistic service is taken into account, the respondents to the market investigation indicated that the Parties are the only suppliers active on the market with no competitors able to offer a comparable solution.
- (719) Indeed, the participants to the market investigation indicated that the competitors present in the wholesale market in Sweden include Despec, BNT, Isolda, Papyrus, TechData, and Alpha International.⁵⁸² Some also listed Lyreco, RKV, Tingstad and Ocaj. However, those companies are not active at the wholesale level.⁵⁸³ Of those active in wholesale, only Isolda offers the full range of traditional office supplies required by online resells. Nonetheless, this company is not perceived by the customers as a viable supplier on the one-stop-shop segment and only has marginal sales in stationery and paper.⁵⁸⁴ All the other suppliers active in wholesale are specialised in one or several product categories.
- (720) Table 22 presents the activities of the Parties and their competitors in the wholesale market in Sweden:

Table 22: Activities of the Parties and their main competitors in the wholesale market in Sweden

	Stationery	Ink & Toner	Paper	Other
EMO/Staples	X	X	X	X
Office Depot	X	X	X	X
Despec/Bungers	X		X	X
Actebis/Also		X		X
BNT	X			X
Isolda	X	X	X	X
Papyrus			X	X
TechData		X		X
Alpha International		X	X	X

Source: Phase I questionnaire Q2 – question 2, agreed minutes of the calls with competitors, Annex 6 of the reply to the RFI on wholesale in Sweden submitted on 27/10/2015, www.alpha-international.eu.

- (721) In light of the specific needs of online resellers with regard to the one-stop-shop on the one hand and the provision of the specialised IT platform and logistic solutions

⁵⁸² Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 9 and to Phase II Questionnaire Q11 to customers (wholesale) – Question 11.

⁵⁸³ Agreed minutes of the conference call with competitors of 3 September and 7 September 2015; replies to Phase II Questionnaire to competitors Q9 to competitors (contract stationers) – Question 1.

⁵⁸⁴ Agreed minutes of the conference call with a competitor of 8 September 2015, Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 9 and to Phase II Questionnaire Q11 to customers (wholesale) – Question 11.

for resellers, the competitive constraints exerted by the manufacturers and purchasing groups, as indicated in the previous Commission decisions, are minimal. The manufacturers and purchasing groups do not offer a one-stop-shop or specialised IT and logistic solutions and whereas they could be an alternative supplier for larger resellers who have own warehouses and logistics, they are not a viable alternative for the smaller online resellers relying on the Parties to carry out the purchase orders. The customers explained:

*"[...] switching to manufacturers would require own warehouse, splitting orders, more complicated logistics etc. Going for that solution would require a very high investment and restructuring of the whole business model."*⁵⁸⁵

*"the manufacturers do not send the products directly to the end customers (which would require [customer] to find a partner with a warehouse and a distribution centre). Also, the manufacturers do not offer a wide range of products, therefore it would be necessary to build up own stock which is very costly."*⁵⁸⁶

(722) A customer explained:

*"Currently on the Swedish market there are the EMO/Staples and Office Depot's wholesale businesses and one or two smaller competitors, but nobody else is present in this market. [...] Many [dealers] are purchasing directly from manufacturers, but for the smaller ones it is sometimes necessary to source the products from wholesalers. After the merger, the Parties will be very dominant in the wholesale market and will thus have considerable control over the office suppliers' downstream market."*⁵⁸⁷

(723) The results of the market investigation indicated indeed that smaller dealers do not have their own warehouses and rely on the Parties for the deliveries to the end-customers.

7.3.2. Competitive constraints exerted by the Parties on each other

(724) The participants to the market investigation indicated that the Parties are the closest competitors to each other. All of the respondents to the market investigation listed only two credible suppliers: Office Depot and Staples as viable alternatives in the wholesale supply of the full range of office supplies (one-stop-shop). None of the respondents named Isolda.⁵⁸⁸

(725) Furthermore, participants to the market investigation indicated that the customers use the Parties for benchmarking purposes and negotiating better prices. The customers told the Commission:

*"The price offer of Staples/EMO is quite good, especially that [customer] compares the offer of Staples and Office Depot. It can negotiate prices with Staples on the basis of pricing information gathered from Office Depot."*⁵⁸⁹

⁵⁸⁵ Agreed minutes of the phone call with customer 3 – 4 November 2015.

⁵⁸⁶ Agreed minutes of the phone call with customer 1 – 4 November 2015.

⁵⁸⁷ Agreed minutes of the phone call with a customer of 9 September 2015.

⁵⁸⁸ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Question 9 and to Phase II Questionnaire Q11 to customers (wholesale) – Question 11. As explained in recital (719), some participants indicated as alternatives suppliers not active at all in the wholesale channel or active in one product category only. Those suppliers however cannot be treated as credible alternatives to the Parties, as they do not fulfil the requirements of the customers who need a one-stop-shop wholesale supplier.

⁵⁸⁹ Agreed minutes of the phone call with customer 1 – 4 November 2015.

*"[customer] compares prices for certain products with those of Staples, but the company has a strong preference to have one single supplier and not source from different wholesalers. [customer] can use the quotes from Staples as an argument when negotiating lower prices with Office Depot for the important products."*⁵⁹⁰

- (726) In light of the fact that there are no viable competitors in the provision of the full range of office supplies as well as in the provision of the IT platform service for resellers, the Parties exercise currently an important competitive constraint on each other as regards this segment.

7.3.3. *Competitive conditions following the transaction*

- (727) Post-transaction, the Parties would have a significant and increased market power in the provision of the full range of office supplies as well as in the provision of the IT platform and logistics service for resellers. A number of participants to the market investigation expressed concerns with regard to the possibility the Parties raise prices after the merger. The customers further indicated that in case of a price increase they would not have an alternative supplier:

*"[after the merger] Staples would become very strong and able to raise prices with no competition present on the Swedish market."*⁵⁹¹

"If the new entity increased prices, [customer] would have limited alternative suppliers to go to, therefore it could consider building an own warehouse. It is however a very costly solution that requires time."

"If input prices were to increase, [customer] would be unable to offer good prices to the end customers."

*"The transaction could affect pricing as the merger would effectively create a monopoly. At the moment there are at least 2 alternative suppliers (Staples and Office Depot), so the merger would be detrimental by reducing it to only one option. If the Merged Entity raised prices for the products, [customer] would have to follow, as it would have no alternative supplier."*⁵⁹²

- (728) The merged entity's ability to increase prices for online resellers is due to the lack of alternative suppliers capable of meeting the requirements of this type of customers. Indeed, as explained above in recital (714), while retailers, bookshops and other dealers with own warehouses and larger volumes might turn to manufacturers and other specialised wholesalers to cover their needs, the merged entity will be the only supplier left for small online resellers in Sweden. This particular segment of customers has low bargaining strength. The Parties would be in a position to price discriminate against them given that they negotiate on an individual basis with each of them specific deals including the provision of products and also services.
- (729) According to some participants in the market investigation since the recent announcement of the merger the Parties have already increased prices.⁵⁹³

⁵⁹⁰ Agreed minutes of the phone call with customer 2 – 4 November 2015.

⁵⁹¹ Agreed minutes of the phone call with customer 1 – 4 November 2015.

⁵⁹² Agreed minutes of the phone call with customer 2 – 4 November 2015.

⁵⁹³ Agreed minutes of the phone call with customer 1 – 4 November 2015: *"If Staples takes over Office Depot, [...], Staples would become very strong and able to raise prices with no competition present on the Swedish market. This is already happening since some time [...], [customer] feels it has very weak*

(730) As regards potential competition, a participant to the market investigation indicated, in the context of B2B and the Swedish market in general, that the market for office supplies in Sweden is very mature and expansion is mostly possible via acquiring an already existing supplier.⁵⁹⁴ There were no recent entries to the Swedish wholesale market, which is a further indication that it is unlikely for a new entry in the nearest future.⁵⁹⁵ Furthermore, the need to offer a full range of products together with a specialised IT and logistic service required by the online resellers constitute an additional entry barrier for any new potential competitors on this segment.

7.3.4. Conclusion

(731) In conclusion, in the light of the arguments set out in sections 7.3.1 to 7.3.3 and in light of the results of the market investigation and of the information available to the Commission, the Commission considers that the transaction would lead to a significant impediment to effective competition in the wholesale market for office supplies in Sweden.

7.4. Competitive assessment of the direct channel

(732) The Parties' activities in the direct channel overlap in 8 countries: Austria, Belgium, France, Germany, Italy, Netherlands, Spain and the UK. Office Depot is active via the catalogue sales as well as online through its subsidiary Viking. In 1998 Office Depot merged with Viking Office Products, a public company based in the Netherlands and one of the world's largest direct mail marketers of office supplies, which allowed Office Depot to expand its activities in Europe. Also in 1998 Office Depot created the first eCommerce site using the Viking brand. Currently, Viking has websites in over 30 countries and globally accounts for almost a quarter of Office Depot's overall revenue. Staples is active in the direct channel either via the Staples brand or other subsidiaries, including Pressel which was acquired by Staples in 2004. Pressel Versand International GmbH was a mail order company based in Austria and operating in nine European countries.

(733) The Parties provide both printed catalogues regularly sent to the customers by post, who can then place orders on the phone or via other means. Whereas a number of customers are still expecting to receive a printed catalogue and prefer this form of ordering, there is a growing trend in using an online catalogue available on the website of the supplier, in which case the orders can be placed directly online.⁵⁹⁶

(734) According to the Notifying Party, affected markets could possibly arise in 7 countries: Austria, Belgium, France, Germany, Italy, Netherlands and UK.⁵⁹⁷

(735) The Notifying Party submits that in each overlapping country there are numerous competitors active in the direct channel. One of the most important competitors in the online channel is Amazon, followed by other suppliers, including:

- (a) Austria: Buerohandel GmbH, Office Discount GmbH, Pagro Handelsgesellschaft GmbH
- (b) Belgium: King Belgium, Manutan, Rajapack and Verpa

negotiating power and is not getting very good prices that Staples would be able to offer if more competitors were there."

⁵⁹⁴ Agreed minutes of the phone call with a competitor of 28 July 2015.

⁵⁹⁵ Replies to Phase I Questionnaire Q7 to customers (wholesale) – Questions 15 and 16 and to Phase II Questionnaire Q11 to customers (wholesale) – Questions 20 and 21.

⁵⁹⁶ Form CO, paragraph 108.

⁵⁹⁷ Form CO, Annex 24, Table 9: Direct market share estimates for traditional categories (150 EUR spend).

- (c) France: Bureau Vallee, JM Bruneau, Raja and Top Office
 - (d) Germany: Bueroshop24, Bueromarkt Boettcher AG, Mercateo and Printus Fachvertrieb fuer Buerobedarf
 - (e) Italy: Adveo, Errebian, Gruppo Buffetti S.p.A.
 - (f) Netherlands: Bol.com BV, Coolblue, Media Markt Saturn Nederland B.V. and 123inkt.nl / Digital Revolution BV
 - (g) Spain: Adveo
 - (h) UK: Ebuyer.com, Eurooffice, Office Team, Ryman and Tesco Direct⁵⁹⁸
- (736) In addition to the already existing offer in the direct channel, Amazon is currently a rapidly growing supplier, very well-known by the industry. Although the customers requiring a contract stationer indicated in the market investigation that they would not be able to use Amazon, there is strong acceptance of Amazon among business community. Many participants expressed an interest in using Amazon's service if they were not bound by the tender rules (or if Amazon complied with those rules) and virtually all participants to the market investigation were familiar with Amazon as a major direct supplier on the European market.⁵⁹⁹ Customers using the direct channel also increasingly source office supplies from Amazon. According to Office Depot, one in three Office Depot contract end-users in the UK claim to have purchased workplace supplies from Amazon in 2013, while in 2012, only one in seven Office Depot contract end-users did so.⁶⁰⁰
- (737) According to the data gathered by the Commission during the market investigation, there are many competitors active in the direct sales channel, especially distributors active only via the online channel (and not issuing printed catalogues). Apart from Amazon and other competitors indicated by the Parties, there are also numerous smaller distributors and resellers. The smaller distributors indicated that it is relatively easy to start a new business and start distributing office products via the direct channel, especially since it is possible to use outsource the whole logistics to a wholesaler.⁶⁰¹ This business model is offered by the Parties in Sweden (see section 7.3), but also by Quantore in the Netherlands.⁶⁰²
- (738) The market investigation provided evidence that in case of orders made via the direct channel, the customers can easily switch suppliers with every newly placed order, as there are no contracts or long-term commitments attributed to the purchases. Some customers traditionally use one particular supplier with whom they are familiar, as they used to the catalogue, delivery modalities and the customer service, however the customers are also price sensitive and can easily switch away from their previous supplier if they receive a better offer elsewhere.
- (739) A number of online websites allow for price comparison between different online suppliers, including Mercateo, Kelkoo, Google.com/shopping and many more. Those websites gather offers from different suppliers and allow for price transparency and pricing benchmark for customers (the comparison websites do not sell office supplies

⁵⁹⁸ Form CO, Annex 38 and reply to the RFI of 4 August 2015 questions 37, 43 and 44.

⁵⁹⁹ Replies to Phase I Questionnaire Q4 to customers (contract) – Question 28; replies to Phase II Questionnaire Q8a-j to customers – Question 51.

⁶⁰⁰ These estimates come from a customer survey conducted in October 2013 by Office Depot. See Form CO, paragraph 60.

⁶⁰¹ Agreed minutes of a phone call with a customer of 4 November 2015.

⁶⁰² Agreed minutes of a phone call with a competitor of 11 June 2015.

to end users). The comparison websites allow for greater price transparency on the market and therefore facilitate sales by smaller competitors who may not benefit from the economies of scale, but thanks to more flexibility can lower their fixed costs and therefore offer competitive prices.

- (740) The Notifying Party furthermore submits that there are a number of new entrants to the direct sales channel of office products. Some of them include mass merchandisers, such as CostCo who increased its presence in office supplies in the UK also through its online channel. Other mass merchandisers, such as Tesco and Carrefour also provide office supplies via their online sales channel. eBuyer is an example of a specialist supplier who used to be active in related product categories and who currently also offers traditional office supplies.⁶⁰³
- (741) In conclusion, in the light of the arguments set out in recitals (732) to (740) and in view of the results of the market investigation and of the information available to it, the Commission considers that the transaction would not lead to a significant impediment to effective competition in the direct sales channel for office supplies at the EEA and national level.

7.5. Conclusion on the compatibility of the transaction with the internal market

- (742) In conclusion, in the light of the assessment in sections 5 to 7.4 and in light of the results of the market investigation and of the information available to the Commission, the Commission considers that the transaction would lead to a significant impediment to effective competition in the markets for (i) international contracts for the supply of traditional office supplies and for the supply of stationery in the EEA, (ii) national contracts for the supply of traditional office supplies and for the supply of stationery to business customers with more than 100-200 office worker or more than 250 employees in Sweden and the Netherlands and (iii) wholesale supply of traditional office supplies in Sweden.
- (743) On the other hand, the Commission considers that the transaction would not lead to a significant impediment to effective competition in the markets for (i) national contracts for the supply of traditional office supplies and for the supply of stationery to large business customers in Austria, Belgium, France, Germany, Ireland, Italy, Spain and the United Kingdom, (ii) national contracts for the supply of traditional office supplies and for the supply of stationery to smaller business customers in any of the overlapping countries, (iii) direct supply of office supplies in any of the overlapping countries and (iv) retail supply of office supplies in Sweden.

8. COMMITMENTS

- (744) In order to render the transaction compatible with the internal market in relation to the markets for (i) international contracts for the supply of traditional office supplies and for the supply of stationery in the EEA, (ii) national contracts for the supply of traditional office supplies and for the supply of stationery to business customers with more than 100-200 office worker or more than 250 employees in Sweden and the Netherlands and (iii) wholesale supply of traditional office supplies in Sweden, the Parties submitted commitments pursuant to Article 8 (2) of the Merger Regulation on 27 November 2015 ("the Commitments of 27 November 2015"). The Commission subjected those commitments to a market test. The Commission considered on the basis of the results of the market test, that the Commitments of 27 November 2015

⁶⁰³ Form CO, paragraph 373.

were generally suitable to address the Commission's competition concerns but contained certain risks for the viability and competitiveness of the business to be divested.

- (745) In order to address the issues raised by the Commission, the Parties submitted a final set of commitments on 10 December 2015 ("the Final Commitments").

8.1. Analytical framework

- (746) The following principles from the Remedies Notice⁶⁰⁴ apply where parties to a merger choose to offer commitments in order to restore effective competition.

- (747) Where a concentration raises competition concerns in that it could significantly impede effective competition, in particular as a result of the creation or strengthening of a dominant position, the parties may seek to modify the concentration in order to resolve the competition concerns and thereby gain clearance of their merger.⁶⁰⁵

- (748) The Commission only has power to accept commitments that are capable of rendering the concentration compatible with the internal market in that they will prevent a significant impediment to effective competition in all relevant markets where competition concerns were identified.⁶⁰⁶ To that end, the commitments have to eliminate the competition concerns entirely⁶⁰⁷ and have to be comprehensive and effective from all points of view.⁶⁰⁸

- (749) In assessing whether proposed commitments are likely to eliminate its competition concerns, the Commission considers all relevant factors including, among other criteria, the type, scale and scope of the commitments, judged by reference to the structure and particular characteristics of the market in which those concerns arise, including the position of the parties and other participants on the market.⁶⁰⁹ Moreover, commitments must be capable of being implemented effectively within a short period of time.⁶¹⁰

- (750) Where a proposed concentration threatens to significantly impede effective competition the most effective way to maintain effective competition, apart from prohibition, is to create the conditions for the emergence of a new competitive entity or for the strengthening of existing competitors via divestiture by the parties.⁶¹¹

- (751) The divested activities must consist of a viable business that, if operated by a suitable purchaser, can compete effectively with the merged entity on a lasting basis and that is divested as a going concern. The business must include all the assets which contribute to its current operation or which are necessary to ensure its viability and

⁶⁰⁴ Commission's Notice on Remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 ("Remedies Notice"), OJ C 267, 22.10.2008, p. 1.

⁶⁰⁵ Remedies Notice, paragraph 5.

⁶⁰⁶ Remedies Notice, paragraph 9.

⁶⁰⁷ Case C-202/06 P *Cementbouw Handel & Industrie v Commission* [2007] ECR 2007 I-12129, paragraph 54: "*it is necessary, when reviewing the proportionality of conditions or obligations which the Commission may, by virtue of Article 8(2) of Regulation No 4064/89, impose on the parties to a concentration, not to determine whether the concentration still has a Community dimension after those conditions or obligations have been complied with, but to be satisfied that those conditions and those obligations are proportionate to and would entirely eliminate the competition problem that has been identified*".

⁶⁰⁸ Remedies Notice, paragraphs 9 and 61.

⁶⁰⁹ Remedies Notice, paragraph 12.

⁶¹⁰ Remedies Notice, paragraph 9.

⁶¹¹ Remedies Notice, paragraph 22.

competitiveness and all personnel which are currently employed or which are necessary to ensure the business' viability and competitiveness.⁶¹²

- (752) Personnel and assets which are currently shared between the business to be divested and other businesses of the parties, but which contribute to the operation of the business or which are necessary to ensure its viability and competitiveness, must also be included. Otherwise, the viability and competitiveness of the business to be divested would be endangered. Therefore, the divested business must contain the personnel providing essential functions for the business such as, for instance, group R&D and information technology staff even where such personnel are currently employed by another business unit of the parties —at least in a sufficient proportion to meet the on-going needs of the divested business.⁶¹³
- (753) Normally, a viable business is a business that can operate on a stand-alone-basis, which means independently of the parties as regards the supply of input materials or other forms of cooperation other than during a transitory period.⁶¹⁴
- (754) The intended effect of the divestiture will only be achieved if and once the business is transferred to a suitable purchaser in whose hands it will become an active competitive force in the market. The potential of a business to attract a suitable purchaser is an important element already of the Commission's assessment of the appropriateness of the proposed commitments. In order to ensure that the business is divested to a suitable purchaser, the commitments must include criteria to define the suitability of potential purchasers. This will allow the Commission to conclude that the divestiture of the business to such a purchaser will likely remove the competition concerns identified.⁶¹⁵

8.2. Description of the Commitments of 27 November 2015

- (755) Under the Commitments of 27 November 2015, the Parties propose to divest the legal entity [...] following a restructuring to exclude from the divestiture (i) any business activities, assets, personnel and legal entities which relate exclusively to the direct, wholesale and retail channels (except in Sweden) and (ii) any business activities, assets, personnel and legal entities outside the EEA (hereinafter referred to as "the divestment business of 27 November 2015").
- (756) This would in principle result in the divestment of Office Depot's activities in
- (a) the B2B distribution of office supplies through the contract channel in the EEA and Switzerland (hereinafter referred to as the "EEA Contract Business"); and
 - (b) the B2B distribution of office supplies through the contract, direct, retail and wholesale channels in Sweden (hereinafter referred to as "the Swedish divestment business").⁶¹⁶
- (757) The Commitments of 27 November 2015 allow for the Commission to approve the sale of the divestment business of 27 November 2015 without the business activities of one or more countries if this does not affect the viability and competitiveness of the divestment business after the sale, taking account of the proposed purchaser.⁶¹⁷

⁶¹² Remedies Notice, paragraphs 23-25.

⁶¹³ Remedies Notice, paragraph 26.

⁶¹⁴ Remedies Notice, paragraph 32.

⁶¹⁵ Remedies Notice, paragraph 47.

⁶¹⁶ Paragraph 6 of the Commitments of 27 November 2015 in conjunction with paragraph 1 of the Schedule to the Commitments of 27 November 2015.

⁶¹⁷ Paragraph 19 of the Commitments of 27 November 2015.

This clause extends the scope of the relevant clause in the model text for divestiture commitments of the Commission which allows for the Commission to approve the sale of the divestment business without one or more assets or parts of the personnel or by substituting one or more Assets or parts of the Personnel with one or more different assets or different personnel.⁶¹⁸

(758) The Commitments of 27 November also include an up-front buyer clause. The transaction shall not be implemented before a final binding sale and purchase agreement for the sale of the divestment business has been signed and the Commission has approved the purchaser and terms of sale.⁶¹⁹

8.2.1. *Main assets, contracts and personnel*

(759) The divestment business of 27 November 2015 comprises the following main assets, contracts⁶²⁰ and personnel:⁶²¹

- (a) a warehouse/distribution centre in Senlis, France;
- (b) leases on a total of 17 additional warehouses/distribution centres in the Czech Republic, France, Germany, Ireland, Italy, the Netherlands, Spain, Sweden, Switzerland and the UK;
- (c) the inventory in the warehouses which are relevant for the divestment business of 27 November 2015;
- (d) the current customer contracts for the EEA Contract Business and international key account customers;
- (e) customer lists for the EEA contract business and international key account customers;
- (f) agreements with the logistics providers that supply the relevant products for the EEA Contract Business;
- (g) the partnership agreements for the distribution of office supplies for the EEA Contract Business;
- (h) to the extent their geographical scope is limited within the EEA, the assignment of the "Office Depot" trademarks which are related to and used predominantly by the EEA Contract Business;
- (i) to the extent their geographical scope is beyond the EEA, an irrevocable, assignable, sub-licensable and royalty-free license to use the "Office Depot" brand and the "Office Depot" trademarks in the EEA which are related to and used predominantly by the EEA Contract Business;
- (j) IT software and hardware used by Office Depot predominantly for the EEA Contract Business;
- (k) Personnel related to the EEA Contract Business and personnel employed by the Swedish divestment business as well as indispensable key personnel.

⁶¹⁸ Paragraph 17 of the model text, available at http://ec.europa.eu/competition/mergers/legislation/template_commitments_en.pdf.

⁶¹⁹ Paragraph 3 of the Commitments of 27 November 2015.

⁶²⁰ The transfer of the contracts is subject to the consent of third parties to the extent such consent is contractually required.

⁶²¹ Paragraph 2 (a)-(g) of the Schedule to the Commitments of 27 November 2015.

(760) If there is any asset or personnel which is not covered by the lists in the Schedule to the Commitments of 27 November 2015, but which is both used, exclusively or not, in the divestment business of 27 November 2015 and is necessary for the continued viability and competitiveness of the divestment business of 27 November 2015, that asset or adequate substitute will be offered to potential purchasers.⁶²²

8.2.2. *Transitional agreements*

(761) The Parties also propose, at the option of the purchaser, to enter into transitional agreements with the purchaser concerning the following main products and services to be provided to the divestment business of 27 November 2015 by Staples:⁶²³

- (a) own-brand products of Office Depot currently distributed through the contract channel for a period of [...] after transfer of the legal title of the divestment business of 27 November 2015 to the purchaser (that transfer will hereafter be referred to as "closing");
- (b) merchandising / procurement and supply chain services for a period of [...] after closing;
- (c) IT and marketing support for a period of [...] after closing;
- (d) IT software and hardware which is shared between the EEA Contract Business and the direct business retained by the merged entity for a period of [...] after closing.

(762) Upon request of the monitoring trustee, the period for the transitional arrangements could be further extended [...], in consultation with the Commission, if required to preserve the viability and competitiveness of the divestment business of 27 November 2015, unless any delays in the operation of the divestment business are due to the negligence or bad faith of the purchaser.⁶²⁴

8.2.3. *Purchaser requirements*

(763) The requirements for the purchaser of the divestment business set out in the Commitments of 27 November 2015 correspond to the standard requirements contained in the model text for divestiture commitments of the Commission.⁶²⁵ They require, in particular, that (i) the purchaser must be independent of and unconnected to Staples, (ii) the purchaser must have the financial resources, proven expertise and incentive to maintain and develop the divestment business of 27 November as a viable and competitive force, and (iii) the acquisition by the purchaser must not be likely to create *prima facie* competition concerns nor give rise to a risk that the implementation of the commitments will be delayed.

⁶²² Paragraph 4 of the Schedule to the Commitments of 27 November 2015; that clause also applies to the products and services offered through transitional agreements under paragraph 2 (h) of the Schedule to the Commitments of 27 November 2015.

⁶²³ Paragraph 2 (h) of the Schedule to the Commitments of 27 November 2015.

⁶²⁴ Paragraph 8 of the Commitments of 27 November 2015.

⁶²⁵ Paragraph 17 of the model text, available at http://ec.europa.eu/competition/mergers/legislation/template_commitments_en.pdf.

8.3. Assessment of the Commitments of 27 November 2015

8.3.1. The views of the Parties

(764) The Parties submit that the divestiture of the divestment business of 27 November 2015 would remove any potential competition concerns with respect to the contract channel in the EEA by removing the entire overlap in the EEA contract channel.

(765) Furthermore, according to the Parties, the object of the Commitments of 27 November 2015 is to provide a purchaser with the capacity and resources necessary to distribute office supplies through the contract channel to B2B customers in the EEA and through the wholesale and direct channels to customers in Sweden. Therefore, according to the Parties, the purchaser would replace Office Depot as a competitor in the relevant markets and the competitive dynamics would not be adversely affected by the transaction as modified by the Commitments of 27 November 2015.⁶²⁶

8.3.2. Results of the market test and Commission's assessment

(766) The Commission's assessment focused on (i) whether the Commitments of 27 November 2015 were suitable and sufficient to remove the competition concerns caused by the transaction; (ii) whether the divestment business of 27 November 2015 constituted a viable business able to compete effectively with the merged entity on a lasting basis; (iii) whether there were specific conditions that a potential purchaser should fulfil and (iv) whether the divestment business of 27 November 2015 was sufficiently attractive to find a suitable purchaser.

(767) On 30 November 2015, the Commission launched a market test regarding the Commitments of 27 November 2015 covering all of the questions outlined in recital (766). The results of the market test showed that the Commitments of 27 November 2015 were in principle deemed a suitable solution to resolve the competition concerns identified by the Commission. Yet a limited number of issues impacting the viability and competitiveness of the divestment business of 27 November 2015 were also identified. Those issues were addressed by the Parties through improvements made in the Final Commitments.

8.3.2.1. Suitability of the Commitments of 27 November 2015 and removal of competition concerns

(768) The Commitments of 27 November 2015 include Office Depot's activities in Sweden and Office Depot's activities in the distribution of office supplies through the contract channel in the EEA and Switzerland. As regards the contract channel in particular, the divestment business is active through its own distribution activities in Austria, Belgium, the Czech Republic, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Slovakia, Spain, Sweden, Switzerland and the United Kingdom. In addition, it has distribution agreements in the contract channel with third party distributors in Croatia, Denmark, Finland, Norway, and Poland.⁶²⁷ Furthermore, Office Depot is [...]. The divestment business will thus be active in the contract channel in 21 countries (20 EEA countries and Switzerland).

(769) As the Commitments include the divestment of all of Office Depot's activities in the contract channel in the EEA and Switzerland and all of Office Depot's activities in Sweden, the Commitments of 27 November 2015 remove the entire overlap between

⁶²⁶ Form RM of 27 November 2015, paragraphs 5 and 14.

⁶²⁷ Form RM of 27 November 2015, paragraph 4.

the Parties' activities in all of the markets in which the transaction would lead to a significant impediment to effective competition as summarised in recital (742). In particular, as regards the contract channel, the Commitments of 27 November include all of the activities of Office Depot in the distribution of traditional office supplies as well as the distribution of stationery through contracts so that the Commitments of 27 November 2015 remove the overlaps in the two alternative product markets assessed by the Commission in section 7.2.

- (770) Subject to the assessment in sections 8.3.2.2 to 8.3.2.4, in particular as regards the viability and competitiveness of the divestment business of 27 November 2015, the Commitments are therefore suitable to remove entirely the competition concerns identified by the Commission. This view was shared by the vast majority of customers and competitors who replied to the Commission's market test and who expressed an opinion on that question.⁶²⁸
- (771) As regards the scope of the divestment in the EEA contract channel in particular, the divestment of operations in most of the EEA countries, including its largest economies, and Switzerland is necessary to ensure that the divestment business can become a viable supplier in international contracts in the EEA. The Parties' sales under international contracts are spread over many countries of the EEA: About [...] of the Parties' international contracts and about [...] of Office Depot's international contracts cover more than four EEA countries while about half of the Parties' international contracts cover more than five EEA countries.⁶²⁹
- (772) Similarly, the Parties' 2015 International survey showed that many of the international customers surveyed had responsibility for purchasing office supplies in Germany, the United Kingdom, France, the Netherlands, Spain and Italy, followed by Belgium, Sweden and other countries.

Figure 7: Staples internal document entitled "Data Readout – Key findings for Europe", 17 June 2015, slide 13

[...]

- (773) A similar picture emerged from the Commission's market investigation according to which the customers with international contracts who replied to the investigation purchased office supplies for a number of countries and particularly for Germany, France, the United Kingdom, Belgium, the Netherlands, Sweden, Poland and Spain.⁶³⁰
- (774) Therefore, a competitor for international contracts (i) has to be able to cover at least the large Western European economies to reach the majority of the customers with demand for international contracts but (ii) needs also to rely on a presence in more countries due to the wide geographic spread of the demand. It was thus necessary for the commitments to cover most of the EEA to ensure the preservation of a credible alternative supplier for the international demand.
- (775) Nevertheless, the Commitments of 27 November 2015 provide for some flexibility as regards the assets, legal entities and business activities to be divested. Under the Commitments of 27 November, the Commission may approve the sale of the

⁶²⁸ Replies to Questionnaire R1 – Market test of the Commitments – Competitors - Question 27, and to Questionnaire R2 – Market test of the Commitments – Customers - Question 15.

⁶²⁹ Form CO, Annex 23.

⁶³⁰ Replies to Phase I Questionnaire Q5 to customers (international contracts) – Question 4; replies to Phase II Questionnaire Q8a-j to customers, Question 42.

divestment business without one or more assets or part of the personnel or – and this extends the scope of the equivalent clause in the model text for divestiture commitments of the Commission⁶³¹ – without the business activities of one or more countries, taking account of the proposed purchaser. Thus, if, for example, the purchaser already has business activities in a country which are sufficient in scope to compete effectively for international contracts covering that country, the divestiture could be approved without the sale of those country activities. This clause will thus allow preventing unnecessary divestments in the interest of proportionality.

8.3.2.2. Viability and competitiveness of the divestment business of 27 November 2015

8.3.2.2.1. Current profitability of the divestment business of 27 November 2015

(776) The divestment business of 27 November 2015 had a total turnover of EUR [...] in 2014.⁶³² It achieved an internal gross margin⁶³³ of around [...] and a gross profit margin⁶³⁴ of [...] in the last two and a half years of operation. The distribution costs are accounted for in the gross profit margin. Due to general costs and the costs of selling and administration, the earnings before interest and tax ("EBIT") and the earnings before interest, tax, depreciation and amortisation ("EBITDA") were [...] in that period.⁶³⁵ [...].⁶³⁶

(777) The Commission considers that the profitability of the divestment business appears satisfactory when only the variable costs of sourcing and distributing the products are considered (that is to say the gross profit margin). In addition, the profitability after deduction of all costs will be determined to a large extent by the organisation and structure of the purchaser's existing business and the way the purchaser integrates the divestment business of 27 November 2015 with its existing operations, including any potential synergies.

(778) Therefore, the divestment business of 27 November 2015 appears to be sufficiently profitable to operate as a viable business in the hands of a suitable purchaser. The Commission will be able to further assess those profitability issues also in the context of the buyer approval process when assessing whether the purchaser has the financial resources and incentive to maintain and develop the business as a viable and competitive force in the market.⁶³⁷

8.3.2.2.2. Viability of the divestment business of 27 November in the contract channel

(779) The divestment of Office Depot's distribution activities is limited to the distribution by way of contracts – with the exception of Sweden where all of Office Depot's distribution activities are divested. Contrary to Office Depot's operations before the divestment, the divestment business of 27 November 2015 will thus be active almost entirely in the contract distribution without any significant initial activities in other distribution channels. The Commission has therefore assessed whether operating a business in the contract channel only is a viable option enabling the divestment business of 27 November 2015 to compete in the relevant markets on a lasting basis.

⁶³¹ Paragraph 18 of the model text, available at http://ec.europa.eu/competition/mergers/legislation/template_commitments_en.pdf.

⁶³² See the Parties' reply to the Request for Information of 30 November 2015, question 6.

⁶³³ The internal gross margin is calculated as the sales minus the costs of goods sold.

⁶³⁴ The gross profit is calculated as the sales minus the cost of goods sold and minus the distribution costs.

⁶³⁵ Form RM of 27 November 2015, paragraph 39.

⁶³⁶ *Ibid.*

⁶³⁷ Paragraphs 18 (b) and 19 of the Commitments of 27 November 2015.

- (780) Focussing on one sales channel, including focussing on the contract sales channel only, is not uncommon in the industry.⁶³⁸ The most noteworthy example is Lyreco which focuses its business on the contract sales channel and has only minor operations in other sales channels.⁶³⁹ Lyreco has operated successfully for many years and is currently one of the leading suppliers of office supplies in the contract channel in Europe, as discussed in the competitive assessment for the international level and several national markets in section 8 above. Lyreco's global turnover is around EUR 2 billion⁶⁴⁰ while its European turnover is lower and is therefore closer to the turnover of the divestment business of EUR 1.05 billion. Similarly, the French competitor Fiducial and the Italian competitor MyO currently focus mainly on the contract channel with turnover smaller than the future turnover of the divestment business of 27 November 2015.⁶⁴¹
- (781) The vast majority of market participants who expressed an opinion on this issue during the market test considered that a supplier active only in the contract channel could compete successfully in this market. Only a minority of market participants argued that the presence in other sales channels was necessary, in particular the online channel which is a growing business for office supply companies.⁶⁴²
- (782) The Commission agrees with the view of the majority of respondents to the Commission's market test for the following main reasons: first, as set out in recital (780), there are examples of successful companies which focus only on the contract channel; second, the divestment business' turnover will be substantial and larger than some of the competitors which likewise have a strong focus on the contract channel; third, the divestment business' asset base in logistics and supply chain management consists mainly of leased warehouses which should give it the flexibility to adjust its asset footprint to its reduced scale of operations limited to the contract channel. Therefore, it appears to be a viable business option for the divestment business to be active almost entirely in the contract sales channel.

8.3.2.2.3. Carve-out of the retained business

- (783) The divestment business with its focus on the distribution of office supplies by way of contracts – with the exception of Sweden where all of Office Depot's distribution activities are divested – will have to be separated from the remaining Office Depot distribution activities which are currently integrated with the contract business and which will be retained by the merged entity. While such a carve-out carries implementation risks, the carve-out – taking into account the principle of proportionality – is an adequate solution in this case since such risks have been limited sufficiently in the Commitments of 27 November 2015.⁶⁴³

⁶³⁸ In contrast, focussing on the sale of stationery only is uncommon in the industry. Thus, divesting only the sale of stationery – a solution not discussed by the Parties with the Commission in this case – would potentially have led to issues concerning the viability of the divested business.

⁶³⁹ Agreed minutes of the conference call with Lyreco of September 2015.

⁶⁴⁰ See Lyreco's website at <http://group.lyreco.com/gbr/about-lyreco,22/our-story,2955.html> (last accessed on 16 December 2015).

⁶⁴¹ Response of Fiducial and MyO to Questionnaire R1 – Market test of the Commitments – Competitors, question 4.

⁶⁴² Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 3, and Questionnaire R2 – Market test of the Commitments – Customers – Question 4.

⁶⁴³ In contrast, divesting only the sale of stationery – a potential approach to the remedies which was not discussed by the Parties with the Commission in this case – would potentially have led issues with the carve-out and with ensuring the divestment of a stand-alone business.

- (784) First, the Commitments of 27 November 2015 include an up-front buyer clause according to which the transaction shall not be implemented before a final binding sale and purchase agreement for the sale of the divestment business has been signed and the Commission has approved the purchaser and terms of sale.⁶⁴⁴ This provision results in a higher degree of certainty that the carve-out will be carried out in a timely and efficient manner before the transaction is closed.
- (785) Second, as regards the carve-out of certain centralised functions, the divestment business of 27 November 2015 relies on centralised functions only through the EEA headquarters in Venlo/Netherlands and two offices in Leicester/United Kingdom (merchandising/ procurement and supply chain services as well as IT and marketing support) and Cluj/Romania (accounts receivable and accounts payable services). The transitional agreements included in the Commitments of 27 November 2015 – to be entered into at the request of the purchaser – ensure that the purchaser will have access to the central functions in Leicester and Cluj for a period of [...] and that the purchaser can use the venues and facilities in Venlo for [...]. The periods can be extended upon request by the monitoring trustee [...]. This will give the purchaser sufficient time to set up its own functions in this respect.
- (786) Third, as regards the personnel, there is a lack of clarity in the Commitments of 27 November 2015 as to how the personnel are to be attributed between the divestment business of 27 November 2015 and the merged entity in practice. The Commitments refer to the transfer of all personnel "*related to*" the EEA Contract Business without specifying how this is to be interpreted, in particular with respect to any shared personnel. However, even if the merged entity tries to retain personnel who work for the divestment business of 27 November 2105 and who are necessary for its continued viability and competitiveness, the purchaser will be able to demand that such personnel or adequate substitutes are offered. Therefore, the risks of carving out the divestment business of 27 November 2015 in terms of personnel are limited under the Commitments of 27 November 2015.

8.3.2.2.4. Access to office supplies

- (787) The replies received from market participants in the market test underline the importance of having competitive access to office supply products from wholesalers and manufacturers, both for own-brand and branded products, for the divestment business of 27 November 2015 to be competitive. This is particularly important in the period immediately following the divestment to ensure that the divestment business of 27 November 2015 does not lose its client base. One competitor explained: "*The key will be the capability of the purchaser to manage the transition period rapidly, and re-gain employees and customer confidence.*"⁶⁴⁵
- (788) The clear majority of competitors answering to that question in the market test considered that the purchaser of the divestment business of 27 November 2015 will be able to source products from manufacturers at prices that will allow it to be a viable and competitive supplier on the market at the national and international level.⁶⁴⁶ In their explanations, the competitors referred mainly to the scale of the divestment business of 27 November 2015. One competitor explained for instance: "*The new player will remain in the Top 5 players on the OS distribution and in the top 3 of the contract business in EEA.*" Other competitors explained that the

⁶⁴⁴ Paragraph 3 of the Commitments of 27 November 2015; see also Remedies Notice, paragraph 36.

⁶⁴⁵ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 6.1.

⁶⁴⁶ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 24.

manufacturers would have an interest in keeping the divestment business of 27 November 2015 competitive which would provide incentives for them to offer competitive prices to the divestment business of 27 November 2015.⁶⁴⁷ The clear majority of customers and competitors also considered that the purchaser of the divestment business of 27 November 2015 will be able to develop and source its own private label products at prices allowing it to be competitive on the market.⁶⁴⁸

- (789) Nevertheless, some competitors came forward with certain reservations during the market test concerning the divestment business' competitive access to office supplies. According to those competitors, the divestment business of 27 November 2015 may have to off-set its less advantageous access to office supplies with an enhanced service reliability or quality to be able to compete successfully.⁶⁴⁹
- (790) The Commission considers that the scale of the divestment business of 27 November 2015 is likely to enable it to have competitive access to office supplies in the longer term. Nevertheless, the divestment business of 27 November 2015 could be vulnerable in the period immediately following the divestment because it will have to honour the existing agreements with customers to keep its sales at the current levels and it will have to win customers' trust. The transitional agreements for office supplies included in the Commitments of 27 November 2015 are limited to the supply of Office Depot's own branded products, however, and do not cover other office supplies. This weakens the competitiveness of the divestment business of 27 November 2015 in the short term.

8.3.2.2.5. Transfer of customer contracts

- (791) The Commission has also assessed the risk of transferring the customer contracts to the divestment business in the light of potential consent required by the customers and in the light of the non-exclusivity of the contracts.
- (792) The Commission notes in this respect that Office Depot estimates that customer contracts with change of control clauses represent at most approximately [...] of the overall contract sales and [...] of the overall number of contracts. Therefore, a significant number of contracts and associated sales volume should in principle transfer to the purchaser automatically.
- (793) Furthermore, Office Depot's current customers who replied to the market test questionnaire showed a willingness to adhere to the present contracts and to continue purchasing from the divestment business in the future, provided that the purchaser will be able to offer the same prices, quality of products and conditions as currently offered by Office Depot. The following comment is representative of the comments received from many current Office Depot customers in the market test: *"If the purchaser can provide the same service, competitive pricing and customer care as Office Depot we would consider to keep purchasing office supplies from the purchaser"*. The limited number of current customers who replied that they would not continue purchasing from the divestment business either pointed to circumstances not specific to the divestment (such as the contract period having

⁶⁴⁷ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 24.1.

⁶⁴⁸ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 20; replies to Questionnaire R2 – Market test of the Commitments – Customers – Question 12.

⁶⁴⁹ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 24.1. One competitor explained: *"The purchaser must have access to vendor commitments that warrant same, or similar, purchase pricing as Office Depot/Staples currently have"*.

come to an end) or explained that a new tender would have to be carried out before deciding on that question.⁶⁵⁰

- (794) Similarly, the replies received from the customers contacted in the market test – regardless of whether they are currently customers of Office Depot or not – were generally positive as regards the customers' willingness to consider concluding a contract for office supplies with the divestment business in the future. Again, the limited number of negative replies was overwhelmingly related to circumstances unrelated to the divestment.⁶⁵¹
- (795) As regards international contracts in particular, the competitors are confident that the divestment business of 27 November 2015 will be able to be competitive in international contracts. The vast majority of competitors answering to that question in the market test consider that the divestment business of 27 November 2015 will be able to provide the necessary services that international contracts require, in particular in terms of logistics solutions.⁶⁵² Furthermore, the majority of the competitors answering to that question in the Commission's market test considered that the customers with global contracts – thus covering more countries than the countries in EEA – would continue purchasing their office supplies needs in the EEA from the divestment business of 27 November 2015 after the contracts would be split between the divested business in the EEA and the merged entity outside of the EEA.⁶⁵³
- (796) While some competitors and international customers considered that splitting the contracts between the EEA and the rest of the world was not a favourable option,⁶⁵⁴ the Commission recalls its findings from the discussion of the geographic market definition (section 6.2.1). While the overwhelming majority of Office Depot's customers with international contracts have some spending outside of the EEA, EEA sales represent approximately [...] of Office Depot's sales to international customers.⁶⁵⁵ Furthermore, a majority of those customers purchase under a European or regional contract as opposed to a global contract. This indicates that many customers with international customers already have split contracts in place, one for the EEA and at least one for the rest of the world. Therefore, the risk of losing international business due to the need to split global contracts is likely to be limited for the viability and competitiveness of the divestment business of 27 November 2015.

8.3.2.2.6. Terms of the transitional agreements

- (797) The Commitments of 27 November 2015 do not contain any pricing clause for the transitional agreements and thus leave that question to the future negotiations between Staples, Office Depot and the purchaser of the divestment business of 27 November 2015.
- (798) In addition to extending the scope of the transitional agreements to include all office supply products as discussed in recital (790), the responses to the Commission's market test indicated that the products and services under the transitional agreements

⁶⁵⁰ Replies to Questionnaire R2 – Market test of the Commitments – Customers – Question 6.

⁶⁵¹ Replies to Questionnaire R2 – Market test of the Commitments – Customers – Question 8.

⁶⁵² Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 16.

⁶⁵³ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 9.

⁶⁵⁴ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 9; responses to Questionnaire R2 – Market test of the Commitments – Customers – Question 7.

⁶⁵⁵ See reply to RFI of 13 November 2015, question 1.

should be provided to the divestment business of 27 November 2015 at cost. The objective should be that the divestment business will have at least as favourable input costs for those products and services as Office Depot has today.⁶⁵⁶

- (799) The Commission considers that leaving the pricing open in the Commitments leads to the risk that the divestment business will have to agree to terms and conditions in the transitional agreements which might negatively affect its competitiveness in the crucial period after the divestment. Therefore, the Commitments of 27 November 2015 do not contain sufficient safeguards to guarantee that the products and services under the transitional agreements will be provided at terms and conditions that allow a smooth transition and guarantee the competitiveness of the divestment business of 27 November 2015 immediately after the divestment.

8.3.2.3. Purchaser criteria

- (800) As regards the criteria to identify a suitable purchaser for the divestment business of 27 November 2015, the competitors answering to that question in the market test considered that experience in the industry was required to run the divestment business viably and competitively.⁶⁵⁷ Furthermore, the competitors underlined that the divestment business of 27 November 2015 included many capabilities required by the purchaser, for example in terms of management, sales, logistics and IT expertise, but also maintained that the business could potentially benefit from synergies to be achieved through divesting the divestment business of 27 November 2015 to an existing office supply company.⁶⁵⁸

- (801) The Commission considers that – after the carve-out to be carried out by the Parties as set out in the Commitments of 27 November 2015 – the divestment business of 27 November 2015 will constitute a stand-alone business with significant in-house capacities, including in terms of management, logistics, IT and sales. Therefore, it is not necessary to restrict the pool of potential purchasers of the divestment business of 27 November 2015 to those with prior activities in the office supply business. Pursuant to the purchaser criteria of the Commitments of 27 November 2015, the purchaser will have to show that it has, among other things, the financial resources, proven expertise and incentive to maintain and develop the divestment business of 27 November as a viable and competitive force. Therefore, the considerations brought forward by the competitors during the market test can be taken into account in a satisfactory manner when the Commission will assess the conditions of the purchaser criteria of the Commitments of 27 November 2015 during the buyer approval process.

8.3.2.4. Attractiveness of the divestment business of 27 November 2015 for potential purchasers

- (802) The vast majority of the customers and competitors who expressed an opinion on that question in the Commission's market test considered that the divestment business of 27 November 2015 was sufficiently interesting to attract suitable purchasers.⁶⁵⁹ Issues raised by a limited number of market participants concerned the scale of the divestment business and its access to products at low purchasing prices, which the

⁶⁵⁶ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 23.

⁶⁵⁷ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 29.

⁶⁵⁸ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Questions 30 and 31.

⁶⁵⁹ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 28, and Questionnaire R2 – Market test of the Commitments – Customers – Question 13.

Commission does not consider to constitute significant obstacles for the divestment business' competitiveness as discussed in recitals (779) to (782) and (787) to (790).

- (803) The Commission received tentative expressions of interest from a handful of potential purchasers in the course of the market test, both from industry buyers and private equity companies.⁶⁶⁰ This indicates that the divestment business of 27 November 2015 may be sufficiently attractive to generate interest in the market. To alleviate any remaining concerns in this regard, the Commitments of 27 November 2015 include an up-front buyer clause, as outlined in recital (758).
- (804) Therefore, the Commission considers that there is a sufficient likelihood that the divestment business of 27 November 2015 will find a suitable buyer.

8.3.2.5. Conclusion

- (805) In the light of the market test, the Commission considered that the Commitments of 27 November 2015 were generally suitable to address the Commission's competition concerns but contained risks for the viability and competitiveness of the divestment business of 27 November 2015 as regards the terms and scope of the transitional agreements, in particular for the supply of office products to the divestment business of 27 November 2015, and as regards the splitting of assets and in particular of personnel between the divestment business of 27 November 2015 and the merged entity.

8.4. Description of the Final Commitments

- (806) The Parties submitted the Final Commitments on 10 December 2015 which maintain the basic scope and structure of the Commitments of 27 November 2015 and make limited changes to the Commitments of 27 November 2015 mainly in the following ways:
- (a) The definition of the divestment business,⁶⁶¹ the separation of assets between the divestment business and the Parties, including the separation of shared personnel,⁶⁶² and the modalities of the divestment⁶⁶³ are clarified in the Commitments and its Schedule.
 - (b) All transitional agreements will be offered to the purchaser at cost.⁶⁶⁴
 - (c) The transitional agreements are extended to cover the supply of all office products from Office Depot's vendors for [...].⁶⁶⁵ The transitional supply agreement was previously limited to own-brand products under the

⁶⁶⁰ Replies to Questionnaire R1 – Market test of the Commitments – Competitors – Question 33.

⁶⁶¹ Paragraph 6 of the Final Commitments; paragraphs 1 and 2 of the Schedule to the Final Commitments.

⁶⁶² The Final Commitments provide for the divestment of all entities comprising the divestment business while allowing a reverse carve-out of those business activities, assets, personnel and legal entities which relate exclusively or predominantly to the business retained by the merged entity, see paragraph 2 of the Schedule to the Final Commitments. As regards the personnel, any personnel not used predominantly by any of the distribution channels will transfer with the divestment business of 27 November 2015, see footnote 2 of the Final Commitments.

⁶⁶³ There is now some flexibility regarding the legal entities to be divested. That flexibility is complemented by an additional safeguard clause pursuant to which any carve-out of business activities, assets, personnel, and legal entities by Staples can only be carried out provided that the exclusion does not have any adverse effect on the viability and competitiveness of the divestment business and that the divestment business is transferred to the purchaser under the supervision of the monitoring trustee, see paragraph 2 of the Schedule to the Final Commitments.

⁶⁶⁴ Clause 8 of the Commitments.

⁶⁶⁵ Paragraph 3(h)(ii) of the Schedule to the Final Commitments.

Commitments of 27 November 2015. The new clause in the Final Commitments intends to allow the purchaser to continue purchasing the office products from Office Depot's vendors under currently agreed terms for the transitional period.

- (d) The list of leases of warehouses has been updated and reduced to include only the leases of the 15 leased warehouses currently in use.⁶⁶⁶
- (e) The Parties will be able to enter into transitional agreements with the purchaser relating to (i) support from previously shared personnel for [...], (ii) use of the Office Depot trademarks in the EEA for [...] and (iii) access and use rights for previously shared warehouses for [...].⁶⁶⁷
- (f) The list of assets includes more systematic references to the assets to be divested for Office Depot's business in Sweden.⁶⁶⁸

8.5. Assessment of the Final Commitments

- (807) The Commission considers that the Final Commitments fully address its concerns with respect to the Commitments of 27 November 2015, in particular as regards the scope and terms of the transitional agreements and the splitting of assets between the divestment business and the merged entity. In all other respects, the Commission's assessment of the suitability of the Commitments of 27 November 2015 set out in section 8.3 applies in the same way to the Final Commitments.

8.6. Conclusion on the remedies

- (808) In light of the assessment set out in sections 8.1 to 8.5, the Commission concludes that the Final Commitments are adequate and sufficient to eliminate the significant impediment to effective competition identified by the Commission.

9. CONDITIONS AND OBLIGATIONS

- (809) Pursuant to the second subparagraph of Article 8(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the internal market.
- (810) The fulfilment of a measure that gives rise to a structural change of the market is a condition, whereas the implementing steps which are necessary to achieve that result are generally obligations on the parties. Where a condition is not fulfilled, the Commission's decision declaring the concentration compatible with the internal market is no longer applicable. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(6) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2) and 15(1) of the Merger Regulation.
- (811) In accordance with the basic distinction described in recital (810) as regards conditions and obligations, this Decision should be made conditional on the full compliance by Staples with section B and the Schedule of the Commitments of

⁶⁶⁶ Paragraph 3(d) of the Schedule to the Final Commitments.

⁶⁶⁷ Footnote 2 and paragraphs 3(b)(i) and 3(d)(xii) of the Schedule to the Final Commitments.

⁶⁶⁸ Paragraph 3 of the Schedule to the Final Commitments.

10 December 2015. All other sections should be obligations within the meaning of Article 8(2) of the Merger Regulation. The full text of the commitments is set out in the Annex to this Decision and forms an integral part thereof.

HAS ADOPTED THIS DECISION:

Article 1

The notified operation whereby Staples, Inc. acquires sole control of Office Depot, Inc. within the meaning of Article 3(1)(b) of the Regulation (EC) No 139/2004 is hereby declared compatible with the internal market and the EEA Agreement.

Article 2

Article 1 is subject to compliance with the conditions set out in section B and the Schedule of the Annex.

Article 3

Staples, Inc. shall comply with the obligations set out in sections A, C, D, E and F of the Annex.

Article 4

This Decision is addressed to:

Staples, Inc.

500 Staples Drive

Framingham MA 01702

United States of America

Done at Brussels, 10.2.2016

For the Commission

(Signed)

Margrethe VESTAGER

Member of the Commission

Case M. 7555 – Staples/Office Depot

COMMITMENTS TO THE EUROPEAN COMMISSION

Pursuant to Articles 8(2) and 10(2) of Council Regulation (EC) No 139/2004 (the "*EU Merger Regulation*"), Staples, Inc (the "*Notifying Party*" or "*Staples*") and Office Depot, Inc. ("*Office Depot*") hereby enter into the following commitments (the "*Commitments*") vis-à-vis the European Commission (the "*Commission*") with a view to rendering the acquisition by Staples of sole control over Office Depot (the "*Concentration*") compatible with the internal market and the functioning of the EEA Agreement.

This text shall be interpreted in light of the Commission's decision pursuant to Article 8(2) of the EU Merger Regulation to declare the Concentration compatible with the internal market and the functioning of the EEA Agreement (the "*Decision*"), in the general framework of European Union law, in particular in light of the EU Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the "*Remedies Notice*").

Section A. Definitions

1. For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled from time to time by the Parties and/or by the ultimate parents of the Parties, whereby the notion of control shall be interpreted pursuant to Article 3 of the EU Merger Regulation and in light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (the "*Consolidated Jurisdictional Notice*").

Assets: the assets that contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Business as indicated in Section B, paragraph 6 (a), (b) and (c) and described more in detail in the Schedule.

Closing: the transfer of the legal title to the Divestment Business to the Purchaser.

Closing Period: the period of [...] from the approval of the Purchaser and the terms of sale by the Commission.

Confidential Information: any business secrets, know-how, commercial information, or any other information of a proprietary nature that is not in the public domain.

Conflict of Interest: any conflict of interest that impairs the Trustee's objectivity and independence in discharging its duties under the Commitments.

Divestment Business: the business or businesses as defined in Section B and the Schedule, which Staples commits to divest.

Divestiture Trustee: one or more natural or legal person(s) who is/are approved by the Commission and appointed by Staples and who has/have received from Staples the exclusive Trustee Mandate to sell the Divestment Business to a Purchaser at no minimum price.

Effective Date: the date of adoption of the Decision.

First Divestiture Period: the period of [...] from the Effective Date.

Hold Separate Manager: the person appointed by the Parties for the Divestment Business to manage the day-to-day business under the supervision of the Monitoring Trustee.

HSR Act: the Hart-Scott-Rodino Antitrust Improvements Act of 1976 as amended

HSR Closing Date: the date that the Parties are legally able to close the Concentration under the HSR Act (and so long as this date is on or after the Effective Date)

Key Personnel: all personnel necessary to maintain the viability and competitiveness of the Divestment Business, as listed in the Schedule, including the Hold Separate Manager.

Monitoring Trustee: one or more natural or legal person(s) who is/are approved by the Commission and appointed by the Parties, and who has/have the duty to monitor the Parties' compliance with the conditions and obligations attached to the Decision.

Office Depot: Office Depot, Inc., incorporated under the laws of Delaware, with its registered office at Boca Raton, Florida and registered under Employer Identification Number 59-2663954.

Parties: Staples and Office Depot.

Personnel: all staff currently employed by the Divestment Business, including staff seconded to the Divestment Business, shared personnel as well as the additional personnel listed in the Schedule.

Purchaser: the entity approved by the Commission as acquirer of the Divestment Business in accordance with the criteria set out in Section D.

Purchaser Criteria: the criteria laid down in paragraph 19 of these Commitments that the Purchaser must fulfil in order to be approved by the Commission.

Schedule: the schedule to these Commitments describing more in detail the Divestment Business.

Trustee(s): the Monitoring Trustee and/or the Divestiture Trustee as the case may be.

Trustee Divestiture Period: the period of [...] from the end of the First Divestiture Period.

Section B. The commitment to divest and the Divestment Business

Commitment to divest

2. In order to maintain effective competition, Staples commits to divest, or procure the divestiture of, the Divestment Business by the end of the Trustee Divestiture Period as a going concern to a purchaser and on terms of sale approved by the Commission in accordance with the procedure described in paragraph 20 of these Commitments. To carry out the divestiture, Staples commits to find a purchaser and to enter into a final binding sale and purchase agreement for the sale of the Divestment Business within the First Divestiture Period. If Staples has not entered into such an agreement at the end of the First Divestiture Period, Staples shall grant the Divestiture Trustee an exclusive mandate to sell the Divestment Business in accordance with the procedure described in paragraph 32 in the Trustee Divestiture Period.
3. The Concentration shall not be implemented before Staples or the Divestiture Trustee has entered into a final binding sale and purchase agreement for the sale of the Divestment Business and the Commission has approved the purchaser and the terms of sale in accordance with paragraph 20. The divestiture of the Divestment Business shall only be consummated if, and after, the Concentration is consummated. In the event that the Concentration lapses, these Commitments shall lapse.
4. The Parties shall be deemed to have complied with this commitment if:
 - (a) by the end of the Trustee Divestiture Period, Staples or the Divestiture Trustee has entered into a final binding sale and purchase agreement and the Commission approves the proposed Purchaser and the terms of sale as being consistent with the Commitments in accordance with the procedure described in paragraph 20; and
 - (b) the Closing of the sale of the Divestment Business to the Purchaser takes place within the Closing Period.
5. In order to maintain the structural effect of the Commitments, Staples shall, for a period of 10 years after Closing, not acquire, whether directly or indirectly, the possibility of exercising influence (as defined in paragraph 43 of the Remedies Notice, footnote 3) over the whole or part of the Divestment Business, unless, following the submission of a reasoned request from the Notifying Party showing good cause and accompanied by a report from the Monitoring Trustee (as provided in paragraph 46 of these Commitments), the Commission finds that the structure of the market has changed to such an extent that the absence of influence over the Divestment Business is no longer necessary to render the proposed concentration compatible with the internal market.

Structure and definition of the Divestment Business

6. The Divestment Business consists of Office Depot's business-to-business distribution of office supplies through the contract channel in the EEA, including Switzerland and of Office Depot's business-to-business distribution of office suppliers through all distribution channels in Sweden.

The legal and functional structure of the Divestment Business as operated to date is described in the Schedule. The Divestment Business, as described in more detail in the Schedule, includes all assets and staff that contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Business, in particular:

- (a) all tangible and intangible assets (including intellectual property rights);
 - (b) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Divestment Business;
 - (c) all contracts, leases, commitments and customer orders of the Divestment Business; all customer, credit and other records of the Divestment Business; and
 - (d) the Personnel.
7. To the extent the transfer of the assets described in paragraphs (3) (d) and (3) (e) (i) in the Schedule is subject to a third parties contractually required consent, the Parties commit to endeavour best efforts to obtain such consents.
8. In addition, the Divestment Business includes the benefit of various transitional arrangements on an at cost basis, as detailed in the Schedule. Upon request of the Monitoring Trustee, the period for the transitional arrangements as detailed in the Schedule will be further extended up to [...], in consultation with the Commission, if required to preserve the viability and competitiveness of the Divestment Business, unless any delays in the operation of the Divestment Business are due to negligence or bad faith of the Purchaser.
9. Strict firewall procedures will be adopted so as to ensure that any competitively sensitive information related to, or arising from such supply arrangements (for example, product roadmaps) will not be shared with, or passed on to, anyone other than for the purpose of implementation of these Commitments.

Section C. Related commitments

Preservation of viability, marketability and competitiveness

10. From the HSR Closing Date until Closing, the Parties shall preserve or procure the preservation of the economic viability, marketability and competitiveness of the Divestment Business, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Business. In particular the Parties undertake:
- (a) not to carry out any action that might have a significant adverse impact on the value, management or competitiveness of the Divestment Business or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of the Divestment Business;

- (b) to make available, or procure to make available, sufficient resources for the development of the Divestment Business, on the basis and continuation of the existing business plans; and
11. From the Effective Date until Closing, the Parties undertake to take all reasonable steps, or procure that all reasonable steps are being taken, including appropriate incentive schemes (based on industry practice), to encourage all Key Personnel to remain with the Divestment Business, and not to solicit or move any Personnel to the Parties remaining business. Where, nevertheless, individual members of the Key Personnel exceptionally leave the Divestment Business, the Parties shall provide a reasoned proposal to replace the person or persons concerned to the Commission and the Monitoring Trustee. The Parties must be able to demonstrate to the Commission that the replacement is well suited to carry out the functions exercised by those individual members of the Key Personnel. The replacement shall take place under the supervision of the Monitoring Trustee, who shall report to the Commission.

Hold-separate obligations

12. From the HSR Closing Date until Closing the Parties commit to procure that the Divestment Business is kept separate from the businesses that the Parties will be retaining and, after Closing to keep the Divestment Business separate from the business Staples is retaining and to ensure that unless explicitly permitted under these Commitments: (i) management and staff of the business retained by the Parties have no involvement in the Divestment Business; (ii) the Key Personnel and Personnel of the Divestment Business have no involvement in any business retained by the Parties and do not report to any individual outside the Divestment Business.
13. From the HSR Closing Date until Closing, the Parties shall assist the Monitoring Trustee in ensuring that the Divestment Business is managed as a distinct and saleable entity separate from the business which the Parties are retaining and in accordance with paragraph 10 above. Immediately after the HSR Closing Date, the Parties shall appoint a Hold Separate Manager, who shall be part of the Key Personnel. The Hold Separate Manager shall manage the Divestment Business independently and in the best interests of the business with a view to ensuring its continued economic viability, marketability and competitiveness and its independence from the business retained by the Parties. The Hold Separate Manager shall closely cooperate with and report to the Monitoring Trustee and, if applicable, the Divestiture Trustee. Any replacement of the Hold Separate Manager shall be subject to the procedure laid down in paragraph 10(c) of these Commitments. The Commission may, after having heard the Parties, require the Parties to replace the Hold Separate Manager.

Ring-fencing

14. From the HSR Closing Date until Closing, the Parties shall, to the extent reasonably practicable, implement, or procure to implement, all necessary measures to ensure that they do not, after the HSR Closing Date, obtain any Confidential Information relating to the Divestment Business and that any such Confidential Information obtained by the Parties before the HSR Closing Date will

be eliminated and not be used by the Parties. In particular, the participation of the Divestment Business in any central information technology network shall be severed to the extent possible, without compromising the viability of the Divestment Business. The Parties may obtain or keep information relating to the Divestment Business (i) which is reasonably necessary for the divestiture of the Divestment Business and the implementation of the transitional arrangements; (ii) which is reasonably required to maintain the viability of the Divestment Business; or (iii) the disclosure of which to the Parties is required by law.

Non-solicitation clause

15. The Parties undertake, subject to customary limitations, not to solicit, and to procure that Affiliated Undertakings do not solicit, the Key Personnel transferred with the Divestment Business for a period of 24 months, after Closing.

Due diligence

16. In order to enable potential purchasers to carry out a reasonable due diligence of the Divestment Business, the Parties shall, subject to customary confidentiality assurances and dependent on the stage of the divestiture process:
 - (a) provide to potential purchasers sufficient information as regards the Divestment Business; and
 - (b) provide to potential purchasers sufficient information relating to the Personnel and allow them reasonable access to the Personnel.

Reporting

17. Staples shall submit written reports in English on potential purchasers of the Divestment Business and developments in the negotiations with such potential purchasers to the Commission and the Monitoring Trustee no later than ten working days after the end of every month following the Effective Date (or otherwise at the Commission's request). Staples shall submit a list of all potential purchasers having expressed interest in acquiring the Divestment Business to the Commission at each and every stage of the divestiture process, as well as a copy of all the offers made by potential purchasers within five working days of their receipt.
18. Staples shall inform the Commission and the Monitoring Trustee on the preparation of the data room documentation and the due diligence procedure and shall submit a copy of any information memorandum to the Commission and the Monitoring Trustee before sending the memorandum out to potential purchasers, unless duly justified.

Section D. The Purchaser

19. In order to be approved by the Commission, the Purchaser must fulfil the following criteria:

- (a) The Purchaser shall be independent of and unconnected to Staples and its Affiliated Undertakings (this being assessed having regard to the situation following the divestiture);
- (b) The Purchaser shall have the financial resources, proven expertise and incentive to maintain and develop the Divestment Business as a viable and active competitive force in competition with the Parties and other competitors;
- (c) The acquisition of the Divestment Business by the Purchaser must neither be likely to create, in light of the information available to the Commission, *prima facie* competition concerns nor give rise to a risk that the implementation of the Commitments will be delayed. In particular, the Purchaser must reasonably be expected to obtain all necessary approvals from the relevant regulatory authorities for the acquisition of the Divestment Business.

20. The final binding sale and purchase agreement (as well as ancillary agreements) relating to the divestment of the Divestment Business shall be conditional on the Commission's approval. When Staples has reached an agreement with a purchaser, it shall submit a fully documented and reasoned proposal, including a copy of the final agreement(s), within one week to the Commission and the Monitoring Trustee. Staples must be able to demonstrate to the Commission that the purchaser fulfils the Purchaser Criteria and that the Divestment Business is being sold in a manner consistent with the Commission's Decision and the Commitments. For the approval, the Commission shall verify that the purchaser fulfils the Purchaser Criteria and that the Divestment Business is being sold in a manner consistent with the Commitments including their objective to bring about a lasting structural change in the market. The Commission may approve the sale of the Divestment Business without one or more Assets or parts of the Personnel or without the business activities of one or more countries, or by substituting one or more Assets or parts of the Personnel with one or more different assets or different personnel, if this does not affect the viability and competitiveness of the Divestment Business after the sale, taking account of the proposed purchaser.

Section E. Trustee

I. Appointment procedure

21. The Parties shall appoint a Monitoring Trustee to carry out the functions specified in these Commitments for a Monitoring Trustee. Staples commits not to close the Concentration before the appointment of a Monitoring Trustee.

22. If Staples has not entered into a binding sale and purchase agreement regarding the Divestment Business one month before the end of the First Divestiture Period or if the Commission has rejected a purchaser proposed by Staples at that time or thereafter, Staples shall appoint a Divestiture Trustee. The appointment of the Divestiture Trustee shall take effect upon the commencement of the Trustee Divestiture Period.

23. The Trustee shall:

- (i) at the time of appointment, be independent of the Parties and their Affiliated Undertakings;
- (ii) possess the necessary qualifications to carry out its mandate, for example have sufficient relevant experience as an investment banker or consultant or auditor; and
- (iii) neither have nor become exposed to a Conflict of Interest.

24. The Trustee shall be remunerated by Staples in a way that does not impede the independent and effective fulfilment of its mandate. In particular, where the remuneration package of a Divestiture Trustee includes a success premium linked to the final sale value of the Divestment Business, such success premium may only be earned if the divestiture takes place within the Trustee Divestiture Period.

Proposal by the Parties

25. No later than two weeks after the Effective Date, the Parties shall submit the name or names of one or more natural or legal persons whom the Parties propose to appoint as the Monitoring Trustee to the Commission for approval. No later than one month before the end of the First Divestiture Period or on request by the Commission, the Parties shall submit a list of one or more persons whom the Parties propose to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the person or persons proposed as Trustee fulfil the requirements set out in paragraph 23 and shall include:

- (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;
- (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks;
- (c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether different trustees are proposed for the two functions.

Approval or rejection by the Commission

26. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, the Parties shall appoint or cause to be appointed the person or persons concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Parties shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Parties

27. If all the proposed Trustees are rejected, the Parties shall submit the names of at least two more natural or legal persons within one week of being informed of the rejection, in accordance with paragraphs 21 and 26 of these Commitments.

Trustee nominated by the Commission

28. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom the Parties shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

29. The Trustee shall assume its specified duties and obligations in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or Staples, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee

30. The Monitoring Trustee shall:
- (i) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision.
 - (ii) oversee, in close co-operation with the Hold Separate Manager, the on-going management of the Divestment Business with a view to ensuring its continued economic viability, marketability and competitiveness and monitor compliance by the Parties with the

conditions and obligations attached to the Decision. To that end the Monitoring Trustee shall:

- (a) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Business, and the keeping separate of the Divestment Business from the business retained by the Parties, in accordance with paragraphs 10 and 12 of these Commitments;
 - (b) supervise the management of the Divestment Business as a distinct and saleable entity, in accordance with paragraph 13 of these Commitments;
 - (c) with respect to Confidential Information,:
 - determine all necessary measures to ensure that Staples does not after the HSR Closing Date obtain any Confidential Information relating to the Divestment Business,
 - in particular strive for the severing of the Divestment Business' participation in a central information technology network to the extent possible, without compromising the viability of the Divestment Business,
 - make sure that any Confidential Information relating to the Divestment Business obtained by Staples before the HSR Closing Date is eliminated and will not be used by Staples, and
 - decide whether such information may be disclosed to or kept by the Parties as the disclosure or retention is reasonably necessary to allow the Parties to carry out the divestiture of the Divestment Business and the implementation of the transitional arrangements, is reasonably required to maintain the viability of the Divestment Business until Closing, or as the disclosure is required by law;
 - (d) monitor the splitting of assets and the allocation of Personnel between the Divestment Business and Staples or Affiliated Undertakings;
- (iii) propose to the Parties such measures as the Monitoring Trustee considers necessary to ensure Staples' or Office Depot's compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability or competitiveness of the Divestment Business, the holding separate of the Divestment Business and the non-disclosure of competitively sensitive information;

- (iv) review and assess potential purchasers as well as the progress of the divestiture process and verify that, dependent on the stage of the divestiture process:
 - (a) potential purchasers receive sufficient and correct information relating to the Divestment Business and the Personnel in particular by reviewing, if available, the data room documentation, the information memorandum and the due diligence process, and
 - (b) potential purchasers are granted reasonable access to the Personnel;
- (v) act as a contact point for any requests by third parties, in particular potential purchasers, in relation to the Commitments;
- (vi) provide to the Commission, sending Staples a non-confidential copy at the same time, a written report within 15 days after the end of every month that shall cover the operation and management of the Divestment Business as well as the splitting of assets and the allocation of Personnel so that the Commission can assess whether the business is held in a manner consistent with the Commitments and the progress of the divestiture process as well as potential purchasers;
- (vii) promptly report in writing to the Commission, sending Staples a non-confidential copy at the same time, if it concludes on reasonable grounds that Staples or Office Depot is failing to comply with these Commitments;
- (viii) within one week after receipt of the documented proposal referred to in paragraph 20 of these Commitments, submit to the Commission, sending Staples a non-confidential copy at the same time, a reasoned opinion as to the suitability and independence of the proposed purchaser and the viability of the Divestment Business after the sale and as to whether the Divestment Business is sold in a manner consistent with the conditions and obligations attached to the Decision, in particular, if relevant, whether the sale of the Divestment Business without one or more Assets or not all of the Personnel affects the viability of the Divestment Business after the sale, taking account of the proposed purchaser;
- (ix) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision.

31. If the Monitoring and Divestiture Trustee are not the same legal or natural persons, the Monitoring Trustee and the Divestiture Trustee shall cooperate closely with each other during and for the purpose of the preparation of the Trustee Divestiture Period in order to facilitate each other's tasks.

Duties and obligations of the Divestiture Trustee

32. Within the Trustee Divestiture Period, the Divestiture Trustee shall sell at no minimum price the Divestment Business to a purchaser, provided that the Commission has approved both the

purchaser and the final binding sale and purchase agreement (and ancillary agreements) as in line with the Commission's Decision and the Commitments in accordance with paragraphs 20 and 21 of these Commitments. The Divestiture Trustee shall include in the sale and purchase agreement (as well as in any ancillary agreements) such terms and conditions as it considers appropriate for an expedient sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the sale and purchase agreement such customary representations and warranties and indemnities as are reasonably required to effect the sale. The Divestiture Trustee shall protect the legitimate financial interests of Staples, subject to Staples' unconditional obligation to divest at no minimum price in the Trustee Divestiture Period.

33. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the end of every month with a simultaneous copy to the Monitoring Trustee and a non-confidential copy to Staples.

III. Duties and obligations of the Notifying Parties

34. The Parties shall provide and shall cause their advisors to provide the Trustee with all such co-operation, assistance and information as the Trustee may reasonably require to perform its tasks. The Trustee shall have full and complete access to any of Staples' or Office Depot's books, records, documents, management or other personnel, facilities, sites and technical information necessary for fulfilling its duties under the Commitments and the Parties shall provide the Trustee upon request with copies of any document. The Parties shall make available to the Trustee one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of its tasks.
35. The Parties shall provide the Monitoring Trustee with all managerial and administrative support that it may reasonably request on behalf of the management of the Divestment Business. This shall include all administrative support functions relating to the Divestment Business which are currently carried out at headquarters level. The Parties shall provide and shall cause their advisors to provide the Monitoring Trustee, on request, with the information submitted to potential purchasers, in particular give the Monitoring Trustee access to the data room documentation and all other information granted to potential purchasers in the due diligence procedure. Staples shall inform the Monitoring Trustee on possible purchasers, submit lists of potential purchasers at each stage of the selection process, including the offers made by potential purchasers at those stages, and keep the Monitoring Trustee informed of all developments in the divestiture process.
36. Staples shall grant or procure Affiliated Undertakings to grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee to effect the sale (including ancillary agreements), the Closing and all actions and declarations which the Divestiture Trustee considers necessary or appropriate to achieve the sale and the Closing, including the appointment of advisors to assist with the sale process. Upon request of the Divestiture Trustee, Staples shall cause the documents required for effecting the sale and the Closing to be duly executed.

37. Staples shall indemnify the Trustee and its employees and agents (each an "**Indemnified Party**") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to Staples for, any liabilities arising out of the performance of the Trustee's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee, its employees, agents or advisors.
38. At the expense of Staples, the Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to Staples' approval (this approval not to be unreasonably withheld or delayed) if the Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate, provided that any fees and other expenses incurred by the Trustee are reasonable. Should Staples refuse to approve the advisors proposed by the Trustee the Commission may approve the appointment of such advisors instead, after having heard Staples. Only the Trustee shall be entitled to issue instructions to the advisors. Paragraph 37 of these Commitments shall apply *mutatis mutandis*. In the Trustee Divestiture Period, the Divestiture Trustee may use advisors who served Staples during the Divestiture Period if the Divestiture Trustee considers this in the best interest of an expedient sale.
39. The Parties agree that the Commission may share Confidential Information proprietary to Staples or Office Depot with the Trustee. The Trustee shall not disclose such information and the principles contained in Article 17 (1) and (2) of the EU Merger Regulation apply *mutatis mutandis*.
40. The Parties agree that the contact details of the Monitoring Trustee are published on the website of the Commission's Directorate-General for Competition and they shall inform interested third parties, in particular any potential purchasers, of the identity and the tasks of the Monitoring Trustee.
41. For a period of 10 years from the Effective Date the Commission may request all information from the Parties that is reasonably necessary to monitor the effective implementation of these Commitments.

IV. Replacement, discharge and reappointment of the Trustee

42. If the Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a Conflict of Interest:
- (a) the Commission may, after hearing the Trustee and Staples, require Staples to replace the Trustee; or
 - (b) Staples may, with the prior approval of the Commission, replace the Trustee.

43. If the Trustee is removed according to paragraph 42 of these Commitments, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in paragraphs 21-28 of these Commitments.
44. Unless removed according to paragraph 42 of these Commitments, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section F. The review clause

45. The Commission may extend the time periods foreseen in the Commitments in response to a request from Staples or, in appropriate cases, on its own initiative. Where Staples requests an extension of a time period, it shall submit a reasoned request to the Commission no later than one month before the expiry of that period, showing good cause. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to the Notifying Party. Only in exceptional circumstances shall Staples be entitled to request an extension within the last month of any period.
46. The Commission may further, in response to a reasoned request from Staples showing good cause waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to Staples. The request shall not have the effect of suspending the application of the undertaking and, in particular, of suspending the expiry of any time period in which the undertaking has to be complied with.

Section G. Entry into force

47. The Commitments shall take effect upon the date of adoption of the Decision.

Date: 10 December 2015

SCHEDULE : DIVESTMENT BUSINESS

1. The Divestment Business as operated to date has the following legal and functional structure. The Divestment Business consists of:
 - (i) the business to business ("**B2B**") distribution of office supplies through the contract channel ("**Contract Channel**") in the EEA¹; and
 - (ii) the B2B distribution of office supplies through the contract, direct, retail and wholesale channels in Sweden.

2. The divestiture of the Divestment Business will be carried out through the transfer of the legal entity Office Depot (Operations) Holdings BV or any other legal entity or entities comprising the Divestment Business following a restructuring to exclude:
 - (i) any business activities, assets, personnel² and legal entities which relate exclusively or predominantly to the direct, wholesale or retail channels (except in Sweden);
 - (ii) certain dormant companies and intermediate holding companies not conducting Contract Channel business; and
 - (iii) any business activities, assets, personnel and legal entities exclusively or predominantly outside the EEA.

provided that the exclusion of any business activities, assets, personnel or legal entities does not have any adverse effect on the viability and competitiveness of the Divestment Business and, provided further, that all business activities, assets, personnel or legal entities of the Divestment Business as defined in paragraph 1 of the Schedule are transferred to the Purchaser under the supervision of the Monitoring Trustee in accordance with paragraph 30 (ii) (d) of the Commitments.

3. In accordance with paragraph 6 of these Commitments, the Divestment Business includes, but is not limited to:
 - (a) the following main tangible assets:
 - (i) The warehouse in Senlis, France;
 - (ii) The whole inventory in the warehouses which are relevant for Office Depot's EEA Contract Channel business (and, in Sweden, also the direct, wholesale and retail businesses).

¹ Switzerland is included in the Divestment Business as it forms part of Office Depot's European business. Any reference throughout this Schedule to EEA includes Switzerland.

² For the avoidance of doubt, any personnel not working predominantly for the business of one of the distribution channels, i.e. of the contract, direct, retail or wholesale channel, is included in the Divestment Business, subject to a transitional support arrangement for Staples on an at cost basis for a period of up to [...] after Closing.

- (b) the following main intangible assets:
 - (i) The assignment of the "Office Depot" trademarks to the extent their geographical scope is limited to the EEA or any part thereof and related to and used predominantly by the EEA Contract Channel business and of the "Office Depot" trademarks with geographical scope limited to Sweden, subject to a transitional licence to Staples for up to [...] after Closing, as included but not limited to in **Annex 1** of the Schedule; and
 - (ii) IT software and hardware, used by Office Depot predominantly for the Contract Channel in the EEA and by Office Depot in Sweden as included but not limited to in **Annex 2** of the Schedule; and
- (c) the following main licences, permits and authorisations:
 - (i) all of the licences, permits and authorisations used by the Office Depot Contract Channel business in the EEA and of Office Depot in Sweden;
- (d) the following main contracts, agreements, leases, commitments and understandings, subject to third parties consent to the extent such consent is contractually required:
 - (i) The agreements with the logistics providers that supply the relevant products in the EEA for the Contract Channel business and in Sweden for all distribution channels;
 - (ii) the partnerships agreements for the distribution of office supplies in the EEA for the Contract Channel business ;
 - (iii) The lease of the warehouse located in Zwolle, Netherlands;
 - (iv) The leases of the warehouse located in Grossostheim, Germany;
 - (v) The leases of the warehouses located in Saint Martin de Crau and Meung sur Loire, France;
 - (vi) The leases of the warehouses in Belvedere, Leicester, Northampton and Manchester, UK;
 - (vii) The leases of the warehouses in Dublin, Ireland;
 - (viii) The lease of the warehouse in Siziano, Italy;
 - (ix) The lease of the warehouse in Hostivice, Czech Republic;
 - (x) The lease of the warehouse in Madrid, Spain;
 - (xi) The lease of the warehouse in Stränggäs, Sweden; and
 - (xii) The lease of the warehouse in Lenzburg, Switzerland.

A list of the leases to be transferred is attached in **Annex 3** of the Schedule. The transfer of leases are subject to transitional access and use rights to Staples for the warehouses used for the direct and retail

business (except for Sweden) on an at cost basis for a period of up to [...] after Closing.³

- (e) the following customer, credit and other records:
 - (i) The current customer contracts for Office Depot's EEA Contract Channel business and international key accounts customers, subject to the consent of the customers to the extent such consent is contractually required;
 - (ii) The current customer lists for Office Depot's EEA Contract Channel business and international key accounts customers (see **Annex 4** of the Schedule) and for Office Depot in Sweden;
- (f) the following Personnel:
 - (i) all personnel employed by Office Depot in the EEA related to and working predominantly for the Contract Channel business; and
 - (ii) all personnel employed by Office Depot Svenska AB or Office Depot Sweden (Holding) related to the B2B distribution of office supplies through the direct, retail or wholesale channels;

subject to applicable labour laws;

- (g) the following Key Personnel:
 - (i) a list of employees who are indispensable (see **Annex 5** of the Schedule), including executives; and
- (h) at the option of the Purchaser, the arrangements for the supply of the following products or services by Staples or Affiliated Undertakings for the transitional period specified below (such period might be extended in accordance with paragraph 8 of the Commitments) :
 - (i) merchandising/procurement and supply chain services from the Office Depot facility in Leicester, UK for a transitional period of up to [...] after Closing;
 - (ii) all office products for the Divestment Business, including own-brand products of Office Depot currently distributed via the Contract Channel, from the Office Depot's vendors for a transitional period of up to [...] after Closing;
 - (iii) IT and marketing support from the Office Depot facility in Leicester, UK for a transitional period of up to [...] after Closing;

³ For the avoidance of doubt, Staples may need to have access to certain confidential information to the extent necessary for the implementation of this transitional arrangement.

- (iv) IT support from the eCommerce team at the Office Depot facility in Venlo, the Netherlands for a transitional period of up to [...] after Closing;
- (v) IT software and hardware which is shared between the Contract Channel business of Office Depot and the retained business of Office Depot and not divested under 3(b)(ii) for a transitional period of up to [...] after Closing;
- (vi) accounts receivable (AR) and accounts payable (AP) services from the Office Depot service centre in Cluj, Romania for a transitional period of up to [...] after Closing;
- (vii) use of the venues and facilities in the headquarters of Office Depot BV in Venlo, the Netherlands, to the extent necessary for the operation of the Contract Channel business for a transitional period of up to [...] after Closing; and
- (viii) Support for back-office functions (including HR and payroll) for a transitional period of up to [...] after Closing;

4. The Divestment Business shall not include:

- (a) any personnel of the Parties, other than the Personnel or Key Personnel as set out in paragraphs 3(f) and 3(g) above;
- (b) any asset, interests, customer records or contracts, rights or property (including intellectual property, know-how or trademarks) not part of the Divestment Business or which is used predominantly in relation to a business of Office Depot other than the Divestment Business;
- (c) monies owed to Office Depot; and
- (d) any assets, interests, rights or property (including any intellectual property, know-how or trademarks) of Staples or its Affiliated Undertakings other than assets, interests, rights or property that Staples acquires from Office Depot pursuant to the Concentration.

5. If there is any business activities, assets, legal entities or personnel which is not be covered by paragraph 2 and 3 of this Schedule but which is both used (exclusively or not) in the Divestment Business and necessary for the continued viability and competitiveness of the Divestment Business, that asset or adequate substitute will be offered to potential purchasers.

Annex 1 of the Schedule - List of the IP rights of the Divestment Business

[...]

Annex 2 of the Schedule - List of IT system used by the Divestment Business

[...]

Annex 3 of the Schedule - Overview of warehouses

[...]

Annex 4 of the Schedule - List of current contract customers

[...]

Annex 5 of the Schedule - Headcount of personnel of the Divestment Business

[...]



EUROPEAN COMMISSION
DG Competition

Case M.7861 - DELL / EMC

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 29/02/2016

***In electronic form on the EUR-Lex website under document
number 32016M7861***



EUROPEAN COMMISSION

Brussels, 29.02.2016
C(2016) 1356 final

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE

To the notifying party:

Dear Sir/Madam,

Subject: Case M.7861 - Dell / EMC
Commission decision pursuant to Article 6(1)(b) of Council Regulation No 139/2004¹ and Article 57 of the Agreement on the European Economic Area²

- (1) On 25 January 2016, the European Commission received notification of a proposed concentration pursuant to Article 4 of the Merger Regulation by which Denali Holding, Inc. ("Denali", USA), the owner of Dell Inc. ("Dell", USA) acquires within the meaning of Article 3(1)(b) of the EU Merger Regulation sole control of the whole of the undertaking EMC Corporation ("EMC", USA) by way of purchase of shares (the "transaction").³ Denali/Dell is designated hereinafter as the "Notifying Party". Denali/Dell and EMC are collectively referred to as the "Parties" or "the merging parties", while the company resulting from the transaction is referred to as "the merged entity"

¹ OJ L 24, 29.1.2004, p. 1 ("the Merger Regulation"). With effect from 1 December 2009, the Treaty on the Functioning of the European Union ("TFEU") has introduced certain changes, such as the replacement of "Community" by "Union" and "common market" by "internal market". The terminology of the TFEU will be used throughout this decision.

² OJ L 1, 3.1.1994, p.3 ("the EEA Agreement").

³ Publication in the Official Journal of the European Union No C 37, 30.1.2016, p. 4.

1. THE PARTIES AND THE CONCENTRATION

- (2) Denali is a holding company, the parent of Dell. Denali is solely controlled by Michael S. Dell, the founder and CEO of Dell. Dell is active in the development, sales, repairs, and support for computers and related products and services, including storage products. Dell was founded in 1984 and is headquartered in Round Rock, Texas.
- (3) EMC is active in data storage, information security, virtualization, analytics, cloud computing, and other products and services that enable businesses to store, manage, protect and analyse data. Organised as a federation, EMC owns, inter alia, approximately 81% of VMware, Inc., a publicly-traded provider of virtualization software. It also owns [...]% of VCE Company LLC, a joint venture with Cisco that sells converged infrastructure appliances, and specifically converged data centre units.⁴ EMC's federation also includes businesses active in backup software, identity and access management, and cloud technologies.
- (4) Pursuant to an agreement and plan of merger dated 12 October 2015, Denali is to acquire 100% of the share capital of EMC via a newly created acquisition company. Upon completion of the merger, EMC shareholders will receive shares of tracking stock that will be publicly traded and that are intended to track, in the aggregate, an approximately 53% of economic interest in the VMware business.⁵ EMC will become a wholly-owned subsidiary of Denali and a sister company of Dell. The transaction therefore constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.
- (5) The Notifying Party submits that the transaction seeks to combine the complementary strengths of Dell (in personal computers and servers) and EMC (in storage and software) to offer large and small customers a full range of solutions, including storage, security, software, cloud, converged and virtualized environments.⁶ In particular, the proposed concentration will position the combined company to capitalise on trends in the information technology ("IT") industry, such as the rapid explosion in data and the need for sophisticated data analytics, and the transition from on-premises to cloud infrastructures. Internal documents confirm that the parties seek to combine their expertise to expand and strengthen their portfolio in these areas, [...].⁷

2. UNION DIMENSION

- (6) The Parties concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million⁸ (Dell: EUR [...]; EMC: EUR [...]). Each of them has a

⁴ Cisco has a 10% stake in VCE and VMware owns the remaining [...]%. The converged data centre units are known as vBlocks, and incorporate Cisco servers and networking hardware, EMC storage systems and VMware software.

⁵ A tracking stock is a separate class or series of a company's common stock that is intended to reflect the economic performance of a defined set of assets and liabilities, usually consisting of a specific business or subsidiary.

⁶ See internal documents, for example: [...].

⁷ See Internal documents: [...].

⁸ Turnover calculated in accordance with Article 5 of the Merger Regulation.

Union-wide turnover in excess of EUR 250 million (Dell: EUR [...]; EMC: [...]), but they do not achieve more than two-thirds of their aggregate Union-wide turnover within one and the same Member State. The transaction therefore has a Union dimension under Article 1(2) of the Merger Regulation.

3. RELEVANT MARKETS

- (7) The transaction combines two global providers of IT systems and IT software, resulting in a horizontal overlap mainly in relation to storage systems and, in particular, external enterprise storage systems ("external ESS").⁹
- (8) In addition, the transaction gives rise to non-horizontal links since Dell is active in servers and storage systems, and VMware (owned by EMC) is a supplier of virtualization software that can be used in conjunction with servers and storage. Customers can buy their IT equipment separately and integrate the components themselves, or acquire pre-integrated "converged" systems, combining server hardware, external ESS, networking equipment, virtualization software, unified management software and/or other software applications.
- (9) In light of the above, the Commission will examine the relevant market definition in relation to the following product areas: (i) storage systems; (ii) servers; (iii) virtualization software; and (iv) converged infrastructure solutions.

3.1. Storage systems and external ESS

- (10) The storage resources of a business' IT infrastructure allow for information to be written to a storage solution (hard disk drive or flash drive), retained and retrieved (read).
- (11) Broadly speaking, there are two types of storage: internal storage and external storage. Internal storage is the storage housed within the server enclosure: servers typically come with a limited amount of storage, dedicated to the server. External storage consists of the additional storage resources of a data centre, outside the servers: external storage systems are commonly required, due to the massive amount of data involved in modern enterprise operations.
- (12) Another relevant distinction is enterprise storage as opposed to client storage. Enterprise storage is storage for use in corporate environments (such as data centres), while client storage refers to storage for lower workload environments, usually for use by individual consumers.
- (13) External ESS is one component of a typical data centre, which works in conjunction with other IT components (such as servers, networking hardware such as cables and switches), security hardware (*e.g.*, firewalls), and redundant power and cooling systems to store, manage and disseminate data for an enterprise.

⁹ The merging parties' activities also overlap in the supply of identity and access management software and back-up software. Based on the information provided by the Notifying Party, under any plausible relevant product and geographic market definition the combined shares are below 20%. Moreover, none of the respondents to the market investigation raised any concern arising from the combination of these activities. As a result, these overlaps will no longer be discussed in the remainder of this decision.

- (14) External ESS (also referred to as "storage arrays") are composed of one or more physical controllers (each a processor and firmware) that manage and provide a common interface to multiple hard disk drives ("HDDs") or solid-state (flash) drives ("SSDs") (or a combination of both HDDs and SSDs)¹⁰ as well as other components such as cables, housing, and host bus adapters.
- (15) The array then presents its multiple component drives as one resource to the data centre servers and frequently external clients, allowing them to read and write data. Traditional storage systems can be directly attached to the server (so-called "directly attached storage" or "DAS"), or connected via a computer network, which has the additional advantage of providing a shared pool of storage accessible across multiple servers.

3.1.1. *Product market definition*

- (16) In previous decisions, the Commission has considered several markets in the IT industry including IT services, IT software, and IT systems (comprising electronic information processing systems including servers and storage systems).¹¹ The Commission identified a separate product market for storage solutions in its *HP/Compaq* decision.¹²
- (17) The Commission also investigated relevant storage systems markets in cases *Sun/Storagetek*¹³ and *Oracle/Sun Microsystems*.¹⁴
- (18) In *HP/Compaq*, *Sun/Storagetek* and *Oracle/Sun Microsystems*, the Commission considered whether, within the overall storage solutions market, separate markets could be identified based on the type of media used (disk, optical and tape).¹⁵ In addition, in *HP/Compaq* and *Sun/Storagetek*, the Commission considered whether disk storage should be further segmented by the type of the installation/architecture of the storage system, into DAS, storage area networks ("SAN") and network attached storage ("NAS").¹⁶ Finally in *Sun/Storagetek*, the Commission also examined the possibility of further segmenting tape storage solutions.¹⁷ Ultimately, the Commission left the market definition in those cases open. Moreover, in those

¹⁰ HDDs contain mechanical components such as spinning disks and read/write heads, while SSD technology is based on electronic interfaces and has lower power requirements. Flash memory has no moving parts and can be erased and reprogrammed in units of memory. Those units are called "blocks" and can be altered in a single command, in a "flash".

¹¹ Commission decision of 15 December 2014 in Case M.7458 – *IBM/INF Business of Deutsche Lufthansa*, paragraphs 12 and 13.

¹² Commission decision of 31 January 2002 in Case M.2609 – *HP/Compaq*; see also Commission decision of 26 August 2005 in Case M.3866 – *Sun/Storagetek*, paragraph 7.

¹³ Commission decision of 26 August 2005 in Case M.3866 – *Sun/Storagetek*.

¹⁴ Commission decision of 21 January 2010 in Case M.5529 – *Oracle/Sun Microsystems*.

¹⁵ Commission decision of 31 January 2002 in Case M.2609 – *HP/Compaq*, paragraph 24; Commission decision of 26 August 2005 in Case M.3866 – *Sun/Storagetek*, paragraph 7; Commission decision of 21 January 2010 in Case M.5529 – *Oracle/Sun Microsystems*, paragraphs 942 and 943.

¹⁶ Commission decision of 31 January 2002 in Case M.2609 – *HP/Compaq*, paragraph 25; Commission decision of 26 August 2005 in Case M.3866 – *Sun/Storagetek*, paragraph 10.

¹⁷ Commission decision of 26 August 2005 in Case M.3866 – *Sun/Storagetek*, paragraphs 8 to 10.

previous decisions no distinction was made between enterprise and client storage, and internal and external storage.

3.1.1.1. The Notifying Party's view

- (19) According to the Notifying Party, the market for storage systems has evolved considerably over the last few years, which has rendered past Commission decisions to some extent obsolete.
- (20) The Notifying Party submits that internal storage (storage contained within a server) is not part of the relevant product market. Internal storage capacity is limited by the physical size of the server enclosure and the unused internal storage capacity generally cannot be accessed by or reallocated to other server systems. External storage, however, can be either directly attached to a server or connected via a computer network, so as to create a shared pool of storage accessible simultaneously by several servers.
- (21) According to the Notifying Party, internal storage systems are not substitutes for external storage systems because of the limited ability, scalability and performance of internal storage systems. As internal storage belongs to a server, without software that makes the server behave like a storage system (*i.e.*, software-defined storage or "SDS") or a hyperconverged appliance with storage, it would not be possible – according to the Notifying Party – for an internal storage system to perform as an external storage. Moreover, unlike external storage that can be shared between various servers, internal storage (without SDS) cannot be shared and is unique to a server. From a supply-side perspective, the Notifying Party notes that companies such as EMC, NetApp or Nimble Storage are focused on their external storage offering and do not offer internal storage systems at all, as opposed to companies such as Dell and HP selling servers which do offer internal storage systems. In summary, according to the Notifying Party the relevant product market is not narrower than the supply of external ESS.
- (22) In addition, according to the Notifying Party the relevant product includes enterprise storage only, as opposed to consumer storage which is offered to individuals.
- (23) The Notifying Party further submits that a categorization of the market for storage solutions by type of media used, *i.e.* between disk, optical and tape, is not relevant. According to the Notifying Party the main type of media used today are disks, while optical or tape are used less frequently.¹⁸
- (24) The Notifying Party further submits that, both for demand and supply-side considerations, it is not possible to segment the market for external ESS between HDD arrays, all-flash arrays ("AFA") and hybrid flash arrays ("HFA"), which would belong to the same product market.

¹⁸ The Notifying Party submits that optical and tape served as the media of choice for all backup, recovery, and archive functions in the past, but increasingly have been replaced by disk based systems and purpose-built backup appliances ("PBBAs"), which is a combination of a general purpose storage array, a server engine and software used for backup storage, rather than primary storage. According to the Notifying Party, optical and tape are now almost exclusively the domain of very long-lived archives and tape backups, and are not used for primary storage.

- (25) Furthermore, according to the Notifying Party the distinction between storage systems directly attached to the server (so-called "directly attached storage" or "DAS"), network-attached storage ("NAS") and storage area networks ("SAN"), would no longer be relevant, both from the demand and the supply side.
- (26) Finally, in support of its claim that the Parties' respective ESS portfolios are complementary, the Notifying Party has submitted market share data for different price bands of external ESS, namely (i) **entry-level** storage systems, comprising all systems with an average selling value below USD 25 000; (ii) **mid-range** enterprise storage systems, consisting of all systems with an average selling value of USD 25 000 to USD 249 999; and, (iii) the **high-end** band, covering all systems with an average selling value of USD 250 000 and above. The International Data Corporation ("IDC"), a market analyst, publishes data based on these three segments.¹⁹
- (27) According to the Notifying Party, the prices reflect the sophistication of the storage products in terms of workload capabilities, scalability performance, reliability, data processing efficiency, data recoverability, data sharing features, data security and energy efficiency. However, none of the three segments would have niche customers with specific feature requirements. On the supply-side, the Notifying Party submits that there are no storage vendors providing external ESS with special features that no other vendor is able to replicate.

3.1.1.2. The results of the market investigation and the Commission's assessment

- (28) With regard to the possible distinction between internal and external storage, the majority of respondents to the market investigation consider that within the overall storage systems sector, there are separate markets for internal and external storage.²⁰ Respondents pointed out that external storage has significantly different characteristics compared to internal storage and that the segmentation is common practice in the industry.²¹
- (29) As to enterprise storage (storage for servers and for storage systems in high workload environments, such as corporate data centres) and client storage (storage for lower workload environments that are usually for use by individual consumers, such as personal computers and portable electronic devices) most respondents to the market investigation consider that these constitute separate markets.²²
- (30) Most respondents to the market investigation also submitted that the possible market for external ESS should be segmented based on type of media used (disk, optical and tape).²³ Respondents pointed out, among other things, differences in

¹⁹ International Data Corporation (IDC) is a global provider of market intelligence for information technology, telecommunications and consumer technology markets.

²⁰ See replies to Q1 – questionnaire to competitors, question 10.

²¹ See replies to Q1 – questionnaire to competitors, question 10.

²² See replies to Q1 – questionnaire to competitors, question 9.

²³ See replies to Q1 – questionnaire to competitors, question 13.

terms of price and use, as tape (and increasingly optical) media are being used for archiving / backup.²⁴

- (31) With regard to a possible segmentation into HDD arrays, AFAs and HFAs (depending on the use of HDDs, SSDs or both), the majority of respondents to the market investigation disagreed with such a segmentation.²⁵ Respondents pointed out that – despite SSDs' lower capacity, higher price and higher speed – these types of drives can be used interchangeably in most ESS solutions and that frequently a combination of both types of drives is used.²⁶ The Commission notes that in previous decisions, the Commission found that SSDs and HDDs do not belong to the same relevant product markets.²⁷ However, the Commission notes that the present investigation concerns the market for external ESS, *i.e.*, storage arrays, rather than the market for HDDs or SSDs contained in such arrays.
- (32) As to the segmentation by type of installation / architecture (DAS, NAS, SAN), the majority of respondents to the market investigation disagreed with this distinction.²⁸ Respondents pointed out the demand-side and supply-side substitutability among these storage topographies and the development of new technologies (network unified storage or "NUS", software-defined storage or "SDS", hyper-converged solutions).²⁹
- (33) As regards another possible segmentation of external ESS by price bands (in line with the segmentation included in the IDC reports),³⁰ most respondents agreed with this segmentation.³¹ Respondents pointed out differences in terms of volume of storage offered, performance of storage and advanced features (such as replication, deduplication, compression, and manageability features). However, competitors indicated that they are typically present in two or three price bands and that it is possible to switch production from one segment,³² though with differing degrees of difficulty (*e.g.*, it would not be easily feasible to switch production from low-end to high-end).

²⁴ See replies to Q1 – questionnaire to competitors, question 13.

²⁵ See replies to Q1 – questionnaire to competitors, question 14.

²⁶ See replies to Q1 – questionnaire to competitors, question 14.

²⁷ Commission decision of 19 October 2011 in Case M.6214 – *Seagate Technology/The HDD Business of Samsung Electronics*, recitals 256-259; and Commission decision of 23 November 2011 in Case M.6203 – *Western Digital Ireland/Viviti Technologies*, recitals 362-365.

²⁸ See replies to Q1 – questionnaire to competitors, question 15.

²⁹ See replies to Q1 – questionnaire to competitors, question 15.

³⁰ High-end (all systems with an average selling value over USD 250 000), mid-range (USD 25 000 to USD 249 999); low-end (below USD 25 000).

³¹ See replies to Q1 – questionnaire to competitors, question 11.

³² See replies to Q1 – questionnaire to competitors, question 12.

3.1.2. *Geographic market definition*

- (34) In previous decisions, the Commission considered that the market for storage solutions was at least EEA-wide, if not worldwide, but ultimately left the exact geographic market definition open.³³

3.1.2.1. *The Notifying Party's view*

- (35) The Notifying Party submits that the relevant geographic market for ESSs should be considered as worldwide in scope, since (i) manufacturers offer the same products under the same brands to all their customers regardless of geographic location; (ii) almost all suppliers of storage have a presence (in their own name or through distributors) in all parts of the globe; (iii) transportation costs are low; (iv) technical requirements and language differences do not have any impact on cross-border trade; and (v) prices are broadly similar across geographic regions.

3.1.2.2. *The results of the market investigation and the Commission's assessment*

- (36) Most respondents to the market investigation confirmed the Notifying Party's view indicating that the geographic scope of the market for external storage solutions is worldwide.³⁴

3.1.3. *Conclusion on market definition for storage systems*

- (37) In light of the considerations in this section, and for the purpose of this decision, the exact delineation of the relevant product and geographic market(s) for storage systems can be left open, as the transaction does not give rise to serious doubts about its compatibility with the internal market under any plausible market definition.

3.2. **Servers**

3.2.1. *Product market definition*

- (38) Servers are the computing power of the data centre. Servers can be used in many ways, and in large companies usually have a single function per server, for example file servers, web servers, printer servers, application servers. Servers also have a limited amount of internal storage capacity. A server can take different forms, such as rack, blade, tower or cloud physical servers, or a cloud logical server, which is delivered through server virtualization.
- (39) Dell only sells servers based on open x86 architecture (as opposed to proprietary CPU architecture designed to run proprietary operating systems). The Notifying Party notes that the virtualisation software of VMware, Red Hat, Microsoft and other competitors only works on x86 servers, and that x86 servers represent more than 80% of all servers sold by revenue and more than 90% by units sold. EMC is

³³ Commission decision of 15 December 2014 in Case M.7458 – *IBM/INF Business of Deutsche Lufthansa*, paragraph 41; Commission decision of 31 January 2002 in Case M.2609 – *HP/Compaq*, paragraph 25; Commission decision of 26 August 2005 in Case M.3866 – *Sun/Storagetek*, paragraph 13; Commission decision of 21 January 2010 in Case M.5529 – *Oracle/Sun Microsystems*, paragraph 950.

³⁴ See replies to Q1 – questionnaire to competitors, question 18.

not active in the server business. For the purposes of this investigation, "servers" is therefore understood to refer to x86 servers.

- (40) In previous decisions, the Commission considered the "IT stack", of which the first layer is hardware, including servers. In *Oracle/Sun Microsystems*, the Commission looked at the party's claim that the relevant market for servers should be subdivided into three segments, for low-end, mid-range and high-end servers.³⁵ In *HP/Compaq*, the parties argued that all servers constitute one market but considered alternative market definitions based on price and platform.³⁶ The Commission's market investigation in *HP/Compaq* confirmed its previous approach to delineate on the basis of price bands, as proxies to reflect different functionalities by band (entry-level below USD 100 000, mid-range USD 100 000 to USD 999 999, high-end above USD 1 million). In both those decisions, the Commission ultimately left the product market for servers open.

3.2.1.1. The Notifying Party's view

- (41) The Notifying Party refers to the Commission's previous decisions, in which the Commission suggested a possible segmentation of servers by price band as proxies reflecting the different functionalities, while ruling out a further segmentation by operating systems and/or applications served. The Notifying Party submits that it is ultimately not necessary to decide on the relevant product market as the transaction does not give rise to any competition (non-horizontal) concerns under any possible product market definition.

3.2.1.2. The results of the market investigation and the Commission's assessment

- (42) During the market investigation in this case the possible segmentations of the server market were tested. Most respondents to the market investigation agreed with the segmentation of servers by price-band into low-end, mid-range and high-end, as a proxy for functionality or task.³⁷ The market investigation did not provide a clear result as to a possible segmentation of servers by operating systems or by the applications they serve.

3.2.2. *Geographic market definition*

3.2.2.1. The Notifying Party's view

- (43) The Notifying Party refers to previous decisions by the Commission in which it has considered the server market to be at least EEA-wide, if not world-wide. It submits that, due to low transport costs, similar customer preferences, product specifications and patterns of sales of most major manufacturers, the relevant geographic market is world-wide in scope.

³⁵ Commission decision of 21 January 2010 in case M.5529 – *Oracle/Sun Microsystems*.

³⁶ Commission decision of 31 January 2002 in case M.2609 – *HP/Compaq*.

³⁷ See replies to Q1 – Questionnaire to competitors, of 27 January 2016, question 8.

3.2.2.2. The results of the market investigation and the Commission's assessment

- (44) The results of the market investigation indicated that the geographic scope of the market for servers is at least EEA-wide or even worldwide, in line with previous Commission merger decisions.³⁸

3.2.3. *Conclusion on market definition for servers*

- (45) In light of the considerations in this section, the Commission considers that, for the purpose of this decision, the exact delineation of the relevant product and geographic market(s) for servers can be left open, as the transaction does not give rise to serious doubts about its compatibility with the internal market under any plausible market definition.

3.3. **Virtualization software**

3.3.1. *Product market definition*

- (46) In computing, virtualization refers to the act of creating virtual versions of computer resources, like computer hardware, operating systems, storage devices, or network resources. Virtualization is, therefore, an intermediary layer between hardware and other software components, such as operating systems and applications. Virtualization software is one of the main software products marketed by VMware.³⁹
- (47) VMware provides x86-based⁴⁰ virtualization and management software for the entire data centre, including server, storage and network virtualization.⁴¹
- (48) Combined with servers, virtualization software technology makes it possible to run multiple operating systems and multiple applications on the same server at the same time, by separating them in virtual machines. Virtualization software is therefore used by customers to increase the efficiency of a given physical server and, more generally, a data centre, by running multiple isolated workloads on a single server, rather than requiring multiple physical servers, as might have been the case in the absence of server virtualization technology.
- (49) Server virtualization is also a key component of cloud computing, which typically depends on the ability to dynamically allocate new virtual machines, storage

³⁸ See replies to Q1 – Questionnaire to competitors, of 27 January 2016, question 17.

³⁹ Customers use virtualization platforms for different (and sometimes multiple) reasons, such as: i) to facilitate decentralized IT organization, allowing different groups or business units to choose their own platform; ii) to align different application stacks; iii) to use different platforms for different IT environments.

⁴⁰ The x86 architecture is an instruction set architecture (ISA) series for computer processors.

⁴¹ VMware refers to this overall approach as building software-defined data centres (“SDDCs”). Key VMware products in this space are vSphere (server virtualization for x86 servers), vSAN (storage virtualization, VMware NSX (network virtualization) and VMware Horizon (desktop virtualization). More specifically vSphere can be purchased as a stand-alone component or as part of broader virtualization suites that can include management, storage and network solutions.

resources, networking, etc. to meet changing demand, and to automate the management of those resources through software interfaces.

- (50) Combined with storage, virtualization software technology aims to provide a layer of abstraction by pooling physical storage from multiple network storage devices into a single virtual storage interface. More specifically, storage virtualization software (or "SDS") maps storage space by logical location (virtual) rather than physical location (hardware), which provides more efficiency, flexibility and scalability. These features allow workloads to be deployed faster, operations to become automated, and create significant cost savings for data centres.
- (51) Combined with physical network components,⁴² virtualization software technology creates virtual networks which are programmatically created, provisioned and managed, with the underlying physical network serving as a simple packet-forwarding backplane. More specifically, the software allocates network and security services to each virtual machine according to its needs while the virtual machine moves among hosts in the dynamic virtualized environment.
- (52) Combined with desktops, virtualization software technology separates the desktop environment and associated application software from the hardware device that is used to access it. In essence, this software is decoupling a PC desktop environment from a physical device so that the virtual machine ("VM") of the PC desktop stored in a centralised server can be accessed from a remote client device through a network.⁴³
- (53) In previous decisions in *Computer Sciences Corporation / iSOFT Group*⁴⁴ and *IMB / INF Business of Deutsche Lufthansa*,⁴⁵ the Commission considered a segmentation of software based on (i) the different functionalities of the software and the sector concerned, and (ii) the end uses offered by that particular software.
- (54) As regards functionality, the Commission found that distinctions in the software industry are generally made between (i) infrastructure software (*i.e.*, servers and databases); (ii) middleware (*i.e.*, integration platforms); (iii) application software and office software; and (iv) operating/browser software. As regards end uses, the software industry was generally segmented between high and low-end or between high-end, mid-range and low-end. The exact product market definition was ultimately left open.
- (55) In its decision *Oracle / Sun Microsystems*⁴⁶ the Commission considered a further segmentation of middleware⁴⁷ into, among other things, virtualization software. The product market definition was ultimately left open.

⁴² Such as logical switches, routers, firewalls, load balancers and VPNs.

⁴³ There are various desktop virtualization technologies targeting different use cases, such as hosted virtual desktop ("HVD"), local VM, streaming desktop and hosted shared desktop.

⁴⁴ Case M.6237 – *Computer Sciences Corporation / iSoft Group*, Commission decision of 26 June 2011, paragraph 22.

⁴⁵ Case M.7458 – *IBM / INF Business of Deutsche Lufthansa*, Commission decision of 15 December 2014, paragraph 42.

⁴⁶ Case M.5529 – *Oracle / Sun Microsystems*, Commission decision of 21 January 2010, paragraph 769.

- (56) With regard to middleware, in *Oracle/Sun Microsystems*⁴⁸ and *Oracle/BEA*,⁴⁹ the Commission investigated whether all types of middleware belonged to a single market or needed to be further segmented according to the end use of the product, including a sub-segment for virtualization software. Ultimately, the market definition was left open.

3.3.1.1. *The Notifying Party's view*

- (57) The Notifying Party submits that the four segmentations considered in previous decisions are now out-dated, as the software industry is currently fragmented and in flux. In support of its submission, the Notifying Party provided the Commission with IDC industry report data, according to which the industry should be segmented into three "primary" segments, namely: (i) application development and deployment, (ii) applications, and (iii) system infrastructure software (including virtualization software).
- (58) The Notifying Party additionally submits IDC data⁵⁰ according to which the industry is further segmented into eighteen "secondary markets", namely: (i) Application Development Software; (ii) Application Platforms; (iii) Collaborative Applications; (iv) Content Applications; (v) Customer Relationship Management (CRM) Applications; (vi) Data Access, Analysis and Delivery; (vii) Engineering Applications; (viii) Enterprise Resource Management (ERM) Applications; (ix) Integration and Orchestration middleware; (x) Network Software; (xi) Operations and Manufacturing Applications; (xii) Quality and Life-Cycle Tools; (xiii) Security Software; (xiv) Storage Software; (xv) Structured Data Management Software; (xvi) Supply Chain Management (SCM) Applications; (xvii) System Management Software and (xviii) System Software (which is the parent secondary market for virtualization software).
- (59) The Notifying Party does not consider "server virtualization software" to constitute a relevant market. It submits that the relevant market in which VMware operates is likely to be broader than server virtualization software. According to the Notifying Party, VMware competes against a wide range of different software, hardware and service providers that offer customers a variety of ways to run applications and workloads within an x86 environment. Examples of such providers are: operating system vendors, traditional and software-defined storage vendors, traditional and software-defined networking vendors, application remoting/delivery vendors, management vendors, public cloud providers, containers-related technology companies, and mobile device and application management vendors. Nonetheless,

⁴⁷ Middleware refers to a wide category of software products that provide the infrastructure for applications to run on a server, be accessed from a variety of clients over a network and be able to connect a variety of information sources. This includes several products that could constitute sub-segments such as application server software, web server software, transaction processing monitors ("TPM"), application integration, enterprise portals, event management software, enterprise service bus software ("ESB") etc.

⁴⁸ Case M.5529 – *Oracle / Sun Microsystems*, Commission decision of 21 January 2010, paragraphs 763 and 764.

⁴⁹ Case M.5080, *Oracle/BEA*, Commission decision of April 29, 2008, paragraph 10.

⁵⁰ Data based on the *IDC WW Semiannual Software Tracker 2015H1*.

the Notifying Party notes the absence of independent market research data allowing appropriate business models to be measured.

- (60) In any event, the Notifying Party suggests that the relevant product market definition for virtualization software can be left open because the transaction would not significantly impede effective competition under any plausible market definition.

3.3.1.2. *The results of the market investigation and the Commission's assessment*

- (61) The market investigation tested the possible segmentations of the software market. More specifically, it tested whether virtualization software can be considered as a separate sub-segment of middleware and whether virtualization software should be further sub-segmented based on the hardware or other components it is paired with (*e.g.*, servers, storage systems and networking).
- (62) Most of the respondents to the market investigation confirmed that virtualization software should be considered as a separate market within middleware.⁵¹
- (63) The respondents indicated that the virtualization market, though part of the overall middleware software sector, has different functions and characteristics. In particular, virtualization software is a software that converts a physical IT asset into a virtual resource and creates logical representations of all of the components that it functions on top of (*e.g.*, CPU, memory, BIOS,⁵² and the Operating System) in order to deliver unique capabilities, not duplicated by other products in the middleware space. Middleware, on the other hand, traditionally focuses on application stacks, such as application servers, enterprise service bus and other SOA software technologies.⁵³ It has greater functionality and features, and is commonly understood as the “glue” that provides services to software applications beyond those available from the operating system.
- (64) As regards a possible further segmentation of virtualization software, the responses to the market investigation were mixed.⁵⁴ Some of the respondents consider that virtualization software should be further segmented based on the hardware or other components it is paired with (*e.g.*, servers, storage systems, networking and desktop) as these are typically treated as distinct markets. In their view, virtualization market segmentation typically follows the market dynamics of each of those components. The hardware affinity of virtualization is very strong; hence, it could be categorised closer to the hardware technologies. Additionally, the different types of virtualization software may have different key players depending on the underlying hardware they virtualize.

⁵¹ See replies to Q1 – questionnaire to competitors, question 4 and replies to Q2 – questionnaire to VMware customers, question 6.

⁵² BIOS refers to Basic Input/Output system: type of firmware used to perform hardware initialization during the booting process.

⁵³ SOA refers to Service-Oriented Architecture, which is an architectural pattern in computer software design.

⁵⁴ See replies to Q1 – questionnaire to competitors, question 5 and replies to Q2 – questionnaire to VMware customers, question 7.

- (65) On the other hand, some respondents did not agree with a possible further segmentation of virtualization software. In their view, virtualization software products which are functional across servers, storage, networking, and desktop products all share common concepts, and may at times have overlapping capabilities.
- (66) Furthermore, the market investigation tested whether technologies, such as container technology,⁵⁵ can be considered to belong to a separate product market than virtual machine-based virtualization software, by taking into account demand and supply-side substitutability, main features, strengths and weaknesses.
- (67) The responses to the market investigation indicated that containers, despite providing a simplified way to deploy an application on shared infrastructure, deliver a different type of virtualization than traditional virtual machine-based virtualization software. The two technologies are not functionally interchangeable as they have different fundamental features and functionalities.⁵⁶ Therefore, containers should not be considered as belonging in the same product market.

3.3.2. *Geographic market definition*

- (68) In previous decisions, the Commission took the view that the geographic scope of the market for software was at least EEA-wide. In relation to middleware, in *Oracle/Sun Microsystems*,⁵⁷ the Commission considered the relevant geographic market for the overall middleware market and sub-segments thereof to be worldwide.
- (69) The Notifying Party agrees with this finding in relation to VMware's virtualization software and believes that the relevant geographic market is no narrower than global.
- (70) From the results of the market investigation it can be inferred that the relevant geographic market for middleware and its sub-segments (including virtualization software) is global in scope. The majority of the respondents confirmed that, when considering middleware, the market could be viewed as global because (i) transportation costs are low compared to the price of the products; (ii) customers have similar preferences and requests worldwide; and (iii) product specifications and distribution patterns are similar throughout Europe and worldwide.

3.3.3. *Conclusion on market definition for virtualization software*

- (71) In any event and in light of the outcome of the market investigation, the Commission considers that, for the purposes of this decision, as regards virtualization software, the precise product market definition can be left open, as

⁵⁵ A "container" is a virtual machine that provides OS-level virtualization and can replace hypervisors in certain contexts, thereby reducing virtual machine overheads. As is the case for server virtualization software, this alternative technology aims at increasing server efficiency and lowering IT costs.

⁵⁶ See replies to Q1 – questionnaire to competitors, question 6.1 and replies to Q2 – questionnaire to VMware customers, question 8.1.

⁵⁷ Case M.5529 – *Oracle / Sun Microsystems*, Commission decision of 21 January 2010, paragraph 769.

the transaction does not raise serious doubts as to its compatibility with the internal market under any plausible market definition.

3.4. Converged infrastructure systems

3.4.1. Product and geographic market definition

- (72) Converged infrastructure systems (“CI” systems) refer to pre-bundled and pre-integrated data centre infrastructure which brings together products from one or more vendors across servers, storage, networking and supporting software.
- (73) As an additional convenience for some end-customers, CI systems offer an alternative to the traditional mix-and-match model of integration of the various components of the data centre, also known as “best-of-breed”. However, servers, storage devices, networking systems and supporting software can still be sold on a standalone basis and can be integrated by either customers, value-added resellers (“VARs”)⁵⁸ or System Integration Vendors (“SIs”).⁵⁹
- (74) CI systems can be assembled by VARs or SIs which procure hardware components separately, following a reference architecture supplied by any component manufacturer. Alternatively, CI systems can be pre-assembled by a single component manufacturer or in a partnership involving several vendors.
- (75) Hyper-converged infrastructure systems (“HCI” systems) are physically integrated systems combining a commodity server and supporting software allowing the server to present itself as a single system that has both computing and storage capabilities. Similar to converged systems, customers may purchase a single hyper-converged system, or instead obtain similar functionality by purchasing servers and storage systems separately, or by purchasing commodity servers and developing or licensing software separately to make them hyper-converged.
- (76) In the CI systems' space, neither Dell nor EMC are able to offer a converged system on their own, but each is able to partner with third party vendors on an *ad hoc* basis to make a converged offer. More specifically, EMC sells CI appliances through “VCE”, a joint venture with Cisco, which incorporate Cisco servers and networking hardware, EMC storage systems, and VMware software.⁶⁰
- (77) In the HCI systems' space, Dell does not offer HCI systems by itself but has cooperative agreements with a number of vendors in order to develop and market

⁵⁸ A Value-Added Reseller (VAR) is an organization that buys equipment from a vendor at a discount, adds value (such as application software packaged and sold with underlying system software) and re-markets it.

⁵⁹ A Systems Integrator (SI) is an individual or a business that builds computing systems for clients by combining hardware and software products from multiple vendors.

⁶⁰ The CI system offering is named VCE VBlock Systems (see paragraph 3 above).

such appliances.⁶¹ EMC does not have a HCI system offering either, but markets such a product based on VMware's virtualization software reference architecture.⁶²

3.4.1.1. *The Notifying Party's view*

- (78) The Notifying Party submits that most enterprises with a data centre infrastructure are sophisticated consumers with dedicated IT procurement, operations, and engineering staff. Enterprise customers leverage this in-house expertise to build their data centres and to employ various strategies to maximize and diversify their range of product and technology choices, increase their flexibility, and lower their cost of operation.
- (79) Moreover, the Notifying Party notes that both sophisticated and less sophisticated enterprises further augment their IT expertise and purchasing power by buying through VARs and SIs who build and deploy complex IT systems and provide valuable services in selecting, integrating and installing IT infrastructure from different vendors.
- (80) The Notifying Party further submits that, given their own sophistication and that of VARs and SIs, enterprise customers normally mix and match different IT systems and platforms from best-of-breed vendors in order to best meet their needs, instead of purchasing CI or HCI solutions. As a result, most customers have several different server, storage and networking products and platforms in their IT infrastructure, which all need to work well together. Due to this industry practice, enterprises, VARs and SIs demand a high level of interoperability from servers, storage, networking and software vendors.
- (81) The Notifying Party takes the view that mixing and matching remains the preferred option for most end-customers. Given that most server, storage and networking systems are still sold on a standalone basis and are integrated by end-customers, VARs or SIs, each of these components of a CI system can be viewed as exercising a competitive constraint on the standalone products.
- (82) In any event, the Notifying Party submits that CI and HCI systems do not constitute a distinct relevant product market. They are alternative modes of purchasing used by some end-customers instead of buying best-of breed hardware and integrating the components themselves. CI and HCI systems are fully interchangeable with comparable non-converged, "best-of-breed" alternatives. While some customers may choose a CI or HCI system for convenience, they can and would switch to a non-converged system in the face of a Small Significant Non-transitory Increase in Price or an attempt to foreclose them from the ability to efficiently use their chosen hardware and software. Therefore, in the Notifying Party's view, customers always have the option of obtaining similar functionality by purchasing hardware and software components separately and assembling them themselves or through a VAR or SI.

⁶¹ Dell currently cooperates with [...] for the development and marketing of HCI systems.

⁶² VMware's reference architecture is named EVO:RAIL. It is designed for a pre-configured, fully-integrated hyper-converged appliance based on VMware software for virtualization, storage, networking and management combined with server and disk hardware from qualified vendors.

3.4.1.2. The results of the market investigation and the Commission's assessment

- (83) Most respondents to the market investigation agreed that CI and HCI systems provide an alternative approach to the traditional mix and match of different hardware and software components from best-of-breed vendors. However, the market investigation was inconclusive as to whether CI and HCI systems constitute a distinct product market.⁶³
- (84) While the market investigation revealed that the traditional mix and match of different hardware and software components from best-of-breed vendors remains the preferred approach for end-customers, some respondents noted the increase of purchases of CI and HCI systems over the last few years.⁶⁴

3.4.2. Conclusion on market definition for converged infrastructure systems

- (85) The question whether CI and HCI systems as pre-assembled solutions bundling a number of hardware and software components (namely, servers, storage, networking and supporting software, including virtualization software) constitute a separate product market from each of their components, as well as the geographic scope of any such possible relevant market, can be left open, as the transaction does not raise serious doubts as to its compatibility with the internal market.

4. COMPETITIVE ASSESSMENT

4.1. Horizontal overlaps

- (86) The Parties' activities overlap in relation to external ESS and in some of its possible segments, in particular (i) in the entry-level and mid-range price bands (based on IDC); (ii) in DAS, NAS and SAN; and (iii) in HDD arrays and HFAs.⁶⁵ EMC does not manufacture internal storage, optical and tape storage. Dell is not active in the high-end segment and in AFAs.

4.1.1. Overall external ESS and price band segments

4.1.1.1. The Notifying Party's view

- (87) According to the Notifying Party, the Parties' activities overlap with respect to the supply of external ESSs, in particular in the mid-range systems, as Dell does not

⁶³ See replies to Q1 – questionnaire to competitors, questions 6.3 and 6.4 and replies to Q2 – questionnaire to VMware customers, questions 8.3 and 8.4.

⁶⁴ Minutes of conference calls with competitors on 16 December 2015, on 18 December 2015 and on 4 February 2016 as well as with customers, on 7 December 2015 and on 17 December 2015

⁶⁵ Since the competitive assessment will not change, other possible markets will not be analysed for the purpose of this decision, in particular a possible overall market for external and internal storage and a possible overall market for client and enterprise storage.

offer any high-end systems⁶⁶, while EMC does not offer any true “entry-level” systems.⁶⁷

- (88) The Notifying Party submits that the transaction would not lead to a significant impediment to effective competition in the market for the supply of external ESSs for the following reasons.
- (89) First, the Parties would not be close competitors as they only compete in the sale of mid-range systems and, in that space, each of the Parties faces greater competition from other vendors.
- (90) Second, the costs of switching in ESS would be low. Dell's server customers would not be locked into a Dell storage solution and could easily replace their Dell storage product with a storage product from a competitor without incurring any material additional costs.
- (91) Third, competitors would increase supply if the merged entity were to restrict its output or raise its prices. It would not be profitable for the merged entity to reduce output, as competitors are not subject to capacity constraints. The growth in the storage market would be such that competitors are likely to increase supply to meet the increased demand.
- (92) Fourth, the merged entity would not be able to hinder entry or expansion by competitors, many of which have recently entered the market or expanded their offerings.⁶⁸
- (93) Fifth, external ESS would be highly competitive and dynamic. The transaction would allow the merged entity to develop new products addressing important IT trends, notably the explosion in data and real-time analytics and the transition from on-premises to hybrid public/private cloud infrastructure. In addition, neither EMC nor Dell would be a "maverick" player in the market.
- (94) Sixth, the merged entity would face sophisticated customers able to play the many different storage vendors off against each other to secure the most optimal and cost-effective storage solution for their IT needs.

⁶⁶ The Notifying Party notes that [...]. IDC has reported negligible sales of Dell in the high-end price class. The high-end segment is therefore not further discussed for the purpose of this decision.

⁶⁷ The IDC market share data presented in this decision indicate that EMC has entry-level products in its portfolio. However, the Notifying Party submits that EMC's VNXe product should be categorized as a mid-range storage solution by IDC and has submitted recalculated market shares for entry-level and mid-range. On the basis of these recalculated market shares, the Parties' activities would no longer overlap in the entry-level segment. In addition, the Parties' combined worldwide market share in the mid-range (including VNXe) would be [30-40]% by revenue (in 2014) (instead of [30-40]%). In view of this, the Commission considers that the competitive assessment of the transaction would not substantially change. The competitive assessment in this decision is therefore based on the market shares as provided by IDC.

⁶⁸ The Notifying Party submits that in the last five years, several start-ups (such as Pure Storage, Nimble Storage, Nimbus Data and Kaminario) have entered the ESS market and expanded their product offerings. In addition, traditional IT suppliers have entered and expanded in ESS, notably Huawei (2009), Oracle (2010) and Sugon (2011). Furthermore, white-box manufacturers would have increased output, offering an alternative to traditional OEMs. Finally, cloud storage providers would continue to expand and better compete with external ESSs.

(95) Seventh, coordinated effects would not arise as a result of the transaction.

4.1.1.2. Competitive landscape and the Commission's assessment

(96) Tables 1 and 2 below illustrate the market shares of the Parties and their competitors in external ESS in 2014 and 1H2015.

Table 1: Market shares on the market for external ESS (2014)

		EEA		Worldwide	
		Volume (Units)	Revenue	Volume (Units)	Revenue
External ESS	Dell	[10-20%]	[5-10%]	[10-20%]	[5-10%]
	EMC	[5-10%]	[20-30%]	[10-20%]	[30-40%]
	Combined	[20-30%]	[30-40%]	[20-30%]	[30-40%]
	NetApp	[5-10%]	[10-20%]	[5-10%]	[10-20%]
	IBM	[10-20%]	[10-20%]	[5-10%]	[10-20%]
	HP	[10-20%]	[10-20%]	[10-20%]	[5-10%]
	Hitachi	[0-5%]	[5-10%]	[0-5%]	[5-10%]
	Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	NEC	-	-	[0-5%]	[0-5%]
	Sugon	-	-	[0-5%]	[0-5%]
	Inspur	-	-	[0-5%]	[0-5%]
Others	[30-40%]	[10-20%]	[30-40%]	[10-20%]	

Source: Notifying Party's estimates based on third parties' reports

Table 2: Market shares on the market for external ESS (1H2015)

		EEA		Worldwide	
		Volume (Units)	Revenue	Volume (Units)	Revenue
External ESS	Dell	[10-20%]	[5-10%]	[10-20%]	[5-10%]
	EMC	[5-10%]	[20-30%]	[10-20%]	[20-30%]
	Combined	[20-30%]	[30-40%]	[20-30%]	[30-40%]
	NetApp	[10-20%]	[10-20%]	[5-10%]	[10-20%]
	IBM	[5-10%]	[10-20%]	[5-10%]	[5-10%]
	HP	[10-20%]	[10-20%]	[10-20%]	[5-10%]
	Hitachi	[0-5%]	[5-10%]	[0-5%]	[5-10%]
	Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	NEC	-	-	[0-5%]	[0-5%]
	Sugon	-	-	[0-5%]	[0-5%]
	Inspur	-	-	[0-5%]	[0-5%]
Others	[30-40%]	[10-20%]	[40-50%]	[10-20%]	

Source: Notifying Party's estimates based on third parties' reports

(97) As regards a possible overall market for external ESS, Tables 1 and 2 show that the Parties' combined market share by revenue would remain below 40% worldwide and around 30% in the EEA, [...]. Expressed in units, the combined market shares

would be around 25% both in the EEA and worldwide. In a possible worldwide market, the largest competitors would be NetApp, with a market share based on revenue of [10-20]% in 2014 and [10-20]% in 1H2015, followed by HP ([5-10]% / [5-10]%), IBM ([10-20]% / [5-10]%) and Hitachi ([5-10]% / [5-10]%), among others. Similarly, the largest competitor in an overall external ESS market in the EEA would be NetApp, with a market share based on revenue of [10-20]% in 2014 and [10-20]% in 1H2015, followed by HP ([10-20]% / [10-20]%), IBM ([10-20]% / [10-20]%), Hitachi ([5-10]% / [5-10]%).

- (98) In possible market segments based on price bands, the Parties' activities mainly overlap in the mid-range and less in the entry-level. The Parties' activities do not overlap in high-end external ESS (which is therefore not discussed further).

Table 3: Market shares on the market for mid-range external ESS (2014)

		EEA		Worldwide	
		Volume (Units)	Revenue	Volume (Units)	Revenue
Mid-range external ESS	Dell	[5-10%]	[5-10%]	[5-10%]	[5-10%]
	EMC	[20-30%]	[20-30%]	[30-40%]	[30-40%]
	Combined	[30-40%]	[30-40%]	[30-40%]	[30-40%]
	NetApp	[10-20%]	[20-30%]	[10-20%]	[20-30%]
	HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
	IBM	[10-20%]	[10-20%]	[10-20%]	[5-10%]
	Hitachi	[0-5%]	[0-5%]	[5-10%]	[5-10%]
	Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	NEC	-	-	[0-5%]	[0-5%]
	DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Sugon	-	-	[0-5%]	[0-5%]
	Inspur	-	-	[0-5%]	[0-5%]
Others	[5-10%]	[5-10%]	[10-20%]	[10-20%]	

Source: Notifying Party's estimates based on third parties' reports

Table 4: Market shares on the market for mid-range external ESS (1H2015)

		EEA		Worldwide	
		Volume (Units)	Revenue	Volume (Units)	Revenue
Mid-range external ESS	Dell	[5-10%]	[5-10%]	[5-10%]	[5-10%]
	EMC	[20-30%]	[20-30%]	[20-30%]	[20-30%]
	Combined	[30-40%]	[20-30%]	[30-40%]	[30-40%]
	NetApp	[10-20%]	[20-30%]	[10-20%]	[10-20%]
	HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
	IBM	[10-20%]	[5-10%]	[5-10%]	[5-10%]
	Hitachi	[0-5%]	[0-5%]	[5-10%]	[5-10%]
	Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	NEC	-	-	[0-5%]	[0-5%]
	DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Sugon	-	-	[0-5%]	[0-5%]
	Inspur	-	-	[0-5%]	[0-5%]
Others	[5-10%]	[10-20%]	[10-20%]	[10-20%]	

Source: Notifying Party's estimates based on third parties' reports

- (99) In the mid-range segment, the Parties' combined market share by revenue is similar as in a possible overall external ESS market, but the market share measured in units is higher (still well below 40% worldwide and closer to 30% in the EEA). [...]. The largest competitors to the Parties would be again NetApp, with a worldwide market share based on revenue of [20-30]% in 2014 and [20-30]% in 1H2015, followed by HP ([10-20]% / [10-20]%), IBM ([5-10]% / [5-10]%) and Hitachi ([5-10]% / [5-10]%), among others. Similarly, the largest competitor in the mid-range segment in the EEA would be NetApp, with a market share based on revenue of [20-30]% in 2014 and [20-30]% in 1H2015, followed by HP ([10-20]% / [10-20]%), IBM ([10-20]% / [5-10]%), Hitachi ([0-5]% / [0-5]%).

Table 5: Market shares on the market for entry-level external ESS (2014)

		EEA		Worldwide	
		Volume (Units)	Revenue	Volume (Units)	Revenue
Entry-level external ESS	Dell	[10-20%]	[20-30%]	[10-20%]	[10-20%]
	EMC	[0-5%]	[5-10%]	[5-10%]	[5-10%]
	Combined	[20-30%]	[20-30%]	[20-30%]	[20-30%]
	HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
	NetApp	[5-10%]	[10-20%]	[5-10%]	[10-20%]
	IBM	[5-10%]	[10-20%]	[5-10%]	[5-10%]
	Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Inspur	-	-	[0-5%]	[0-5%]
	Hitachi	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	NEC	-	-	[0-5%]	[0-5%]
	Sugon	-	-	[0-5%]	[0-5%]
	DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Others	[40-50%]	[20-30%]	[40-50%]	[30-40%]	

Source: Notifying Party's estimates based on third parties' reports

Table 6: Market shares on the market for entry-level external ESS (1H2015)

		EEA		Worldwide	
		Volume (Units)	Revenue	Volume (Units)	Revenue
Entry-level external ESS	Dell	[10-20%]	[20-30%]	[10-20%]	[10-20%]
	EMC	[0-5%]	[5-10%]	[0-5%]	[5-10%]
	Combined	[20-30%]	[20-30%]	[10-20%]	[20-30%]
	HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
	NetApp	[5-10%]	[10-20%]	[5-10%]	[10-20%]
	IBM	[5-10%]	[5-10%]	[0-5%]	[5-10%]
	Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	Inspur	-	-	[0-5%]	[0-5%]
	Hitachi	[0-5%]	[0-5%]	[0-5%]	[0-5%]
	NEC	-	-	[0-5%]	[0-5%]
	Sugon	-	-	[0-5%]	[0-5%]
	DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Others	[40-50%]	[20-30%]	[50-60%]	[30-40%]	

Source: Notifying Party's estimates based on third parties' reports

- (100) In a possible market for the entry-level external ESS, the Parties' combined market shares would remain below 30% worldwide and in the EEA, with a slightly higher share in the EEA ([20-30]% in 2014 and [20-30]% in 1H2015) than worldwide. The Parties' combined market share expressed in units is close to 20% in the entry-level segment, which is only [<5] points higher than the market share of the largest competitor (HP) in the EEA. In this possible entry-level market, HP is also the largest competitor worldwide, with a market share based on revenue of [10-20]% both in 2014 and in 1H2015, followed by NetApp ([10-20]% / [10-20]%), IBM ([5-10]% / [5-10]%) and Huawei ([0-5]% / [0-5]%), among others. Similarly, the largest competitor in an entry-level external ESS market in the EEA would be HP, with a market share based on revenue of [10-20]% in 2014 and [10-20]% in 1H2015, followed by NetApp ([10-20]% / [10-20]%), IBM ([10-20]% / [5-10]%) and Huawei ([0-5]% / [0-5]%).
- (101) First, based on the above Parties' pre-transaction market shares, the Commission notes that the addition of market shares by Dell in the possible markets for external ESS and mid-range external ESS and of EMC in the possible entry-level external ESS market are moderate.
- (102) Second, the possible markets for overall external ESS, mid-range external ESS and entry-level external ESS are characterised by the presence of a sufficient number of competitors that will remain active post-transaction ensuring effective competition.
- (103) In particular, NetApp is a major vendor of storage arrays and is considered by the Notifying Party to be a "pure storage" company like EMC, focusing on storage (and not on servers). In particular, it is strong in a possible EEA market for mid-range systems, where NetApp's [20-30]% market share in 1H2015 is close to EMC's [20-30]% (pre transaction).
- (104) Hewlett Packard Enterprise ("HPE" or "HP") is active in the computing and non-computing portions of the data centre. Besides being a competitor of the Parties in storage devices, HP is a competitor of Dell in a number of other IT product and service markets, namely servers, networking, software and cloud-based services. With [10-20]% market share (EEA, 2014), HP is pre-transaction the largest competitor to Dell in a possible entry-level external ESS market. HP's share in this segment increased 1.2 points in 1H2015. In the mid-range segment, HP has enjoyed a steady increase in its (worldwide) share year-on-year with a total increase of 2.8 points added between 2012 and 2014 and another 1.2 points in 1H2015. In the EEA, HP is pre-transaction the strongest player by units in a possible overall external ESS market and in the entry-level. Post-transaction, the merged entity's market share in the EEA (in units) in the possible entry-level external ESS market would only be 1.2 points higher (1H2015) than HP's share.
- (105) IBM is a provider of IT infrastructure and services worldwide including servers and storage technology along with virtualization software. At entry-level external ESS, the market shares of IBM peaked at [10-20]% (EEA) in 2014.
- (106) Hitachi is a strong competitor in the overall external ESS market and also in the possible mid-range external ESS market.
- (107) Huawei almost tripled its worldwide market share between 2012 and 1H2015 in external ESS, as it has expanded its business beyond China and Asia into other parts of the world. In the entry-level, Huawei's worldwide market share is [0-5]%

- (by revenue). In addition, Huawei has almost doubled its share in the mid-range segment since 2012, accounting for [0-5]% in 1H2015.
- (108) In addition, there are many other players, such as Oracle, Fujitsu, DataDirect Networks, NEC, Sugon, Inspur, as well as other competitors which are not individually tracked by IDC. The latter category includes (i) companies such as Pure Storage, Nimbus Data, and Kaminario which have developed all-flash or hybrid-flash arrays; (ii) start-ups such as Nimble Storage, Tintri, Tegile, and Dot Hill, which offer general-purpose disk storage systems that support multiple virtual or physical servers, and multiple databases and files; and, (iii) original design manufacturers (“ODMs”, also known as “white box manufacturers”), often based in Asia which focus heavily on providing entry-level ESS (such as Quanta, Wistron and Foxconn). ODMs serve cloud service providers and large owners of hyperscale data centers such as Google or Facebook directly, without any involvement from a storage original equipment manufacturer (“OEM”).⁶⁹
- (109) The majority of respondents who provided a response to the market investigation also consider that post-merger there will be a sufficient number of actual competitors in the possible market for external ESS and in each price band.⁷⁰
- (110) Second, the merging firms are not particularly close competitors. Considering a possible overall market of external ESS, Dell’s focus is on entry-level external ESS, which is also due to the fact that Dell is well-established as a provider of servers. [Most] of Dell’s storage sales are in fact generated by Dell’s server customers. EMC on the other hand derives more than [one third] of its storage revenues from solutions priced above USD 250 000 (*i.e.* the high-end segment). Dell does not offer any high-end product and EMC is not very strong in the entry-level.
- (111) Even in relation to the sale of mid-range systems, Dell and EMC are not each other’s closest competitors. While Dell’s EqualLogic line of storage arrays line (like EMC’s VNX line) qualifies as a mid-range system, EqualLogic focuses on simplicity of use over features, functions and performance and does not contain the advanced features of EMC’s VNX line. In addition, in the sales of Dell’s Compellent line, Dell faces greater and closer competition from HP than any other vendor, followed by NetApp and then EMC and other vendors (Huawei, Nimble Storage and Pure Storage).
- (112) The respondents to the market investigation also considered that in the possible overall external ESS market and in all the possible price bands, Dell is not EMC's close competitor.⁷¹ NetApp, followed by IBM and HP, is considered to be EMC's closest competitor in the possible overall external ESS market and the mid-range external ESS.

⁶⁹ IDC, Storage Tracker Taxonomy, [...].

⁷⁰ See replies to Q1 – questionnaire to competitors, question 62. See also agreed minutes of the call with a customer of 17 December 2015.

⁷¹ See replies to Q1 – questionnaire to competitors, question 61.

- (113) Third, customers have the possibility to switch to one of the numerous other storage providers. While switching storage supplier may involve costs and time, respondents to the market investigation indicated that switching is technically feasible and does occur.⁷²
- (114) Fourth, the market investigation did not provide any indication that competitors could not increase supply. In fact, IBM confirmed that it "*could easily increase supply*" if, post-transaction, the merged entity were to increase its prices or restrict its output of external ESS. Microsoft noted that it was "*not aware of any resource constraints that would preclude it from increasing supply*".⁷³
- (115) Fifth, there has been entry in the storage market in the past years. Several start-ups, such as Pure Storage, Nimble Storage, Nimbus Data and Kaminario have entered the external ESS market and expanded their product offerings. Other traditional IT suppliers have also recently entered and expanded in ESS: notably Huawei (2009), Oracle (2010) and Sugon (2011). [...]:

Figure 1: [...]

[...]

- (116) Furthermore, white box suppliers have increased their shares in the ESS market and in particular in the entry-level and mid-range.⁷⁴ The merging parties therefore do not have the ability to hinder expansion of their competitors in ESS.
- (117) Finally, no significant concerns were raised with regard to the impact of the transaction on the market for external ESS due to the horizontal overlap.⁷⁵

4.1.1.3. Conclusion on overall external ESS and price band segments

- (118) In light of the considerations set out in paragraphs (96) to (117) and of the outcome of the market investigation and the information available to the Commission, and taking particular account of the moderate combined market share of the Parties as well as of the important number of competitors of varying size that will remain active post-merger, the Commission considers that the transaction does not give rise to serious doubts as to its compatibility with the internal market with respect to the possible markets for external ESS.

⁷² See replies to Q1 – questionnaire to competitors, question 64.

⁷³ See replies to Q1 – questionnaire to competitors, question 65.

⁷⁴ In 2014, the category “Others” of the IDC market share figures, including white box suppliers, accounted for more than one third of the value of ESS at entry-level.

⁷⁵ See replies to Q1 – questionnaire to competitors, question 67.3. See also agreed minutes of the call with a customer of 17 December 2015.

4.1.2. Other possible markets

(119) The IDC market shares of the Parties and their competitors in 2014 and 1H2015 (by revenue) in (i) DAS NAS and SAN and (ii) HDD arrays and HFAs, as submitted by the Parties, are set out below.

4.1.2.1. DAS, NAS and SAN

Table 7: DAS market shares⁷⁶

	Worldwide 2014	Worldwide 1H2015	EEA 2014	EEA 1H2015
Dell	[10-20%]	[10-20%]	[10-20%]	[20-30%]
EMC	[5-10%]	[0-5%]	[10-20%]	[5-10%]
Combined	[20-30%]	[20-30%]	[30-40%]	[30-40%]
HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
Fujitsu	[5-10%]	[5-10%]	[0-5%]	[0-5%]
NEC	[0-5%]	[0-5%]	-	-
Hitachi	[0-5%]	[0-5%]	[0-5%]	[0-5%]
IBM	[0-5%]	[0-5%]	[5-10%]	[5-10%]
Others	[40-50%]	[40-50%]	[40-50%]	[40-50%]
Total	100.0%	100.0%	100.0%	100.0%

Source: Notifying Party's estimates based on third parties' reports

(120) The combined market shares of the Parties in a possible external ESS for DAS are moderate worldwide ([20-30]% in 2014 and [20-30]% in 1H2015). In the EEA, the shares are [30-40]% (2014) and [30-40]% (1H2015). The Parties also face strong competition from other vendors, including HP, Fujitsu, NEC and Hitachi (on a possible worldwide market), and HP, IBM and Fujitsu (in the EEA).

⁷⁶ There are two types of DAS systems, as detailed by the Parties: (i) the normal DAS system, which is Just a Bunch Of Disks without storage intelligence apart from the server; and (ii) DAS-connected SANs, which consist of directly-attached Fibre Channel, ESCON and FICON systems wired directly to the system. Dell mainly provides the former, and EMC only the latter, which is very common in high-end set-ups. According to the Parties, the DAS-connected SAN storage better fits the SAN systems classification, although is reported as DAS by IDC.

Table 8: NAS market shares

	Worldwide 2014	Worldwide 1H2015	EEA 2014	EEA 1H2015
Dell	[0-5%]	[0-5%]	[0-5%]	[0-5%]
EMC	[40-50%]	[40-50%]	[40-50%]	[40-50%]
Combined	[50-60%]	[40-50%]	[50-60%]	[50-60%]
NetApp	[20-30%]	[20-30%]	[30-40%]	[30-40%]
DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
HP	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Hitachi	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
IBM	[0-5%]	[0-5%]	[0-5%]	[0-5%]
<i>Others</i>	[10-20%]	[10-20%]	[10-20%]	[10-20%]
Total	100.0%	100.0%	100.0%	100.0%

Source: Notifying Party's estimates based on third parties' reports

- (121) The combined market shares of the Parties would be around 50% in a possible market for NAS. However, the increment brought about by the transaction would be small.
- (122) The Parties also face strong competition from other vendors, including NetApp with a market share of [20-30]% (2014) and [20-30]% (1H2015) worldwide and [30-40]% (2014) and [30-40]% (1H2015) in the EEA. Other players in this possible market include HP, Oracle, Hitachi, Fujitsu and IBM.

Table 9: SAN market shares

	Worldwide 2014	Worldwide 1H2015	EEA 2014	EEA 1H2015
Dell	[5-10%]	[5-10%]	[5-10%]	[5-10%]
EMC	[20-30%]	[20-30%]	[10-20%]	[10-20%]
Combined	[30-40%]	[30-40%]	[20-30%]	[20-30%]
HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
IBM	[10-20%]	[10-20%]	[10-20%]	[10-20%]
NetApp	[5-10%]	[10-20%]	[10-20%]	[10-20%]
Hitachi	[5-10%]	[5-10%]	[5-10%]	[5-10%]
Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
<i>Others</i>	[10-20%]	[10-20%]	[5-10%]	[10-20%]
Total	100.0%	100.0%	100.0%	100.0%

Source: Notifying Party's estimates based on third parties' reports

- (123) In a possible market for SAN the combined market shares of the Parties would be moderate, namely around 30% worldwide and around 25% in the EEA.

- (124) The Parties also face strong competition from other vendors, including HP (the market leader in the EEA pre-transaction), IBM, NetApp, Hitachi, Oracle, Huawei and Fujitsu.
- (125) Finally, no significant concerns were raised with regard to the impact of the transaction on the possible markets for DAS, NAS and SAN external ESS due to the horizontal overlap. Most respondents who provided a meaningful response to the market investigation also consider that post-transaction, there will be a sufficient number of actual competitors and potential new entrants in each possible segment.⁷⁷

4.1.2.2. HDD arrays and HFAs

- (126) The IDC market shares of the Parties and their competitors in 2014 and 1H2015 in HFAs and HDD arrays (by revenue), as submitted by the Parties, are set out below.

Table 10: HFA market shares

	Worldwide 2014	Worldwide 1H2015	EEA 2014	EEA 1H2015
Dell	[0-5%]	[0-5%]	[0-5%]	[5-10%]
EMC	[30-40%]	[30-40%]	[20-30%]	[20-30%]
Combined	[30-40%]	[30-40%]	[30-40%]	[20-30%]
NetApp	[10-20%]	[10-20%]	[10-20%]	[10-20%]
Hitachi	[10-20%]	[10-20%]	[10-20%]	[5-10%]
IBM	[10-20%]	[10-20%]	[10-20%]	[10-20%]
Oracle	[0-5%]	[5-10%]	[5-10%]	[5-10%]
HP	[0-5%]	[5-10%]	[5-10%]	[5-10%]
DataDirect Networks	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
<i>Others</i>	[5-10%]	[10-20%]	[5-10%]	[5-10%]
Total	100.0%	100.0%	100.0%	100.0%

Source: Notifying Party's estimates based on third parties' reports

- (127) The combined market shares of the Parties would be [30-40]% (2014) and [30-40]% (1H2015) in a possible market for HFAs worldwide. In the EEA, the combined market share of the Parties would be lower, *i.e.* [30-40]% (2014) and [20-30]% (1H2015). The increment brought about by the transaction would be moderate (around [0-5]%).
- (128) The Parties also face strong competition from other vendors, including NetApp (with a market share of around [10-20]%), IBM, Hitachi, Oracle, HP, DataDirect Networks, Huawei and Fujitsu.

⁷⁷ See replies to Q1 – questionnaire to competitors, questions 62.5 and 63.5. See also agreed minutes of the call with a customer of 17 December 2015.

Table 11: HDD arrays market shares

	Worldwide 2014	Worldwide 1H2015	EEA 2014	EEA 1H2015
Dell	[5-10%]	[10-20%]	[10-20%]	[10-20%]
EMC	[20-30%]	[20-30%]	[20-30%]	[20-30%]
<i>Combined</i>	<i>[30-40%]</i>	<i>[30-40%]</i>	<i>[30-40%]</i>	<i>[30-40%]</i>
HP	[10-20%]	[10-20%]	[10-20%]	[10-20%]
NetApp	[5-10%]	[5-10%]	[10-20%]	[10-20%]
IBM	[5-10%]	[5-10%]	[10-20%]	[5-10%]
Hitachi	[5-10%]	[5-10%]	[0-5%]	[0-5%]
Fujitsu	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Huawei	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]
<i>Others</i>	<i>[10-20%]</i>	<i>[20-30%]</i>	<i>[10-20%]</i>	<i>[10-20%]</i>
Total	100.0%	100.0%	100.0%	100.0%

Source: Notifying Party's estimates based on third parties' reports

- (129) The combined market shares of the Parties would be [30-40]% (2014) and [30-40]% (1H2015) in a possible market for HDD arrays worldwide. In the EEA, the combined market share of the Parties would be lower, *i.e.* [30-40]% (2014) and [30-40]% (1H2015).
- (130) The Parties also face strong competition from other vendors, including HP, NetApp, IBM, Hitachi, Fujitsu, Huawei and Oracle.
- (131) Finally, no significant concerns were raised with regard to the impact of the transaction on the possible markets for HFAs and HDD arrays due to the horizontal overlap. Most respondents who provided a meaningful response to the market investigation also consider that post-transaction, there will be a sufficient number of actual competitors and potential new entrants in each possible segment.⁷⁸

4.1.2.3. Conclusion on other possible markets

- (132) In light of above, and in particular in view of the moderate combined market share of the Parties in DAS, SAN, HFAs and HDD arrays and the small increment brought by the transaction in NAS and HFAs, as well as the important number of competitors of varying size that will remain active post-merger, the Commission considers that the transaction does not give rise to serious doubts as to its compatibility with the internal market with respect to the possible markets for DAS, NAS, SAN as well as HDD arrays and HFAs.

4.1.3. Conclusion on the horizontal assessment

- (133) In light of the considerations in paragraphs (96) to (117) and (119) to (131) and of the outcome of the market investigation and the evidence available to it, the Commission considers that the transaction does not give rise to serious doubts as to

⁷⁸ See replies to Q1 – questionnaire to competitors, questions 62.4 and 63.4. See also agreed minutes of the call with a customer of 17 December 2015.

its compatibility with the internal market with respect to the horizontal overlaps of the Parties' activities under any plausible segmentation.

4.2. Non-horizontal assessment

- (134) The transaction gives rise to non-horizontal links on some of the markets on which the Parties are active. In particular, VMware's virtualization software can be used in conjunction with some of Dell's hardware products, namely, servers, external ESSs, as well as CI and HCI solutions.
- (135) Thus, there might be a risk that, post-transaction, the merged entity could attempt to restrict or degrade access to VMware's software to competing hardware vendors and/or to foreclose other storage virtualization software vendors by depriving them of a sufficient customer base.
- (136) According to the Non-Horizontal Merger Guidelines, foreclosure occurs when actual or potential rivals' access to supplies or markets is hampered, thereby reducing those companies' ability and/or incentive to compete. Such foreclosure may discourage entry or expansion of rivals or encourage their exit.⁷⁹
- (137) The Non-Horizontal Merger Guidelines distinguish between two forms of foreclosure: input foreclosure occurs where the merger is likely to raise the costs of downstream rivals by restricting their access to an important input and customer foreclosure occurs where the merger is likely to foreclose upstream rivals by restricting their access to a sufficient customer base.⁸⁰
- (138) In order for foreclosure to be a concern, three conditions need to be met post-merger: (i) the merged entity needs to have the ability to foreclose its rivals⁸¹; (ii) the merged entity needs to have the incentive to foreclose its rivals⁸²; and (iii) the foreclosure strategy needs to have a significant detrimental effect on the parameters of competition on the downstream market (input foreclosure)⁸³ or on consumers (customer foreclosure). In practice, these factors are often examined together since they are closely intertwined.⁸⁴
- (139) In this section, the Commission will thus assess whether there is a risk that the integration brought about by the transaction might lead to foreclosure with respect to the potential markets for: (i) servers and virtualization software (section 4.2.1); (ii) storage and virtualization software (section 4.2.2); and (iii) CI and HCI solutions (section 4.2.3).

⁷⁹ Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentration between undertakings (the Non-Horizontal Merger Guidelines) OJ C 265/6, 18.1.0.2008, , paragraphs 29-30.

⁸⁰ See Non-Horizontal Merger Guidelines, paragraph 30.

⁸¹ See Non-Horizontal Merger Guidelines, paragraphs 33 to 39 and 60 to 67.

⁸² See Non-Horizontal Merger Guidelines, paragraphs 40 to 46 and 68 to 71.

⁸³ See Non-Horizontal Merger Guidelines, paragraphs 47 to 57.

⁸⁴ See Non-Horizontal Merger Guidelines, paragraphs 72 to 77.

- (140) The Commission will not assess any vertical links in the desktop virtualization space⁸⁵ as: (i) Dell does not offer any proprietary desktop platform⁸⁶, (ii) VMware's market shares in this type of software are very low ([10-20]% worldwide, behind Microsoft⁸⁷ with [20-30]% and Citrix with [40-50]%) and Dell's market share in desktops and notebooks combined is equally very low ([10-20]% worldwide⁸⁸, behind Apple with [10-20]%, HP with [10-20]% and Lenovo with [10-20]%).
- (141) Additionally, no respondents to the market investigation raised any concerns with regard to the vertical link between desktop virtualization software and desktops.
- (142) Similarly, the Commission notes the absence of any vertical links in the network virtualization space⁸⁹ as Dell does not offer a software-defined networking product.

4.2.1. Servers and virtualization software

4.2.1.1. Notifying Party's view

- (143) The Notifying Party submits that the merged entity would not have the ability to foreclose.
- (144) According to the Notifying Party, VMware does not have significant market power in virtualization software, given the competitive environment in which it operates. VMware virtualization software is far from unique and, to the contrary, it faces strong competition from a number of traditional server virtualization software vendors (such as Microsoft, Red Hat or Citrix), open-source solutions, public cloud providers, as well as new technologies such as containers.
- (145) Customers, including major corporations with sophisticated needs, could easily switch to those alternative providers without much effort, and many have already done so in the past. Therefore, any indication of a move towards even partial foreclosure would encourage customers to seek alternative solutions, making such strategy unsuccessful.
- (146) Moreover, the Notifying Party submits that VMware's vSphere is structured to function in an open ecosystem, and claims that it is both hardware and operating system-neutral. The Notifying Party explains that VMware's vSphere product is the first piece of software that sits on an x86 server, and therefore VMware needs to keep fostering relationships both with hardware companies such as Dell, HP, Lenovo, NetApp, Hitachi and IBM, and with enterprises selling operating system and enterprise applications that sit above the virtualization software layer (different operating systems). Promoting an open and non-discriminatory architecture strategy has been the basis of VMware's success. Abandoning such strategy would

⁸⁵ See definition above, under section 3.3.1.

⁸⁶ Dell's desktop platform product vWorkspace is built on top of offers from other vendors.

⁸⁷ Microsoft's main desktop virtualization product is called RemoteApp and Citrix's main product is called Xen Desktop.

⁸⁸ According to the Notifying Party, Dell's share in desktops-only was estimated at [10-20]% and of notebooks-only was [10-20]%, worldwide.

⁸⁹ See definition above, under section 3.3.1.

undermine VMware's value, risk customer backlash and cause irreparable harm not only to VMware and Dell's server business, but also to Dell's storage business, ultimately damaging Dell's brand.

- (147) As to the merged entity's incentive to engage in foreclosure, the Notifying Party submits that moving away from the current VMware's hardware/software-neutral strategy would have severe consequences because it would alienate all or a significant proportion of customers, who value flexibility and freedom to choose best-of-breed hardware and software from different vendors.
- (148) Moreover, from a financial point of view, it would not be plausible for the merged entity to adopt a foreclosure strategy designed to "force" prospective customers to buy a Dell server, due to the high percentage of such sales that would have to be achieved to be profitable.⁹⁰
- (149) Finally, the Notifying Party concludes that there would be no anti-competitive effects. It submits that the extent and range of effective competitors in both hardware and virtualization software means that competition is unlikely to deteriorate following the merger, that barriers to entry and expansion are low, and that new technologies pose a significant competitive constraint.

4.2.1.2. The results of the market investigation and the Commission's assessment

- (150) The Commission will assess the risk of input foreclosure of VMware's server virtualization software, considering whether the transaction would change the merged entity's (i) ability and (ii) incentive to grant access to its server virtualization software and, (iii) if this were to have an impact on the servers' market.

a. Ability to engage in input foreclosure

- (151) During the pre-notification phase and the market investigation,⁹¹ some companies (competitors of Dell and EMC in server and/or storage hardware) raised the concern that the merged entity might partially foreclose VMware's software from competing server vendors, thus making their server offerings less attractive.
- (152) This could be achieved in a number of ways, for example, by adopting specific software or hardware design choices favouring Dell, tying services and support offerings, engaging in bundling/discount strategies, and/or degrading or delaying access to updates/new versions, certification, application programming interfaces ("APIs"), and customer support.

⁹⁰ The Notifying Party bases its submission on a study it commissioned from Compass Lexecon.

⁹¹ See replies to Q1 – questionnaire to competitors, question 36 and replies to Q2 – questionnaire to VMware customers, question 31.

- (153) According those competitors, customers would not be able to switch to competing offers, in light of the very high costs and significant length of switching and the fact that vSphere's specific advanced features make it the only suitable option especially for large corporations.
- (154) Moreover, those competitors submit that the transaction would harm competition and enhance the merged entity's long-term ability to raise prices and limit choices for customers.
- (155) The Commission notes that, given the proprietary nature of VMware's software vSphere, the merged entity would have the technical ability to limit or prevent access to it for competing servers' vendors.
- (156) However, for input foreclosure to be a concern, the merged entity must have a significant degree of market power, and a significant influence on the conditions of competition in the upstream market.⁹² In the following paragraphs the Commission will assess whether the merged entity would have such a market power.
- (157) As to the most appropriate metric to be used in this regard, market intelligence firm IDC⁹³ as well as the majority of the respondents to the market investigation submit, in line with the Notifying Party's view, that the number of virtualization hosts is a reliable proxy for market power in the server virtualization software. In fact, some vendors (such Microsoft) do not separately charge for their software because they either bundle it with other products or because they offer open source-based software and monetize their business by charging for services. Therefore, their sales are not entirely captured by IDC data.⁹⁴
- (158) In particular, according to IDC data, VMware's share of server virtualization software in terms of volume (measured on the basis of the number of virtualizations hosts) has been declining from [50-60]% in 2010 to [40-50]% in the 1Q2015 at a worldwide level.⁹⁵

⁹² See Non-Horizontal Merger Guidelines, paragraph 35.

⁹³ See IDC, Worldwide Virtual Machine and Cloud System Software Market Shares, 2014: Open Source Disruption in Cloud, September 2015, pages 4-5.

⁹⁴ See replies to Q1 – questionnaire to competitors, question 25 and replies to Q2 – questionnaire to VMware customers, question 21.

⁹⁵ At EEA level, the shares have been declining in the same period from [50-60]% to [40-50]%.

Table 12: Worldwide – Server virtualization software Shares based on Virtualized Hosts – 2008-1Q2015⁹⁶

	2008	2009	2010	2011	2012	2013	2014	1Q2015
Citrix	[0-5%]	[5-10%]	[5-10%]	[5-10%]	[5-10%]	[5-10%]	[5-10%]	[5-10%]
HP	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
IBM	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Microsoft	[20-30%]	[20-30%]	[20-30%]	[20-30%]	[20-30%]	[30-40%]	[30-40%]	[30-40%]
Oracle	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Parallels	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Red Hat	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Sun Microsystems	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
Virtual Iron	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]	[0-5%]
VMware	[60-70]%	[50-60]%	[50-60]%	[50-60]%	[50-60]%	[40-50]%	[40-50]%	[40-50]%
Others	[5-10%]	[5-10%]	[5-10%]	[5-10%]	[5-10%]	[5-10%]	[10-20%]	[10-20%]
Total	100%	100%	100%	100%	100%	100%	100%	100%

Table 13 – Worldwide – Server virtualization software Shares based on Number of Virtualization Hosts – 2008-1Q2015⁹⁷

	2008	2009	2010	2011	2012	2013	2014	1Q2015
Citrix	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
HP	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
IBM	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Microsoft	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Oracle	-	-	-	[...]	[...]	[...]	[...]	[...]
Parallels	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Red Hat	-	-	-	[...]	[...]	[...]	[...]	[...]
Sun Microsystems	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Virtual Iron	[...]	[...]	-	-	-	-	-	-
VMware	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Others	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Total	2 065 687	1 695 679	2 645 540	2 886 847	3 131 622	3 674 901	4 112 990	766 399

⁹⁶ IDC Server Virtualization Tracker, 1Q2015. These shares are calculated using "virtualization hosts," which refers to virtualization licenses on the host server.

⁹⁷ IDC Server Virtualization Tracker, 1Q2015.

(159) Figure 2 below shows the decline in VMware's share in volume.⁹⁸

**Figure 2: Share based on number of virtualization hosts
[graphic]**

(160) To the contrary, VMware's share in revenue has been relatively stable in the last few years at more than [70-80]% ([70-80]% in the 1Q2015, [70-80]% in 2014, [70-80]% in 2013, [70-80]% in 2012, [70-80]% in 2011, and [70-80]% in 2010 at worldwide level). As evidenced also by Table 13 above, the difference with the evolution of VMware's declining shares in volume can be ascribed to the fact that customers are increasingly deploying alternative options from competing vendors, including those who do not charge separately for their server virtualization software.

(161) In fact, VMware's server virtualization software is facing an increasing competitive pressure by other providers of server virtualization software.

(162) In particular, the market investigation showed that a number of alternative server virtualization vendors are active in this segment, *e.g.*, Microsoft, Citrix, Red Hat, or Oracle.

(163) According to the respondents to the market investigation,⁹⁹ there are varying degrees of maturity and features in each of those competing products, which have dynamically evolved in the last years. While most of respondents consider that vSphere is the leading virtualization software solution offering a broad set of functionalities,¹⁰⁰ most respondents (including major customers) consider that the features of VMware's product can be replicated by competitors.¹⁰¹ According to market participants, server virtualization offerings "are largely comparable to each other,"¹⁰² "as [of] today, all server virtualization solutions are close [to] each other in term[s] of feature"¹⁰³ and "for the core function of server virtualization, different products from different providers generally offer the same functionality,"¹⁰⁴ while another player noted that "the maturity of virtualization products in the market are of sufficient technical and performance level."¹⁰⁵

⁹⁸ IDC Worldwide Virtualization Software Tracker, 2015-1Q.

⁹⁹ See replies to Q1 – questionnaire to competitors, question 31, 32 and 33 and replies to Q2 – questionnaire to VMware customers, question 12 and 14.

¹⁰⁰ See replies to Q1 – questionnaire to competitors, question 32 and 33, and replies to Q2 – questionnaire to VMware customers, question 12 and 14.

¹⁰¹ Only one respondent suggested that the NSX product (network virtualization) cannot be replicated but did not provide further reasons for this claim. See replies to Q1 – questionnaire to competitors, question 32 and replies to Q2 – questionnaire to VMware customers, question 14.

¹⁰² See replies to Q1 – questionnaire to competitors, question 31.1.

¹⁰³ See replies to Q1 – questionnaire to competitors, question 34.1.

¹⁰⁴ See replies to Q1 – questionnaire to competitors, question 26.1.

¹⁰⁵ See replies to Q1 – questionnaire to competitors, question 26.1.

- (164) In particular, the overwhelming majority of respondents to the market investigation¹⁰⁶ submitted that the closest competitor and main alternative to VMware's vSphere is Microsoft's Hyper-V.¹⁰⁷ When comparing HyperV to vSphere, a major IT player explained that "there is almost feature parity between the two virtualization options" and another participant to the market investigation submitted that "Hyper-V does very well against VMware in terms of cost and in terms of integration with Windows Server."¹⁰⁸ In fact, as shown by Figure 2 above, the gap between VMware's and Microsoft's deployments has narrowed from more than 40% in 2008 (when Hyper-V was launched) to just under 17% in 2014.¹⁰⁹
- (165) Microsoft's HyperV is offered for free as a standalone downloadable product or as a feature to customers of Microsoft's Windows Server¹¹⁰ and has progressively expanded its feature set over the years,¹¹¹ making it an increasingly viable option for customers, including major ones. This is evidenced also by the fact that several major clients across a variety of industries, including ones that have mission-critical needs (such large financial institutions, healthcare providers, as well as telecom and media companies), have selected Hyper-V as their virtualization software or have switched away from VMware in favour of Hyper-V.¹¹²
- (166) In addition, Red Hat's Enterprise Virtualization product ("RHEV") uses the Linux kernel as a hypervisor with virtual machines having direct access to the hardware resources. As shown by internal documents and publicly available information,¹¹³ VMware monitors closely RHEV, comparing it regularly against vSphere either through internal evaluations or third party studies. As with Microsoft's Hyper-V, many customers, including major banking clients, energy companies and government departments, select RHEV for new deployments or switch away from VMware.¹¹⁴
- (167) Other offerings include Citrix's Xen (which has no licensing fees and is freely available, with Citrix charging customers only for support and maintenance) and open-source based software KVM, which "are very attractive because of the open

¹⁰⁶ All respondents with the exception of one customer (which identified RedHat as the main competitor and Microsoft as the second one). See replies to Q2 – questionnaire to VMware customers, question 12.

¹⁰⁷ See replies to Q1 – questionnaire to competitors, question 31 and replies to Q2 – questionnaire to VMware customers, question 12.

¹⁰⁸ See replies to Q1 – questionnaire to competitors, question 31 and replies to Q2 – questionnaire to VMware customers, question 12.

¹⁰⁹ See also presentation at Microsoft's Ignite conference "Spark the Future", May 6-8 2015, p. 7.

¹¹⁰ See replies to Q1 – questionnaire to competitors, question 1.

¹¹¹ See, *e.g.*, "Why Hyper-V? Competitive Advantages of Windows Server 2012 R2 Hyper-V over VMware vSphere 5.5 - October 2013 v1.0" and "Microsoft Private Cloud - A Comparative Look at Functionality, Benefits, and Economics November 2012."

¹¹² See presentation at Microsoft's Ignite conference "Spark the Future", May 6-8 2015, p. 8 as well the several customers case studies available on Microsoft's website (<https://customers.microsoft.com/Pages/Home.aspx>).

¹¹³ See Annexes D.023, D.024, and D.025 to the Form CO.

¹¹⁴ See examples on RedHat's website (<https://www.redhat.com/en/success-stories>).

source nature and community associated with them [and] also do very well in terms of cost."¹¹⁵ In particular, KVM "makes the most sense"¹¹⁶ for cloud solutions based on OpenStack (a free and open-source software platform for cloud computing).

- (168) Regarding alternatives to server virtualization software, although not in a conclusive manner, the market investigation¹¹⁷ provided some indications that VMware might be facing competitive pressure from public cloud providers, such as Amazon (Amazon Web Services, "AWS"), Microsoft (Azure) or Google (Google Cloud). In fact, as research firm Gartner reports, in 2014 "the majority of new VM [virtual machines] were deployed to public cloud IaaS providers, rather than on-premise."¹¹⁸
- (169) Similarly to traditional hypervisors, public cloud providers allow users to create and execute as many virtual machines as they need, the difference being that customers enjoy more flexibility as they only pay for the computing resources they actually use (converting upfront hardware and software costs into a per-minute rental) and, most importantly, they are indifferent to the underlying hardware used by the public cloud provider.
- (170) Therefore, public cloud offerings might potentially affect the demand for hardware as well as traditional virtualization software, since virtual machines are increasingly created in the cloud instead of in a traditional virtualized data centre.¹¹⁹ Moreover, the current largest providers of public cloud offerings (AWS, Microsoft and Google) do not need and are not major customers of VMware's products,¹²⁰ either because they rely on open source hypervisor technology or because they have their own virtualization technology.
- (171) Moreover, a number of major customers in a variety of industries (*e.g.*, in automotive, energy, banking and hotel sectors) have either decided against incremental additions to their traditional data centre in favour of a public cloud solution or completely replaced their data centre with a public cloud solution.¹²¹
- (172) In addition, although the market investigation provided mixed views on the subject,¹²² the emerging technology of containers might in the future evolve to displace the need for traditional virtualization software,¹²³ especially for next-

¹¹⁵ See replies to Q1 – questionnaire to competitors, question 31.1.

¹¹⁶ See replies to Q1 – questionnaire to competitors, question 28.1.

¹¹⁷ See replies to Q1 – questionnaire to VMware customers, question 8.1.

¹¹⁸ Gartner, Four Trends Changing Server Virtualization Decisions, March 5, 2015, page 2. "IaaS" is the acronym of "Infrastructure as a service", which is a form of cloud computing that provides virtualized computing resources over the Internet.

¹¹⁹ Gartner, Four Trends Changing Server Virtualization Decisions, March 5, 2015.

¹²⁰ See replies to Q1 – questionnaire to competitors, question 1.

¹²¹ See, *e.g.*, case studies on Amazon's website (<https://aws.amazon.com/solutions/case-studies/>).

¹²² See replies to Q1 – questionnaire to competitors, questions 6, 19 and 20.1 and replies to Q2 – questionnaire to VMware customers, question 27.

¹²³ Gartner, Four Trends Changing Server Virtualization Decisions, March 5, 2015, page 8.

generation workloads, with one respondent to the market investigation remarking that "we are watching the emergence of containers as a potential alternative to virtualization, and will continue to evaluate the maturity of containers."¹²⁴

- (173) If the merged entity were to attempt to degrade access to VMware to competing servers' vendors, a number of alternative server virtualization software options could be available to customers, depending on their needs and business models. In this respect, the market investigation showed that, although it typically involves significant time and resources, it is possible to switch to alternative solutions, also thanks to a number of *ad hoc* tools that facilitate migration.¹²⁵
- (174) Moreover, as confirmed by the market investigation,¹²⁶ clients typically multi-source with more than one server virtualization software supplier for a variety of reasons. Therefore, if the merged entity would attempt to partially foreclose its server virtualization software, customers might switch to a competing product which they already use. There is a view that switching is difficult in terms of cost and time, however, respondents to the market investigation also reported that the process of switching was technically possible and fairly straightforward.¹²⁷
- (175) Most of the end customers who participated in the market investigation considered that there would be sufficient credible alternative options post-transaction.¹²⁸
- (176) In light of the findings of this section and of the outcome of the market investigation, the Commission concludes that the effect on VMware of competition from alternative server virtualization software vendors is such that the merged entity would lack the ability to engage in input foreclosure.

b. Incentive to engage in input foreclosure

- (177) The Commission notes that, according to the large majority of market participants,¹²⁹ VMware has so far adopted a hardware/software-neutral approach, fostering relationships with a very large number of vendors without limiting or degrading access to, *e.g.*, certification, support, or new updates.¹³⁰
- (178) In fact, on the basis of the market investigation,¹³¹ the Commission considers that customers value the freedom to combine best-of-breed hardware and software offerings and typically multi-source x86 servers and server virtualization software

¹²⁴ See replies to Q1 – questionnaire to competitors, question 35.2.

¹²⁵ See replies to Q1 – questionnaire to competitors, question 34.1.

¹²⁶ See replies to Q1 – questionnaire to competitors, question 28 and replies to Q2 – questionnaire to VMware customers, question 33.

¹²⁷ See replies to Q2 – questionnaire to VMware customers, questions 16 & 17

¹²⁸ See replies to Q2 – questionnaire to VMware customers, questions 19 and 28. .

¹²⁹ See replies to Q1 – questionnaire to competitors, question 24.

¹³⁰ According to the Notifying Party, VMware has over [...] technology partnership agreements and more than [...] active service providers partners.

¹³¹ See replies to Q1 – questionnaire to competitors, question 27 and replies to Q2 – questionnaire to VMware customers, question 32.

from multiple vendors. Therefore, in order to promote a large adoption of its product, VMware had to endorse an open and non-discriminatory architecture policy.

- (179) In this regard, the Commission also notes that the CEO of Dell (Michael S. Dell) has made a public commitment not to change VMware's approach and keeping it independent and open.¹³²
- (180) Some market players who participated in the investigation submit that changing such business strategy, by foreclosing or degrading access to vSphere, is "extremely unlikely [...] as it would open up a large opportunity for competitive hypervisors to take market share."¹³³
- (181) The Commission considers that, if the merged entity were to engage in such a strategy, customers would likely switch to one or more of the alternative solutions available in the market (discussed in the section 4.2.1.2.a)), in order to avoid the risk of being locked-in into a specific solution.
- (182) Furthermore, the incentive to pursue a foreclosure strategy depends on the extent to which such strategy would be profitable from a financial point of view. In particular, the cost to the merged entity in terms of lost sales of VMware's software (that – absent the strategy – would have been made to customers deploying it on non-Dell's servers) would have to be lower than the benefit coming from the increased sales of Dell's servers (*i.e.*, the sales of Dell's servers that are diverted from Dell's competitors as a result of the foreclosure strategy).
- (183) In this regard, an economic paper submitted by the Notifying Party focuses on the question of how many customers would need to switch from a rival hardware vendor to the merged entity (with a view to obtaining VMware's virtualization software) for the merged entity to find it profitable to engage in a foreclosure strategy. Based on average selling prices and gross margins, the economic paper calculated the profit generated by Dell and VMware on the sale of a typical server and a licence, respectively.¹³⁴ Using these figures, it then calculated the proportion of VMware virtualization software customers that would need to divert to the merged entity's for the foreclosure strategy to be profitable.
- (184) The proportion of new customers (that wished to buy VMware's virtualization software and a server) that would need to be diverted is more than [...]%, which – given the alternative solutions available in the market – is considered implausibly

¹³² Michael Dell has declared that "we intend for VMware to remain an independent public company [...] Once the transaction closes, we plan to handle VMware the same way as EMC by keeping VMware independent, leaving VMware free to continue using its cash flow to invest in its business and to continue its committed relationships with its VMware Partner Network [...] Our intent is only to continue to help it thrive, innovate and grow, as an independent company with an independent and open ecosystem." Message from Michael Dell: Committed to VMware Independence and to Open Ecosystem, October 19, 2015. Available at <http://en.community.dell.com/dellblogs/direct2dell/b/direct2dell/archive/2015/10/19/message-from-michael-dell-committed-tovmwareindependence-and-to-open-ecosystem>.

¹³³ See replies to Q1 – questionnaire to competitors, question 36.2.

¹³⁴ The economic paper also takes into account also the profit from potential incremental sales of ESS, bought in conjunction with the server.

high.¹³⁵ Moreover, in order to be sustainable, the foreclosure strategy would need to keep diverting such an implausibly high proportion of customers regardless of the possible future alternatives that server virtualization's competitors might develop over time in reaction to the strategy.

- (185) Complainants argued that, in light of the issuance of tracking stock under the corporate structure of the transaction, Denali would have only a 28% economic interest in VMware (*i.e.*, the 35% of 81% VMware interest currently owned by EMC) and, if it were to engage in a foreclosure strategy, it would thus forego only 28% of profits for the lost sales of VMware's software. As such, the sales of incremental Dell's servers would compensate such foregone profit, making a foreclosure strategy profitable. Finally, the public shareholders who will be holding 19% of VMware's stock post-transaction would not be able to discipline such adverse conduct because they would only have limited legal protection.
- (186) In this regard, the Notifying Party submits, first, that the issuance of tracking stock has a clear rationale, which is unrelated to any foreclosure strategy.¹³⁶ Second, a foreclosure strategy would run counter to Denali's tracking stock policy, which obliges it to pursue the best interests of VMware. Third, even taking into account a reduced economic interest in VMware, a foreclosure strategy would still be financially harmful and thus unlikely for the same reasons explained in paragraphs 183 and 184 above. Finally, post-transaction, the shareholders of VMware other than the Denali shareholders, would have sufficient legal protection against any attempt to favour Dell's servers to the detriment of VMware's software.
- (187) Based on the results of the market investigation and on the available evidence, the Commission considers that it is unlikely that the value of foregone vSphere's sales would be more than compensated by the value of incremental sales of Dell's servers.
- (188) This is also because, as discussed in section 4.2.1.2.a, customers would be able to switch to competing server virtualization offerings and therefore would move away from the merged entity's servers.
- (189) In light of the findings of this section based on the results of the market investigation and the evidence available to it, the Commission concludes that the merged entity will lack the incentive to engage in input foreclosure.

c. Overall impact of input foreclosure

- (190) Even if *arguendo* the merged entity were to have the ability and incentive to engage in input foreclosure, the impact of those attempts on effective competition would depend on the possibility of customers to source servers from alternative providers.

¹³⁵ Similar results apply in the case of customers who wished to buy VMware's virtualization software and a server together with external ESS.

¹³⁶ According to the Notifying Party, tracking stocks are intended to provide EMC shareholders with the opportunity to benefit from any value creation resulting from any revenue synergies of the portion of Dell's economic interest in VMware. Additionally, the issuance of tracking stock enables the payment of a higher purchase price for EMC than it could in a transaction consisting entirely of 100% cash consideration.

- (191) In this respect, as shown by Tables 13 and 14 below, Dell's worldwide market share for x86 servers is [20-30]% (in value, and [20-30]% volume) and [20-30]% at EEA-level (value, and [20-30]% volume), facing strong competition from a large number of established players such as HP (having a larger market share at [20-30]% and [40-50]% in value, at worldwide and EEA-level respectively), IBM, Cisco or Fujitsu, as well as a large number of ODMs.¹³⁷

Table 14: Worldwide shares of x86 servers, 2014

	Value (in USD millions)	Value (in EUR millions)	Share	Units	Share
HP	[...]	[...]	[20-30]%	[...]	[20-30]%
Dell	[...]	[...]	[20-30]%	[...]	[20-30]%
ODM Direct	[...]	[...]	[10-20]%	[...]	[10-20]%
IBM	[...]	[...]	[5-10]%	[...]	[5-10]%
Cisco	[...]	[...]	[5-10]%	[...]	[0-5]%
Lenovo	[...]	[...]	[0-5]%	[...]	[5-10]%
Fujitsu	[...]	[...]	[0-5]%	[...]	[0-5]%
Oracle	[...]	[...]	[0-5]%	[...]	[0-5]%
Inspur	[...]	[...]	[0-5]%	[...]	[0-5]%
NEC	[...]	[...]	[0-5]%	[...]	[0-5]%
Huawei	[...]	[...]	[0-5]%	[...]	[0-5]%
Sugon	[...]	[...]	[0-5]%	[...]	[0-5]%
Cray Inc.	[...]	[...]	[0-5]%	[...]	[0-5]%
SGI	[...]	[...]	[0-5]%	[...]	[0-5]%
Unisys	[...]	[...]	[0-5]%	[...]	[0-5]%
Hitachi	[...]	[...]	[0-5]%	[...]	[0-5]%
Groupe Bull	[...]	[...]	[0-5]%	[...]	[0-5]%
DEPO Computers	[...]	[...]	[0-5]%	[...]	[0-5]%
Aquarius	[...]	[...]	[0-5]%	[...]	[0-5]%
Wortmann	[...]	[...]	[0-5]%	[...]	[0-5]%
Others	[...]	[...]	[0-5]%	[...]	[5-10]%
Total	44 320.77	33 361.5	100%	9 137 980	100%

Source: Notifying Party's estimates based on third parties' reports

¹³⁷ EEA market data supplied by the Parties in the Form CO is an approximation, based on available country data. In the EEA, the market leader is HP on [40-50]% / [30-40]% (value / volume), with Dell second, followed by IBM with [5-10]% / [0-5]%. Worldwide, HP leads with [20-30]% / [20-30]%, then Dell, then Original Design Manufacturers (ODM) with [10-20]% / [10-20]%, then followed by IBM with [5-10] % / [5-10]%.

Table 15: EEA shares of x86 servers, 2014

	Value (in USD millions)	Value (in EUR millions)	Share	Units	Share
HP	[...]	[...]	[40-50]%	[...]	[30-40]%
Dell	[...]	[...]	[20-30]%	[...]	[20-30]%
IBM	[...]	[...]	[5-10]%	[...]	[0-5]%
Fujitsu	[...]	[...]	[5-10]%	[...]	[5-10]%
Cisco	[...]	[...]	[5-10]%	[...]	[0-5]%
ODM Direct	[...]	[...]	[0-5]%	[...]	[10-20]%
Lenovo	[...]	[...]	[0-5]%	[...]	[0-5]%
Oracle	[...]	[...]	[0-5]%	[...]	[0-5]%
Cray Inc.	[...]	[...]	[0-5]%	[...]	[0-5]%
Groupe Bull	[...]	[...]	[0-5]%	[...]	[0-5]%
SGI	[...]	[...]	[0-5]%	[...]	[0-5]%
Wortmann	[...]	[...]	[0-5]%	[...]	[0-5]%
Unisys	[...]	[...]	[0-5]%	[...]	[0-5]%
Hitachi	[...]	[...]	[0-5]%	[...]	[0-5]%
Huawei	[...]	[...]	[0-5]%	[...]	[0-5]%
Transtec	[...]	[...]	[0-5]%	[...]	[0-5]%
Action	[...]	[...]	[0-5]%	[...]	[0-5]%
NEC	[...]	[...]	[0-5]%	[...]	[0-5]%
Stratus Computer	[...]	[...]	[0-5]%	[...]	[0-5]%
E4	[...]	[...]	[0-5]%	[...]	[0-5]%
Others	[...]	[...]	[0-5]%	[...]	[5-10]%
Total	8 595.0	6 470.0	100%	1 742 380	100%

Source: Notifying Party's estimates based on third parties' reports

- (192) Therefore, even if the merged entity had the ability and incentive to engage in the claimed input foreclosure strategy, the Commission considers it unlikely that any such conduct would result in the foreclosure or marginalisation of Dell's server competitors to such an extent that competition would be negatively affected on the server market.¹³⁸ The Commission also considers that the fact that none of the server customers who responded to the market investigation raised any concerns in relation to the possible impact of the transaction further supports this conclusion.
- (193) In light of the evidence available to it and based on the result of the market investigation, the Commission concludes that an input foreclosure strategy is unlikely.

¹³⁸ This conclusion applies also considering other possible sub-segmentations of the server market (addressed above in section 3.2).

4.2.2. *Storage and virtualization software*

4.2.2.1. *The Notifying Party's view*

- (194) As with server virtualization software, described in section 4.2.1, the Notifying Party submits that the merged entity would not have the ability to foreclose its hardware competitors in the storage market. It submits that VMware does not have significant market power in storage virtualization software, and operates within a very competitive virtualization software environment, where it faces competition from traditional virtualization software vendors, open-source solutions, public cloud providers, new technology such as containers, and new market entrants. Customers could switch to these alternative providers.
- (195) The Notifying Party refers to IDC data for 2014, showing that EMC/VMware's share in storage virtualization was [10-20]% by revenue, behind IBM, the market leader, with [30-40]%. According to IDC figures, Microsoft's share was [10-20]%, DataCore Software [5-10]% and "Others" a total of [10-20]%.
- (196) The Notifying Party submits that when EMC acquired VMware in 2004, EMC did not attempt to disadvantage storage competitors by restricting access to VMware software. It argues that any attempt to change the business model by abandoning its open and non-discriminatory architecture strategy would undermine VMware's value and success in the marketplace, risk customer backlash and cause reputational damage.
- (197) Regarding incentive, the Notifying Party submits that the merged entity would not have the incentive to foreclose, as any indication of a move towards foreclosure would encourage customers to seek alternative storage virtualization solutions. The Notifying Party submits that it would not be plausible for the merged entity to adopt a foreclosure strategy designed to "force" prospective customers that wished to buy VMware, to purchase a Dell server and Dell storage, due to the high percentage of such sales that would have to be achieved to be profitable.¹³⁹
- (198) The Notifying Party concludes that there would be no anti-competitive effects. It submits that the extent and range of effective competitors in both hardware and virtualization software means that competition is unlikely to deteriorate following the merger, that barriers to entry and expansion are low and that new technologies pose a significant competitive constraint.

4.2.2.2. *The results of the market investigation and the Commission's assessment*

- (199) As a preliminary remark, the Commission notes that pre-transaction EMC is already active both upstream in the supply of virtualisation software and downstream in the provision of external ESS. As a result, the only merger-specific change resulting from the transaction is the limited increase of the merged entity's market position downstream in relation to external ESS (see section 4.1).

¹³⁹ The Notifying Party bases its submission on a study it commissioned from Compass Lexecon.

a. Ability of the merged entity to engage in a foreclosure strategy

- (200) For the merged entity to be able to engage in foreclosure strategies it must enjoy market power in a market and be in a position to leverage it in another market through conditioning sales in separate markets.¹⁴⁰
- (201) As analysed above in section 4.2.1 and as confirmed by the market investigation, VMware is a leading player in the server virtualization sector. However, this does not seem to be the case in the storage virtualization sector, where VMware has a market share of [10-20]% by revenue worldwide, behind IBM who is the market leader with a share of [30-40]% worldwide. Other strong competitors are present in this sector including Microsoft with a share of [10-20]%, DataCore Software with [5-10]% and “Others” a total of [10-20]%.
- (202) Additionally, the market investigation revealed that, despite VMware's leading position in the server virtualization sector¹⁴¹, this is no longer true for its storage virtualization offering, due to other vendors' stronger presence. A number of respondents to the market investigation described VMware's storage virtualization product "vSAN" as being an immature product in terms of features and functionalities compared to other offerings on the market.¹⁴²
- (203) Furthermore, the majority of respondents to the market investigation said they would consider storage virtualization software offerings from different providers to be substitutable in terms of their characteristics, performance, price and intended end use.¹⁴³
- (204) Regarding the ability of customers to switch to an alternative storage virtualization provider, in terms of technical characteristics, time and cost of switching, the responses to the market investigation were mixed. Some respondents mentioned that switching would be difficult due to the required switching time. They also mentioned that this would depend on each particular customer's scale, performance, management, and complexity of IT implementation. However, other respondents described switching to be doable and generally easy.¹⁴⁴
- (205) In light of the above information and of the results of the market investigation, the Commission considers that, post-transaction the merged entity would not have the ability to foreclose other storage vendors from accessing VMware's storage virtualization software.

b. Incentives of the merged entity to engage in a foreclosure strategy

- (206) Respondents to the market investigation considered that it would not be in the merged entity's interests to engage in a total foreclosure strategy as part of the merged entity. Some suggested that partial foreclosure could be achieved through

¹⁴⁰ Non-Horizontal Merger Guidelines, paragraph 95.

¹⁴¹ See above, analysis under section 4.2.1.

¹⁴² See replies to Q1 – questionnaire to competitors, question 43.

¹⁴³ See replies to Q1 – questionnaire to competitors, question 38.

¹⁴⁴ See replies to Q1 – questionnaire to competitors, question 39.

subtle delays in access to certification, interfaces, customer service and support, timely access to new versions and / or updates.¹⁴⁵

- (207) Moreover, the majority of respondents to the market investigation acknowledged that they had not observed any past attempts by EMC/VMware to limit the interoperability of its storage virtualization software either with (i) certain hardware,¹⁴⁶ or (ii) by limiting access to certification, interfaces, customer services or new versions and updates.¹⁴⁷ Although respondents considered this to be possible, they also considered this unlikely.¹⁴⁸
- (208) Since, as noted, the only merger-specific effect of the transaction in relation to storage virtualisation software and external ESS is the limited increase of the merged entity's position in external ESS, the Commission does not consider it likely that, only by virtue of this limited increase, the merged entity's incentives to engage in input foreclosure would materially differ from those of EMC/VMware pre-merger.

c. Overall impact of a foreclosure strategy on competition

- (209) Even if the merged entity would have the ability and the incentive to engage in a foreclosure strategy in relation to storage systems and storage virtualization software, the Commission considers that such a strategy is unlikely to succeed.
- (210) As shown in Tables 3 – 6, there are alternative providers of external storage systems in the market. In the market for storage virtualization software, VMware's share (by revenue) is less than half that of the market leader IBM, and there are other strong players as set out in (201) above.
- (211) Therefore, even if the merged entity had the ability and incentive to engage in the claimed input foreclosure strategy, the Commission considers it unlikely that any such conduct would result in the foreclosure or marginalisation of the merged entity's ESS competitors or that competition would be negatively affected on the storage market. Moreover, such conclusion is supported by the fact that none of the respondents to the market investigation raised any concerns in relation to the possible impact of the transaction in relation to storage virtualization software.
- (212) In light of the results of the market investigation and of all available evidence, the Commission considers that even if the merged entity were to engage in a foreclosure strategy in relation to storage virtualization software and external ESS, it is unlikely that such practices would lead to significant impediment to effective competition.

¹⁴⁵ See replies to Q1 – questionnaire to competitors, question 42.

¹⁴⁶ See replies to Q1 – questionnaire to competitors, question 24.1 and replies to Q2 – questionnaire to customers, question 30.

¹⁴⁷ See replies to Q1 – questionnaire to competitors, question 24.2.

¹⁴⁸ See replies to Q1 – questionnaire to competitors, questions 36 and 48 and replies to Q2 – questionnaire to customers, question 31.

4.2.3. *Converged infrastructure systems*

- (213) As described in section 3.4, CI systems are pre-assembled solutions bundling a number of hardware and software components (namely servers, storage, networking and supporting software, including virtualization software). HCI systems are physically integrated systems combining a commodity server and supporting software (including virtualization software) allowing the server to present itself as a single system that has both computing and storage capabilities.
- (214) As noted above, despite the reported increase in sales of CI and HCI systems over the last few years, the market investigation revealed that the traditional mix and match of different hardware and software components from best-of-breed vendors remains the preferred approach for end-customers.¹⁴⁹ On the basis of the fact that the traditional mix and match approach currently reflects consumers' behaviour, for the purposes of this decision, the Commission will view CI and HCI systems in relation to each of their individual components, namely servers, storage, networking and/or supporting software, including virtualization software.
- (215) On this basis, with regards to the potential components of CI and HCI systems, the Commission notes that, pre-transaction, EMC is already active both upstream in the supply of virtualisation software (through VMware) and downstream in the provision of external ESS. Dell is active in the provision of servers. Neither Dell nor EMC are active in the market for networking components for CI systems (also known as "software-defined networking products").
- (216) The Commission will therefore assess whether the integration of Dell's server and external ESS portfolio with EMC's external ESS products and VMware's virtualization software could affect the merged entity's (i) ability and (ii) incentive to grant access to its virtualization software to competing providers of CI and HCI systems and, (iii) if this were to have an impact in the provision of CI and HCI systems.

4.2.3.1. *Market shares*

- (217) The following tables set out the shares of the Parties and their competitors at worldwide and EMEA level (being the data available to the Notifying Party and a proxy for EEA-level shares) in all components of Integrated Infrastructure and Platform sales, depicting the relative weight of sales of the Parties in CI and HCI systems. For the market share tables of the Parties and their competitors in (i) servers and in (ii) external ESS, see above at sections 4.2.1 and 4.1 respectively.

¹⁴⁹ See above, paragraph 83.

**Table 16: Worldwide Sales of All Components in Integrated Infrastructure and Platforms
2012 to 1H 2015 – Revenue (in USD million)**

	2012		2013		2014		1H2015	
	Revenue	Share	Revenue	Share	Revenue	Share	Revenue	Share
Dell	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%
EMC	[...]	[0-5]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%
VCE	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%
Combined	[...]	[10-20]%	[...]	[20-30]%	[...]	[30-40]%	[...]	[30-40]%
Oracle	[...]	[20-30]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%
Cisco/NetApp	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%
HP	[...]	[5-10]%	[...]	[5-10]%	[...]	[10-20]%	[...]	[10-20]%
Lenovo	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%
Hitachi	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%
IBM	[...]	[10-20]%	[...]	[10-20]%	[...]	[5-10]%	[...]	[0-5]%
Others	[...]	[20-30]%	[...]	[20-30]%	[...]	[10-20]%	[...]	[10-20]%
Total size of market (in million USD)	4,901.5	100.0%	7,283.1	100.0%	9,411.8	100.0%	4,571.3	100.0%

Source: Notifying Party's estimates based on third parties' reports

In a worldwide market comprising of all components of Integrated Infrastructure and Platforms, Dell has a market share of [0-5]% by revenue, EMC has a market share of [10-20]% and VCE¹⁵⁰ has a market share of [10-20]% while being the second player after Oracle with [10-20]%. Other players occupy a [10-20]% market share by revenue. Competitors to Dell include Oracle, Cisco/NetApp, HP, IBM, Hitachi and Lenovo.

¹⁵⁰ See above, paragraph 75.

Table 17: EMEA – Sales of All Components in Integrated Infrastructure and Platforms 2012 to 1H 2015 – Revenue (in USD million)

	2012		2013		2014		1H2015	
	Revenue	Share	Revenue	Share	Revenue	Share	Revenue	Share
Dell	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%
EMC	[...]	[0-5]%	[...]	[5-10]%	[...]	[5-10]%	[...]	[5-10]%
VCE	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%
Combined	[...]	[10-20]%	[...]	[20-30]%	[...]	[20-30]%	[...]	[20-30]%
Oracle	[...]	[30-40]%	[...]	[20-30]%	[...]	[10-20]%	[...]	[20-30]%
HP	[...]	[5-10]%	[...]	[5-10]%	[...]	[10-20]%	[...]	[10-20]%
Cisco/NetApp	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[5-10]%
Lenovo	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%	[...]	[5-10]%
Hitachi	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%	[...]	[0-5]%
IBM	[...]	[5-10]%	[...]	[5-10]%	[...]	[5-10]%	[...]	[0-5]%
Others	[...]	[20-30]%	[...]	[10-20]%	[...]	[10-20]%	[...]	[10-20]%
Total size of market (in million USD)	1,077.6	100.0%	1,762.5	100.0%	2,547.0	100.0%	1,256.6	100.0%

Source: Notifying Party's estimates based on third parties' reports¹⁵¹

- (218) At EMEA-level, for all components of Integrated Infrastructure and Platforms, Dell has a share of [0-5]% by revenue, EMC has a share of [5-10]% and VCE has a share of [10-20]%, with Oracle having a share of [10-20]%. "Other" players occupy a [10-20]% share by revenue. Competitors to Dell include Cisco/NetApp, HP, IBM, Hitachi and Lenovo.
- (219) The Notifying Party submits that, for the moment, there are no third-party reports tracking the sales of HCI systems as this space is still nascent. Furthermore, the Notifying Party suggests that Nutanix, SimpliVity and Scale Computing are in all likelihood the largest providers of the software for HCI systems, at least for the time being. As HCI system offerings are still in their early stages, these leading players may well change in the near future.

4.2.3.2. The Notifying Party's view

- (220) The Notifying Party submits that the transaction raises no concerns of post-merger partial or input foreclosure involving VMware in connection with CI systems and HCI systems. Any attempts to foreclose – whether partially or totally, whether limited to CI and HCI systems or applied to servers generally – would be unprofitable to the combined company under any realistic set of assumptions.

¹⁵¹ According to the Notifying Party, the figures provided in Tables 15 and 16 take into account the components frequently found in converged systems and accounted for in the IDC numbers (i.e. server, storage, network, system infrastructure software, application development and deployment and finally applications).

- (221) In this regard, the Notifying Party points out that any foreclosure attempts would violate VMware's long-lasting commitment to hardware neutrality and irreparably destroy much of the value of VMware's business which stems from VMware's long history of close cooperation with all its hardware and software partners, regardless of ownership. Furthermore, the Notifying Party refers to the ready availability of virtualization software alternatives for both customers and OEM partners (most notably Microsoft Hyper-V and KVM-based hypervisors such as Red Hat Enterprise virtualization and Nutanix's Acropolis), making any attempted foreclosure irrational and self-destructive.

4.2.3.3. *The results of the market investigation and the Commission's assessment*

a. Ability of the merged entity to engage in a foreclosure strategy

- (222) For the merged entity to be able to engage in foreclosure strategies it must enjoy market power in a market and be in a position to leverage it in another market through conditioning sales in separate markets.
- (223) As analysed in section 4.2.1, Dell's presence in the provision of servers is relatively small with [20-30]% market share worldwide and [20-30]% EEA-wide, while HP is the leader in this market with a market share of [20-30]% worldwide and [30-40]% EEA-wide. Other strong competitors in this market include, among others, Lenovo, Cisco, Fujitsu, IBM and ODMs.
- (224) Furthermore, as analysed in section 4.1, the transaction would only lead to a limited increase in the provision of external ESS. Additionally, other strong competitors are present in this space, including NetApp, HP, IBM and Hitachi. On this basis, it should be concluded that, despite the limited increase in the merged entity's shares post-transaction, the merged-entity would have limited market power in external ESS.
- (225) In addition, the market shares' increment resulting from the transaction in relation to CI and HCI systems is limited. Therefore, the merged entity's position in the supply of these products will not materially change following the transaction.
- (226) Based on the market investigation and as analysed above in sections 4.2.1 and 4.2.2, the Commission considers that the merged entity would not have market power neither in the market for server virtualization software nor in the market for storage virtualization software.
- (227) More specifically, in relation to CI and HCI systems, the majority of the respondents to the market investigation who expressed an opinion agreed that there are alternative virtualization software products other than VMware's.¹⁵²
- (228) A small number of respondents argued that, due to VMware's strong market share in the server virtualization market, it would be difficult or impossible to make a commercially viable CI or HCI product without VMware's software.¹⁵³ However, the market investigation showed that VMware's presence in CI and HCI systems

¹⁵² See replies to Q1 – questionnaire to competitors, questions 51 and 52.

¹⁵³ See replies to Q1 – questionnaire to competitors, questions 51 and 52.

stems from its current market position in server virtualization and not from any technical features that make CI and HCI products reliant on VMware.¹⁵⁴

- (229) In this regard, the market investigation showed that there are currently CI and HCI system offerings in the market utilizing virtualization software from vendors other than VMware, such as Microsoft's Hyper-V, Xen, Nutanix's virtualization software, Oracle's virtualization software and IBM's virtualization software named Power VM and Power KVM.¹⁵⁵
- (230) As regards switching virtualization software providers of CI and HCI systems, the majority of the respondents to the market investigation agreed that switching, although involving significant resources,¹⁵⁶ is technically possible and relatively straightforward.¹⁵⁷ Some of the respondents also pointed out that the same switching costs from one virtualization technology to another would apply to CI and HCI systems as they apply to mix and match of best-of-breed solutions.¹⁵⁸
- (231) Additionally, the Commission concluded in sections 4.2.1 and 4.2.2 that the merged entity would not have the ability to engage in a foreclosure strategy in relation to Dell's servers, Dell's external ESS and VMware's virtualization software.
- (232) Even if it were to consider a possible bundling strategy whereby the merged entity would link the sales of VMware's virtualization software together with its own servers or external ESS products when offering CI and HCI systems, the effects of such a strategy would not be substantial due to the amount of relevant alternatives to VMware's virtualization software for CI and HCI systems. In addition, the market investigation revealed that the majority of customers do not consider VMware to have any specific characteristics that make it the only real option for converged products.¹⁵⁹
- (233) In light of the considerations in paragraphs 223 to 231, based on the results of the market investigation and all the information available to it, the Commission considers that, post-transaction, the merged entity would not have the ability to foreclose other hardware vendors from accessing VMware's virtualization software used in CI and HCI systems.

b. Incentives of the merged entity to engage in a foreclosure strategy

- (234) Most respondents to the market investigation expressed the view that it is unlikely that the merged entity would limit the availability of VMware's virtualization software to other vendors who are active in the provision of components of CI and HCI systems.

¹⁵⁴ See replies to Q1 – questionnaire to competitors, question 51 and replies to Q2 – questionnaire to customers, question 25.

¹⁵⁵ See replies to Q1 – questionnaire to competitors, question 50.

¹⁵⁶ See replies to Q1 – questionnaire to competitors, question 54.

¹⁵⁷ See replies to Q1 – questionnaire to competitors, question 54.

¹⁵⁸ See replies to Q1 – questionnaire to competitors, question 54.

¹⁵⁹ See replies to Q2 – questionnaire to customers, question 25.

- (235) According to those views, a strategy whereby the merged entity limits the access of VMware's virtualization software in terms of certification, interfaces, customer services, customer support, new software versions, software updates and time to market, would inevitably (i) limit the size of the merged entity's business, (ii) allow competing offerings other than VMware's to take market share and (iii) cause irreparable reputational damage to the merged entity.¹⁶⁰
- (236) In addition, the incentive to pursue a foreclosure strategy depends on the extent to which such a strategy would be profitable.
- (237) In relation to servers and virtualization software as components of CI and HCI systems, the cost to the merged entity in terms of lost sales of VMware's software would have to be lower than the benefit coming from the increased sales of Dell's servers. As analysed above in paragraph 182, based on the available evidence, it is unlikely that the value of lost sales in VMware's server virtualization software would be more than compensated by the value of incremental sales of Dell's servers. The merged entity could, therefore, incur a loss if it were to engage in a foreclosure strategy.
- (238) In relation to external ESS and virtualization software as components of CI systems, the only merger-specific effect of the transaction is the limited increase of the merged entity's position in external ESS. As indicated in paragraph 208, the Commission does not consider it likely that, only by virtue of this limited increase, the merged entity's incentives to engage in input foreclosure would materially differ from those of EMC/VMware pre-merger.
- (239) Even if it were to look at CI and HCI systems space as a separate product market, EMC (including VCE) is currently a much stronger player in this space than Dell¹⁶¹. Thus, its incentives are unlikely to be affected, post-merger.
- (240) On the basis of the information available as well as in light of the preceding analysis in sections 4.2.1 and 4.2.2, the Commission considers that, post-transaction, the merged entity would not have the incentive to foreclose other hardware (server and storage) vendors from accessing VMware's virtualization software used in CI and HCI systems.

c. Overall impacts of a foreclosure strategy on competition

- (241) Even if the merged entity would have the ability and the incentive to engage in a foreclosure strategy in relation to other hardware providers of components of CI and HCI systems, as regards its virtualization software, the Commission considers that such a strategy is unlikely to succeed or to give rise to a significant impediment to effective competition.
- (242) As analysed in sections 4.2.1 and 4.2.2, there are a number of strong competitors in both server and storage virtualization software. Should the merged entity decide to

¹⁶⁰ See replies to Q1 – questionnaire to competitors, question 53.

¹⁶¹ As can be seen in Tables 16 and 17 above, the worldwide share of EMC is [10-20]% and of VCE is [10-20]% over a share of [0-5]% of Dell. In EMEA level, EMC has a share of [5-10]% and VCE a share of [10-20]% over a share of [0-5]% of Dell.

engage in a foreclosure strategy in relation to VMware's virtualization software intended for CI and HCI systems, its hardware competitors are in a position to compete and provide CI and HCI systems in partnership with virtualization software providers other than VMware.

- (243) If *arguendo* CI and HCI systems were to be seen as a separate product market, Dell's share by revenue in all components of CI systems is [0-5]% worldwide and [0-5]% in the EMEA market, with Oracle being the leading player ([10-20]% market share worldwide and [10-20]% in EMEA). Dell's shares in this sector are very low, especially when seen in relation to the shares of its competitors in this sector, namely Oracle, Cisco/NetApp, HP, IBM, and Hitachi.¹⁶²
- (244) Even if it were to consider a bundling strategy whereby the merged entity would link the sales of VMware's virtualization software together with its own servers or external ESS products when offering CI and HCI systems, as analysed in sections 4.2.1 and 4.2.2 above, a number of strong competitors to the merged entity in either servers, external ESS or virtualization software would be in a position to ensure the provision of competitive CI and HCI system offerings.
- (245) Therefore, in light of the above, the Commission considers that even if the merged entity had the ability and incentive to engage in a foreclosure strategy in relation to virtualization software for CI and HCI systems, it is unlikely that any such conduct would result in the foreclosure or marginalisation of Dell's server and storage competitors, active in the provision of CI and HCI systems. .

5. CONCLUSION

- (246) For the above reasons, the European Commission has decided not to oppose the notified operation and to declare it compatible with the internal market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of the Merger Regulation and Article 57 of the EEA Agreement.

For the Commission

(Signed)

Margrethe VESTAGER

Member of the Commission

¹⁶² See market share tables 15 and 16.



EUROPEAN COMMISSION
DG Competition

***Case M.7917 - BOEHRINGER INGELHEIM / SANOFI
ANIMAL HEALTH BUSINESS***

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) in conjunction with Art 6(2)
Date: 09/11/2016

***In electronic form on the EUR-Lex website under document
number 32016M7917***



In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

Brussels, 9.11.2016
C(2016) 7295 final

PUBLIC VERSION

To the notifying party:

Subject: Case No COMP M.7917 – BOEHRINGER INGELHEIM/ SANOFI ANIMAL HEALTH BUSINESS
Commission decision pursuant to Article 6(1)(b) in conjunction with Article 6(2) of Council Regulation No 139/2004¹ and Article 57 of the Agreement on the European Economic Area²

Dear Sir/Madam,

- (1) On 19 September 2016, the European Commission received notification of a proposed concentration pursuant to Article 4 of the Merger Regulation by which Boehringer Ingelheim group (BI, Germany) acquires within the meaning of Article 3(1)(b) of the Merger Regulation control over Sanofi's animal health business (Merial, France), by way of purchase of shares and assets (the Transaction).³ BI and Merial are designated hereinafter as the 'Parties' and BI the 'Notifying Party'. The same concentration was initially notified to the Commission on 8 June 2016, however the notification was subsequently withdrawn on 22 July 2016.

I. THE PARTIES

- (2) BI is a pharmaceutical company active in the development, production, distribution, and marketing of pharmaceuticals, in four business segments: prescription products, consumer healthcare products, biopharmaceuticals and animal health products.

¹ OJ L 24, 29.1.2004, p. 1 (the 'Merger Regulation'). With effect from 1 December 2009, the Treaty on the Functioning of the European Union ('TFEU') has introduced certain changes, such as the replacement of 'Community' by 'Union' and 'common market' by 'internal market'. The terminology of the TFEU will be used throughout this decision.

² OJ L 1, 3.1.1994, p. 3 (the 'EEA Agreement').

³ Publication in the Official Journal of the European Union No C349, 24.09.2016, p. 6.

- (3) Merial is Sanofi's subsidiary specialised in animal health. Merial produces a wide range of pharmaceutical products and vaccines for companion and production animals.

II. THE OPERATION AND CONCENTRATION

- (4) Pursuant to the agreement for the sale and purchase of Sanofi's animal health business (SAPA), BI intends to acquire control over Merial, by way of acquisition of shares (including 100% of Merial SAS shares) and assets.
- (5) The operation is part of an asset swap whereby Merial would be transferred to BI in exchange for BI's consumer healthcare business (BI CHC). The proposed acquisition by Sanofi of BI CHC constitutes a separate concentration for the purposes of the EC Merger Regulation.⁴ An additional cash payment from BI to Sanofi will take place in order to bridge the value gap between the two swapped businesses.
- (6) As a result of the Transaction, BI will have sole control over and ownership of Merial.
- (7) The Transaction therefore constitutes a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. EU DIMENSION

- (8) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million⁵. Each of them has an EU-wide turnover in excess of EUR 250 million, but each does not achieve more than two-thirds of its aggregate EU-wide turnover within one and the same Member State.
- (9) The notified operation therefore has an EU dimension pursuant to Article 1(2) of the Merger Regulation.

IV. ASSESSMENT

- (10) In line with previous Commission's decisions,⁶ animal health products can generally be divided into three main areas:
- (i) **Biologicals:** products which trigger an immune response against viral and bacterial diseases as well as occasionally parasitic or fungal infections in animals. Biologicals include in particular animal vaccines.
 - (ii) **Pharmaceuticals:** wide group of products that contain a variety of active substances to prevent or treat a large range of animal diseases and disorders.
 - (iii) **Feed supplements (medicinal and nutritional):** pharmaceutical or nutritional substances which are not natural feedstuffs and are added to made-

⁴ See case M.7919 – *Sanofi / Boehringer Ingelheim Consumer Healthcare Business*.

⁵ Turnover calculated in accordance with Article 5(1) of the Merger Regulation and the Commission Consolidated Jurisdictional Notice (OJ C95, 16.4.2008, p. 1).

⁶ For example M.1681 - *Akzo Nobel/Hoechst Roussel Vet*, 22.11.1999, para 11; M.2922. *Pfizer/Pharmacia*, 27/02/2003, para 114; M.4691 – *Schering-Plough / Organon biosciences*, 11.10.2007, para 22; M.5476 – *Pfizer/Wyeth*, 17.07.2009, para 111.

up and stored feeds for various purposes but chiefly to control infectious disease or to promote growth.

- (11) The Parties' activities overlap in all three areas: animal health biologicals (vaccines) (IV.2), pharmaceuticals (IV.3) and feed supplements (IV.3.4).⁷

IV.1. Introduction - General features of animal health industry

IV.1.1. Animal health sector globally and in the EEA

- (12) BI and Merial are among the largest companies active in animal health globally. Post-Transaction, the merged entity will rank number 2 in terms of net sales with a share of the global animal health business of approximately [10-20]%, after Zoetis.

[Graph on Global Animal Health Landscape in 2014, from BI internal document]

- (13) The global animal health sector is concentrated with 70% of the business controlled by six global pharmaceutical companies, including the Parties as well as Zoetis (until recently the animal health division of Pfizer), Merck, Elanco (animal health division of Eli Lilly) and Bayer (focusing on animal health pharmaceuticals).
- (14) In the EEA, the largest global players, including the Parties, Zoetis, Bayer, Elanco and Merck (known as MSD in Europe), are all active, together with smaller international players, such as Ceva Santé Animale (Ceva), Hipra, Vetoquinol and Virbac.
- (15) Animal health companies expand their portfolio through organic growth, with the development of new products or improvements of existing products (also known as life cycle management), or inorganic growth. Recently, Elanco bought Novartis' animal health division,⁸ after having acquired certain animal health assets from Pfizer⁹ and Janssen Animal health¹⁰ in 2011. In 2013, Ceva acquired Sogeval and more recently, in 2015, Zoetis acquired the animal health division of Abbott.
- (16) The main barriers to entry in animal health markets are development costs and intellectual property rights associated with new products. In the area of swine and ruminant vaccines, BI, MSD and Zoetis are perceived as the strongest innovators.¹¹ BI's R&D budget in vaccines has been growing over the last three years from EUR [...] million in 2013 to EUR [...] million in 2015, while Merial's vaccines R&D budget ranged between EUR [...] million between 2013 and 2015.
- (17) As to the expansion of existing products supplied in a limited number of EEA countries in new geographies, animal health suppliers need to obtain a marketing authorization (as described below), set-up a distribution and sales network and engage

⁷ The Transaction gave rise to vertical relationships derived from Merial's contract manufacturing activities in animal vaccines and pharmaceuticals. However, the Transaction does not lead to any vertically affected markets under all plausible market definitions.

⁸ M.7277 – *Eli Lilly/Novartis Animal Health*.

⁹ M.5843 – *Eli Lilly/Certain Animal Health Assets of Pfizer*.

¹⁰ M.5843 – *Eli Lilly/Janssen Pharmaceutical Animal Health Business Assets*.

¹¹ Responses to Questionnaire Q1 to Competitors of 7 June 2016, questions 50 and 68.

marketing costs. Once the distribution and sales networks are in place, the main investment in time and costs to commercialise additional products in this country generally consists in obtaining the regulatory approval.¹²

IV.1.2. Regulation of veterinary medicines in the EEA

- (18) Like the human health sector, the animal health industry is regulated by both Member States and at the European Union level. More specifically, the manufacture and commercialisation of veterinary medicinal products (VMP) is subject to marketing authorizations.¹³
- (19) However, contrary to the human health sector, VMPs are generally not reimbursed by public authorities except for in specific situations, such as (i) in the context of eradication schemes: by way of example, the German region of Hessen currently subsidises bovine viral diarrhoea (BVD) vaccines, or (ii) in the context of specific subsidies to farmers for some pharmaceuticals which vary by Member States. In some countries, for instance in Scandinavia and the United Kingdom, there is a possibility of private insurance in particular for pets whereby insured pet owners may claim reimbursement from their insurance companies subject to individual policies.
- (20) As a consequence, prices of animal health products are generally not regulated and are freely set by manufacturers. The price of animal health products is thus function of competition in the market.

IV.1.3. Generics and brand importance

- (21) In the animal health sector, competition essentially takes place between brands of various producers, to which customers attribute specific degree of efficacy, safety and price level based on the experience with the product and the manufacturer.¹⁴
- (22) As to the penetration of generic medicines, there are no generics of animal vaccines, as vaccines are biological products which do not exhibit bioequivalence. On the other hand, while animal pharmaceuticals do know generics, generic penetration is still rather limited as generally there is no regulatory incitation to introduce generics as is observed for human pharma.¹⁵ In addition, generic companies must demonstrate that (i) the product is a generic version of the reference VMP with respect to its composition (that it has qualitative and quantitative bioequivalence by demonstrating the equivalence of the rate and extent of drug absorption) and pharmaceutical formulation and that (ii) the generic drug is bioequivalent to the originator product (generic companies are only exempted to provide safety and efficacy documentation).

¹² Responses to Questionnaire Q1 to Competitors of 7 June 2016, questions 25-26 and 96-97.

¹³ Marketing authorizations can be obtained through three different procedures: (i) centralized procedure whereby the European Commission grants Community wide marketing authorization following the positive opinion of the European Medicines Agency (EMA) pursuant to Regulation (EC) No 726/2004 of 31 March 2004, (ii) decentralized procedure whereby manufacturers submit a single identical product dossier and applications simultaneously to multiple EEA Member States regulatory agencies and each agency issue its own approval and (iii) national procedure whereby manufacturers apply separately for marketing approval by individual Member State regulatory agencies, these approvals can be broadened to other Member States by subsequent mutual recognition requests.

¹⁴ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 14.

¹⁵ Agreed minutes of a conference call held with a competitor dated 17 May 2016.

The market investigation in this case confirmed the reluctance from some customers to use generics instead of originator products which are generally perceived as more efficacious. In this context, some customers mentioned that generics have different formulation and in some cases are only around 80% equivalent to originators and therefore not a perfect copy.¹⁶

- (23) The low penetration of generics is also evidenced by high margins in animal vaccines and pharmaceuticals often reaching 70-80%.

IV.1.4. Customer base and purchasing patterns

- (24) The animal health products customer base is split between two main categories, namely veterinarians (independent or attached to a farm or group of farms) and directly the farmers, in particular for production animals.
- (25) The negotiation on prices as well as the choice of brands are generally made by veterinarians,¹⁷ which are the target audience of manufacturers' marketing.¹⁸ Farmers can also influence the decision, in particular the large farms and cooperatives.¹⁹ Price of specific products depends in particular on volume and the range of products purchased.²⁰
- (26) The market investigation indicated that customers typically multi-source in particular for vaccines where they generally have 2 to 4 vaccines suppliers for each specific disease.²¹ Veterinarians explain that multi-sourcing is necessary to negotiate prices and for security of supply. The choice of the vaccine will ultimately depend on its suitability for each farm.²²
- (27) The features of animal health industry described above will be reflected in the competitive assessment of the Transaction in the specific markets.

IV.2. Animal health vaccines

- (28) Vaccines protect animals against future diseases or illnesses caused by exposure to bacterial, viral, parasitical or fungal agents (pathogens). Vaccines achieve this protection by introducing one or several antigens (harmless substances that stimulate an immune system response) into the animal's body, in order to stimulate the production of antibodies (natural substances used by the animal's immune system to protect against the relevant pathogen) or another protective immune response.

¹⁶ Responses to Questionnaires Q4 to Companion Animals customers and to Q5 to Horses customers of 8 June 2016, question 8.

¹⁷ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 13.

¹⁸ Responses to Questionnaire Q1 to competitors of 8 June 2016, questions 11 and 77.

¹⁹ Agreed minutes of a conference call held with a customer dated 13 May 2016 and Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 13.

²⁰ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 9 and the minutes of a conference call held with a customer dated 11 May 2016.

²¹ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 5.

²² Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 5.

- (29) The Parties are among the main players active in animal health vaccines in the EEA, together with Merck (MSD) and Zoetis.

Table 1. Parties' and competitors' share in animal vaccines in the EEA

	2013	2014	2015
BI	[10-20]%	[10-20]%	[10-20]%
Merial	[20-30]%	[20-30]%	[10-20]%
Combined	[30-40]%	[30-40]%	[30-40]%
MSD	[40-50]%	[40-50]%	[40-50]%
Zoetis	[10-20]%	[10-20]%	[10-20]%
Virbac	[0-5]%	[0-5]%	[0-5]%
Ceva	[0-5]%	[0-5]%	[0-5]%
Elanco	[0-5]%	[0-5]%	[0-5]%
Total market size	EUR [1.0-2.0] billion	EUR [1.0-2.0] billion	EUR [1.0-2.0] billion

Source: Form CO, CEESA data.²³

IV.2.1. Market definition – General framework

IV.2.1.1. Product market - Introduction

- (30) In previous decisions dealing with animal health products²⁴, the Commission has defined animal health vaccine product markets according to:

- (i) animal species, since most vaccines target a singled animal species, such as (i) ruminants; (ii) swine; (iii) poultry; (iv) equine; or (v) companion animals, and
- (ii) indication of use, since vaccines target specific diseases/pathogens.

- (31) The Commission also considered on a case-by-case basis whether a distinction should be made between:

- (i) Single or multiple pathogens: monovalent vaccines – which contain one or multiple strains of only a single antigen – protect against one specific disease whereas multivalent vaccines – which contain two or more different antigens – protect against several diseases,
- (ii) Live or inactivated vaccines: live vaccines are made from natural non-virulent cultivated organisms or from organisms that have been modified to be non-virulent and inactivated vaccines are made from killed virulent organisms or from inactivated parts of these organisms, and

²³ The Notifying Party used data from Centre Européen d'Etude pour la Santé Animale (CEESA), a non-profit international association which collects sales data on the animal health market in 21 EEA countries. It must be noted that manufacturers reports sales at different levels, and Merial is the only manufacturer which report at level 3 which means that Merial sales in CEESA are not netted-off end of year customer specific rebates (level 4) or cash discount (level 5). In order to provide the most accurate market shares possible, Merial's sales data into CEESA has been replaced by Merial's actual net sales equivalent to level 5. Additionally, the CEESA data do not cover sales in all EEA countries and captures only the suppliers that report to the organisation. More local suppliers or suppliers of generics do not report into CEESA, as for example Hipra. The Notifying Party therefore provided its best estimate as to Hipra's market position in the different EEA countries where relevant.

²⁴ M.5476 – Pfizer/Wyeth, 17.07.2009 and M.4691 – Schering-Plough / Organon biosciences, 11.10.2007.

(iii) Marker or non-marker vaccines: marker vaccines allow distinguishing between animals that are immunised as a result of vaccination or as a result of exposure to a naturally occurring pathogenic strain of the virus.²⁵

(32) The Commission further identified additional differentiating factors between vaccines, such as (i) animal target group within species (e.g. for swine, vaccines may be targeted at sows and/or piglets), (ii) the route of administration such as intramuscular or subcutaneous and (iii) the frequency of administration or number of doses.²⁶

IV.2.1.2. Geographic market

(33) In previous decisions,²⁷ the Commission found that despite the existence of some pan-European trends and the fact that the main players are active throughout the EEA, the relevant geographic market for animal health products was national in scope. This is mainly due to national legislation determining the selling conditions of the products, different prevalence of certain diseases in certain areas, and different competition landscape in different EEA countries in terms of market penetration, shares, price, distribution systems and local veterinarian preferences.

(34) The Notifying Party submits that the relevant geographic market definition in animal health products is indeed national. The Notifying Party points out the fact that most products on these markets remain subject to national and mutual recognition registration systems, causing products to be sold according to indications and uses prescribed by national registration and approval requirements.

(35) In this case, the market investigation broadly confirmed that markets in the animal health sector are still national, as marketing authorizations are still subject to national regulations, the competitive landscapes varies from one Member State to another while pricing strategies of pharmaceutical companies also seem to be national.

(36) For the purpose of assessing the impact of the Transaction, the Commission therefore concludes that the relevant geographic markets in relation to animal health vaccines are national in scope.

IV.2.2. Swine vaccines

IV.2.2.1. Introduction

(37) At EEA level, the Parties are among the largest players in swine vaccines, together controlling around half of the market. The market has experienced strong growth over the last few years due to, among other things, the growing prevalence of some swine diseases and continuous innovation in the sector creating new demand.

²⁵ The differentiation between marker and non-marker vaccines is not relevant with respect to the overlapping vaccines in this case.

²⁶ M.1681 - Akzo Nobel/Hoechst Roussel Vet, 22.11.1999, para 46.

²⁷ M.7277 - Eli Lilly/Novartis Animal Health, paras. 56-58, M.6205 - Eli Lilly/Janssen, para. 15 and M.4691 - Schering-Plough/Organon Biosciences, paras. 42-45.

Table 2. Parties' and competitors' share in swine vaccines in the EEA

	2013	2014	2015
BI	[30-40]%	[30-40]%	[30-40]%
Merial	[10-20]%	[10-20]%	[10-20]%
Combined	[50-60]%	[50-60]%	[40-50]%
MSD	[30-40]%	[30-40]%	[40-50]%
Zoetis	[10-20]%	[10-20]%	[5-10]%
Elanco	[0-5]%	[5-10]%	[0-5]%
Total market size	EUR [355-360] million	EUR [370-375] million	EUR [380-385] million

Source: CEESA data.

- (38) The transaction leads to affected markets for PCV2 (IV.2.2.2), M.hyo (IV.2.2.3) and PRRS (IV.2.2.4) where both Parties are active and for PPV [CONFIDENTIAL PARTIES ACTIVITIES] (IV.2.2.5)

IV.2.2.2. Porcine Circovirus type 2 (PCV2)

- (39) Diseases associated with PCV2 are referred to as porcine circovirus associated diseases. The most important disease associated with PCV2 infection is Porcine Multisystemic Wasting Syndrome, a slow and progressive disease with a high fatality rate affecting pigs from 6 weeks of age. Weaned pigs lose weight and gradually become emaciated.
- (40) Nearly all herds globally and in the EEA are infected with PCV2, though not all are clinically affected. Substantial economic losses are attributed to PCV2 diseases, reflecting significant increases in mortality, cull rates, and medication costs. Currently, clinical signs attributed to PCV2 infection are seldom observed, as most farms that have experienced porcine circovirus associated diseases have established routine PCV2 piglet vaccination (there is a vaccination rate of more than 80% in major markets).

IV.2.2.2.a. Parties' products

- (41) The Parties offer only monovalent PCV2 vaccines.
- (42) Merial markets a monovalent vaccine under the brand name *Circovac*, which was the first vaccine against circovirus to be approved in the EEA in 2007. Circovac is an inactivated vaccine. Circovac was initially authorized to be used for gilts and sows but obtained a marketing authorization for a use in piglets in 2010. The average profit margin at EEA level of Circovac is [...]%.
- (43) BI markets a monovalent vaccine under the brand *Ingelvac CircoFLEX* (CircoFLEX). CircoFLEX is a subunit²⁸ vaccine. CircoFLEX was initially authorized to be used in piglets from 2 weeks of age but subsequently gained an authorization for sows and for all piglets. Since 2015, CircoFLEX can also be used during pregnancy and during lactation in sows. The average profit margin at EEA level of Circoflex is [...]%.
- (44) A combination of BI's PCV2 vaccine CircoFLEX and BI's M.Hyo vaccine MycoFLEX, for a mixing on site, is also authorized under the name *FLEXCombo*.

IV.2.2.2.b. Product market definition

Notifying Party's view

- (45) The Notifying Party submits that the narrowest relevant product market is the market for monovalent PCV2 vaccines for swine.
- (46) The Notifying Party however submits that multivalent swine vaccines which include PCV2, in particular the combo vaccines including PCV2 and MHyo, exert a competitive constraint on monovalent products since the vast majority of swine farmers would vaccinate against both diseases in the EEA.
- (47) In addition, the Notifying Party submits that it is not necessary to distinguish between inactivated vaccines and subunit vaccines. Subunit vaccines include only the antigens that best stimulate the immune system; in a subunit vaccine only the most immunogenic protein of PCV2 (the capsid protein) is produced and used. A subunit-based vaccine is per definition a killed vaccine, but as a result of the production method it does not require additional inactivation. The Notifying Party submits that from a customer perspective, these concepts do not yield any meaningful differentiation.

The Commission's assessment

- (48) As to the segmentation between monovalent and multivalent vaccines, the market investigation provided indications that, if monovalent PCV2 vaccines (used in combination with monovalent vaccines against other disease(s)) may, in some circumstances, be substitutable to multivalent vaccines including PCV2, the reverse is not true.
- (49) The market investigation indicated that multivalent vaccines including PCV2 (and in particular PCV2/M.Hyo) can in some cases be preferred to administration of two

²⁸ The term “subunit” describes the production of a single antigen using a recombinant expression technology.

monovalent vaccines for convenience reasons, since they require less injections and would therefore be less stressful for animals. However, in this context the market investigation also indicated that, while multivalent vaccines are attractive when cheaper than the corresponding selections of individual monovalent vaccines, they are generally perceived as less efficacious.²⁹ Therefore, there is a trade-off to be made between convenience and price on the one hand and the efficacy on the other hand. Given that, according other market investigation, the efficacy generally seems to be the main driver of choice, multivalent vaccines seem, at this stage, to have less traction in the market. This also seems to be confirmed by the PCV2 market structure where only one company, MSD, offers a multivalent vaccine, *Porcilis PCVM* [CONFIDENTIAL R&D INFORMATION].³⁰ Another company, Zoetis, launched a multivalent vaccine *Fostera*® PCV MH in the US at the end of 2013 and recently obtained an authorization to market it in the EEA under the name *Suvaxyn Circo+MH RTU*.

- (50) As to the possible distinction between inactivated and subunit vaccines, the market investigation confirmed that this is not a meaningful factor for customers of swine vaccines against circovirus. While subunit might be perceived as being more efficacious, it does not appear to be a key criterion. There would be "*no particular circumstance to select this type of vaccine [subunit] vs others*"³¹ and "*no preference or necessity of a specific type of vaccine*".³² Therefore, the market in relation to PCV2 should not be further segmented between subunit and inactivated vaccines.
- (51) In view of the above, for the purpose of the Transaction, the relevant product market in relation to PCV2 vaccines comprises all monovalent PCV2 vaccines. Any (out of market) competitive constraint by multivalent vaccines will be taken in to account in the competitive assessment, to the extent it is relevant.

IV.2.2.2.c. Competitive assessment

- (52) In the EEA, BI is the leading supplier of monovalent PCV2 vaccines with a [50-60]% market share while Merial is a number three player, with a market share of [10-20]% in 2015.

Table 3. Parties' and competitors' share in monovalent PCV2 vaccines in the EEA

	2013	2014	2015
BI	[60-70]%	[50-60]%	[50-60]%
Merial	[10-20]%	[10-20]%	[10-20]%
Combined	[70-80]%	[70-80]%	[70-80]%
MSD	[20-30]%	[20-30]%	[20-30]%
Zoetis	[5-10]%	[5-10]%	[5-10]%
Total market size	EUR [160-165] million	EUR [170-175]million	EUR [155-160] million

Source: Form CO, CEESA data adjusted by third-party databases and BI's own estimates

²⁹ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 16.

³⁰ BI internal document, [...].

³¹ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 30.

³² Response of a customer to Questionnaire Q2 to Swine customers of 7 June 2016, question 15.

- (53) The Transaction gives rise to affected markets in 23 EEA countries with combined market shares above [50-60]% in 19 countries and above [70-80]% in 14 countries, representing almost [90-100]% of their EEA revenues in the market ([90-100]% for BI and [90-100]% for Merial).

Table 4. Parties' and competitors' share in monovalent PCV2 vaccines in affected markets in the EEA

EEA country	Year	BI	Merial	Combined	MSD	Zoetis	Market size (EUR 000)
AT	2015	[70-80]%	[0-5]%	[70-80]%	[20-30]%	[0-5]%	[2000-3000]
	2014	[60-70]%	[0-5]%	[60-70]%	[20-30]%	[10-20]%	[3000-4000]
	2013	[60-70]%	[0-5]%	[60-70]%	[20-30]%	[5-10]%	[3000-4000]
BE	2015	[50-60]%	[10-20]%	[60-70]%	[20-30]%	[10-20]%	[5000-6000]
	2014	[60-70]%	[10-20]%	[70-80]%	[20-30]%	[5-10]%	[5000-6000]
	2013	[70-80]%	[10-20]%	[80-90]%	[10-20]%	[0-5]%	[5000-6000]
BG	2015	[40-50]%	[30-40]%	[80-90]%	[10-20]%	[5-10]%	[0-1000]
	2014	[40-50]%	[30-40]%	[80-90]%	[10-20]%	[5-10]%	[0-1000]
	2013	[40-50]%	[30-40]%	[80-90]%	[10-20]%	[0-5]%	[0-1000]
CY	2015	na	na	na	na	na	na
	2014	[50-60]%	[10-20]%	[60-70]%	[20-30]%	[10-20]%	[0-1000]
	2013	na	na	na	na	na	na
CZ	2015	[50-60]%	[20-30]%	[80-90]%	[10-20]%	[0-5]%	[1000-2000]
	2014	[50-60]%	[20-30]%	[70-80]%	[10-20]%	[10-20]%	[1000-2000]
	2013	[50-60]%	[10-20]%	[70-80]%	[10-20]%	[10-20]%	[1000-2000]
DK	2015	[60-70]%	[10-20]%	[70-80]%	[10-20]%	[10-20]%	[20000-21000]
	2014	[50-60]%	[10-20]%	[60-70]%	[10-20]%	[10-20]%	[19000-20000]
	2013	[50-60]%	[10-20]%	[60-70]%	[20-30]%	[5-10]%	[15000-16000]
FI	2015	[40-50]%	[0-5]%	[40-50]%	[30-40]%	[10-20]%	[2000-3000]
	2014	[40-50]%	[0-5]%	[40-50]%	[40-50]%	[10-20]%	[2000-3000]
	2013	[40-50]%	[5-10]%	[40-50]%	[40-50]%	[5-10]%	[2000-3000]
FR	2015	[50-60]%	[30-40]%	[80-90]%	[5-10]%	[5-10]%	[18000-19000]
	2014	[40-50]%	[30-40]%	[80-90]%	[5-10]%	[5-10]%	[18000-19000]
	2013	[50-60]%	[30-40]%	[90-100]%	[5-10]%	[0-5]%	[17000-18000]
DE	2015	[60-70]%	[10-20]%	[70-80]%	[10-20]%	[0-5]%	[33000-34000]
	2014	[60-70]%	[5-10]%	[70-80]%	[20-30]%	[0-5]%	[32000-33000]
	2013	[60-70]%	[5-10]%	[70-80]%	[20-30]%	[0-5]%	[35000-36000]

EEA country	Year	BI	Merial	Combined	MSD	Zoetis	Market size (EUR 000)
		70]%			30]%		36000]
EL	2015	[30-40]%	[20-30]%	[50-60]%	[20-30]%	[20-30]%	[0-1000]
	2014	[20-30]%	[20-30]%	[40-50]%	[40-50]%	[10-20]%	[0-1000]
	2013	[20-30]%	[30-40]%	[50-60]%	[30-40]%	[10-20]%	[0-1000]
HU	2015	[40-50]%	[10-20]%	[60-70]%	[30-40]%	[5-10]%	[2000-3000]
	2014	[50-60]%	[10-20]%	[70-80]%	[20-30]%	[0-5]%	[3000-4000]
	2013	[50-60]%	[10-20]%	[70-80]%	[20-30]%	[0-5]%	[2000-3000]
IE	2015	[70-80]%	[0-5]%	[70-80]%	[20-30]%	[0-5]%	[5000-6000]
	2014	[70-80]%	[0-5]%	[70-80]%	[20-30]%	[0-5]%	[5000-6000]
	2013	[70-80]%	[0-5]%	[70-80]%	[20-30]%	[0-5]%	[5000-6000]
IT	2015	[60-70]%	[10-20]%	[70-80]%	[10-20]%	[10-20]%	[7000-8000]
	2014	[50-60]%	[10-20]%	[70-80]%	[10-20]%	[5-10]%	[8000-9000]
	2013	[50-60]%	[10-20]%	[70-80]%	[20-30]%	[10-20]%	[8000-9000]
LT	2015	[60-70]%	[10-20]%	[70-80]%	[0-5]%	[20-30]%	[0-1000]
	2014	[5-10]%	[40-50]%	[50-60]%	[0-5]%	[50-60]%	[0-1000]
	2013	[50-60]%	[40-50]%	[90-100]%	[0-5]%	[0-5]%	[0-1000]
NL	2015	[70-80]%	[10-20]%	[80-90]%	[5-10]%	[5-10]%	[26000-27000]
	2014	[70-80]%	[5-10]%	[80-90]%	[10-20]%	[5-10]%	[26000-27000]
	2013	[70-80]%	[5-10]%	[80-90]%	[10-20]%	[0-5]%	[25000-26000]
NOR	2015	[10-20]%	[80-90]%	[90-100]%	[10-20]%	/	[0-1000]
	2014	[5-10]%	[70-80]%	[80-90]%	[10-20]%	/	[0-1000]
	2013	[5-10]%	[70-80]%	[80-90]%	[10-20]%	/	[0-1000]
PL	2015	[40-50]%	[0-5]%	[40-50]%	[40-50]%	[0-5]%	[7000-8000]
	2014	[40-50]%	[0-5]%	[40-50]%	[40-50]%	[5-10]%	[8000-9000]
	2013	[40-50]%	[0-5]%	[40-50]%	[40-50]%	[5-10]%	[7000-8000]
PT	2015	[10-20]%	[30-40]%	[50-60]%	[40-50]%	[5-10]%	[2000-3000]
	2014	[20-30]%	[30-40]%	[50-60]%	[40-50]%	[5-10]%	[2000-3000]
	2013	na	na	na	na	na	na
RO	2015	[40-50]%	[5-10]%	[50-60]%	[30-40]%	[10-20]%	[2000-3000]
	2014	[40-50]%	[5-10]%	[50-60]%	[40-50]%	[5-10]%	[1000-2000]
	2013	[40-50]%	[10-20]%	[50-60]%	[30-40]%	[5-10]%	[1000-2000]

EEA country	Year	BI	Merial	Combined	MSD	Zoetis	Market size (EUR 000)
SI	2015	[90-100]%	[5-10]%	[90-100]%	[0-5]%	[0-5]%	[0-1000]
	2014	[80-90]%	[5-10]%	[80-90]%	[10-20]%	[0-5]%	[0-1000]
	2013	[70-80]%	[0-5]%	[70-80]%	[20-30]%	[0-5]%	[0-1000]
ES	2015	[40-50]%	[10-20]%	[50-60]%	[40-50]%	[5-10]%	[39000-40000]
	2014	[40-50]%	[10-20]%	[50-60]%	[30-40]%	[10-20]%	[34000-35000]
	2013	[30-40]%	[10-20]%	[50-60]%	[30-40]%	[10-20]%	[32000-33000]
SE	2015	[70-80]%	[0-5]%	[80-90]%	[10-20]%	[0-5]%	[1000-2000]
	2014	[70-80]%	[0-5]%	[80-90]%	[10-20]%	[0-5]%	[3000-4000]
	2013	[80-90]%	[0-5]%	[80-90]%	[10-20]%	[0-5]%	[2000-3000]
UK	2015	[80-90]%	[0-5]%	[80-90]%	[10-20]%	[0-5]%	[9000-10000]
	2014	[70-80]%	[0-5]%	[70-80]%	[20-30]%	[0-5]%	[10000-11000]
	2013	[80-90]%	[0-5]%	[80-90]%	[10-20]%	[0-5]%	[10000-11000]

Sources: CEESA data adjusted by Merial's actual sales, BI's estimates, CEESA data adjusted by BI estimates, AIEMV data, GfK data, Vetindex data, Veterindustria data³³

Notifying Party's views

- (54) The Notifying Party submits that the significant combined market shares for monovalent PCV2 vaccines would not reflect the true competition between BI and Merial's products.
- (55) First, the Notifying Party claims that the Parties' products are not closest competitors since:
- (i) BI's CircoFLEX was originally designed to target vaccination in piglets and Merial's Circovac vaccination in gilts and sows. While the two products are now authorised for the additional claims, Circovac's focus is still on sows, while CircoFLEX is clearly more focused on piglets.
 - (ii) Merial's Circovac is generally perceived as being less efficacious than BI's CircoFLEX and MSD Porcilis PCV vaccines. Circovac is a conventional vaccine, while BI and MSD's vaccines are subunit. In general, Porcilis PCV is more comparable to CircoFLEX in terms of efficacy, safety/reactivity and convenience.
- (56) Second, the Notifying Party submits that the market shares of the Parties on the market for monovalent PCV2 vaccines do not accurately reflect the significant competitive constraints exerted by multivalent vaccines including PCV2, such as MSD's multivalent offering for PCV2 and M.Hyo.

Commission's assessment

³³ Market share tables for Group 1 markets, Form CO, p. 42-50.

- (57) In the area of PCV2 vaccines, BI is a clear market leader in the EEA and across the majority of EEA countries, with a value based market share of up to [90-100]% in Slovenia. While Merial's Circovac is generally a smaller player (in most EEA countries behind BI's CircoFLEX and MSD's Porcilis PCV), it still holds a substantial market share in many EEA countries, reaching up to [80-90]% in Norway.
- (58) The market investigation generally confirmed BI's clear leading position. Many customers and competitors indicated that BI is dominating the market.³⁴ BI's own internal documents qualify CircoFLEX as the leading and "gold standard"³⁵ brand. In one internal document, BI states that "*CircoFLEX is by far the global market leader ([60-70]% of market share). This is primarily based on the strong brand image [CONFIDENTIAL INFORMATION ON BI PRICES]*".³⁶
- (59) As concerns Merial's position, the market investigation indicated that Merial's product would be less efficacious which is reflected in its generally lower market shares³⁷ and more targeted at sows than piglets³⁸. However, the market investigation also revealed a specific positioning of Circovac being priced at the lower end thus providing an interesting "value for money" proposition especially for large farms.³⁹ By way of example, one veterinarian indicated that "*Merial's product is a good price product which is important, approximately [...] % cheaper than the others, and used by big farms to reduce their costs*"⁴⁰ while another mentions that the "*lowest price per dose for pig is Merial's vaccine.*"⁴¹ This is also confirmed by internal documents of BI [BI INTERNAL ANALYSIS OF MERIAL'S COMMERCIAL STRATEGY].⁴² [BI INTERNAL ANALYSIS OF MERIAL'S COMMERCIAL STRATEGY]⁴³ [BI INTERNAL ANALYSIS OF MERIAL'S COMMERCIAL STRATEGY].
- (60) As to other competitors active in the market, Zoetis' Suvaxyn CV product is generally perceived as less safe and efficacious.⁴⁴ Customers did not comment on Zoetis' multivalent offering Suvaxyn Circo+MH RTU since it is not launched yet in the EEA.
- (61) As to the Parties' argument that MSD multivalent product *Porcilis PCVM* exert a competitive constraint on the Parties' monovalent PCV2 vaccines, in addition to the fact that Porcilis' PCVM is generally not substitutable to the Parties' monovalent

34 Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 20 and responses to Questionnaire Q1 to competitors of 8 June 2016, question 33.

35 BI internal document, [...].

36 BI internal document, [...].

37 Agreed minutes of a conference call held with a customer dated 11 May 2016 and of a conference call held with a competitor dated 11 May 2016. See also responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 18.

38 Responses to Questionnaire Q2 to Swine customers of 7 June 2016, questions 17 and 18.

39 Responses to Questionnaire Q1 to competitors of 8 June 2016, question 31 and responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 18.

40 Agreed minutes of a conference call held with a customer dated 13 May 2016.

41 Response of a customer to Questionnaire Q2 to Swine customers of 7 June 2016, question 19.

42 BI internal document, [...].

43 BI internal document, [...].

44 Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 18.

PCV2 vaccines as explained above, even if its sales were all to be included in the market, the market shares of the Parties and of MSD would not substantially differ, the combined entity still leading by far the market in the 23 EEA affected countries in 2015 with more than [50-60]% of market shares in 16 EEA countries.⁴⁵ This is because in general sales of multivalent vaccines are significantly less than sales of monovalent vaccines.

- (62) Finally, some market participants identified a risk of price increase and reduced choice of products post-Transaction for PCV2 vaccines across EEA countries.⁴⁶ One customer indicated that "*the price [will] climb; [since] circoflex [is] on cheap [side]*" while others indicated that "*the risk is that BI will suppress the products of Merial, and deprive the market of an alternative*"⁴⁷ and another one that the operation will have an impact on availability and choice as there is a "*possibility that Circoflex will be withdrawn*" and on price because "*market share close to 90% for BI and Merial could have impact on prices*".⁴⁸
- (63) As a result, the Transaction will eliminate actual competition for PCV2 vaccines in all 23 EEA countries where both Parties are active, which represent almost [90-100]% of each Party's EEA turnover, but also potential competition in other EEA countries where the two Parties are natural entrants.
- (64) In view of the above, the Transaction raises serious doubts as to its compatibility with internal market in relation to monovalent PCV2 vaccines in the EEA in general and in Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Lithuania, Netherlands, Norway, Poland, Portugal, Romania, Slovenia, Spain, Sweden and the UK in particular.

IV.2.2.3. *Mycoplasma hyopneumoniae* (M.hyo)

- (65) M.Hyo is the primary etiological agent of enzootic pneumonia and a leading cause of respiratory disease throughout the swine industry. The typical clinical sign is a non-productive dry cough. Though mortality associated with the disease is typically low, significant losses are caused by reduced weight gain, increase feed conversion ratio and increased medication costs.

IV.2.2.3.a. Parties' products

- (66) The Parties both only offer M.Hyo monovalent vaccines.
- (67) BI sells its monovalent M.Hyo vaccines for swine under the brands *IngelvacMycoFLEX* (MycoFLEX) and *Ingelvac M.Hyo*. The main difference between the two products is that MycoFLEX enables mixing with BI's PCV2 vaccine CircoFLEX. BI is currently phasing out Ingelvac M.Hyo. MycoFLEX is indicated for active immunization of pigs from three weeks of age or older to reduce lung lesions following the M.Hyo infection.

⁴⁵ Form CO, Chapter B, Table 14.

⁴⁶ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 38 and Responses to Questionnaire Q1 to competitors of 8 June 2016, question 69.

⁴⁷ Agreed minutes of a conference call held with a customer dated 13 May 2016.

⁴⁸ Response of a customer to Questionnaire Q2 to Swine customers of 7 June 2016, question 38.

- (68) Merial's monovalent vaccine is marketed under the brand *Hyoresp*. It is used for active immunization of suckling piglets from five weeks of age to reduce injection and lung lesions caused by M.Hyo.

IV.2.2.3.b. Market definition

- (69) In its previous decisions,⁴⁹ the Commission defined a market for monovalent mycoplasma (M.Hyo) vaccines for swine. The Commission further indicated that the distinction between live and inactivated is not relevant, given the fact that the products exist in an inactivated form only.

Notifying Party's views

- (70) The Notifying Party submits that the narrowest relevant product market is the market for monovalent M.Hyo vaccines for swine, however multivalent swine vaccines which include M.Hyo, in particular the combo vaccines PCV2 and MHyo, exert a competitive constraint on monovalent products since the vast majority of swine farmers would vaccinate against both diseases in the EEA.

Commission's assessment

- (71) As to the segmentation between monovalent M.Hyo vaccines and multivalent PCV2 and M.Hyo vaccines, in line with the developments in the section on PCV2, the market investigation indicated that multivalent vaccines address a specific customer demand and are thus likely to be part of a different product market.
- (72) In view of the above, for the purpose of assessing this Transaction, the relevant product market in relation to MHyo vaccines comprises all monovalent MHyo vaccines. Any (out of market) competitive constraint by multivalent vaccines will be taken in to account in the competitive assessment, to the extent it is relevant.

IV.2.2.3.c. Competitive assessment

- (73) In the EEA, BI is among the top 3 companies active in M.Hyo vaccines while Merial's presence is negligible at the EEA level and several strong competitors are active.

⁴⁹ M.5476 – Pfizer/Wyeth, 17.07.2009 and M.4691 – Schering-Plough / Organon biosciences, 11.10.2007.

Table 5. Parties' and competitors' share in monovalent M.Hyo vaccines in the EEA

	2013	2014	2015
BI	[30-40]%	[20-30]%	[20-30]%
Merial	[0-5]%	[0-5]%	[0-5]%
Combined	[30-40]%	[20-30]%	[20-30]%
Elanco	[20-30]%	[20-30]%	[20-30]%
Zoetis	[20-30]%	[20-30]%	[20-30]%
MSD	[10-20]%	[10-20]%	[10-20]%
Ceva	[0-5]%	[0-5]%	[0-5]%
Total market size	EUR [60-65]million	EUR [65-70] million	EUR [55-60] million

Source: Form CO, CEESA data adjusted by third-party databases and BI's own estimates

- (74) The Transaction gives rise to affected markets for monovalent M.Hyo vaccines in 6 EEA countries. The increment brought about by the Transaction is below [5-10]% in all cases except for Austria where it reaches [10-20]% in 2015.

Table 6. Parties' and competitors' share in monovalent M.Hyo vaccines in affected markets in the EEA

EEA country	Year	BI	Merial	Combined	Elanco	Zoetis	MSD	Market size (EUR 000)
AT	2015	[20-30%]	[10-20%]	[30-40%]	[10-20%]	[10-20%]	[30-40%]	[0-1000]
	2014	[20-30%]	[10-20%]	[30-40%]	[0-5%]	[30-40%]	[30-40%]	[1000-2000]
	2013	[20-30%]	[5-10%]	[20-30%]	[20-30%]	[20-30%]	[20-30%]	[1000-2000]
BE	2015	[20-30%]	[0-5%]	[20-30%]	[30-40%]	[20-30%]	[5-10%]	[6000-7000]
	2014	[20-30%]	[0-5%]	[20-30%]	[30-40%]	[20-30%]	[5-10%]	[6000-7000]
	2013	[20-30%]	[0-5%]	[20-30%]	[40-50%]	[20-30%]	[5-10%]	[6000-7000]
DE	2015	[30-40%]	[0-5%]	[30-40%]	[20-30%]	[20-30%]	[20-30%]	[10000-11000]
	2014	[40-50%]	[0-5%]	[40-50%]	[10-20%]	[10-20%]	[30-40%]	[10000-11000]
	2013	[40-50%]	[0-5%]	[40-50%]	[10-20%]	[10-20%]	[20-30%]	[11000-12000]
IT	2015	[20-30%]	[5-10%]	[20-30%]	[30-40%]	[30-40%]	[20-30%]	[2000-3000]
	2014	[20-30%]	[0-5%]	[20-30%]	[30-40%]	[20-30%]	[20-30%]	[3000-4000]
	2013	[20-30%]	[0-5%]	[30-40%]	[20-30%]	[30-40%]	[20-30%]	[3000-4000]
NL	2015	[40-50%]	[0-5%]	[40-50%]	[10-20%]	[30-40%]	[5-10%]	[10000-11000]
	2014	na	na	na	na	na	na	na
	2013	na	na	na	na	na	na	na
PL	2015	[20-30%]	[0-5%]	[20-30%]	[20-30%]	[10-20%]	[30-40%]	[1000-2000]
	2014	[30-40%]	[0-5%]	[30-40%]	[20-30%]	[10-20%]	[20-30%]	[1000-2000]
	2013	[30-40%]	[0-5%]	[30-40%]	[20-30%]	[10-20%]	[30-40%]	[1000-2000]

Source: Form CO, CEESA data, CEESA data adjusted by third-party databases, BI's own estimates and Merial's actual sales, GfK data, Vetindex data⁵⁰

Notifying Party's views

- (75) The Notifying Party submits that the proposed acquisition of Merial's Hyoresp product will not lead to any notable reinforcement of BI's existing market position in relation to monovalent M.hyo vaccines since Merial's increment is practically non-existent (below [0-5]%) and the combined market share of the Parties, in particular at the EEA level, is not particularly high (around [20-30]%).
- (76) Moreover, the Notifying Party submits that the market for monovalent M.Hyo vaccines will remain very competitive post-Transaction since:
- (i) At least three significant suppliers, namely Elanco, MSD and Zoetis, will remain on the market, and they represent strong competitors gaining market shares over the last years. Two additional smaller suppliers, Fatro and Hipra, are also present in some EEA countries markets and should quickly expand their geographic footprint.
 - (ii) Ceva entered the EEA market in the third quarter of 2015. The Notifying Party expects Ceva to exert significant competitive constraint in the future.

Commission's assessment

- (77) For M.Hyo vaccines, BI holds significant market shares in the EEA and across EEA countries, with up to [40-50]% in Netherlands. Merial's position is however limited, with a market share up to a maximum of [10-20]% in Austria and generally below [5-10]%.
- (78) The market investigation confirmed Merial's limited presence in monovalent M.Hyo vaccines across EEA countries.⁵¹ By way of example, one competitor indicated that "*Hyoresp is a small and not significant Mhyo vaccine in the EEA market place*", while another stressed that "*after 20 years on the market, its product is at the end of its lifecycle and barely competitive.*"⁵²

⁵⁰ Market share tables for Group 1 and Group 2 markets, Form CO, p. 90-91 and Annex A.12 to the Form CO.

⁵¹ Agreed minutes of conference calls with competitors dated 11 May 2016 and of a conference call with a competitor dated 18 May 2016.

⁵² Agreed minutes of conference calls with competitors dated 11 May 2016 and of a conference call with a competitor dated 18 May 2016.

- (79) The market investigation also indicated that the merged entity will continue to face strong competition from the remaining players, such as Elanco, Zoetis and MSD in all overlapping EEA countries. One market participant mentioned for instance that, for M.Hyo, "[there is] *no defined leader. Similar sales [are generated by] Boehringer (Ingelvac Mycoflex), Elanco (Stellamune), Merck (Porcilis Mhyo), Zoetis (Suvaxyn Mhyo/Respisure)*".⁵³
- (80) In view of the above and of all the evidence available to the Commission, the Commission considers that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the market for monovalent MHyo vaccines.

IV.2.2.4. Porcine reproductive and respiratory syndrome (PRRS)

- (81) PRRS is a highly variable ribonucleic acid (RNA) virus causing both respiratory and reproductive patterns. Infected animals run a high temperature, develop severe respiratory disease and succumb to other illness, grow poorly and some may even die. Infected sows produce significantly fewer piglets and more stillborn pigs, mummified fetuses and weak piglets. The disease is grouped under Type 1 and Type 2, which were originally respectively restricted to Europe (Type 1) and North America (Type 2). Currently, both types are spread globally, although Type 1 is still highly predominantly present in Europe while Type 2 is prevalent in North America.

IV.2.2.4.a. Parties' products

- (82) Both Parties supply only monovalent PRRS vaccines.
- (83) BI's original PRRS vaccine is *Ingelvac PRRS MVL*, a modified-live vaccine based on Type 2 virus. BI subsequently obtained marketing authorizations for the commercialisation of two new products, *Ingelvac PRRS FLEXEU* (PRRS FLEXEU) and *ReproCyc PRRS EU* which are both modified-live vaccines targeting Type 1 virus. While the marketing authorization covers 24 EEA countries the products were launched since October 2015 in 10 EEA countries. PRRS FLEXEU is used for pigs, while ReproCyc PRRSEU is used for breeding gilts and sows and can be used at all stages of the reproductive cycle. In 2015, BI discontinued the sale of its killed PRRS vaccine, *Ingelvac PRRS KL*, which was the same as Merial's product (see below) and was manufactured by Merial under a contract manufacturing agreement.

⁵³ Response of a competitor to to Questionnaire Q1 to competitors of 8 June 2016, question 37.

- (84) Merial is currently active in the PRRS market only with its killed vaccine Progressis, which is a Type 1 vaccine specifically designed for sows and gilts to reduce reproductive disorders caused by PRRS. [CONFIDENTIAL INFORMATION ON THE PARTIES' ACTIVITIES]⁵⁴ [CONFIDENTIAL INFORMATION ON THE PARTIES' ACTIVITIES].

IV.2.2.4.b. Market definition

Notifying Party's views

- (85) The Notifying Party submits that monovalent PRRS vaccines for swine constitute a distinct product market.
- (86) The Notifying Party however submits that the product characteristics and usage of PRRS vaccines can be differentiated between inactivated/killed (KV) and modified live (MLV) vaccines as well as by Type 1 and Type 2 vaccines. Killed PRRS vaccines are mainly used in sows and offer a high safety profile but arguably lower efficacy than MLVs. The Notifying Party submits that these factors should be taken into consideration in the competitive assessment of the Transaction.

Commission's assessment

- (87) The market investigation broadly confirmed that the relevant product market should be defined as monovalent PRRS vaccines. Neither the Notifying Party nor market participants identified any competing multivalent vaccines in the EEA.
- (88) The market investigation also confirmed that the type of vaccines (Type 1 or Type 2) and whether the vaccine is modified-live or killed are differentiating factors to be taken into consideration in the competitive assessment when assessing closeness of competition of available products. In this context, the market investigation indicated that:

⁵⁴ Animal health research programmes include three main phases: (i) the discovery phase, (ii) the exploratory development phase (or pre-development phase) and (iii) the full development phase. The discovery phase begins with a molecule or antigen identified as having potential therapeutic or prophylactic utility and being tested for approx. 18 months. The exploratory development phase is aimed at showing proof of efficacy and safety as well as determining key elements of the end product (e.g. formulation, target species, dosage etc.). This phase takes on average approx. 18 months. The full development phase can take four to five years, including regulatory review and approval. Testing is largely determined by the regulators involved and aims at proving shelf-life stability of the product, rationale and efficacy of the selected dose, and safe withdrawal periods. An environmental assessment is also mandatory.

- (i) Customers would generally take into consideration the Type of vaccine when choosing a PRRS vaccine based on the epidemiology the farm.⁵⁵ However, the claim of a vaccine against one type generally means that it would be more efficient against this type but it could also have cross protection against the other type.⁵⁶
- (ii) Customers indicated that MLV or KV could be preferred in some situations. For instance, MLV vaccines may be preferred for prime vaccination but there could be safety concerns stemming from the risk of a virus outbreak, while KV vaccines may be preferred for revaccination of immunized animals and can be perceived as safer but are less efficacious.⁵⁷
- (89) In view of the above, for the purpose of this decision, the relevant product market in relation to PRRS vaccines includes all monovalent PRRS vaccines.

IV.2.2.4.c. Competitive assessment

- (90) At the EEA level, BI and Merial are currently the number 2 and number 4 suppliers of PRRS vaccines MSD being the market leader in this space.

Table 7. Parties' and competitors' share in monovalent PRRS vaccines in the EEA

	2013	2014	2015
BI	[10-20]%	[10-20]%	[10-20]%
Merial	[5-10]%	[5-10]%	[5-10]%
Combined	[10-20]%	[10-20]%	[20-30]%
MSD	[70-80]%	[70-80]%	[60-70]%
Hipra	[0-5]%	[5-10]%	[5-10]%
Syva	[0-5]%	[0-5]%	[0-5]%
Total market size	EUR [45-50] million	EUR [50-55] million	EUR [55-60] million

Source: Form CO, CEESA data adjusted by third-party databases and BI's own estimates

- (91) Based on 2015 data, the Transaction gives rise to affected markets for monovalent PRRS vaccines in 7 EEA countries, which represent more than [90-100]% of BI's EEA turnover in relation to PRRS vaccines.

⁵⁵ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 24.

⁵⁶ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 26.

⁵⁷ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 23 and minutes of a conference call held with a competitor dated 11 May 2016 " *As a killed vaccine Merial's Progressis is perceived to be safer , in particular in sows, while the MLV vaccines have better efficacy* ". See also minutes of a conference call held with a customer dated 11 May 2016 "[KV vaccines] *is essentially used for niche markets, in particular in PRRS free herds to boost the immunity without the risk of spreading the live virus*" .

Table 8. Parties' and competitors' share in monovalent PRRS vaccines in affected markets in the EEA

EEA country	Year	BI	Merial	Combined	MSD	Hipra	Market size (EUR 000)
BE	2015	[20-30]%	[10-20]%	[30-40]%	[50-60]%	[5-10]%	[5000-6000]
	2014	[20-30]%	[10-20]%	[30-40]%	[50-60]%	[5-10]%	[3000-4000]
	2013	[20-30]%	[10-20]%	[40-50]%	[50-60]%	[0-5]%	[3000-4000]
DK	2015	[40-50]%	[0-5]%	[50-60]%	[50-60]%	/	[3000-4000]
	2014	[40-50]%	[0-5]%	[40-50]%	[50-60]%	/	[2000-3000]
	2013	[40-50]%	[0-5]%	[40-50]%	[50-60]%	/	[2000-3000]
DE	2015	[20-30]%	[0-5]%	[20-30]%	[70-80]%	/	[16000-17000]
	2014	[20-30]%	[0-5]%	[20-30]%	[70-80]%	/	[17000-18000]
	2013	[20-30]%	[0-5]%	[20-30]%	[70-80]%	/	[15000-16000]
HU	2015	[0-5]%	[10-20]%	[20-30]%	[80-90]%	/	[0-1000]
	2014	[0-5]%	[20-30]%	[20-30]%	[70-80]%	/	[0-1000]
	2013	na	na	na	na	na	na
IT	2015	[10-20]%	[10-20]%	[30-40]%	[60-70]%	/	[1000-2000]
	2014	[0-5]%	[10-20]%	[10-20]%	[80-90]%	/	[1000-2000]
	2013	[0-5]%	[10-20]%	[10-20]%	[80-90]%	/	[1000-2000]
PT	2015	[5-10]%	[20-30]%	[20-30]%	[70-80]%	/	[0-1000]
	2014	[0-5]%	[10-20]%	[20-30]%	[70-80]%	/	[0-1000]
	2013	[0-5]%	[10-20]%	[20-30]%	[70-80]%	/	[0-1000]
SK	2015	[30-40]%	[5-10]%	[40-50]%	[50-60]%	/	[0-1000]
	2014	[0-5]%	[0-5]%	[0-5]%	[90-100]%	/	[0-1000]
	2013	[20-30]%	[0-5]%	[20-30]%	[40-50]%	/	[0-1000]

Source: Form CO, CEESA data, CEESA data adjusted by third-party databases and BI's own estimates, CEESA data adjusted by Merial's actual sales, OPU Belgium data.⁵⁸

- (92) However, 2015 market shares do not accurately reflect the current market position of the Parties as BI's two products are new and were launched only in October 2015.
- (93) Indeed, at the end of October 2015 BI launched two new modified live Type 1 vaccines. These products are likely to generate substantially more sales than its older Type 2 product. The market investigation confirmed that BI's market shares have been growing. BI's own estimate is that it will grow from [5-10]% in 2015 to [20-30]% in 2016 for modified live PRRS Type 1 vaccines in the EEA.⁵⁹ This estimate was confirmed by one competitor in the market investigation indicating that "[BI is] gaining market share from initial [5-10]% (with the type 2 vaccine and KV) and

⁵⁸ Market share tables for Group 1 and Group 2 markets, Form CO, p. 74 and Annex A.11 to the Form CO.

⁵⁹ Form CO, Chapter B – Vaccines, paragraph 255.

actually (all vaccines, type 1 and 2 plus KV) are around [20-30]%."⁶⁰ Moreover, this is in line with BI's own ambition set out in an internal document, whereby its objective is to [CONFIDENTIAL INFORMATION ON BI'S COMMERCIAL STRATEGY].⁶¹

- (94) More importantly, the current market structure is generally contestable since the PRRS disease is not well controlled yet and there is a strong competition to innovate in this market which is set to grow. Many competitors indicated during the market investigation that PRRS vaccine is a major area of innovation: "*PRRS is probably the biggest disease concern for the pig industry in the EEA. Vaccines have significant limitations in relation with efficacy and safety*".⁶² The PRRS market has been growing over the last three years from EUR 45 million in 2013 to EUR 58 million in 2015. According to BI's own estimates, the market size would increase up to EUR [70-80] million in 2024.⁶³
- (95) In this context, while BI just launched two innovative products at the end of last year, [CONFIDENTIAL INFORMATION ON THE PARTIES' ACTIVITIES]⁶⁴ [CONFIDENTIAL INFORMATION ON THE PARTIES' ACTIVITIES]⁶⁵ [CONFIDENTIAL INFORMATION ON THE PARTIES' ACTIVITIES]⁶⁶.
- (96) As to competitors' products, MSD's product Porcilis which is the oldest modified live type 1 on the market and the current market leader is losing market share for the benefit of BI and possibly Hipra. This could be due to efficacy and safety issues, one veterinarian indicating that "*the good attenuation [of MSD Porcilis] means that the vaccine is very sensitive to vaccination errors and vaccine storage conditions. I have studied several cases where the vaccine failed to induce significant immunity*".⁶⁷ As to Hipra's product Unistrain, which was introduced in the market in 2013, it seems its penetration remains limited in comparison to other modified-live vaccines. This is also confirmed in BI's internal documents indicating that Hipra's product has [BI INTERNAL ANALYSIS OF HIPRA'S MARKET POSITION].⁶⁸ This could be explained by Hipra not having a large portfolio of swine vaccines and thus having a marketing disadvantage and more limited access to customers. Indeed, BI INTERNAL ANALYSIS OF HIPRA'S MARKET POSITION].⁶⁹ In this context the market investigation confirmed the importance of having a portfolio of swine vaccines to be

⁶⁰ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 44.

⁶¹ BI internal document, [...].

⁶² Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 40.

⁶³ Form CO, Chapter B – Vaccines, paragraph 370.

⁶⁴ Merial internal document, [...].

⁶⁵ Merial internal document, [...].

⁶⁶ Agreed minutes of a conference call held with a customer dated 13 May 2016.

⁶⁷ Response of a customer to Questionnaire Q2 to Swine customers of 7 June 2016, question 26.

⁶⁸ BI internal document, [...].

⁶⁹ BI internal document, [...].

successful, swine veterinarians mentioned that discounts are often based on the range of swine vaccines purchased.⁷⁰

- (97) In view of the above, and in particular of BI's growing position and the importance of innovation in the PRRS area, [CONFIDENTIAL INFORMATION ON R&D].⁷¹
- (98) As a result, the Transaction will eliminate actual competition for PRRS vaccines in all EEA countries where both Parties are active, which represent more than [90-100]% of BI's EEA turnover in relation to PRRS vaccines, as well as potential competition in other EEA countries, [CONFIDENTIAL INFORMATION ON R&D] and BI could expand the geographic coverage of its recently launched products.
- (99) In view of the above, the Transaction raises serious doubts as to its compatibility with the internal market in relation to monovalent PRRS vaccines in the EEA in general and in Belgium, Denmark, Germany, Hungary, Italy, Portugal and Slovakia in particular.

IV.2.2.5. Porcine parvovirus (PPV)

- (100) Porcine parvovirus (PPV) causes reproductive losses during pregnancy by infecting the fetus of naïve dams. PPV is the most common cause of infectious infertility in pigs.

IV.2.2.5.a. Parties' products

- (101) Merial supplies both a monovalent PPV vaccine, Parvovax, and a multivalent PPV vaccine combined with erysipelas, Parvovurax.
- (102) [INFORMATION ON BI ACTIVITIES].

IV.2.2.5.b. Market definition

- (103) In a previous decision dated 1999⁷² the Commission defined distinct product markets for, on the one hand, monovalent vaccines against PPV and, on the other hand, multivalent vaccines against both PPV and erysipelas.

Notifying Party's views

- (104) The Notifying Party submits that monovalent PPV vaccines for swine form a distinct relevant product market. The Notifying Party however considers that there is a degree of competition between monovalent PPV vaccines and multivalent vaccines including PPV, although some farmers may choose to use a multivalent vaccine as a first shot and a monovalent vaccine as a booster.
- (105) The Notifying Party further submits that a distinction between modified-live and killed vaccines is not relevant, since modified live and killed vaccines are sufficiently similar in terms of price, efficacy and safety to be viewed as equivalent from a veterinary and customer's perspective.

⁷⁰ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 9 and responses to Questionnaire Q1 to competitors of 8 June 2016, question 18.

⁷¹ Agreed minutes of a conference call held with a customer dated 13 May 2016.

⁷² M.1681 Akzo Nobel / Hoechst Roussel Vet, 22 November 1999. Para. 40 and following.

Commission's assessment

- (106) As to the distinction between monovalent and multivalent vaccines, the market investigation provided indications that customers consider that multivalent vaccines for PPV and erysipelas are much cheaper than two monovalent vaccines (PPV and erysipelas) and can be more convenient.⁷³ Customers may however still prefer in some situation to use two monovalent products, PPV and Erysipelas, to ensure a better immunization. The strong demand for multivalent offerings including PPV is reflected in the EEA-wide market structure, with a multivalent market representing more than EUR 22 million and a monovalent market representing EUR 1.5 million. Also, while two monovalent vaccines can be substituted by a multivalent offering as indicated above, multivalent vaccines cannot however be fully substituted to a monovalent one.
- (107) In view of the above, for the purpose of the Transaction, the relevant product market in relation to PPV vaccines comprises all monovalent PPV vaccines. Any (out of market) competitive constraint by multivalent vaccines will be taken in to account in the competitive assessment, to the extent it is relevant.

IV.2.2.5.c. Competitive assessment

- (108) At the EEA level, Meril is currently the number three supplier of monovalent PPV vaccines controlling 20% of the market in 2015. The market is currently very concentrated with only 4 players having a product. MSD is the market leader.

Table 9. Meril and its competitors' share in monovalent PPV vaccines in the EEA

	2013	2014	2015
Meril	[10-20]%	[20-30]%	[20-30]%
Zoetis	[60-70]%	[30-40]%	[20-30]%
MSD	[20-30]%	[40-50]%	[50-60]%
Total market size	EUR [0-5] million	EUR [0-5] million	EUR [0-5] million

Source: Form CO, CEESA data

- (109) The Transaction gives rise to affected markets (where Meril has a market share above [20-30]% in 2015) for monovalent PPV vaccines in 3 EEA countries.

⁷³ Agreed minutes conference call of 28 July with a competitor.

Table 10. Parties' and competitors' share in monovalent PPV vaccines in affected markets in the EEA

EEA country	Year	Merial	MSD	Zoetis	Market size (EUR 000)
FR	2015	[90-100]%	[0-5]%	/	[0-1000]
	2014	[90-100]%	[0-5]%	/	[0-1000]
	2013	[90-100]%	[0-5]%	/	[0-1000]
IT	2015	[40-50]%	[40-50]%	[0-5]%	[0-1000]
	2014	[40-50]%	[50-60]%	[0-5]%	[0-1000]
	2013	[40-50]%	[50-60]%	[0-5]%	[0-1000]
SK	2015	[90-100]%	[0-5]%	/	[0-1000]
	2014	/	[0-5]%	[90-100]%	[0-1000]
	2013	/	[0-5]%	[90-100]%	[0-1000]

Source: Form CO, CEESA data⁷⁴

- (110) Merial holds a strong market position for monovalent PPV vaccines in France, Italy and Slovakia. More specifically, in France, no other competitors were active in the last three years and in Italy and Slovakia only one significant competitor, MSD in Italy and Zoetis in Slovakia, was also active in the same period.
- (111) [CONFIDENTIAL INFORMATION ON BI ACTIVITIES]⁷⁵
- (112) In view of Merial's current position [...], the merger reinforces Merial's already strong position – and even monopoly situation in France – for monovalent PPV vaccines.
- (113) The possible competitive constraints from multivalent offering would not change this assessment. In addition to the fact that multivalent vaccines are not substitutable to a monovalent vaccine, even if sales of multivalent vaccines were to be taken into consideration, Merial still holds a very strong position on a hypothetical market comprising monovalent vaccines and multivalent PPV/Erysipelas vaccines, in particular with around [70-80]% of market share in France and [50-60]% in Italy, and an even stronger market position in many other EEA countries, since Merial is the leader in terms of sales of multivalent PPV/Erysipelas vaccines at EEA level.
- (114) As a result, the Transaction will eliminate [...] competition for PPV in all EEA countries [CONFIDENTIAL INFORMATION ON BI ACTIVITIES] and Merial is active in almost all EEA countries with PPV vaccines.
- (115) In view of the above, the Transaction raises serious doubts as to its compatibility with the internal market in relation to monovalent PPV vaccines in the EEA in general and in France, Italy, Slovakia in particular.

IV.2.3. Ruminant vaccines: Bovine viral diarrhoea (BVD)

- (116) BVD is a viral disease caused by the BVD virus (BVDV) to ruminants. Ruminants include cattle, sheep and goats. The primary symptoms of BVD are acute diarrhoea, fever, and lesions in the mucous membranes. There are two distinct types of BVDV reported; BVDV-1 (Type 1) and BVDV-2 (Type 2). In Europe, the prevalence of BVDV-1 is significantly higher than that of BVDV-2.

⁷⁴ Market share tables, Form CO, p. 96.

⁷⁵ [CONFIDENTIAL INFORMATION ON BI ACTIVITIES]

IV.2.3.1.a. Parties' products

- (117) Both Parties produce and sell monovalent bovine viral diarrhoea (BVD) vaccines for ruminants. Merial also supplies a multivalent vaccine for respiratory cattle diseases including protection against BVD.
- (118) BI entered the BVD market with its product Bovela in March 2015. Bovela is a modified-live vaccine that can be used for the control of both BVDV-1 and BVDV-2, it is the only vaccine in the EU licenced for the prevention of both types. Bovela is also currently the only BVD vaccine available on the market which offers foetal protection for both Type 1 and Type 2 BVDV as all other products are Type 1 vaccines which only offer cross-protection (not foetal protection) against BVDV-2.
- (119) Merial's monovalent BVD vaccine is marketed under the brand Mucosiffa. Mucosiffa is a modified-live vaccine. It is used for the active immunization of ruminants against BVDV-1 and mucosal disease. As regards multivalent vaccines Merial recently launched Bovalto Respi 4 which includes protection against BRSV, PI3, M.Haemolytica and BVD. [CONFIDENTIAL INFORMATION ON R&D]

IV.2.3.1.b. Market definition

The Notifying Party's view

- (120) The Notifying Party submits that the relevant product market as regards vaccines against BVD should be a broader market for multivalent cattle respiratory vaccines including BVD. According to the Notifying Party, there is a non-negligible degree of competition between monovalent BVD vaccines and multivalent cattle vaccines which include protection against BVD. The Notifying Party however submits that while monovalent BVD vaccines are designated to eradicate BVD from the cattle population and therefore offer foetal protection (targeting breeding animals), multivalent vaccines including BVD protection do not offer foetal protection but are mainly focused at tackling the respiratory effects of BVD (and other pathogens included in the vaccine).
- (121) The Notifying Party further submits that the distinction between live and inactivated vaccines would not be relevant in the case of BVD vaccines, since the Parties produce only modified-live BVD vaccines.

Commission's assessment

- (122) As to the segmentation between monovalent and multivalent vaccines, the Commission has previously found that multivalent cattle respiratory vaccines, possibly including protection against BVD, constitute a distinct market from monovalent vaccines targeting only one pathogen.⁷⁶ The market investigation in this case has not revealed any elements which would confirm the Notifying Party's arguments. Indeed, customers did not identify any multivalent product as competing closely with the Parties' monovalent products and only one identified multivalent vaccines as a BVD offering.⁷⁷ The market structure also seems to reflect this distinction, the two most important players in the area of BVD vaccines, namely MSD and BI, have only monovalent vaccines. Similarly, BI's internal documents focus on the monovalent

⁷⁶ Case M.5476 – *Pfizer/Wyeth*, paras 179-181.

⁷⁷ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, questions 10 and 16.

market, with the ambition to achieve [...] % market share "in the monovalent BVD market in Europe"⁷⁸

- (123) The market investigation did not suggest any further segmentation of the monovalent BVD market, although the distinction between modified live and killed vaccine, Type1/Type2 and the number of doses can be important distinctive features to be taken into consideration in the competitive assessment as further detailed below.
- (124) In view of the above, for the purpose of the Transaction, the relevant product market in relation to BVD vaccines comprises all monovalent BVD vaccines. Any (out of market) competitive constraint by multivalent vaccines will be taken in to account in the competitive assessment, to the extent it is relevant.

IV.2.3.1.c. Competitive assessment

- (125) At the EEA level, BI is the second largest player in BVD vaccines with a market share of [20-30] % while Merial is the third player with a [10-20] % market share.

Table 11. Parties' and competitors' share in monovalent BVD vaccines in the EEA

	2013	2014	2015
BI	[0-5] %	[0-5] %	[20-30] %
Merial	[10-20] %	[10-20] %	[10-20] %
Combined	[10-20] %	[10-20] %	[30-40] %
MSD	[60-70] %	[70-80] %	[50-60] %
Elanco	[10-20] %	[5-10] %	[5-10] %
Zoetis	[0-5] %	[0-5] %	[5-10] %
Virbac	[0-5] %	[0-5] %	[0-5] %
Total market size	EUR [20-25] million	EUR [20-25] million	EUR [25-30] million

Source: Form CO, CEESA data adjusted by third-party databases and BI's own estimates

- (126) The Transaction gives rise to affected markets for monovalent BVD vaccines in four EEA countries.

⁷⁸ BI internal document, [...].

Table 12. Parties' and competitors' share in monovalent BVD vaccines in affected markets in the EEA

EEA country	Year	BI	Merial	Combined	MSD	Virbac	Zoetis	Market size (EUR 000)
FR	2015	[10-20]%	[30-40]%	[50-60]%	[20-30]%	[0-5]%	[10-20]%	[9000-10000]
	2014	[0-5]%	[40-50]%	[40-50]%	[30-40]%	[5-10]%	[10-20]%	[8000-9000]
	2013	[0-5]%	[40-50]%	[40-50]%	[30-40]%	[5-10]%	[10-20]%	[6000-7000]
DE	2015	[30-40]%	[10-20]%	[50-60]%	[30-40]%	[10-20]%	/	[1000-2000]
	2014	[0-5]%	[10-20]%	[10-20]%	[50-60]%	[20-30]%	/	[1000-2000]
	2013	[0-5]%	[10-20]%	[10-20]%	[70-80]%	[10-20]%	/	[2000-3000]
IT	2015	[30-40]%	[10-20]%	[40-50]%	[30-40]%	/	[10-20]%	[3000-4000]
	2014	[0-5]%	[10-20]%	[10-20]%	[70-80]%	/	[10-20]%	[2000-3000]
	2013	[0-5]%	[10-20]%	[10-20]%	[70-80]%	/	[5-10]%	[2000-3000]
PL	2015	[10-20]%	[0-5]%	[20-30]%	[70-80]%	/	[0-5]%	[0-1000]
	2014	[0-5]%	[0-5]%	[0-5]%	[90-100]%	/	[0-5]%	[0-1000]
	2013	[0-5]%	[0-5]%	[0-5]%	[90-100]%	/	[0-5]%	[0-1000]

Source: Form CO, CEESA data, CEESA data adjusted by Merial's actual sales, AIEMV data⁷⁹

Notifying Party's view

- (127) The Notifying Party submits that despite the relatively high combined market shares in some affected markets (up to [50-60]% in France), the Transaction will not result in any significant impediment to effective competition for monovalent BVD vaccines on these markets for various reasons.
- (128) First, the Notifying Party claims the market for BVD vaccines will remain competitive post-Transaction since MSD is the clear market leader with its product *Bovilis*, a killed vaccine with a long-standing market history and strong technical customer support.
- (129) Second, the market shares do not reflect competition from multivalent cattle vaccines which include protection against BVD and account for a large proportion of the demand. The Parties' competitors, in particular Zoetis and Hipra, offer these types of multivalent vaccines which exert competition constraint on BI's product.
- (130) Third, the Parties' products are not close competitors since BI's Bovela offers foetal protection for both Type 1 and Type 2 BVD, whereas Merial's Mucosiffa offers foetal protection against BVD-1 only.

⁷⁹ Market share table, Form CO, p. 124 and and p. 131-132.

The Commission's assessment

- (131) BI and Merial are two significant suppliers of monovalent BVD vaccines across the EEA, with a combined market share up to more than [50-60]% in France and Germany in 2015.
- (132) In addition, BI's market shares are not fully representative of its real market position as BI entered the market only in March 2015. Since its entry, BI already gained [20-30]% of the market in 2015 at EEA level and up to [30-40]% in Germany. Respondents to the market investigation expect BI's market share to continue to grow and eventually take over MSD as the market leader.⁸⁰ One market participant indicated for instance that "*Bovela has performed well since launch and has already reached #1 position in Germany and is already in a #2 position in most markets where it has launched. It looks set to take #1 position in Italy this year and also has the potential to do so in a number of key European markets over the next 9-18 months.*"⁸¹
- (133) BI's internal documents confirm its growing position and show that BI expects to become the market leader in the near term. By way of example, one document mentions that "*Bovela will MAKE HISTORY [...] The secret of Bovela success will be [CONFIDENTIAL INFORMATION REGARDING BI COMMERCIAL STRATEGY] [...] Mid-term 1-3 years (2016-2018): achieve at least 55% MS [market share] in Europe" / Long term > 3 years: extend market share in EU to 70%*" and ultimately "*achieve 80% of market share in the monovalent BVD market in Europe*".⁸²
- (134) The market investigation indicated that the success of Bovela is due to a combination of factors including the fact that it is a single dose, modified live product and has cross protection against type 2 as opposed to the currently leading MSD Bovilis which is a two doses, killed vaccine with no cross protection against type 2. Indeed, market participants insisted on the importance of these criteria when choosing a BVD vaccine. For instance, one market participant indicated that "*These factors are of important consideration only where the live vaccine is indicated as a single shot regime without the need for a 2 dose primary course*",⁸³ while others insisted on the "*preference if it is a single dose by reducing labour cost it will increase BVD vaccination uptake (convenience)*"⁸⁴ and the fact that "*although BVD type II is very rarely isolated in EU, farmers and vets like having a broader protection*".⁸⁵
- (135) Moreover, the market investigation indicated that Merial's Mucossifa is the closest competitor to BI's Bovela.⁸⁶ By way of example, one market participant indicated that "*the closest competitor to Bovela is Mucosiffa where it is sold as it offers broadly the*

⁸⁰ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 14 and responses to Questionnaire Q1 to competitors of 8 June 2016, question 64.

⁸¹ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 64.

⁸² BI internal document, [...]

⁸³ Response of a customer to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 8.

⁸⁴ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 54.

⁸⁵ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 57.

⁸⁶ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 16 and responses to Questionnaire Q1 to competitors of 8 June 2016, question 65.

same convenience/usage attributes".⁸⁷ Indeed, they are the only two modified live vaccines and one dose products.⁸⁸ In addition, Mucossifa recently gained new claims which make the product even closer to Bovela.⁸⁹ In particular, Merial recently obtained foetal protection in France and cross protection against type 2 in Italy. In addition, some market participants also noted that Mucossifa and Bovela both have twelve months duration of immunity.⁹⁰ The strong competitive constraint exerted by Mucossifa on Bovilis can also be illustrated by BI's internal documents [CONFIDENTIAL INFORMATION REGARDING BI ANALYSIS OF COMPETITOR PRODUCT].⁹¹

- (136) The market investigation did not confirm the competition exerted from multivalent offerings. Customers never identified any multivalent product as competing closely with the Parties' monovalent products.⁹² BI's internal documents also rarely mention multivalent vaccines within the BVD competitive landscape.⁹³
- (137) As a result, the Transaction will eliminate actual competition for BVD in all EEA countries where the Parties are both active, which represent almost [90-100]% of Merial's EEA turnover in the EEA for monovalent BVD vaccines, as well as potential competition in other countries and in particular in the UK and Spain in view of BI's presence and Merial's expansion plan in these countries.⁹⁴
- (138) In view of the above and in particular the strong market position and closeness of competition between the Parties' products, the Commission considers that the Transaction raises serious doubts as to its compatibility with the internal market with respect to the market for monovalent BVD vaccines in the EEA in general and in France, Germany, Italy and Poland in particular.

IV.3. Animal health pharmaceuticals

- (139) Animal pharmaceuticals are a wide group of medicines containing a large variety of active pharmaceutical ingredients (APIs) that prevent or treat a range of animal diseases and disorders. Pharmaceuticals include (i) anti-inflammatories, (ii) antimicrobials (also known as antibiotics) and (iii) specialty products such as cardiopulmonary therapy for companion animals.
- (140) In the present case, the Parties' activities overlap in all those three areas.
- (141) The parties are among the main players active in animal health pharmaceuticals in the EEA, together with Zoetis, MSD, Elanco and Bayer.

⁸⁷ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 65.

⁸⁸ Merial's Mucossifa is a single dose vaccine for animals aged over six months.

⁸⁹ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 5 and responses to Questionnaire Q1 to competitors of 8 June 2016, question 54.

⁹⁰ Responses to Questionnaire Q1 to competitors of 8 June 2016, question 65.

⁹¹ BI internal document, [...].

⁹² Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, questions 10 and 16.

⁹³ BI's internal document, [...].

⁹⁴ Form CO, Chapter B – Vaccines, paragraph 313 and footnote 137.

Table 13. Parties' and competitors' share in pharmaceuticals in the EEA

	2013	2014	2015
BI	[5-10]%	[5-10]%	[5-10]%
Merial	[10-20]%	[10-20]%	[10-20]%
Combined	[10-20]%	[10-20]%	[10-20]%
Zoetis	[10-20]%	[10-20]%	[10-20]%
MSD	[10-20]%	[10-20]%	[10-20]%
Elanco	[10-20]%	[10-20]%	[10-20]%
Bayer	[10-20]%	[10-20]%	[10-20]%
Ceva	[5-10]%	[5-10]%	[5-10]%
Virbac	[5-10]%	[5-10]%	[5-10]%
Vetoquinol	[5-10]%	[0-5]%	[0-5]%
Total market size	EUR [0-5] billion	EUR [0-5] billion	EUR [0-5] billion

Source: Form CO, CEESA data⁹⁵

IV.3.1. Market definition – General framework for animal health pharmaceuticals

IV.3.1.1. Product market

(142) In previous decisions,⁹⁶ the Commission considered that the following factors may be relevant in defining product markets in relation to pharmaceutical products:

- i. the animal species or groups of species, distinguishing between (i) companions animals, (ii) cattle, (iii) ruminants, (iv) horses and (v) multi-species,
- ii. the active substance of the pharmaceutical,
- iii. the target pathology, distinguishing pharmaceuticals against certain diseases such as mastitis in cows,
- iv. the mode of administration, distinguishing for instance between (i) injectable and (ii) oral,
- v. the duration of efficacy,
- vi. the duration of the withdrawal period, period after treatment during which an animal's meat or milk is deemed unsuitable for human consumption.

(143) The Notifying Party agrees with this general approach with regards to pharmaceuticals and submits its opinion on the relevance of all the above mentioned factors on a case-by-case basis for each overlapping animal pharmaceutical.

(144) The market investigation also confirmed the general approach set out above and the need to conduct a case by case analysis for pharmaceuticals, which is conducted in the relevant sections below.

⁹⁵ See also Annex C.2 to the Form CO.

⁹⁶ E.g. M.4691 - Schering-Plough/Organon Biosciences, para. 40. Case M.5476 – Pfizer/Wyeth, paras. 121 and 122.

IV.3.1.2. Geographic market

- (145) In previous decisions,⁹⁷ the Commission found that despite the existence of some pan-European trends and the fact that the main players are active throughout the EEA, the relevant geographic market for animal health pharmaceuticals was national in scope. This is mainly due to the fact that most products on these markets remain subject to national and mutual recognition registration systems. In addition, national legislation determines the selling conditions of the products, while competitive landscapes in EEA countries differ in terms of market penetration, shares, price, distribution systems and local veterinarian preferences.
- (146) The Notifying Party agrees the geographic scope of the markets is national.
- (147) In this case, the market investigation broadly confirmed that markets for pharmaceuticals in the animal health sector are still national, as marketing authorizations are still subject to national regulations, the competitive landscapes varies from one Member State to another while pricing strategies of pharmaceutical companies also seem to be national.
- (148) For the purpose of assessing the impact of the Transaction, the Commission therefore concludes that the relevant geographic markets in relation to animal health pharmaceuticals are national in scope.

IV.3.2. *Anti-inflammatories*

IV.3.2.1. Market definition

- (149) Anti-inflammatories are used to treat inflammation and to reduce the pain and fever associated with inflammation. In previous decisions,⁹⁸ the Commission found that anti-inflammatories may be sub-divided into two categories: (i) non-steroidal anti-inflammatory drugs (NSAIDs) and (ii) corticosteroids. Although NSAIDs and corticosteroids both have anti-inflammatory properties, only NSAIDs have analgesic (anti-pain) and anti-pyretic (anti-fever) properties. Furthermore, NSAIDs can relieve pain and inflammation without the immunosuppressive and metabolic side-effects associated with corticosteroids. NSAIDs also tend to be more expensive than corticosteroids. NSAIDs are used in animal health primarily for pain relief and for treating inflammation. NSAIDs act by inhibiting the formation of prostaglandins synthesized via the cyclooxygenase pathway or the formation of leukotrienes via the lipoxygenase pathway to mediate the body's inflammatory response to injury. Adverse effects of treating pain with NSAIDs are most commonly gastrointestinal ulceration and renal impairment.

⁹⁷ Case M.4691 - *Schering-Plough/Organon Biosciences*, paras. 42-45. M.7277 - *Eli Lilly/Novartis Animal Health*, paras. 56-58, Case M.6205 - *Eli Lilly/Janssen*, para. 15.

⁹⁸ Case M.5476 – *Pfizer/Wyeth*, Paragraph 122.

- (150) In previous decisions, the Commission considered distinction between NSAIDs based on :
- i. the mode of administration, distinguishing between (i) injectable and (ii) oral; and
 - ii. the animal species or groups of species, distinguishing between (i) companions animals, (ii) horses and (iii) ruminants, swine, horses and companion animals ("multi-species").⁹⁹
- (151) First, the market investigation generally confirmed the distinction between injectable and oral NSAIDs, injectable solutions being used for treating acute pain post-surgery for instance while oral solutions are typically administered by the animal owners for chronic pain.¹⁰⁰
- (152) Second, the market investigation confirmed the distinction by animal species or group of species, pharmaceuticals being generally authorized per animal species or group of species.
- (153) The Notifying Party adds that other distinguishing factors should be accounted for when analysing the NSAID markets. While they may not impede substitutability between NSAID products to the extent that they form separate relevant product markets, they may still be relevant for the competitive assessment. These factors include (i) animal size for injectable NSAIDs, (ii) non selective Cyclooxygenase (COX-1)/cyclooxygenase 2 (COX-1) (**COX**) and selective COX-2 inhibitors (**COXIB**) treatments, (iii) treatment of acute or chronic inflammation and (iv) active substance of the pharmaceutical.
- (154) The market investigation indeed indicated that in the area of animal pharmaceuticals the market should not be segmented by active pharmaceutical ingredients (API), since all NSAIDs compete together from a demand perspective.¹⁰¹

Injectable multiple species NSAIDs

Notifying Party's views

- (155) The Notifying Party submits that multi-species injectable NSAIDs constitute a distinct product market. The Notifying Party points out that most injectable NSAIDs are truly multi-species and that further segmentation according to species could lead to unrealistically small markets. However, the Notifying Party adds that certain injectables are specifically targeted for specific species.

⁹⁹ Case M.4691 – Schering-Plough / Organon biosciences, paras. 305 and 306.

¹⁰⁰ Responses to Questionnaire Q1 to competitors of 8 June 2016, question 79.

¹⁰¹ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 55 and responses to Questionnaire Q1 to competitors of 8 June 2016, question 101.

Commission's assessment

- (156) The Commission has previously found that although there are some injectable NSAIDs that are specifically targeted for horses, dogs and cats respectively, there are also injectable NSAIDs that are truly multi-species, which makes the task of estimating their use for each species very difficult.¹⁰²
- (157) The market investigation in this case broadly confirmed that the market for injectable NSAIDs would be multispecies. However, a distinction might be drawn between large animals (production animals such as cattle, horses and pigs) and small animals (companion animals such as dogs and cats) since products tend to have different concentrations and dosages depending on the animal's size and some of the Parties' products are used only for production animals (and one of Merial's product is even used for horses only). As a consequence, for specific specie (e.g. cattle), competition takes place between truly multi-species products and products authorized for use for this specie in particular (e.g. injectable NSAIDs for production animals such as cattle and swine).
- (158) For the purpose of assessing the Transaction, the exact relevant product market in relation to injectable NSAIDs can be left open, since the Transaction raises serious doubts as to its compatibility with the internal market in relation to injectable multispecies NSAIDs, irrespective of the exact segmentation of that market.

Oral NSAIDs

Notifying Party's views

- (159) In line with previous Commission decisions, the Notifying Party submits that orally administrated NSAIDs constitute a distinct product market.¹⁰³ The Notifying Party also refers to the Commission's previous practice of further segmenting oral NSAIDs by the animal species for which they are intended. Thus, the Notifying Party submits that oral NSAIDs for horses and oral NSAIDs for companion animals constitute distinct product markets.

¹⁰² Case M.4691, Schering-Plough/Organon Biosciences, decision of 11 October 2007, paragraph 305.

¹⁰³ Case M.4691 – Schering-Plough / Organon biosciences, paragraphs 303 to 306.

Commission's assessment

- (160) In line with the principles identified above the Commission has previously defined product markets for oral NSAIDs for horses and oral NSAIDs for dogs and cats.¹⁰⁴ The market investigation in this case confirmed this approach.
- (161) In addition, the market investigation indicated that COX and COXIB also compete from a customer's perspective. Although COXIBs would be marketed as safer, many customers expressed doubts as to this better safety profile.¹⁰⁵ It might however be a differentiating factor in particular for companion animals and horses (owners being more receptive to the safety argument).¹⁰⁶
- (162) For the purpose of assessing this Transaction, the relevant product markets are therefore the market for oral NSAIDs for horses and oral NSAIDs for pets.
- (163) Based on the above, the Transaction leads to overlaps between the Parties' activities in:
- i. injectable multiple species NSAIDs,
 - ii. oral NSAIDs for horses, and
 - iii. oral NSAIDs for pets.

IV.3.2.2. Competitive assessment

IV.3.2.2.a. Injectable multi-species NSAIDs

IV.3.2.2.a.i. Parties' products

- (164) BI sells its injectable NSAIDs under the brands Metacam and Novem. *Meloxicam* is the API of both brands of injectable NSAIDs. Metacam is licensed for use in several species and has different concentration and dosage depending on the animal's size: 40mg/ml for cattle and horses, 20mg/ml for cattle, pigs and horses, 5 mg/ml and 2 mg/ml for dogs and cats. Novem is licensed for use in cattle and swine only.

¹⁰⁴ Case M.4691 – Schering-Plough / Organon biosciences, para. 306.

¹⁰⁵ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 82.: "*COXIB would be safer*". See reply of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 82: "*originally marketed as safer alternative but Any advantages have not borne out in the market place.*" See reply of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 82: "*According to our opinion, the products are interchangeable. Left for individual preferences of a vet.*"

¹⁰⁶ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 39, responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 7. and responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 50.

- (165) Merial supplies four injectable NSAIDs: Ketofen, whose API is *ketoprofen*, used for multi-species and has different concentration and dosages depending on the animal's size: Ketofen 10% for horses, cattle and pigs and Ketofen 1% for dogs and cats only; Equioxx Injectable, whose API is *firocoxib*, used solely in horses; Wellicox/Allevinix and Genixine (France only), which are generics of *flunixin*, and are used in cattle, swine and horses.

IV.3.2.2.a.ii. Assessment

- (166) At the EEA level, BI is the leading player in injectable multispecies NSAIDs as well as NSAIDs for production animals, while Merial is second largest player.

Table 14 Parties' and competitors' share in injectable NSAIDs in the EEA in 2015 (multi-species and for production animals)

Company	Multi-species 2015	Production animals 2015
BI	[20-30]%	[20-30]%
Merial	[10-20]%	[10-20]%
Combined	[30-40]%	[40-50]%
MSD	[10-20]%	[5-10]%
Vetoquinol	[5-10]%	[10-20]%
Zoetis	[5-10] %	[5-10]%
Ceva	[5-10]%	[5-10]%
Norbrook	[5-10]%	[5-10]%
Virbac	[0-5]%	[0-5]%
Elanco	[0-5]%	-
Bayer	[0-5]%	[0-5]%
Total market size	EUR [70-75] million	EUR [45-50] million

Source: Form CO, CEESA data adjusted by generics/local products sales.

- (167) The Transaction gives rise to affected markets for multi species injectable NSAIDs in 14 EEA countries, namely Austria, Belgium, Denmark, France, Germany, Italy, Ireland, Lithuania, Netherlands, Norway, Poland, Slovakia, Sweden and UK.

**Table 15. Parties' and competitors' share for multi-species injectable NSAIDs in
2015**

EEA country	Year	BI	Merial	Combined	MSD	Zoetis	Veto-quinol	Market size (EUR 000)
DK	2015	[30-40]%	[0-5]%	[30-40]%	[5-10]%	[0-5]%	na	[4000-5000]
	2014	[40-50]%	[0-5]%	[40-50]%	[5-10]%	[0-5]%	na	[3000-4000]
	2013	[50-60]%	[0-5]%	[50-60]%	[5-10]%	[0-5]%	na	[3000-4000]
FR	2015	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[5-10]%	[20-30]%	[30000-31000]
	2014	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[5-10]%	[20-30]%	[31000-32000]
	2013	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[5-10]%	[20-30]%	[29000-30000]
DE	2015	[30-40]%	[5-10]%	[30-40]%	[0-5]%	[5-10]%	[0-5]%	[12000-13000]
	2014	[30-40]%	[0-5]%	[30-40]%	[0-5]%	[5-10]%	[0-5]%	[11000-12000]
	2013	[30-40]%	[0-5]%	[40-50]%	[0-5]%	[5-10]%	[0-5]%	[12000-13000]
IT	2015	[10-20]%	[10-20]%	[20-30]%	[10-20]%	[5-10]%	[5-10]%	[7000-8000]
	2014	[10-20]%	[10-20]%	[20-30]%	[10-20]%	[10-20]%	[5-10]%	[8000-9000]
	2013	[10-20]%	[10-20]%	[20-30]%	[10-20]%	[10-20]%	[5-10]%	[7000-8000]
IE	2015	[40-50]%	[0-5]%	[40-50]%	[5-10]%	[0-5]%	[5-10]%	[1000-2000]
	2014	[40-50]%	[5-10]%	[40-50]%	[10-20]%	[0-5]%	[10-20]%	[1000-2000]
	2013	[30-40]%	[5-10]%	[40-50]%	[5-10]%	[0-5]%	[10-20]%	[1000-2000]
LT	2015	[5-10]%	[10-20]%	[20-30]%	[0-5]%	[70-80]%	[0-5]%	[0-1000]
	2014	[10-20]%	[10-20]%	[20-30]%	[0-5]%	[70-80]%	[0-5]%	[0-1000]
	2013	[5-10]%	[0-5]%	[5-10]%	[0-5]%	[90-100]%	[0-5]%	[0-1000]
NL	2015	[30-40]%	[5-10]%	[40-50]%	[5-10]%	[5-10]%	[0-5]%	[3000-4000]
	2014	[30-40]%	[10-20]%	[40-50]%	[0-5]%	[5-10]%	[0-5]%	[3000-4000]
	2013	[20-30]%	[5-10]%	[30-40]%	[0-5]%	[10-20]%	[0-5]%	[3000-4000]
NOR	2015	[60-70]%	[0-5]%	[60-70]%	[10-20]%	[0-5]%	na	[0-1000]
	2014	[50-60]%	[0-5]%	[50-60]%	[10-20]%	[10-20]%	na	[0-1000]
	2013	[50-60]%	[5-10]%	[60-70]%	[20-30]%	[5-10]%	na	[0-1000]
PL	2015	[10-20]%	[5-10]%	[20-30]%	[0-5]%	[20-30]%	[30-40]%	[1000-2000]
	2014	[10-20]%	[5-10]%	[20-30]%	[0-5]%	[10-20]%	[50-60]%	[1000-2000]
	2013	[10-20]%	[5-10]%	[20-30]%	[5-10]%	[5-10]%	[50-60]%	[0-1000]
SK	2015	[20-30]%	[10-20]%	[30-40]%	[5-10]%	[40-50]%	na	[0-1000]
	2014	[30-40]%	[10-20]%	[40-50]%	[5-10]%	[20-30]%	na	[0-1000]
	2013	[20-30]%	[20-30]%	[40-50]%	[10-20]%	[20-30]%	na	[0-1000]
SE	2015	[50-60]%	[0-5]%	[50-60]%	[10-20]%	[5-10]%	[0-5]%	[1000-2000]
	2014	[60-70]%	[0-5]%	[70-80]%	[10-20]%	[0-5]%	[0-5]%	[1000-2000]
	2013	[50-60]%	[5-10]%	[60-70]%	[10-20]%	[5-10]%	[5-10]%	[1000-2000]
UK	2015	[50-60]%	[5-10]%	[50-60]%	[0-5]%	[0-5]%	[0-5]%	[17000-18000]
	2014	[50-60]%	[5-10]%	[50-60]%	[5-10]%	[0-5]%	[0-5]%	[16000-17000]
	2013	[50-60]%	[5-10]%	[50-60]%	[5-10]%	[0-5]%	[0-5]%	[15000-16000]

Source: Form CO, CEESA data adjusted by Merial's actual sales, CEESA data adjusted by BI's estimates, AIEMV data, GfK data.¹⁰⁷

- (168) The Transaction gives rise to affected markets in 16 EEA countries for injectable for production animals (truly multispecies NSAIDs and multispecies used for production animals, namely cattle, swine and horses), which cover the same affected countries as multispecies injectable overall (all injectable NSAIDs) excluding Lithuania and including Greece, Hungary and Spain.

Table 16. Parties' and competitors' share for injectable NSAIDs for production animals

EEA country	Year	BI	Merial	Combi - ned	Vetoqui nol	MSD	Zoetis	Virbac	Market size (EUR 000)
FR	2015	[20-30%]	[20-30]%	[50-60]%	[20-30]%	[5-10]%	[5-10]%	[0-5]%	[10000-11000]
	2014	[10-20]%	[30-40]%	[40-50]%	[20-30]%	[5-10]%	[5-10]%	[0-5]%	[13000-14000]
	2013	[20-30]%	[20-30]%	[50-60]%	[20-30]%	[5-10]%	[5-10]%	[0-5]3%	[12000-13000]
DE	2015	[50-60]%	[0-5]%	[60-70]%	[0-5]%	[5-10]%	[10-20]%	[0-5]%	[4000-5000]
	2014	[50-60]%	[5-10]%	[60-70]%	[0-5]%	[5-10]%	[10-20]%	[0-5]%	[4000-5000]
	2013	[50-60]%	[10-20]%	[60-70]%	[0-5]%	[5-10]%	[5-10]%	[0-5]%	[4000-5000]
IE	2015	[30-40]%	[10-20]%	[40-50]%	[5-10]%	[10-20]%	[0-5]%	/	[1000-2000]
	2014	[30-40]%	[10-20]%	[40-50]%	[5-10]%	[10-20]%	[0-5]%	/	[1000-2000]
	2013	[30-40]%	[10-20]%	[40-50]%	[10-20]%	[10-20]%	[0-5]%	/	[1000-2000]
NL	2015	[40-50]%	[5-10]%	[40-50]%	[0-5]%	[0-5]%	[5-10]%	[0-5]%	[2000-3000]
	2014	[30-40]%	[10-20]%	[40-50]%	[0-5]%	[0-5]%	[10-20]%	[0-5]%	[3000-4000]
	2013	[30-40]%	[10-20]%	[40-50]%	[0-5]%	[0-5]%	[10-20]%	[0-5]%	[3000-4000]

EEA country	Year	BI	Merial	Combi - ned	Vetoquinol	MSD	Zoe tis	Virbac	Market size (EUR 000)
NOR	2015	[60-70]%	[0-5]%	[60-70]%	/	[10-20]%	[0-5]%	/	[0-1000]
	2014	[50-60]%	[0-5]%	[50-60]%	/	[10-20]%	[5-10] %	/	[0-1000]
	2013	[50-60]%	[0-5]%	[50-60]%	/	[10-20]%	[0-5]%	/	[0-1000]
SE	2015	[30-40]%	[0-5]%	[30-40]%	[0-5]%	[10-20]%	[0-5]%	/	[1000-2000]
	2014	[50-60]%	[0-5]%	[50-60]%	[0-5]%	[5-10]%	[0-5]%	/	[1000-2000]
	2013	[40-50]%	[5-10]%	[50-60]%	[5-10]%	[5-10]%	[5-10] %	/	[1000-2000]
UK	2015	[50-60]%	[5-10]%	[50-60]%	[0-5]%	[5-10]%	[0-5]%	[0-5]%	[10000-11000]
	2014	[50-60]%	[5-10]%	[60-70]%	[0-5]%	[5-10]%	[0-5]%	[0-5]%	[10000-11000]
	2013	[50-60]%	[5-10]%	[50-60]%	[0-5]%	[5-10]%	[0-5]%	[0-5]%	[9000-10000]
AT	2015	[10-20]%	[5-10]%	[20-30]%	[30-40]%	20-30%	[10-20] %	[0-5]%	[0-1000]
	2014	[10-20]%	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[5-10] %	[0-5]%	[0-1000]
	2013	[20-30]%	[10-20]%	[30-40]%	[40-50]%	[20-30]%	[5-10] %	[0-5]%	[0-1000]
BE	2015	[10-20]%	[10-20]%	[20-30]%	[50-60]%	[10-20]%	[5-10] %	[0-5]%	[2000-3000]
	2014	[10-20]%	[5-10]%	[20-30]%	[50-60]%	[10-20]%	[5-10] %	[0-5]%	[2000-3000]
	2013	[20-30]%	[0-5]%	[20-30]%	[40-50]%	[10-20]%	[5-10] %	[0-5]%	[2000-3000]
EL	2015	[10-20]%	[5-10]%	[20-30]%	/	[40-50]%	[20-30] %	/	[0-1000]
	2014	[10-20]%	[5-10]%	[20-30] %	/	[40-50]%	[20-30] %	/	[0-1000]
	2013	[5-10]%	[5-10]%	[10-20]%	/	[50-60]%	[10-20] %	/	[0-1000]
HU	2015	[10-20]%	[10-20]%	[20-30]%	[0-5]%	[10-20]%	[10-20] %	[5-10] %	[0-1000]
	2014	[10-20]%	[10-20]%	[20-30] %	[0-5] %	[20-30] %	[20-30] %	[10-20] %	[0-1000]
	2013	[10-20] %	[10-20] %	[20-30] %	[5-10] %	[10-20] %	[20-30] %	[10-20] %	[0-1000]
IT	2015	[5-10] %	[10-20] %	[20-30] %	[0-5] %	[5-10] %	[5-10] %	[0-5] %	[7000-8000]

	2014	[10-20]%	[20-30]%	[30-40]%	[5-10]%	[10-20]%	[5-10] %	[0-5]%	[5000-6000]
	2013	[10-20]%	[10-20]%	[30-40]%	[5-10]%	[10-20]%	[5-10] %	[0-5]%	[4000-5000]
PL	2015	[20-30]%	[5-10]%	[20-30]%	[30-40]%	[0-5]%	[30-40] %	/	[1000-2000]
	2014	[10-20]%	[5-10]%	[20-30]%	[50-60]%	[0-5]%	[10-20] %	/	[0-1000]
	2013	[10-20]%	[5-10]%	[20-30]%	[50-60]%	[0-5]%	[5-10] %	/	[0-1000]
SK	2015	[10-20]%	[10-20]%	[30-40]%	/	[5-10] %	[40-50] %	/	[0-1000]
	2014	[20-30]%	[10-20]%	[40-50]%	/	[0-5] %	[20-30] %	/	[0-1000]
	2013	[20-30]%	[10-20]%	[40-50]%	/	[10-20] %	[20-30] %	/	[0-1000]
ES	2015	[10-20]%	[0-5] %	[20-30] %	[10-20] %	[10-20] %	[10-20] %	[0-5] %	[3000-4000]
	2014	[10-20] %	[5-10] %	[20-30] %	[10-20] %	[10-20] %	[10-20] %	[0-5] %	[3000-4000]
	2013	[10-20] %	[5-10] %	[20-30] %	[20-30] %	[10-20] %	[10-20] %	[0-5] %	[3000-4000]
DK	2015	[30-40] %	[0-5] %	[30-40] %	/	[0-5] %	[0-5] %	/	[2000-3000]
	2014	[30-40] %	[0-5] %	[30-40] %	/	[0-5] %	[0-5] %	/	[3000-4000]
	2013	[60-70] %	[0-5] %	[60-70] %	/	[5-10] %	[0-5] %	/	[2000-3000]

Source: Form CO, CEESA data, CEESA data adjusted by BI's estimates, GfK data

The Notifying Party's view

- (169) The Notifying Party submits that the Parties' combined market shares for any of the hypothetical injectable NSAID markets do not accurately reflect the true nature of competition on the market notably for the following reasons.
- (170) First, the Notifying Party argues its NSAIDs and Merial's NSAIDs are not closest competitors because they contain different molecules and an originator drug's closest competitor on the market is always the generic products that contain the same API. Second, the Notifying Party mentions significant competition on the market coming from MSD, Zoetis, Vetoquinol and Ceva.

The Commission's assessment

- (171) In line with the market share data submitted by the Notifying Party, the market investigation confirmed that BI's Metacam is the leading brand in the EEA and across

EEA countries.¹⁰⁸ Metacam benefits from very strong brand recognition. This is confirmed by BI's internal document where it is stated that "*Metacam is the world leading NSAID for the control of inflammation and pain in farm animals [...] Metacam is and will remain the major global NSAID brand on the market.*"¹⁰⁹ The market investigation confirmed also Merial's strong position, number 2 at EEA level and among the top suppliers across EEA countries, with its products Ketofen and Equioxx.¹¹⁰

- (172) The market investigation generally indicated the importance of branded products, as compared to generics.¹¹¹ Indeed, Customers appear reluctant to consider generic as fully substitutable to originators as they experience issues with generics such as imprecise dosages. By way of example, one veterinarian indicated that "*original products guarantee content and efficacy, based on long term experience. Copies often are experienced to have varying effects.*"¹¹²
- (173) As to competitors active in the market, the market investigation indicated that they have weaker brands; MSD's Finadyna/Banamine (*flunixin*) product would be less efficacious¹¹³ and Vetoquinol, Zoetis and Ceva's products generally have market shares of less than 10% in affected markets.
- (174) Furthermore, BI's Metacam and Merial's Ketofen would be the only two products with label claims for pain management. One market participant explained that "*although all products have similar mechanisms of action, some have more complete set of label claims. For instance: Metacam and Ketofen are the only products with specific label claims for the management of pain.*"¹¹⁴
- (175) The market investigation also provided indications that Merial tends to be cheaper than BI's strong brand and thus post-merger price increases are expected. In this context a customer explained that "*merial is very aggressive with price. I don't think this will be the BI politics.*"¹¹⁵ Similarly, other market participants expressed concerns about a price increase post-Transaction¹¹⁶ one of which for instance stated there is a "*risk of price increase due to significant market share of BI/Merial combined products.*"¹¹⁷
- (176) As a result, the Transaction will eliminate actual competition in injectable NSAIDs in all 17 EEA countries where both Parties are active, where the Parties generated almost

¹⁰⁸ Responses to Questionnaire Q1 to competitors of 8 June 2016, question 88.

¹⁰⁹ BI internal document, [...].

¹¹⁰ Responses to Questionnaire Q5 to Horses customers of 8 June 2016, question 16.

¹¹¹ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, questions 36 and 37, responses to Questionnaire Q2 to Swine customers of 7 June 2016, questions 47 and 48 and responses to Questionnaire Q1 to competitors of 8 June 2016, questions 84 and 85.

¹¹² See reply of a customer to Questionnaire Q5 to Horses customers of 8 June 2016, question 6.

¹¹³ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 52.

¹¹⁴ Responses to Questionnaire Q1 to competitors, question 78.

¹¹⁵ Responses to Questionnaire Q2 to Swine customers, question Q66.

¹¹⁶ Responses to Questionnaire Q2 to Swine customers, question Q66.

¹¹⁷ Responses to Questionnaire Q2 to Swine customers, question Q66.

[90-100]% of their EEA sales in multispecies injectable NSAIDs, as well as potential competition in other EEA countries where the two Parties are natural entrants.

- (177) In view of the above, the Transaction raises serious doubts as to its compatibility with the internal market in relation to injectable NSAIDs in the EEA in general and in Austria, Belgium, Denmark, Italy, Lithuania, France, Germany, Greece, Hungary, Ireland, the Netherlands, Norway, Poland, Spain, the UK, Slovakia and Sweden in particular.

IV.3.2.2.b. Oral NSAIDs for horses

IV.3.2.2.b.i. Parties' products

- (178) BI sells its orally administered NSAIDs for horses under the brand Metacam Horse. Metacam Horse is based on *meloxicam*. Metacam is a COX product.
- (179) Merial's product is marketed under the brand Equioxx Paste. Equioxx Paste is an orally administered NSAID based on *firocoxib*. Equioxx Paste is a COXIB.

(180) The Transaction gives rise to affected markets for oral NSAIDs for horses in 9 EEA countries.

Table 17. Parties' and competitors' share for oral NSAIDs for horses

EEA country	Year	BI	Merrial	Combined	MSD	Virbac	Zoetis	Market size (EUR 000)
AT	2015	[50-60]%	[5-10]%	[60-70]%	-	[20-30]%	[10-20]%	[0-1000]
	2014	[70-80]%	[0-5]%	[70-80]%	-	[10-20]%	[5-10]%	[0-1000]
	2013	[70-80]%	[20-30]%	[90-100]%	-	[0-5]%	[5-10]%	[0-1000]
BE	2015	[10-20]%	[10-20]%	[30-40]%	[20-30]%	[20-30]%	[0-5]%	[0-1000]
	2014	[10-20]%	[10-20]%	[20-30]%	[20-30]%	[20-30]%	[0-5]%	[0-1000]
	2015	[20-30]%	[20-30]%	[40-50]%	[20-30]%	[5-10]%	[0-5]%	[0-1000]
DK	2015	[40-50]%	[0-5]%	[40-50]%	[20-30]%	[10-20]%	[0-5]%	[0-1000]
	2014	[40-50]%	[0-5]%	[40-50]%	[20-30]%	[20-30]%	[0-5]%	[0-1000]
	2013	[40-50]%	[5-10]%	[40-50]%	[20-30]%	[20-30]%	[0-5]%	[0-1000]
FI	2015	[50-60]%	[0-5]%	[60-70]%	[0-5]%	/	[0-5]%	[0-1000]
	2014	[40-50]%	[0-5]%	[40-50]%	[10-20]%	/	[0-5]%	[0-1000]
	2013	[50-60]%	[5-10]%	[50-60]%	[5-10]%	/	[0-5]%	[0-1000]
FR	2015	[10-20]%	[5-10]%	[20-30]%	[5-10]%	[5-10]%	[10-20]%	[2000-3000]
	2014	[10-20]%	[5-10]%%	[20-30]%	[5-10]%	[5-10]%	[5-10]%	[2000-3000]
	2013	[10-20]%	[5-10]%%	[20-30]%	[5-10]%%	[5-10]%%	[0-5]%	[2000-3000]
DE	2015	[30-40]%	[5-10]%%	[30-40]%	[10-20]%	[5-10]%%	[0-5]%	[7000-8000]
	2014	[30-40]%	[5-10]%%	[40-50]%	[5-10]%%	[5-10]%%	[0-5]%	[6000-7000]
	2013	[30-40]%	[5-10]%%	40-50]%	[5-10]%%	[0-5]%	[0-5]%	[6000-7000]
NL	2015	[80-90]%	[0-5]%	[80-90]%	/	[0-5]%	[10-20]%	[0-1000]
	2014	[80-90]%	[0-5]%	[80-90]%	/	[0-5]%	[10-20]%	[0-1000]
	2013	[70-80]%	[0-5]%	[80-90]%	/	[0-5]%	[5-10]%%	[0-1000]
NOR	2015	[70-80]%	[0-5]%	[80-90]%	[0-5]%	/	[5-10]%%	[0-1000]
	2014	[80-90]%	[0-5]%	[80-90]%	[0-5]%	/	[5-10]%%	[0-1000]
	2013	[70-80]%	[0-5]%	[70-80]%	[0-5]%	/	[5-10]%%	[0-1000]
SE	2015	[70-80]%	[0-5]%	[80-90]%	[0-5]%	[0-5]%	[0-5]%	[2000-3000]
	2014	[60-70]%	[0-5]%	[60-70]%	[10-20]%	[0-5]%	[0-5]%	[2000-3000]
	2013	[50-60]%	[0-5]%	[60-70]%	[10-20]%	[0-5]%	[0-5]%	[2000-3000]

The Notifying Party's view

- (181) The Notifying Party submits that the merged entity will face significant competitive pressure across all of its product lines from global, regional and national originator manufacturers and generic suppliers.
- (182) The Notifying party also claims that BI's and Merial's products are not closest competitors, for the following reasons. The Notifying Party points out that:
- (i) Metacam is for short term use, whereas Equioxx is used for long term use,
 - (ii) Metacam is a non-COXIB NSAID, whereas Equioxx is a COXIB, which is an important distinction for veterinarians,
 - (iii) Metacam has a very short detection time whereas Equioxx has a longer detection time,
 - (iv) Metacam is predominantly used for treatment of acute and chronic pain as well as during colic, whereas Equioxx focuses on (long-term) treatment, a chronic condition.

The Commission's assessment

- (183) The market investigation confirmed the leading position of BI's Metacam Horse at EEA level and across EEA countries. Metacam Horse benefits from very strong brand recognition. For instance, a veterinary specialized in horses stated that it is "*Top product for anti-inflammatory joint treatment, safety and brand recognition*".¹¹⁹ This is also confirmed in BI's internal documents. As an example, a BI internal document states that "*Metacam is the original top of mind brand in the main countries. Horse owners also know Metacam very well and ask for it*".¹²⁰
- (184) The market investigation as well as BI's internal documents also showed that Merial's Equioxx although having a more limited market share across the EEA is a strong competitor to BI. For instance a BI internal document states that "*Equioxx (Merial), a firocoxib, is a very strong competitor for us as well [as generics] [...] Equioxx [Merial] has increasing market share*".¹²¹ Merial tends in particular to use the COXIB nature of Equioxx (*firocoxib*) to gain market shares. BI noted in internal documents that "*Merial is branding Equioxx strongly (the new "modern" NSAID has a better efficacy and is safer)*".¹²² In addition, in some EEA countries, such as Sweden, Norway and the Netherlands, Merial's Equioxx is among very few products to compete with BI's leading branded product, which would lead to a combined market share post-Transaction of [80-90]% or more.

¹¹⁸ Market share table, Form CO, p. 66-67 and Annexes A.11 and A.12 to the Form CO.

¹¹⁹ Response of a customer to Questionnaire Q5 to Horses customers of 8 June 2016, question 17.

¹²⁰ BI internal document, [...].

¹²¹ BI internal document, [...].

¹²² BI internal document, [...].

- (185) Finally, some market participants expressed concern about a price increase post-Transaction,¹²³ one of them mentioning that "*the newly combined entity would control the top brand name premium priced equine NSAIDs.*"¹²⁴
- (186) As a result, the Transaction will eliminate actual competition in all countries where the Parties are currently active, where the Parties generated almost [90-100]% of their EEA turnover, as well as potential competition in other EEA countries where the two Parties are natural entrants.
- (187) In view of the above, the Transaction raises serious doubts as to its compatibility with the internal market in relation to oral NSAIDs for horses in the EEA in general and in Austria, Belgium, Denmark, Finland, France, Germany, the Netherlands, Norway and Sweden in particular.

IV.3.2.2.c. Oral NSAIDs for pets

IV.3.2.2.c.i. *Parties' products*

- (188) BI sells its orally administered NSAIDs for pets under the brands Metacam Oral Suspension for Dogs, Metacam Chewable Tablets for Dogs and Metacam Oral Suspension for Cats. BI's Metacam products are all based on *meloxicam*.
- (189) Merial's products are marketed under the brands Previcox CPR and Ketofen CPR. Previcox is used for dogs, it contains the API *firocoxib*, and is a COXIB. Ketofen CPR is used for dogs and cats, and is based on *ketoprofen*.

IV.3.2.2.d. Assessment

- (190) The Transaction gives rise to affected markets for oral NSAIDs for pets in 12 EEA countries.

¹²³ Responses to Questionnaire Q1 to competitors of 8 June 2016, question 119.

¹²⁴ Response of a competitor to Questionnaire Q1 to competitors of 8 June 2016, question 119.

Table 18. Parties' and competitors' share for oral NSAIDs for pets

EEA country	Year	BI	Merial	Combine d	Zoetis	Ceva	Norbro ok	Elanco	Market size (EUR 000)
DK	2015	[30-40]%	[5-10]%	[40-50]%	[10-20]%	[10-20]%	na	[20-30]%	[2000-3000]
	2014	[30-40]%	[10-20]%	[40-50]%	[10-20]%	[10-20]%	na	[10-20]%	[2000-3000]
	2013	[30-40]%	[10-20]%	[50-60]%	[10-20]%	[10-20]%	na	[10-20]%	[2000-3000]
FR	2015	[30-40]%	[10-20]%	[40-50]%	[10-20]%	[10-20]%	na	[5-10]%	[18000-19000]
	2014	[30-40]%	[10-20]%	[40-50]%	[10-20]%	[10-20]%	na	[5-10]%	[19000-20000]
	2013	[30-40]%	[10-20]%	[40-50]%	[10-20]%	[10-20]%	na	[5-10]%	[18000-19000]
DE	2015	[20-30]%	[10-20]%	[30-40]%	[20-30]%	[5-10]%	[0-5]%	[5-10]%	[25000-26000]
	2014	[20-30]%	[10-20]%	[30-40]%	[20-30]%	[0-5]%	[0-5]%	[5-10]%	[24000-25000]
	2013	[20-30]%	[10-20]%	[30-40]%	[20-30]%	[0-5]%	[0-5]%	[5-10]%	[22000-23000]
EL	2015	[20-30]%	[10-20]%	[30-40]%	[30-40]%	[0-3]%	na	[5-10]%	[0-1000]
	2014	[20-30]%	[5-10]%	[30-40]%	[30-40]%	[0-5]%	na	[5-10]%	[0-1000]
	2013	[20-30]%	[5-10]%	[30-40]%	[30-40]%	[0-5]%	na	[5-10]	[0-1000]
IE	2015	[30-40]%	[5-10]%	[40-50]%	[10-20]%	[0-5]%	[10-20]%	[5-10]%	[1000-2000]
	2014	[30-40]%	[0-5]%	[40-50]%	[10-20]%	0%	[5-10]	[10-20]	[1000-2000]
	2013	[40-50]%	[0-5]%	[40-50]	[10-20]	[0-5]	[10-20]	[5-10]	[1000-2000]
IT	2015	[20-30]%	[20-30]	[40-50]	[30-40]	[0-5]	na	[10-20]	[10000-11000]
	2014	[10-20]	[20-30]	[40-50]	[30-40]	[0-5]	na	[10-20]	[9000-10000]
	2013	[10-20]	[20-30]	[40-50]	[30-40]	[0-5]	na	[10-20]	[8000-9000]
LV	2015	[0-5]	[50-60]	[50-60]	na	[0-5]	[30-40]	na	[0-1000]
	2014	[5-10]	[60-70]	[70-80]	na	[0-5]	[20-30]	na	[0-1000]
	2013	[20-30]	[50-60]	[70-80]	na	[0-5]	[10-20]	na	[0-1000]
NOR	2015	[30-40]	[5-10]	[30-40]	[30-40]	na	na	[20-30]	[2000-3000]
	2014	[30-40]	[5-10]	[40-50]	[30-40]	na	na	[10-20]	[2000-3000]
	2013	[30-40]	[5-10]	[40-50]	[30-40]	na	na	[10-20]	[2000-3000]
PT	2015	[5-10]	[40-70]	[50-60]	[10-20]	[5-10]	na	[10-20]	[0-1000]
	2014	[5-10]	[30-40]	[40-50]	[20-30]	[5-10]	na	[10-20]	[0-1000]
	2013	na	na	na	na	na	na	na	na
ES	2015	[10-20]	[30-40]	[40-50]	[10-20]	[5-10]	[0-5]	[5-10]	[7000-8000]
	2014	[10-20]	[20-30]	[40-50]	[20-30]	[5-10]	[0-5]	[5-10]	[6000-7000]
	2013	[10-20]	[20-30]	[40-50]	[20-30]	[0-5]	[0-5]	[5-10]	[6000-7000]

EEA country	Year	BI	Merial	Combine d	Zoetis	Ceva	Norbrook	Elanco	Market size (EUR 000)
SE	2015	[30-40]%	[5-10]%	[40-50]%	[20-30]%	[0-5]%	na	[5-10]%	[6000-7000]
	2014	[30-40]%	[5-10]%	[40-50]%	[30-40]%	[0-5]%	na	[5-10]%	[6000-7000]
	2013	[30-40]%	[5-10]%	[40-50]%	[30-40]%	[0-5]%	na	[0-5]%	[5000-6000]
UK	2015	[40-50]%	[10-20]%	[50-60]%	[10-20]%	[5-10]%	[20-30]%	[5-10]%	[44000-45000]
	2014	[30-40]%	[10-20]%	[40-50]%	[10-20]%	[5-10]%	[10-20]%	[0-5]%	[40000-41000]
	2013	[40-50%]	[10-20]%	[50-60]%	[10-20]%	[5-10]%	[20-30]%	[5-10]%	[36000-37000]

Source: Form CO, CEESA data, CEESA data adjusted by BI's estimates, AIEMV data, CEESA data adjusted by Merial's actual sales and GfK data.¹²⁵

The Notifying Party's view

- (191) The Notifying party submits that the Parties' combined market shares do not accurately reflect the true nature of competition on the market, for the following reasons. First, the Notifying party argues that Zoetis and Ceva will exercise significant competitive constraint post-merger. The Notifying party adds that this market is highly genericised, with players such as Elanco.
- (192) Second, the Notifying party explains that BI and Merial's oral NSAIDs are not closest competitors. In this regard the Notifying Party points out that Metacam is provided as an oral suspension whereas Previcox is sold in a tablet form. The Notifying Party further explains that Metacam is mainly used for small dogs whereas Previcox is used for large dogs. Finally, the Notifying Party explains that Metacam is frequently administered for short term use, whereas Previcox is administered for long term use.

The Commission's assessment

- (193) For oral NSAIDs for companion animals, there is no market leader across EEA countries. At the EEA level, BI is number 1, followed by Zoetis (number 2) and Merial (number 3).
- (194) BI, with its Metacam products, and Zoetis, with its Rymadil products, are both considered as leading players, while Merial is generally ranked as third.¹²⁶ Merial's market share was growing over the last three years, in particular due communication around its COXIB profile. This is confirmed by BI's internal documents, mentioning that "Merial was growing by [10-20]% achieving a MS of [10-20]% (mainly with safety image)."¹²⁷
- (195) The market investigation however provided indications that the Parties' products will continue to face important competitive constraints, in particular (depending on the market) from Zoetis, Elanco and Norbrook. In this context customers generally

¹²⁵ Market share table, Form CO, p. 74-78 and Annexes A.11 and A.12 to the Form CO.

¹²⁶ Responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 21.

¹²⁷ BI's internal presentation [...].

identified Zoetis Rimadyl as the leading player in the oral NSAIDs for companion animals market.¹²⁸ Several customers indicated that its products were "excellent" with regard to their safety and efficacy. Internal documents of BI also seem to confirm that Zoetis "*is still by far the market leader with 40% Market Share*"¹²⁹, has an "*efficacious product + added value services (Vet support...)*" and is together with Metacam a "*first choice*" product.¹³⁰ Ceva's products are also considered by many customers as having a good efficacy and safety profile, and would be close substitutes to BI's Metacam¹³¹.

- (196) In view of the above and all the evidence available to the Commission, the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to oral NSAIDs for companion animals.

IV.3.3. *Anti-microbials*

IV.3.3.1. **Market definition**

- (197) Antimicrobials are pharmaceutical products that belong to the general group of anti-infectives for systemic, local or topical use. They are used to destroy and prevent the growth of microbes such as bacteria, mycoplasma (pathogens that lack cell walls) and treat associated diseases.
- (198) In previous decisions,¹³² the Commission considered that the following factors could be relevant in defining product markets or influence the closeness of competition between antimicrobials:
- (i) active substance (sulphanomides, penicillins, cephalosporins, tetracyclines, etc.)
 - (ii) route of administration (injectable products, products for oral administration and products for topical administration such as intramammary mastitis treatments); and
 - (iii) animal's size (large animals such as horses, ruminants and swines and companion animals such as dogs and cats)
- (199) The Notifying party agrees with this general approach with regard to antimicrobials.
- (200) The overlap areas between the Parties in the antimicrobial segment concern mastitis treatment in dry and lactating cows. Mastitis treatments differ from other antimicrobials because of their singular mode of administration (generally intramammary) and the formulation of the drug that makes these products particularly effective against the relevant bacteria.

¹²⁸ Responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 21.

¹²⁹ BI's internal presentation [...].

¹³⁰ BI's internal presentation [...].

¹³¹ Responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 22.

¹³² Case M.5476 – Pfizer/Wyeth, paras. 324. Case COMP M. 4691-Schering-Plough/Organon Biosciences, paragraphs 325-346; Case COMP/M.2922-Pfizer/Pharmacia, paragraphs 122-123; Case COMP M. 1681-Akzo Nobel/Hoechst, paragraph 19.

- (201) In previous decisions,¹³³ the Commission found that there are two different types of mastitis infections, which belong to separate product markets.
- (i) Acute mastitis which most commonly occurs during the lactation period (i.e., when the cow is producing milk). Treatment requires daily and repeated administration of therapeutic formulations (lactating cow products'). The drugs must produce results quickly and have a carefully controlled time of effectiveness as the milk must be discarded during the period in which the drug is active;
 - (ii) Chronic infections (or sub-clinical mastitis) cause an increased number of white blood cells in the milk (somatic cells), but do not have any obvious clinical symptoms. Sub-clinical mastitis is typically treated during the days of the year when the cow is not milked (the so-called dry period).
- (202) The Notifying party agrees with this approach. The distinction between treatment for dry and lactating cows was also confirmed by the market investigation.¹³⁴
- (203) Therefore, the Commission considers that for the purposes of this Transaction, the relevant product markets are (i) mastitis treatment for lactating cows and (ii) mastitis treatment for dry cows.

IV.3.3.2. Parties' products

IV.3.3.2.a. Parties' products for mastitis treatment for lactating cows

- (204) BI sells its products for the treatment of mastitis in lactating cows under the brand Ubrolexin. The product is used for treatment of bacteria susceptible to the combination of cefalexin and kanamycin such as *Staphylococcus aureus*, *Streptococcus dysgalactiae*, *Streptococcus uberis* and *Escherichia coli*.
- (205) Merial's products are marketed under the brands Cefovet and Mastipent. Cefovet's API is cefazolin, a first-generation cephalosporin antibiotic with a broad spectrum antibiotic indicated against both gram-negative and grampositive bacteria such as streptococci bacteria. Mastipent's APIs are ampicillin and cloxacillin. This product is indicated for the treatment of mastitis caused by a wide range of gram-positive and gramnegative bacteria, such as *Aerobacter aerogenes*, *Klebsiella* species, *Pseudomonas aeruginosa*, and *Escherichia coli*.

¹³³ M.4691 – *Schering-Plough / Organon biosciences*, 11.10.2007, para 341. M.2922 – Pfizer/Pharmacia, paragraphs 126-131 and 346. Case M.5476 – Pfizer/Wyeth, paras. 324 and following.

¹³⁴ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 55.

IV.3.3.2.b. Parties' products for mastitis treatment for dry cows

- (206) BI sells its product for the treatment of mastitis in dry cows under the brand Benestermycin/Ubrostar. The product's APIs are penethamate hydriodide, benethamine penicillin and framycetin sulphate. BI's product is used for treatment of subclinical mastitis at drying off, and the prevention of new bacterial infections of the udder during the dry period in dairy cows.
- (207) Merial's products are marketed under the brands Cloxamam, Cloxagel, Speciorlac and Cefovet DC. Cloxamam is a penicillin (cloxacillin benzathine) antibiotic indicated for dry cows and ewes for the sub-clinical or preventative treatment of infections of the udders. Cloxagel is a suspension containing cloxacillin benzathine and neomycin sulphate as its APIs. This product is used as treatment for infections of the udders and prevention of the new infections during the dry period. Speciorlac is a fixed-dose combination drug combining a macrolide antibiotic with an aminoglycoside antibiotic. It is indicated for dry cows for the subclinical and preventive treatment of infections of the udders. Finally, Cefovet DC is a first-generation cephalosporin antibiotic drug indicated for dry cows and ewes for the sub-clinical of preventive treatment of infections of the udders.

IV.3.3.3. **Competitive assessment**

- (208) At the EEA level, for both mastitis treatments for lactating cows and for dry cows, Zoetis and MSD are leading players, while BI is number 3 for lactating cows and number 4 in dry cows. Merial is a smaller player, with a market share of [0-5]% at EEA level.

Table 19. Parties' and competitors' share for mastitis treatment in lactating cows in the EEA

Company	2013	2014	2015
BI	[10-20]%	[10-20]%	[10-20]%
Merial	[0-5]%	[0-5]%	[0-5]%
Combined	[10-20]%	[10-20]%	[10-20]%
Zoetis	[30-40]%	[30-40]%	[30-40]%
MSD	[40-50]%	[30-40]%	[40-50]%
Virbac	[0-5]%	[0-5]%	[0-5]%
Norbrook	[0-5]%	[0-5]%	[0-5]%
Ceva	[0-5]%	[0-5]%	[0-5]%
Total market size	[75000-80000]	[80000-85000]	[80000-85000]

Source: Form CO, CEESA data

Table 20. Parties' and competitors' share for mastitis treatment in dry cows in the EEA

Company	2013	2014	2015
BI	[10-20]%	[10-20]%	[20-30]%
Merial	[0-5]%	[0-5]%	[0-5]%
Combined	[10-20]%	[10-20]%	[20-30]%
Zoetis	[20-30]%	[20-30]%	[20-30]%
MSD	[30-40]%	[30-40]%	[30-40]%
Virbac	[10-20]%	[10-20]%	[10-20]%
Norbrook	[0-5]%	[0-5]%	[0-5]%

Source: Form CO, CEESA data

(209) With regard to mastitis treatment for lactating cows, the Transaction gives rise to Group3 markets, in 3 EEA countries.

Table 21. Parties' and competitors' share for intra-mammary treatment for lactating cows

EEA country	Year	BI	Merial	Combined	MSD	Zoetis	Vir bac	Market size (EUR 000)
AT	2015	[10-20]%	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[10-20]%	[1000-2000]
	2014	[10-20]%	[10-20]%	[20-30]%	[30-40]%	[30-40]%	[10-20]%	[1000-2000]
	2013	[10-20]%	[10-20]%	[20-30]%	[30-40]%	[20-30]%	[10-20]%	[1000-2000]
BE	2015	[40-50]%	[0-5]%	[40-50]%	[30-40]%	[10-20]%	[5-10]%	[1000-2000]
	2014	[30-40]%	[0-5]%	[30-40]%	[40-50]%	[10-20]%	[5-10]%	[2000-3000]
	2013	[30-40]%	[0-5]%	[30-40]%	[40-50]%	[10-20]%	[5-10]%	[1000-2000]
DE	2015	[20-30]%	[5-10]%	[20-30]%	[30-40]%	[30-40]%	[5-10]%	[17000-18000]
	2014	[20-30]%	[5-10]%	[20-30]%	[40-50]%	[20-30]%	[5-10]%	[17000-18000]
	2013	[10-20]%	[5-10]%	[20-30]%	[40-50]%	[20-30]%	[0-10]	[17000-18000]

Source: Form CO, CEESA data adjusted by Merial's actual sales, CEESA data adjusted by BI's estimates¹³⁵

(210) With regard to mastitis treatment for dry cows, the overlaps of the transaction give rise to Group3 markets, in 2 EEA countries.

¹³⁵ Market share tables for Group 3 markets, Form CO, p. 113 and Annex A.12 to the Form CO.

Table 22. Parties' and competitors' share for intra-mammary treatment for dry cows

EEA country	Year	BI	Merial	Combined	Zoetis	Virbac	MSD	Market size (EUR 000)
AT	2015	[20-30]%	[0-5]%	[20-30]%	[40-50]%	[20-30]%	[5-10] %	[0-1000]
	2014	[20-30]%	[0-5]%	[20-30]%	[40-50]%	[20-30]%	[5-10] %	[0-1000]
	2013	[20-30]%	[0-5]%	[20-30]%	[40-50]%	[20-30]%	[10-20] %	[0-1000]
IT	2015	[20-30]%	[0-5]%	[30-40]%	[5-10]%	[20-30]%	[20-30] %	[6000-7000]
	2014	[20-30]%	[0-5]%	[30-40]%	[5-10]%	[20-30]%	[20-30] %	[6000-7000]
	2013	[30-40]%	[5-10] %	[30-40] %	[5-10] %	[20-30] %	[20-30] %	[5000-6000]

CEESA data for 2015 adjusted by third-party databases and BI's own estimate

Notifying Party's views

- (211) The Notifying Party submits that competition concerns with respect to intra-mammary treatment for mastitis for both lactating and dry cows can be excluded, as none of the overlaps at national level give rise to a Group 1 market. The Notifying Party also points out the minimal increment afforded by Merial to BI's existing position. The Notifying Party further mentions that there are a number of generic competitors on the market that will be able to exert competitive pressure the merged entity post-Transaction.
- (212) The Notifying Party also argues that the merged entity will continue to face significant competitive pressure post-Transaction, in particular MSD and Zoetis will exercise significant competitive constraint on all EEA markets. The Notifying Party adds that MSD and Zoetis will continue to be market leaders on all affected EEA markets.

Commission's assessment

- (213) The market investigation indicated that Merial is not seen as an important player on these markets and that its products do not have wide brand recognition. This is reflected in the relatively small increment afforded by Merial to BI in most markets.
- (214) In addition, the market investigation confirmed that MSD and Zoetis are very strong competitors to BI (as reflected in their market shares) with many respondents seeing MSD or Zoetis as the overall market leader for mastitis treatment for dry and/or

lactating cows¹³⁶. Virbac was also mentioned as the market leader for dry cows by some respondents¹³⁷.

- (215) In view of the above and of all the evidence available to the Commission, the Commission considers that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the market for mastitis treatment for lactating cows and the market for mastitis treatment for dry cows.

IV.3.4. *Specialty products: cardiopulmonary therapy for pets*

- (216) Speciality products target very specific conditions and do not easily fit into any other pharmaceutical category, mainly because they lack the significance that they enjoy in the human health sector. These products include certain niche products such as insulin or diuretics which relieve oedemas.
- (217) In the area of specialty products, the Parties' activities overlap in relation to cardiopulmonary for pets. The Commission has not previously assessed these types of pharmaceuticals.

IV.3.4.1. Market definition

- (218) Cardiopulmonary drugs for pets are used to address congestive heart failure disease. These drugs significantly improve clinical signs and extend the life expectancy of dogs and cats.

The Notifying Party's view

- (219) The Notifying Party submits that a distinction can be made between different modes of administration, such as oral and injectable formats, although cardiopulmonary drugs for pets are generally sold in oral format.
- (220) The Notifying Party further submits that cardiopulmonary treatment for pets generally consists in a combination of different classes of drugs which target different aspects of the disease, including in particular:
- (i) *Pimobendan* which increases the strength of the contraction of the heart and also acts to dilate blood vessels. Pimobendan also relaxes vascular smooth muscle and elicits modest arterial vasodilation;
 - (ii) *ACE inhibitors* which help block the activation of the reninangiotensin-aldosterone system (RAAS), which promotes fluid retention, vasoconstriction and myocardial and vascular remodelling;
 - (iii) *Diuretics* which help to remove the fluid build-up in or around the lungs once signs of congestive heart failure develop;
 - (iv) *Beta blockers* which slow down the heart rate and reduce the oxygen demand on the heart.

¹³⁶ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, questions 59 and 60.

¹³⁷ Responses to Questionnaire Q3 to Ruminants customers of 8 June 2016, question 60.

- (221) The Notifying Party submits that the large majority of pets are treated with a therapy called "triple therapy" that is composed of an ACE inhibitor, a positive inotrope (like Pimobendan) and a diuretic for dogs, and beta-blockers, an ACE inhibitor and a diuretic for cats.
- (222) In the view of the Notifying Party, this distinction does not impede substitutability between products to the extent that they would form separate relevant product markets, although the closest competitors tend to be other products from the same group. The Notifying Party thus submits that the relevant product market is the market for oral cardiopulmonary therapy drug for pets.

Commission's assessment

- (223) The market investigation confirmed the existence of different classes of medication within the cardiopulmonary therapy products. Moreover, several respondents to the market investigation also confirmed that ACE inhibitors and Pimobendans are not substitutable but complementary since they have different modes of action and different therapeutic effects¹³⁸.
- (224) The market investigation also provided indications that cardiopulmonary drugs are used together mainly within a triple therapy, or sometimes within a quadruple therapy which the addition of a spironolactone¹³⁹. According to one competitor, there is even a new trend on the market of cardiopulmonary for pets to produce a pill combining two or more active ingredients of the therapy¹⁴⁰.
- (225) In view of the above, ACE inhibitors for companion animals may constitute a separate relevant market. However, the precise product market definition with respect to cardiopulmonary therapy drugs for pets can be left open for the purpose of this decision as the Transaction does not raise serious doubts as to its compatibility with the internal market in relation to cardiopulmonary therapy drugs for pets irrespective of the precise product market definition.

IV.3.4.2. Parties' products

- (226) BI sells its products under the brands Benefortin, Vetmedin, Vetmedin Chewables and Vetmedin Injection. Benefortin is an angiotensin-converting-enzyme inhibitor (ACE inhibitor) licensed for the treatment of congestive heart failure in dogs and chronic renal insufficiency in cats. Benefortin contains benazepril hydrochloride as its API. Vetmedin is therapy medicine for canine congestive heart failure. Vetmedin belongs to the new class of heart treatments termed inodilators and is indicated for the management of the signs of mild, moderate, or severe congestive heart failure in dogs. Vetmedin's API is pimobendan and it is sold in injectable and chewable tablet form.
- (227) Merial's product is marketed under the brand Enacard which is an ACE inhibitor indicated for the treatment of mild, moderate and severe congestive heart failure in dogs. Enacard's API is enalapril maleate.

¹³⁸ Responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 34.

¹³⁹ Responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 32.

¹⁴⁰ Agreed minutes of a conference call held with a competitor dated 19 May 2016.

IV.3.4.3. Competitive assessment

(228) At the EEA level, BI is the largest supplier of cardiopulmonary therapy drugs for pets, while Merial is ranked seventh.

Table 23. Parties' and competitors' share in cardiopulmonary therapy drugs for pets in the EEA

	2013	2014	2015
BI	[30-40]%	[30-40]%	[30-40]%
Merial	[0-5]%	[0-5]%	[0-5]%
Combined	[40-50]%	[30-40]%	[30-40]%
Elanco	[30-40]%	[30-40]%	[30-40]%
Ceva	[10-20]%	[10-20]%	[10-20]%
MSD	[5-10]%	[5-10]%	[5-10]%
Dechra	[0-5]%	[0-5]%	[0-5]%
Vetoquinol	[0-5]%	[0-5]%	[0-5]%
Total market size	EUR [70-75] million	EUR[60-65] million	EUR [70-75] million

Source : Form CO, CEESA data

(229) The Transaction gives rise to affected markets for cardiopulmonary therapy drugs for pets in 9 EEA countries.

Table 24. Parties' and competitors' share for cardiopulmonary therapy drugs for pets in the EEA

EEA country	Year	BI	Merial	Combined	Elanco	Ceva	Market size (EUR 000)
IT	2015	[30-40]%	[0-5]%	[30-40]%	[30-40]%	[20-30]%	[8000-9000]
	2014	[30-40]%	[5-10]%	[40-50]%	[40-50]%	[10-20]%	[7000-8000]
	2013	[30-40]%	[5-10]%	[30-40]%	[40-50]%	[10-20]%	[7000-8000]
NL	2015	[50-60]%	[0-5]%	[50-60]%	[20-30]%	[5-10]%	[1000-2000]
	2014	[40-50]%	[0-5]%	[40-50]%	[30-40]%	[5-10]%	[1000-2000]
	2013	[30-40]%	[0-5]%	[40-50]%	[40-50]%	[5-10]%	[1000-2000]
SK	2015	[50-60]%	[0-5]%	[60-70]%	[0-5]%	[30-40]%	[0-1000]
	2014	[60-70]%	[0-5]%	[60-70]%	[0-5]%	[20-30]%	[0-1000]
	2013	[60-70]%	[0-5]%	[60-70]%	[10-20]%	[10-20]%	[0-1000]
CZ	2015	[60-70]%	[0-5]%	[60-70]%	[10-20]%	[10-20]%	[0-1000]
	2014	[50-60]%	[0-5]%	[50-60]%	[20-30]%	[10-20]%	[0-1000]
	2013	[50-60]%	[0-5]%	[50-60]%	[20-30]%	[5-10]%	[0-1000]
UK	2015	[40-50]%	[0-5]%	[40-50]%	[20-30]%	[10-20]%	[14000-15000]
	2014	[40-50]%	[0-5]%	[40-50]%	[30-40]%	[10-20]%	[11000-12000]
	2013	[40-50]%	[0-5]%	[40-50]%	[30-40]%	[10-20]%	[11000-12000]
BE	2015	[30-40]%	[0-5]%	[30-40]%	[20-30]%	[10-20]%	[4000-5000]
	2014	[30-40]%	[0-5]%	[30-40]%	[20-30]%	[10-20]%	[3000-4000]
	2013	[30-40]%	[0-5]%	[30-40]%	[30-40]%	[10-20]%	[3000-4000]
DE	2015	[30-40]%	[0-5]%	[40-50]%	[10-20]%	[20-30]%	[14000-15000]
	2014	[40-50]%	[0-5]%	[40-50]%	[10-20]%	[10-20]%	[13000-14000]
	2013	[40-50]%	[0-5]%	[40-50]%	[10-20]%	[10-20]%	[13000-14000]
FR	2015	[20-30]%	[0-5]%	[20-30]%	[20-30]%	[40-50]%	[4000-5000]
	2014	[20-30]%	[0-5]%	[30-40]%	[20-30]%	[30-40]%	[3000-4000]
	2013	[20-30]%	[5-10]%	[30-40]%	[30-40]%	[20-30]%	[3000-4000]
ES	2015	[30-40]%	[0-5]%	[30-40]%	[40-50]%	[20-30]%	[1000-2000]
	2014	[30-40]%	[0-5]%	[30-40]%	[40-50]%	[10-20]%	[1000-2000]
	2013	[30-40]%	[0-5]%	[30-40]%	[50-60]%	[10-20]%	[1000-2000]

Source, Form Co, CEESA data, CEESA data adjusted by Merial's own sales, CEESA data adjusted by BI's estimates¹⁴¹

¹⁴¹ Market share tables, Form CO, p. 119-120 and Annex C.12 to the Form CO.

Notifying Party's view

- (230) The Notifying Party submits that the Parties' combined market shares for cardiopulmonary therapy for pets would not reflect the dynamics of competition in these markets for the following reasons.
- (231) First, the Notifying Party claims that the Parties' products are not closest competitors since Pimobendan and ACE inhibitors are complementary and not substitutable products, even though they belong to the same CEESA category. As a result, the Parties' activities solely overlap as regards ACE inhibitors.
- (232) Second, the Notifying Party submits that the market for cardiopulmonary for pets will remain competitive post-Transaction since at least three strong competitors – namely Ceva, Elanco, MSD – will exert competitive constraints on the merged entity's products in all EEA markets. Moreover, a number of generic manufacturers such as Vetoquinol and Dechra have gained significant market shares in a short period of time and will continue to exert competitive constraint on the merged entity post-Transaction.

Commission's assessment.

- (233) As regards the market for cardiopulmonary for pets, BI's product Vetmedin is one of the premium EEA brands, which benefits from very strong brand recognition and is leading the market together with Elanco's Fortekor.¹⁴² Reversely, Merial's product Enacard has small market shares, thus its increment to BI's position is relatively low, at no more than [5-10]% in all of the affected markets. The market investigation also indicated that BI and Merial are not particularly close competitors¹⁴³.
- (234) The transaction gives rise to Group 1 markets in 9 EEA countries. Nevertheless, in all of those countries, there are at least two strong competitors, namely Elanco and Ceva, which exert significant competitive constraint on BI's product. In addition MSD exercises some competitive constraints in the Netherlands, as does Vetoquinol (a generic manufacturer) in the Czech Republic.
- (235) Moreover, the market investigation confirmed that BI's Vetmedin and Merial's Enacard are not close competitors, since one is a Pimobendan and the other an ACE inhibitor.
- (236) In view of the above and of all the evidence available to the Commission, the Commission considers that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to cardiopulmonary therapy drugs for pets.

IV.4. Animal feed supplements

- (237) Feed supplements are pharmaceutical or nutritional substances that are not natural feedstuffs and are added to made-up and stored feeds for various purposes but chiefly

¹⁴² Agreed minutes of a conference call held with a competitor dated 19 May 2016.

¹⁴³ Responses to Questionnaire Q4 to Companion Animals customers of 8 June 2016, question 39.

to control infectious disease or to promote growth. The Commission has previously considered markets for feed additives¹⁴⁴.

- (238) In the area of Animal feed Supplements, the Parties' activities overlap in relation nutritional feed supplements for osteoarthritis in cats and dogs. This area has not been previously analysed by the Commission.

IV.4.1. Market definition

Product market definition

- (239) Osteoarthritis or degenerative joint disease is a slowly progressive, low-grade inflammatory syndrome causing deterioration of articular cartilage (the “shock absorber”) osteophytosis (new bone formation) and sclerosis of the subchondral bone. Nutraceuticals promote joint health and do not treat osteoarthritis as such because they are mainly intended to slow the progression of primary osteoarthrosis.
- (240) The Notifying party makes a distinction by of species, target disease and method of application. The Notifying Party submits that the nutritional feed supplement for osteoarthritis in cats and dogs constitutes the narrowest possible product market.
- (241) In view of the fact that the Transaction does not raise serious doubts as to its compatibility with the internal market in relation to nutritional feed supplements for osteoarthritis in cats and dogs under any plausible market definition, the exact scope of the product market can be left open for the purposes of the competitive assessment of the Transaction.

Geographic market definition

- (242) In line with the principles mentioned at paragraph (145), the Commission has previously found that the relevant geographic market for animal health products, including feed additives, was national in scope.
- (243) The Notifying Party agrees with this approach, which was also confirmed by the market investigation.
- (244) In view of the above, animal feed supplements may constitute a separate relevant market. However, the precise product market definition with respect to animal feed supplements can be left open for the purpose of this decision as the Transaction does not raise serious doubts as to its compatibility with the internal market in relation to animal feed supplements irrespective of the precise product market definition.

IV.4.2. Parties' products

- (245) BI sells its joint nutritional feed supplement for pets under the brand Seraquin that is intended for support of normal joint function in cats and dogs. Seraquin’s active ingredients are glucosamine hydrochloride, chondroitin sulphate and turmeric extract (curcumin). The product is sold in a chewable tablet format.
- (246) Merial’s product is marketed under the brand Supleneo Flex that is used for the support of joint health in dogs. Supleneo Flex contains a combination of compounds

¹⁴⁴ M.5476 – Pfizer/Wyeth, 17.07.2009, para 123.

consisting of glucosamine hydrochloride, chondroitin sulphate and mixed tocopherols. Meril's product is also sold in a chewable tablet form.

IV.4.3. Competitive assessment

(247) The Transaction gives rise to affected markets for nutritional feed supplements for osteoarthritis in dogs in 3 EEA countries.

Table 25. Parties' and competitors' share for nutritional feed supplements for osteoarthritis in dogs

EEA country	Year	BI	Merial	Combined	Vetoquinol	Virbac	Elanco	Market size (EUR 000)
BE	2015	[30-40]%	[0-5]%	[30-40]%	[30-40]%	[10-20]%	[0-5]%	[1000-2000]
	2014	[30-40]%	[0-5]%	[30-40]%	[20-30]%	[10-20]%	[5-10]%	[0-1000]
	2013	[40-50]%	[0-5]%	[40-50]%	[10-20]%	[10-20]%	[5-10]%	[0-1000]
NL	2015	[10-20]%	[0-5]%	[10-20]%	[40-50]%	[20-30]%	[5-10]%	[0-1000]
	2014	[10-20]%	[0-5]%	[20-30]%	[20-30]%	[20-30]%	[20-30]%	[0-1000]
	2013	[20-30]%	[10-20]%	[30-40]%	[5-10]%	[20-30]%	[10-20]%	[0-1000]

Source: CEESA data , CEESA data adjusted by BI's estimates¹⁴⁵

Table 26. Parties' and competitors' share for nutritional feed supplements for osteoarthritis in dogs in the UK

EEA country	Year	BI	Merial	Combined	Vetoquinol	Vet Plus	Lintbells	Market size (EUR 000)
UK	2015	[20-30]%	[0-5]%	[20-30]%	[0-5]%	[20-30]%	[20-30]%	[9000-10000]
	2014	[30-40]%	[0-5]%	[30-40]%	[0-5]%	[10-20]%	[20-30]%	[9000-10000]
	2013	[30-40]%	[0-5]%	[30-40]%	[0-5]%	[5-10]%	[20-30]%	[8000-9000]

Source: GfK data

Notifying Party's view

(248) The Notifying Party submits that the overlaps between the Parties' activities on the market for nutritional feed supplements for osteoarthritis in cats and dogs will not give rise to any competition concerns for the following reasons.

(249) First, the Notifying Party claims that the market for nutritional feed supplements for osteoarthritis for cats and dogs is highly competitive. In this regard the Notifying Party notes that the CEESA data does not reflect the market reality as CEESA only provides data for the largest animal health companies who report it, whereas nutritional feed

¹⁴⁵ Annex C.12 to the Form CO.

supplements are generally commercialised by pharmaceuticals nutraceutical and pet food manufacturers.

- (250) Consequently, the Notifying Party estimates that the data provided by CEESA represents less than a third of the overall feed supplement market. To the Notifying Party's knowledge, at least six significant manufacturers of nutritional feed supplements are unaccounted for in the CEESA data.
- (251) Second, the market for nutritional feed supplements for osteoarthritis for cats and dogs is a fast developing market with quick entry since regulatory requirements are less burdensome in terms of time and expense than those of vaccines or pharmaceuticals, with no marketing authorisation needed.
- (252) Third, BI and Merial's products are not each other's closest substitutes since there are significant differences between their products with regard to composition and price.

Commission's assessment.

- (253) While BI is an important player on these markets, Merial is a very small player, with an increment of no more than [0-5]% in all of the affected markets.
- (254) The market investigation indicated that even though BI's Seraquin is one of the main premium brands, the market for nutritional feed supplements for osteoarthritis for cats and dogs is very competitive because products can be sold by veterinarians, pet shops, OTC or even supermarkets¹⁴⁶.
- (255) According to CEESA's limited data, at least three main competitors will exert competitive constraints on the merged entity post-Transaction (namely Vetoquinol, Virbac and Elanco, as well as Vet Plus and Lintbells in the UK). The Commission also notes that some of the market players have not been taken into account in CEESA's data and could also exert a constraint on BI's product.
- (256) In view of the above and of all the evidence available to the Commission, the Commission considers that the Transaction does not raise serious doubts as to its compatibility with the internal market with respect to nutritional feed supplements for osteoarthritis for cats and dogs.

IV.5. Conclusion of the Competitive assessment

- (257) In light of the above assessment, the Commission concludes that the Transaction raises serious doubts as to its compatibility with the internal market in relation to (i) monovalent PCV2 vaccines in the EEA (§(64)); (ii) monovalent PPRS vaccines in the EEA (§(99)); (iii) monovalent PPV vaccines in the EEA (§(115)); (iv) monovalent BVD vaccines in the EEA (§(138)); (v) injectable NSAIDs in the EEA (§(177)); (vi) oral NSAIDs for horses in the EEA (§(186)).

V. COMMITMENTS

- (258) In order to render the Transaction compatible with the internal market, the Parties have modified the Notified Transaction by entering into commitments.

¹⁴⁶ Agreed minutes of a conference call held with a competitor dated 19 May 2016.

V.1. Framework of assessment

- (259) As background, the following principles, as referred to in Commission Regulation (EC) No 802/2004, and in the Commission Notice on remedies acceptable under the Merger Regulation ("the Remedies Notice")¹⁴⁷, notably apply where the parties to a merger choose to offer commitments with a view to rendering the concentration compatible with the internal market.
- (260) Where the Commission finds that a concentration raises competition concerns in that it could significantly impede effective competition, in particular as a result of the creation or strengthening of a dominant position, the parties may seek to modify the concentration in order to resolve the competition concerns and thereby gain clearance of their merger.¹⁴⁸
- (261) Under the Merger Regulation, it is the responsibility of the Commission to demonstrate that a concentration would significantly impede effective competition. The Commission then communicates its competition concerns to the parties to allow them to formulate appropriate and corresponding remedies proposals. It is then for the parties to the concentration to put forward commitments.¹⁴⁹ The Commission only has power to accept commitments that are deemed capable of rendering the concentration compatible with the internal market so that they will prevent a significant impediment of effective competition in all relevant markets where competition concerns were identified.¹⁵⁰ To this end, the commitments have to eliminate the competition concerns entirely and have to be comprehensive and effective from all points of view.¹⁵¹
- (262) In assessing whether the proposed commitments will likely eliminate the competition concerns identified, the Commission considers all relevant factors including inter alia the type, scale and scope of the proposed commitments, judged by reference to the structure and particular characteristics of the market in which the competition concerns arise, including the position of the Notifying Party and other participants on the market.¹⁵²
- (263) A divested business has to include all the assets which contribute to its current operation or which are necessary to ensure its viability and competitiveness and all personnel which is currently employed or which is necessary to ensure the business' viability and competitiveness.¹⁵³
- (264) Commitments in Phase I can only be accepted where the competition concerns are readily identifiable and can be easily remedied. The remedies need to be so clear-cut that it is not necessary to enter into an in-depth investigation as to whether they are

¹⁴⁷ Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the "Remedies Notice"), OJ 2008/C 267/01.

¹⁴⁸ See Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the "Remedies Notice"), OJ 2008/C 267/01, paragraph 5.

¹⁴⁹ Remedies Notice, paragraph 6.

¹⁵⁰ Remedies Notice, paragraph 9.

¹⁵¹ Remedies Notice, paragraph 9 and 61.

¹⁵² Remedies Notice, paragraph 12.

¹⁵³ Remedies Notice, paragraph 25.

sufficient to rule out 'serious doubts' within the meaning of Article 6(1)(c) of the Merger Regulation.¹⁵⁴

- (265) As concerns the form of acceptable commitments, the Merger Regulation leaves discretion to the Commission as long as the commitments meet the requisite standard.¹⁵⁵ In general, structural commitments are the best way to eliminate competition concerns resulting from horizontal overlaps. Structural commitments will meet the conditions set out above only in so far as the Commission is able to conclude with the requisite degree of certainty that it will be possible to implement them and that it will be likely that the new commercial structures resulting from them will be sufficiently workable and lasting to ensure that effective competition will be maintained.¹⁵⁶
- (266) In this regard divested activities must consist of a viable business that, if operated by a suitable purchaser, can compete effectively with the merged entity on a lasting basis and that is divested as a going concern.¹⁵⁷ Normally, a viable business is a business that can operate on a stand-alone-basis, which means independently of the merging parties as regards the supply of input materials or other forms of cooperation other than during a transitory period.¹⁵⁸ The Commission has a clear preference for an existing stand-alone business. A divestiture consisting of a combination of certain assets which did not form a uniform and viable business in the past creates risks as to the viability and competitiveness of the resulting business. In such circumstances, the package must be sufficient to allow the Commission to conclude that the resulting business will be immediately viable in the hands of a suitable purchaser.¹⁵⁹
- (267) In addition, in order for the commitments to be effective, commitments must be capable of being implemented effectively within a short period of time as the conditions of competition will not be maintained until the commitments have been fulfilled.¹⁶⁰ The requisite degree of certainty concerning the implementation of the proposed commitments may in particular be affected by risks in relation to the transfer of a business to be divested.¹⁶¹ These risks are generally higher in cases when commitments concern the transfer of production processes and technologies.
- (268) It is against this background that the Commission assessed the viability, the workability, the effectiveness and the ability of the proposed commitments to entirely eliminate the competition concerns identified.

¹⁵⁴ Remedies Notice, paragraph 81.

¹⁵⁵ Case T-177/04 *easyJet v Commission* [2006] ECR II-1913, paragraph 197: "*Article 6(2) of Regulation No 4064/89 provides that the Commission may authorise a merger if the commitments proposed by the parties dispel the serious doubts as to the compatibility of the merger with the common market. Regulation No 4064/89 thus lays down the objective to be achieved by the Commission, but leaves it a wide discretion as to the form which the commitments in question may take.*"

¹⁵⁶ Remedies Notice, paragraph 10.

¹⁵⁷ Remedies Notice, paragraph 23.

¹⁵⁸ Remedies Notice, paragraph 32.

¹⁵⁹ Remedies Notice, paragraph 37.

¹⁶⁰ Remedies Notice, paragraph 9

¹⁶¹ Remedies Notice, paragraph 11.

V.2. Procedure

- (269) To remedy the serious doubts identified following the phase 1 market investigation, on 6 July 2016 the Notifying Party proposed a first set of commitments ("Initial Commitments"). The Initial commitments were market tested by the Commission on 8 July 2016 ("Initial market test").
- (270) The results of the initial market test were negative in that they provided indications that the commitments may not be comprehensive and effective in practice, as the implementation of the Initial commitments was deemed to be highly complex, long in duration and raised a number of risks which were not properly mitigated in the Initial commitments.
- (271) The Commission informed the Parties of the outcome of the market test during a state of play meeting on 20 July 2016. On 22 July 2016, the Notifying Party withdrew the notification.
- (272) The transaction was renotified on 19 September 2016 and a new set of commitments addressing issues identified during the Initial market test were submitted on 17 October 2016. Market test ("Second market test") was launched on 18 October 2016. Following the results of the Second market test the text of the commitments was subsequently amended and finally filed on 7 November 2016 (the "Final Commitments").

V.3. Description of the Initial Commitments

- (273) The Initial Commitments consisted in a divestiture of a number of Merial's animal health vaccines on a global basis (*Vaccines Divestment Business*)¹⁶² and some of Merial' NSAIDs on an EEA basis (*NSAIDs Divestment Business*).

V.3.1. *Vaccines Divestment Business*

- (274) The Initial Commitments consisted in a divestiture of a number of Merial's animal health vaccines on a global basis. More specifically, it comprised the following swine vaccines: Circovac,¹⁶³ Progressis, [OTHER PRODUCTS] and one ruminant vaccine: Mucossifa (the *Divested Vaccines*).
- (275) The divestiture consisted in an upstream and downstream production technology transfer for all these products.

V.3.1.1. *Introduction - Vaccine manufacturing processes*

- (276) The vaccine manufacturing process is composed of two steps: upstream manufacturing and downstream manufacturing.

V.3.1.1.a. Upstream manufacturing

- (277) Upstream manufacturing process consists of the production of antigens, on the basis of a so called *master seed*. All antigen production technologies follow a similar process. The basic principle is to multiply the relevant – inactivated or live – virus or

¹⁶² To the exception of Circovac in the US.

¹⁶³ Excluding the US.

(inactivated) bacteria in growth media using specific equipment. The main difference between growing viruses and bacteria is that viruses require living cells for growth, whereas bacteria can grow by themselves. Media are required to provide the required nutrients for the growth of the bacteria, virus or cell. The required media vary depending on the organism in question.

- (278) There are four major antigen production technologies: fermentors (for bacterial antigen production), bioreactors (for viral production), monolayer technology, and ovoculture. Bioreactors, monolayer technology and ovoculture represent different stages in the evolution of viral antigen manufacturing technology, with bioreactors being the most recent one.
- (279) In terms of equipment, fermentors and bioreactors are similar stainless steel tanks that differ primarily in the stirring mechanism and how air is supplied to the culture.
- (280) The antigen storage process varies depending on whether it is an inactivated or live vaccine. Live antigens are harvested and stored frozen to retain viability. Viruses or bacteria used for inactivated vaccines, on the other hand, are typically treated with chemicals that prevent further growth but retain the structure of the organism. After inactivation, these antigens can be stored at refrigerator temperatures. Further processing may remove water or further purify the antigens from the culture. The equipment used for downstream processing of viruses and bacteria (conventional or recombinant) is the same in most cases.

V.3.1.1.b. Downstream manufacturing

- (281) The mixing process (formulation) for live and inactivated vaccines differs only in the additives used. Live vaccines require specific chemical additives that help keep the organism alive. Inactivated vaccines are mixed with diluents (e.g. water) and adjuvants to formulate the final vaccine. The mixing process for a monovalent versus multivalent vaccine only differs in the number of antigens that are put into the tank.
- (282) Once formulation is completed, filling and finishing takes place; the liquids are filled into bottles or vials. Most live vaccines are freeze-dried (whereby the water content is removed under vacuum in a freezer).
- (283) The unlabelled bottles or vials (intermediate finished products) are then labelled and final packaging takes place.
- (284) By way of example the picture below provides an overview of the manufacturing process for Merial's vaccine Circovac.

[PICTURE SHOWING CIRCOVAC PRODUCTION PROCESS FROM MERIAL INTERNAL DOCUMENT].

V.3.1.2. *Merial's production capabilities for the Divested Vaccines*

- (285) Merial currently manufactures its PCV2, PRRS, BVD, and PPV vaccines at its Lyon Porte-des-Alpes ("LPA") facility, in France.
- (286) LPA is Merial's [...] biological production site globally, producing [...] different live or killed vaccines. Merial's PCV2, PRRS, BVD, and PPV vaccines account for less than [CONFIDENTIAL INFORMATION ON LIMITED PROPORTION OF LPA'S

FINISHED PRODUCT PRODUCTION CAPACITY REPRESENTED BY THE DIVESTED VACCINES] of finished products [CONFIDENTIAL INFORMATION ON LIMITED PROPORTION OF LPA'S FINISHED PRODUCT PRODUCTION CAPACITY REPRESENTED BY THE DIVESTED VACCINES] and less than [CONFIDENTIAL INFORMATION ON LIMITED PROPORTION OF LPA'S ANTIGEN PRODUCTION CAPACITY REPRESENTED BY THE DIVESTED VACCINES] of antigen [CONFIDENTIAL INFORMATION ON LIMITED PROPORTION OF LPA'S ANTIGEN PRODUCTION CAPACITY REPRESENTED BY THE DIVESTED VACCINES] manufactured at LPA.¹⁶⁴

(287) In 2015, the revenues generated by all the products manufactured at LPA represented [...] % of Merial's total EEA revenue and [...] % of Merial's EEA vaccines revenue.¹⁶⁵

V.3.1.3. *Description of the Vaccines Divestment Business*

(288) The Initial Commitments provided that the production technology transfers were to be effected either (i) to the Purchaser's own facility or (ii) to BI's manufacturing plant in [...] which the Purchaser could acquire. As part of the latter option the Notifying Party committed to build the necessary manufacturing equipment (bioreactors) to produce the vaccines which [...] currently does not have (except for monolayer technology used to produce Mucossifa and Parvovax).

(289) In addition, the Notifying Party committed to divest among other assets all IP rights, know-how, brands and customer information in relation to these vaccines. The divestment package also comprised transitional supply agreements under the supervision of a monitoring trustee and an industry expert.

(290) Pursuant to these commitments, the Vaccine Divestment Business should be sold to a single purchaser.

V.3.2. *NSAIDs Divestment Business*

(291) The Initial Commitments consisted in a divestiture of a number of Merial's animal health pharmaceuticals on an EEA basis. More specifically, it is composed of the following Merial's NSAIDs for multi-species; Ketofen, Wellicox, Allevinix, Genixine, Equioxx Injectable and the following oral NSAIDs for horses; Equioxx Paste, [OTHER PRODUCT] (*NSAIDs Divested Products*).

(292) The Initial Commitments consisted in a production transfer of the manufacturing process to the Purchaser's own plant or to a third party contract manufacturer. The divestment package also comprised transitional supply agreements under the supervision of a monitoring trustee and an industry expert.

(293) The NSAIDs divestment business should also be sold to a single purchaser, which could potentially be the same as the purchaser of the vaccine divestment business.

¹⁶⁴ Form RM, paragraph 92.

¹⁶⁵ [...]

V.4. Results of the Initial market test

V.4.1. Vaccines Divestment Business

- (294) The results of the Initial market test provided indications that transferring vaccine production technology is generally extremely complex and may fail in some cases, unless all risk mitigating factors are put in place, including the assurance of a suitable Purchaser being able to effectuate the transfer. In addition, the Initial market test provided indications the proposed technology transfer may not be effective in practice in that it would generate in a short period of time a viable competitor in the markets concerned as the transfer was deemed to be long in duration and raised a number of risks.
- (295) Specifically, the initial market test raised issues that the antigen production transfer of the divested vaccines may not be feasible as the manufacturing processes may not be reproducible in a new manufacturing environment which highly depends on their consistency, stability and robustness.¹⁶⁶ While one market participant indicated that to determine the feasibility of the transfer, information should be included on "*stability test data as well as continued testing of stability batches for the product [...] lab to lab consistency for confirmation testing of the quality attributes [...] validation data for processes and analytical methods*"¹⁶⁷, another stated that "*the consistency and robustness of the production technology available is crucial [...] The lower such consistency/robustness, the higher the technical risks along the transfer process*".¹⁶⁸ The upstream production transfer will depend in particular on the "*compatibility with other antigens and processes currently in place*"¹⁶⁹ at the receiving manufacturing site and more importantly on the equipment specifications, low yields impacting the costs of goods and products stability.¹⁷⁰
- (296) Second, the Initial market test revealed that upstream technology lengthy processes and most take up to 7-8 years (assuming it is successful). In this context a past example was referred to.
- (297) Generally, the Initial market test provided indications that the success of such transfer highly depends on depends on the equipment of the receiving site meeting all specifications, all components, raw materials and packaging being already available and experienced team on both ends being fully dedicated to the project.¹⁷¹
- (298) In this case, however, the market test indicated that it is unlikely that manufacturers would have the available bioreactors manufacturing capacity for the antigen production of the divested vaccines.¹⁷² In addition, the [...] plant which the Notifying

¹⁶⁶ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 1. 2.1, 14.2, 18 and 20.

¹⁶⁷ Response of a competitor to Questionnaire R1 Market Test to competitors of 8 July 2016, question 1.

¹⁶⁸ Response of a competitor to Questionnaire R1 Market Test to competitors of 8 July 2016, questions 20 and 28.

¹⁶⁹ Response of a competitor to Questionnaire R1 Market Test to competitors of 8 July 2016, question 28.

¹⁷⁰ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 28.

¹⁷¹ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, questions 1, 8 and 13.

¹⁷² Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, questions 1, 2 and 3.

Party committed to sell, at the option of the purchaser, does not have the required bioreactor capacity. The market test also indicated that the time to build such manufacturing capability would be 2 to 3 years, which could be implemented in parallel to the downstream manufacturing process but would prevent the purchaser to start upstream transfer steps (qualification, stability batches, training of personnel etc.).¹⁷³

- (299) Therefore, the duration of the upstream production transfer, as of equipment being in place, would depend on multiple factors, including the complexity of the antigens and processes transferred, the culture periods needed and the time required to obtain the regulatory approvals on variations.¹⁷⁴ In this regard market participants also identified risks of equipment validation failures, contamination and low yields, all having implications (amongst others) for the duration of the transfer.¹⁷⁵
- (300) As a result, some market participants raised that the transfer would have been lengthy: *"based on current experience a minimum 5 years is realistic"; " Whole process (manufacturing / STA studies / regulatory) transfer minimum would take a minimum of 5 years and then with more vaccines it will take significantly more than 5 years."*¹⁷⁶
- (301) In this context the Initial market test indicated that it is of crucial importance for the very success of the transfer that a suitable Purchaser be found. Specifically, such suitable purchaser would need to have expertise in bioreactor technology on site, successful track record in vaccines technology transfers, access to all relevant raw materials, R&D capabilities, a distribution network as well as experience with regulatory authorities in order to prevent delayed authorizations, product recalls, and supply interruptions.¹⁷⁷
- (302) In addition, respondents indicated that for successful commercialisation of Merial's Circovac it is important to already have a portfolio of swine vaccines,¹⁷⁸ in particular a MHyo vaccine.¹⁷⁹ This is in line with the market investigation which indicated that in zones where M.hyo is current, customers tend to purchase monovalent PCV2 and M.hyo vaccines from the same supplier, for convenience and pricing reasons.¹⁸⁰ For PPV, the purchaser would need to also have a vaccine against Erysipelas, otherwise it would be a handicap.¹⁸¹ This is in line with the market investigation which showed that the vast majority of the revenue for vaccines against PPV is in multivalent offerings, the suppliers (Merial, Zoetis and MSD) have both monovalent and multivalent vaccines [CONFIDENTIAL INFORMATION ON R&D]..

¹⁷³ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 30.

¹⁷⁴ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 19.

¹⁷⁵ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 28.

¹⁷⁶ Response of a competitor to Questionnaire R1 Market Test to competitors of 8 July 2016, question 19.

¹⁷⁷ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, questions 1, 8, 15 and 32.

¹⁷⁸ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 32.

¹⁷⁹ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, questions 8 and 36.

¹⁸⁰ Responses to Questionnaire Q2 to Swine customers of 7 June 2016, question 10.

¹⁸¹ Agreed minutes of the conference call with a competitor of 30 August 2016. See responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 8.

V.4.2. NSAIDs Divestment Business

- (303) No substantiated concerns were expressed as to the effectiveness of the production transfer as regards the NSAIDs Divestment Business.
- (304) As to the assets included in the Commitments, some market respondents indicated that the know-how, data and regulatory documentations that will be transferred, should include manufacturing documentation, historical data trends for key process variables, equipment specifications, process change control documentation, analytical method documentation and raw data, as well as samples of product, reagents, key raw materials and excipients, packaging components and artwork.¹⁸² Many market respondents also indicated that Meril's patent rights for *firocoxib* should be included.¹⁸³
- (305) As to the Purchaser criteria, several customers indicated that a suitable purchaser would be any well-resourced and reliable pharma company with a local presence and an active commercial team.¹⁸⁴ Customers also emphasised the need for the purchaser to already have a portfolio of animal NSAIDs or to have experience with them.¹⁸⁵

V.4.3. Conclusion on the results of the Initial market test

- (306) In light of the above, the Commission concluded that the Initial Commitments were not sufficiently clear-cut to eliminate the Commission's serious doubts with respect to PCV2, PRRS, PPV and BVD vaccines markets.

V.5. Additional fact finding

- (307) Following the market test, the Commission conducted additional investigation to ascertain whether the technology production transfer is in principle feasible in relation to the vaccines included in the Commitments and what risk mitigating measures can be put in place to ensure that the Commitments will be effective in practice
- (308) Specifically, the Commission gathered data on the manufacturing processes of the Divested Vaccines in their existing manufacturing site, and more specifically status and stability reports, Cpk (measure of process capability) reports, control charts and statistics on batches rejection.
- (309) The analysis of such data (aided by independent experts) showed no remarkable out of scope results and indicated a compliant and consistent manufacturing process with minimal rejection of batches for all Divested Vaccines. While, no conclusion could be made on the specific difficulties that each of the products may pose during transfer, the analysis of the data did not reveal any specific risk factors which would in principle exclude the successful transfer. Indeed, while bioreactor technology (or

¹⁸² Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 38.

¹⁸³ Responses to Questionnaire R1 Market Test to competitors of 8 July 2016, question 40.

¹⁸⁴ Responses to Questionnaire R2 Market Test to customers of 8 July 2016, question 8.

¹⁸⁵ Response of a customer to Questionnaire R2 Market Test to customers of 8 July 2016, question 8: "[...] *this only can assure , that the product will not disappear and will stay alive and available on the market.*" Responses to Questionnaire R2 Market Test to customers of 8 July 2016, question 8.

emulsion for injection) is one of most challenging for vaccine production, all products concerned are of conventional technology that exists for many years in the field.

- (310) The additional investigation also emphasised that experience and expertise of the purchaser and the receiving site in bioreactor technology is crucial for the success of the production transfer.¹⁸⁶ One company explained in particular that in the early stages of the transfer, in the receiving site for Merial's PCV2 vaccine Circovac, there should be skilled technical bioreactor operators and bioengineers to develop the vaccine as well as project leaders.¹⁸⁷
- (311) Furthermore, market respondents indicated that while location of receiving site outside the EEA was not prohibitive in principle it would involve some complexities in relation to regulatory approvals and would generally not put the Purchaser in the same position as Merial is prior to the transfer.¹⁸⁸ Specifically, testing of the products bound for the EEA would be carried out in the US and there would be re-testing once the products arrive in the EEA. If discrepancies are found between these two series of tests additional information will be required by the authorities. Addressing this situation would require a good working relationship and support between the sending site and receiving site in the EEA, in order to avoid a loss of efficiency as compared to the original process.¹⁸⁹
- (312) Finally, market respondents also indicated that an effective transfer of the emulsion and reagents are critical steps to ensure the source of identical starting materials for the transferred vaccines. The success of the transfer would depend on the availability of reagents and other biological material¹⁹⁰.

V.6. Description of the Final Commitments

- (313) Following the results of the Initial market test and the additional investigation, the Final Commitments include improved obligations (in terms of personnel, support and access to reagents) and most importantly identify Ceva Santé Animale (Ceva) as the Purchaser fulfilling the criteria stemming from the Initial market test.
- (314) More specifically, the Final Commitments include the following modifications.

1. Vaccines

i. Assets

As for the marketed vaccines:

¹⁸⁶ Agreed minutes of the conference call with a competitor of 30 August 2016. See also minutes of the conference call with a competitor of 29 August 2016.

¹⁸⁷ Agreed minutes of the conference call with a competitor of 30 August 2016.

¹⁸⁸ Agreed minutes of the conference calls with a competitor and another competitor of 29 and 30 August 2016.

¹⁸⁹ Agreed minutes of the conference call with a competitor of 29 August 2016.

¹⁹⁰ A reagent is a compound or mixture used to confirm the presence or absence of another substance. In this case reagents recognise the amount of antigen in the final product.

- Merial's Parvoruvax (for PPV and erysipelas), in order to ensure the viability and competitiveness of the PPV part of the commitments,
- Related recipes for the testing media and reagents,
- The manufacturing know how now includes, but is not limited to the manufacturing of any reagent and adjuvant¹⁹¹ of the Vaccine Divestment Products,
- The know-how required for or associated with obtaining and/or maintaining the related manufacturing and marketing approvals now includes stability/reproducibility data and periodic safety reports),
- the obligation to provide any support to ensure an effective Production Transfer has been specified to last until six months after Ceva has successfully produced three validation batches of the relevant product in its production unit.

As for the [OTHER PRODUCT]:

- A best efforts obligation to transfer any contract or relationships with third parties concerning services related to [...] Divestment Business
- The recipes for the testing media and reagents that used are for the [...] Divestment Business and relevant documentation required to carry out the relevant quality control tests

ii. Transitional Agreements and Support

- Supply of the reagents necessary for the manufacture and/or testing of any Vaccine Divestment Product for the duration of the TSA agreements. If Ceva is not able to source such reagents: back-to-back supply agreements with reagent suppliers for such period as required by Ceva to establish the Vaccine Divestment Businesses as viable and independent businesses, but not exceeding the duration of the TSA.
- An obligation to provide any support to ensure an effective Production Transfer until six months after Ceva has successfully produced three validation batches of the relevant product in its production unit. The production transfer support will be provided by a team of expert employees of Merial.

¹⁹¹ Inactivated vaccines are often formulated with compounds called adjuvants which enhance the immune response to the inactivated antigen.

2. NSAIDs

- The manufacturing know how, know-how required for or associated with obtaining and/or maintaining the related manufacturing and marketing approvals now includes stability/reproducibility data and periodic safety reports.

V.7. Assessment of the Final Commitments

- (315) On 18 October 2016, the Commission launched the Second market test on the new set of commitments addressing the issues identified in the Initial market test, and specifying Ceva as the Purchaser.¹⁹²
- (316) Overall, the results of the market test were positive both as concerns the scope of the commitments and identity of the Purchaser.
- (317) The commitments cover all product markets identified in paragraph (257) for which the Commission raised serious doubts as to the compatibility of the Transaction with the internal market.
- (318) Concerning the Vaccines Divestment Business, a large majority of respondents to the market test stated that the assets which have been added under the Final Commitments are sufficient for a successful production transfer.¹⁹³ There were no substantiated statements that other assets should be added.
- (319) A large majority of respondents indicated that the commitments provide sufficient safeguards to ensure that all necessary steps will be undertaken to ensure a successful transitional supply of the final and intermediate products.¹⁹⁴
- (320) As regards quality control testing materials, a large majority of respondents indicated that the transferred media and reagents now included are comprehensive and will ensure that Ceva will be in a position to manufacture Divested Vaccines products on a sustainable basis in the same manner as Merial did before the transaction.¹⁹⁵ There were no substantiated statements that additional safeguards should be included.
- (321) As for the duration of the support obligation, in general respondents confirmed it should last until six months after Ceva has successfully produced three validation batches of the relevant product in its production unit. However one respondent indicated it should end following "*satisfactory results after 3 consecutive manufacturing batches*".¹⁹⁶
- (322) As regards Ceva's suitability as the purchaser of the Vaccine Divestment businesses, a large majority of respondents indicated they believe that with Ceva this business will

¹⁹² On 16 September 2016 the Notifying Party and Ceva signed a binding put option, to which an asset purchase agreement (APA) and its exhibits are attached, with respect to the purchase of the Divestment Businesses.

¹⁹³ Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 1.

¹⁹⁴ Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 4.

¹⁹⁵ Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 3.

¹⁹⁶ See reply of a competitor to Questionnaire R3 Market Test to competitors of 18 October 2016, question 5.

- continue to be viable and that Ceva will preserve the business' position in the market post-divestment.¹⁹⁷
- (323) Ceva's main strengths were identified as having an existing vaccine business with a strong reputation including a marketing and sales organization, commercial aggressiveness and R&D capabilities.¹⁹⁸ One respondent stated that "*Ceva is fully established in the European Animal Health sector, present in most of the key markets where this transaction is more relevant to the industry and with a product portfolio in the segments where these divestments will be complementary.*"¹⁹⁹
- (324) Respondents also stated that Ceva's acquisition of the Vaccines Divestment Business would be an opportunity for its development. In this regard one respondent indicated that Ceva was a "*well established company in the Food Producing Animal Segment. [...] the acquisition of innovative vaccine products will enhance company's reputation. Ceva will become an important player in finishing pig vaccines with the introduction of Circovac, together with its M. hyopneumoniae vaccine.*"²⁰⁰ Another respondent indicated that, with the Vaccine Divestment Business, "*Ceva will have the chance to be a significant player in swine bio segment.*"²⁰¹
- (325) Moreover, a few respondents indicated it was possible Ceva could develop a stronger presence on the market than Merial.²⁰² For instance, one respondent stated that Ceva "*[...] will be stronger than Merial because they can complete their portfolio with several products not present in the hands of Merial.*"²⁰³
- (326) With regard to the NSAIDs Divestment business, a large majority of respondents to the market test stated that the assets which have been added under the Final Commitments are sufficient for a successful production transfer.²⁰⁴ There were no substantiated statements that other assets should be added.
- (327) As regards Ceva's suitability as the purchaser of the NSAIDs Divestment businesses, a large majority of respondents indicated they believe that with Ceva this business will continue to be viable and that Ceva will preserve the business' position in the market post-divestment.²⁰⁵ In this regard a respondent described Ceva as having an "*established commercial presence and footprint in key European markets (sales force, marketing, technical services). Proven track record in integrating and growing acquired businesses/assets.*"²⁰⁶ Another respondent stated that Ceva's strengths include

¹⁹⁷ Responses to Questionnaire R4 Market Test to customers of 18 October 2016, question 9 and Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 10.

¹⁹⁸ Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 11.

¹⁹⁹ Response of a competitor to Questionnaire R3 Market Test to competitors of 18 October 2016, question 15.

²⁰⁰ Response of a customer to Questionnaire R4 Market Test to customers of 18 October 2016, question 4.

²⁰¹ Response of a customer to Questionnaire R4 Market Test to customers of 18 October 2016, question 4.

²⁰² Responses to Questionnaire R4 Market Test to customers of 18 October 2016, question 9.

²⁰³ Response of a customer to Questionnaire R4 Market Test to customers of 18 October 2016, question 9.

²⁰⁴ Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 13.

²⁰⁵ Responses to Questionnaire R3 Market Test to competitors of 18 October 2016, question 10.

²⁰⁶ Response of a competitor to Questionnaire R3 Market Test to competitors of 18 October 2016, question 15.

*"aggressive Marketing strategies consisting of providing any product at the lowest possible purchase Price to customers."*²⁰⁷

V.8. Assessment of Ceva as a suitable purchaser

(328) The Notifying Party and Ceva concluded a binding put option on 16 September 2016, which was amended on 5 November 2016 to reflect the Final Commitments, pursuant to which Ceva undertakes to purchase the Divestment Businesses pursuant to an Asset Purchase Agreement and its exhibits (*the Proposed Agreement*).²⁰⁸

(329) Ceva is a global veterinary health company headquartered in Libourne, France which focuses on pharmaceuticals and vaccines for companion animals, livestock, swine and poultry.

V.8.1. Ceva is independent of and unconnected to BI

(330) Ceva is not structurally connected to BI in terms of direct or indirect ownership interests or board presence. Neither Ceva nor its affiliates or subsidiaries have any shares or direct or indirect interest in BI.

(331) As is customary in the pharmaceutical industry, BI and Ceva are part to a number of license and other types of customary commercial agreements. These agreements concern an insignificant number of products as compared to Ceva's overall portfolio of products and [INFORMATION ON BI AND CEVA'S COMMERCIAL ARRANGEMENTS]. As a result, Ceva is not economically dependent on BI.

(332) Based on the information provided, the Commission considers Ceva to be independent of and unconnected to BI, both from a legal and economic perspective.

V.8.2. Ceva has financial resources, proven relevant expertise and the incentive to be a viable and active competitor

V.8.2.1. Ceva has the financial resources to acquire the Divestment Businesses

(333) Ceva has shown a strong and consistent financial performance over the last decade. Ceva reported revenues of EUR 856.4 million in 2015. This represents an increase of 11.9% compared to 2014. In terms of profitability, the EBITDA margin of Ceva decreased in the last three years, from 18.6% in 2013, to 17.5% in 2015.²⁰⁹

(334) In terms of Ceva's capacity to finance the transaction, Ceva has secured the debt and cash requirements to finance the deal of EUR [...] million.

²⁰⁷ Response of a competitor to Questionnaire R3 Market Test to competitors of 18 October 2016, question 15.

²⁰⁸ The binding put option entered into with an identified buyer during the Commission's procedure has similar effects as a "fix-it-first remedy" under paragraph 50 of the Remedies Notice since Ceva (*promesse d'achat*) does not have any opt-out and will enter into the Asset Purchase Agreement and its exhibits attached to the put option once the option is exercised. The signature of a put option, instead of the Asset Purchase Agreement and its exhibits, is justified by the necessity to consult the *Comite d'entreprise* of the seller which is a mandatory requirement under French law. BI has an explicit obligation under the Commitments to sell the Divestments Businesses to Ceva, and therefore exercise the put option to the benefit of Ceva.

²⁰⁹ Ceva Annual Report, 2015, page 75.

- (335) Ceva has a strong acquisition track record, with 30 acquisitions since 2000, such as the acquisition of Sogeval in 2013. Although the acquisition of the Divestment Businesses is one of the larger ones realised by Ceva, it only represents approximately [...] % of its existing business which represents a health ratio.
- (336) In addition, based on comparison of Ceva's key financials over the last three years with the relevant metrics of other pharmaceutical companies focused on animal health, Ceva's indebtedness in terms of the Net Debt/EBITDA ratio appears below industry median and average.
- (337) In view of the above, the Commission considers that Ceva has the financial capability to acquire the Divestment Businesses.

V.8.2.2. Ceva is a recognized animal health supplier with a complementary swine vaccine business

- (338) Ceva is an independent company active in the animal health sector since 1999. Ceva focuses on research, development, production and marketing of pharmaceuticals and vaccines for poultry, swine, ruminants, horses and companion animals and has expertise centers in both pharmacology and biology.
- (339) As to the swine vaccines, at global level, Ceva markets a number of vaccines. Ceva's portfolio is composed of Hyogen (against enzootic pneumonia, MHyo), Coglapix (against porcine pleuro pneumonia), Coglapest (against classical swine fever), Auphyl Plus (against aujeszky disease) and Coglamune (against clostridial enteric disease).²¹⁰ In the EEA, Ceva is supplying Hyogen, Coglapix and Coglamune. Amongst these vaccines, Hyogen is particularly important as M.Hyo vaccines and PCV2 vaccines are often administered and thus sold together.²¹¹ As a result, Ceva has in its portfolio a key complementary product which will allow it to market both products together.
- (340) In addition, besides vaccines, Ceva is currently active in sow reproduction management with a portfolio of products, consisting of Altresyn, Fertipig, Enzaprost and in certain EEA countries also Alphabedyl.²¹²
- (341) Finally, Ceva is also active in R&D in this space [CONFIDENTIAL INFORMATION ON CEVA'S R&D].
- (342) Based on the above, Ceva has an existing customer base and customer recognition in the swine industry which will allow it to access the market with divested products without the hurdle of establishing itself in the market.

V.8.2.3. Ceva has adequate manufacturing and regulatory capability to successfully implement the technology transfer in relation to Divestment Businesses

- (343) As part of the Transaction, Ceva will not acquire any manufacturing assets from BI. Ceva will carry out the production technology transfer for the Vaccines Divestment Business to its Ceva-Phylaxia Campus in Hungary. The production of the NSAID

²¹⁰ <http://www.ceva.com/Products/Swine/Vaccines>

²¹¹ Minutes of the meeting with Ceva of 28 July 2016.

²¹² <http://www.ceva.com/Products/Cattle/Reproduction-Management>.

Divestment Business' products will be transferred to Libourne (France) for injectables and to Laval (France) or Loudeac (France) for tablets.

- (344) In the past, Ceva has successfully transferred the production of multiple products internally, both animal vaccines and pharmaceuticals. By way of examples, [CONFIDENTIAL INFORMATION ON CEVA'S TECHNOLOGY TRANSFERS].
- (345) In addition, Ceva has bioreactor expertise and know-how, including in the facility where the Vaccine Divestment Businesses would be transferred. [CONFIDENTIAL INFORMATION ON CEVA'S DEVELOPMENT PLANS].²¹³
- (346) Ceva has more than [...] experienced staff fully dedicated to the industrial transfers and the process improvement on site. Ceva has gradually built up its bioreactor expertise during the last [...] years, in particular by external hiring of experienced personnel and internal training in bioreactor technology. Therefore, Ceva already has trained and experienced personnel familiar with the bioreactor technology, and will have additional dedicated personnel [...].²¹⁴
- (347) In addition, Ceva has strong experience in dealing with regulatory authorities for the commercialisation of animal health products and vaccines across the EEA and expertise in the required GMP certifications, quality assurance and pharmacovigilance.
- (348) As regards the timeline for the production transfer, the fact that the project is already ongoing would allow Ceva to complete the transfer, i.e. obtain the approval for both antigen and finished dose product, within a shorter period of time than in a scenario where the equipment would yet have to be ordered.²¹⁵
- (349) Based on the above, Ceva has adequate manufacturing capability, in particular as to bioreactor technology in the receiving site, as well as regulatory expertise to successfully implement the technology transfers in a reasonable timeframe.

V.8.2.4. Ceva has adequate R&D capabilities to successfully develop the Divested Products

- (350) Ceva has invested heavily in R&D and has growing R&D spends from EUR 59.6 million in 2013 to EUR 77.8 million in 2015.²¹⁶ Ceva has 13 R&D sites around the world, of which 6 R&D sites are located in Europe, some of which are specialised in biologics R&D.
- (351) Even absent these Commitments Ceva has been developing [CONFIDENTIAL INFORMATION ON CEVA'S R&D].
- (352) Based on the above, Ceva has adequate R&D capabilities to develop the Divested Products.

²¹³ Agreed minutes of the meeting with Ceva of 28 July 2016.

²¹⁴ Ceva's submission of 23 September 2016.

²¹⁵ Agreed minutes of the meeting with Ceva of 28 July 2016.

²¹⁶ Ceva Annual Report, 2015, page 75.

V.8.2.5. Ceva has adequate distribution capabilities to supply the products in all EEA countries where Meril is currently present

- (353) For all countries in which the Divestment Businesses generate revenues, Ceva either has an own distribution network or works with an external distributor. More specifically in relation to swine vaccines, Ceva is already present in all the swine production countries worldwide with dedicated swine teams.
- (354) In addition, Ceva's current personnel will be reinforced in the EEA with 23 additional sales personnel from the Divestment Business located in five EEA countries.
- (355) Based on the above, Ceva will be able to replicate Meril's current distribution and sales network and supply the Divested Products at least in all countries where Meril is currently active.

V.8.2.6. Ceva has strong incentives to develop the business

- (356) The Commission has reviewed an overview of revenue and gross margin actuals and projections for all products in the Divestment Businesses covering the period FY 2013-2022. The Commission compared Ceva's projections to BI's revenue and gross margins projections for the period FY 2016-2018. Ceva's projections show healthy gross margins, which are generally in line with BI's own estimates²¹⁷ and industry practise.
- (357) The Commission also reviewed a complete Business Plan of Ceva for the Divestment Businesses starting in 2017. The Commission analysed in particular Ceva's projections in terms of operating expenses (selling expenses, distribution expenses, general and administrative expenses and R&D expenses), which take into account the one-off advertising and marketing expenses in 2017 following the acquisition, and capital expenditures, in particular in 2017 and 2018 to complete ramping up the bioreactor capacity for the Vaccines Divestment Business. Four alternative business cases were also analysed. Even in the more pessimistic scenarios, assuming a 20% volume and price decrease compared to Ceva's base case, the EBITDA margin of the Divestment Businesses is expected to remain at approximately [0-10]%.
- (358) Therefore, Ceva's business plan for the Divestment Businesses is realistic and ensures continuous viability of the Divestment Businesses in the long run.
- (359) In addition, Ceva demonstrated its commitment to develop the Divested Businesses which fully fit into its overall business development strategy in Europe existing prior to this acquisition.
- (360) Based on the above analysis, the Commission concludes that Ceva has the incentives to develop the Divestment Business and run it in a viable and competitive manner in the long term.
- (361) Based on the above and the evidence available, the Commission considers that Ceva possesses the financial resources, proven relevant expertise and has the incentive and ability to be a viable and active competitive force in the market in competition with

²¹⁷ [INFORMATION ON CEVA'S PROJECTIONS]

the Parties and other competitors in all markets where the Commission identified serious doubts as to the compatibility of the Transaction with the internal market.

V.8.3. *Ceva is unlikely to create prima facie competitive concerns*

(362) As to the Vaccines Divestment Business, the only potential overlap relates to [CONFIDENTIAL INFORMATION ON CEVA'S ACTIVITIES].

(363) However, the acquisition by Ceva of Circovac is not likely to create prima facie competition concerns since:

(i) [CONFIDENTIAL INFORMATION ON CEVA'S ACTIVITIES], there are already two competitors, namely [COMPETITOR NAMES], active on the market with larger market share than Merial.

(ii) More importantly, [CONFIDENTIAL INFORMATION ON CEVA'S ACTIVITIES].²¹⁸ [CONFIDENTIAL INFORMATION ON CEVA'S ACTIVITIES].²¹⁹

(364) As to the NSAIDs Divestment Businesses, the only potential overlap relates to multispecies injectable NSAIDs. However, the acquisition by Ceva of Merial's injectable NSAIDs is not likely to create any prima facie competition concerns since:

(i) Ceva's market position in multispecies injectable NSAIDs is rather limited. At EEA level, Ceva is ranked number 6 supplier, with a market share below [5-10]%.
(ii) Ceva supplies only generic products, while, as explained above, generic penetration in NSAIDs markets is rather low. As indicated above, the market investigation indicated that Ceva's products are perceived as having weaker brand recognition.

(iii) BI, which currently leads the market, will remain Ceva's strongest competitor.

(365) Furthermore, the Proposed Agreement includes the sale of Merial's oral NSAID Ketofen. Although the Commission has not identified competition concerns on the market for oral NSAIDs for pets, Merial's Ketofen oral pet NSAIDs were included in the business which is being divested to Ceva, along with the other Ketofen branded products (multi-species injectable NSAIDs), to avoid that complications arise as a result of a split of the Ketofen brand.

(366) The acquisition by Ceva of Merial's Ketofen oral pet NSAIDs gives rise to a limited overlap:

(i) Ceva's market position in oral NSAIDs for pets is rather limited. At EEA level, Ceva is ranked number 6, with a market share below [5-10]%. Ceva supplies only generic products, while, as explained above, generic penetration in NSAIDs markets is generally low.

²¹⁸ Ceva's submission of 23 September 2016.

²¹⁹ See paragraphs (59) above.

(ii) BI and Zoetis, which currently lead the market, will remain Ceva's strongest competitors. As indicated above, the market investigation indicated that Ceva's products are perceived as being close to BI's. In addition, post-Transaction BI will supply the other oral NSAIDs for pets of Merial and in particular the COXIB Previcox, which currently generates more sales than Ketofen in the EEA.

(367) Finally, as to regulatory approvals, the only condition upon closing is the clearance from the Brazilian competition authority (CADE).

(368) In view of the above, the Commission considers the acquisition by Ceva of the Divestment Businesses pursuant to the Proposed Agreement is not likely to create any *prima facie* competition concerns nor give rise to a risk that the implementation of the Commitments will be delayed.

V.8.4. *Conclusion*

(369) In view of the above, the Commission considers that Ceva is a suitable Purchaser of the Divestment Business as specified in the Final Commitments.

V.9. **Overall Conclusion**

(370) In light of the above and in the very specific circumstances of this case, the Commission considers the Final Commitments capable of rendering the Transaction compatible with the internal market as it will prevent a significant impediment to effective competition in all relevant markets in which competition concerns were identified.

(371) Moreover, the Commission considers that the Proposed Agreement signed between BI and Ceva is in line with the Final Commitments and that Ceva is a suitable purchaser pursuant to the Final Commitments.²²⁰

V.10. **Conditions and Obligations**

(372) Pursuant to the second subparagraph of Articles 8(2) and 10(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the internal market.

(373) The fulfilment of the measure that gives rise to the structural change of the market is a condition, whereas the implementing steps which are necessary to achieve this result are generally obligations on the parties. Where a condition is not fulfilled, the Commission's decision declaring the concentration compatible with the internal market is no longer applicable. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(6) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2) and 15(1) of the Merger Regulation.

²²⁰ This is without prejudice of the fact that the transaction agreements ought to be interpreted in line with the commitments and in case of discrepancy the commitments take precedence.

- (374) In accordance with the basic distinction as regards conditions and obligations, this Decision should be made conditional on full compliance by the Parties with of the Final Commitments and its Schedules and Sections B to C should be obligations within the meaning of Article 8(2) of the Merger Regulation. The other commitments set out in the Annex constitute obligations, as they concern the implementing steps which are necessary to achieve the modifications sought in a manner compatible with the internal market. The full text of the Final Commitments and its Schedules is attached as Annex to this Decision and forms an integral part thereof.

VI. CONCLUSION

- (375) For the above reasons, the Commission has decided not to oppose the notified operation as modified by the commitments and to declare it compatible with the internal market and with the functioning of the EEA Agreement, subject to full compliance with the conditions in sections Sections B and C (including Schedules 1 and 2) of the commitments annexed to the present decision and with the obligations contained in the other sections of the said commitments. This decision is adopted in application of Article 6(1)(b) in conjunction with Article 6(2) of the Merger Regulation and Article 57 of the EEA Agreement.
- (376) On the basis of the above assessment, the Commission approves Ceva Santé Animale (Ceva) as a suitable purchaser. On the basis of the Proposed Agreement, the Commission further concludes that the Divestment Business is being sold in a manner consistent with the Commitments.
- (377) This decision only constitutes approval of the proposed purchaser identified herein and of the Proposed Agreement. This decision does not constitute a confirmation that BI has complied with its Commitments.

For the Commission

(Signed)

*Margrethe VESTAGER
Member of the Commission*

Case M. 7917 – Boehringer Ingelheim/Merial

COMMITMENTS TO THE EUROPEAN COMMISSION

Pursuant to Article 6(2) of Council Regulation (EC) No 139/2004 (the *Merger Regulation*), Boehringer Ingelheim (the *Notifying Party* or *BI*) and, to the extent applicable, Merial SAS (*Merial*) (together "*the Parties*") hereby enter into the following Commitments (the *Commitments*) vis-à-vis the European Commission (the *Commission*) with a view to rendering the acquisition of sole control over the animal health business of Sanofi (*Merial*) (the *Concentration*) compatible with the internal market and the functioning of the EEA Agreement.

This text shall be interpreted in light of the Commission's decision pursuant to Article 6(1)(b) of the Merger Regulation to declare the Concentration compatible with the internal market and the functioning of the EEA Agreement (the *Decision*), in the general framework of European Union law, in particular in light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the *Remedies Notice*).

For the avoidance of doubt, the Schedules form an integral part of the Commitments.

Section A. Definitions

1. For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled by the Parties and/or by the ultimate parents of the Parties, whereby the notion of control shall be interpreted pursuant to Article 3 of the Merger Regulation and in light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (the "*Consolidated Jurisdictional Notice*").

Assets: the assets that contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Businesses as indicated in Section B, paragraph 7 and described more in detail in the Schedules.

Best Efforts: Best effort obligations shall be interpreted in light of the Commission's decision pursuant to Article 6(1)(b) of the Merger Regulation to declare the Concentration compatible with the internal market and the functioning of the EEA Agreement, the Merger Regulation and the general principles of EU law. Any interpretation that may be given to this term under the law of other jurisdictions is not relevant solely for the purpose of interpreting and/or implementing the Commitments.

Binding Put Option: the binding put option agreement attached as Annex A entered into on 16 September 2016 whereby the Purchaser undertakes to acquire the Divestment Businesses in accordance with the terms of the Product Asset Purchase Agreement.

Boehringer Ingelheim (BI): Boehringer Ingelheim International GmbH, incorporated under the laws of Germany with its registered office at Ingelheim am Rhein, Germany and registered with the Commercial Register at the Local Court of Mainz under number HRB21063.

Closing: the transfer of the legal title to the Divestment Businesses to the Purchaser.

Closing Period: the period of [Conf] from the Effective Date, or, if the closing of the Concentration takes place after that period, the period of [Conf] from the closing of the Concentration.

Confidential Information: any business secrets, know-how, commercial information, or any other information of a proprietary nature that is not in the public domain.

Conflict of Interest: any conflict of interest that impairs the Trustee's objectivity and independence in discharging its duties under the Commitments.

Divestment Businesses: the businesses as defined in Section B and in Schedules 1 and 2 which the Notifying Party commits to divest.

Effective Date: the date of adoption of the Decision.

Gerland Antigen Supply: as defined in Schedule 1, Part D.

Hold Separate Manager: the person(s) appointed by the Notifying Party for the Divestment Businesses to manage the day-to-day business under the supervision of the Monitoring Trustee.

Key Personnel: all personnel necessary to maintain the viability and competitiveness of the Divestment Business, as listed in the Schedule, including the Hold Separate Manager(s).

Master Seed: master virus seed and master cell seed.

Merial: the animal health business of Sanofi to be acquired by BI.

Monitoring Trustee: one or more natural or legal person(s) who is/are approved by the Commission and appointed by the Notifying Party, and who has/have the duty to monitor the Notifying Party's compliance with the conditions and obligations attached to the Decision.

Notifying Party: Boehringer Ingelheim. Where Boehringer Ingelheim cannot directly commit to the commitments described in the text below, Boehringer Ingelheim will use its Best Efforts to cause the relevant party to comply with the obligations hereby described below.

NSAIDs: non-steroidal anti-inflammatory drugs.

NSAID Divestment Business: the business as defined in Section B and Schedule 2.

NSAID Divestment Products: the NSAID products as defined in Section B and Schedule 2.

[Conf] Pipeline Product: [Conf] as described in Section B and Schedule 2.

NSAID TSA: as defined in Schedule 2.

Parties: the Notifying Party and the undertaking that is the target of the concentration.

Personnel: all staff currently employed by the Divestment Businesses, including staff seconded to the Divestment Businesses, shared personnel as well as the additional personnel listed in the Schedules.

Products Asset Purchase Agreement: the agreement for the sale and purchase of the Divestment Businesses to be executed between BI and the Purchaser in accordance with the terms of the Binding Put Option.

Production Transfer: as defined in Schedules 1 and 2 for the Vaccine Divestment Business and the NSAID Divestment Business respectively.

Production Transfer Personnel: all personnel necessary to ensure an effective production transfer of the Vaccine Divestment Businesses to a production location of the Purchaser's choice, as described in Part D of Schedules 1 and 2.

Purchaser: Ceva Santé Animale.

Schedule(s): the schedules to these Commitments describing more in detail the Divestment Businesses.

Swine Vaccine Commercial Personnel: the Merial commercial employees in the EEA whom the Parties will allow the Purchaser to make an employment offer to under the terms and conditions described in the Products Asset Purchase Agreement.

Technical Expert: one or more natural or legal person(s), appointed by and reporting to the Monitoring Trustee, who has/have industry expertise relevant to the Divestment Businesses and will assist and advise the Monitoring Trustee with regard to all technical aspects related to the Divestment Businesses, as described in paragraph 27 below.

Trustee: the Monitoring Trustee.

TSA: Transitional Supply Agreement.

Vaccine Divestment Businesses: the vaccine businesses as defined in Section B and Schedule 1.

Vaccine Divestment Products: the vaccine products as defined in Section B and Schedule 1.

Vaccine TSA: as defined in Schedule 1.

Section B. The commitment to divest and the Divestment Businesses

Commitment to divest

2. In order to maintain effective competition in the EEA, the Notifying Party commits to divest, or procure the divestiture of the Divestment Businesses to the Purchaser.
3. The Notifying Party shall be deemed to have complied with this commitment if:

- (a) Pursuant to the Binding Put Option, BI sells at Closing the Divestment Businesses to the Purchaser and the Closing takes place within the Closing Period; and
 - (b) the Production Transfers set forth in the Schedules have been completed.
4. In order to maintain the structural effect of the Commitments, the Notifying Party shall, for a period of 10 years after Closing, not acquire, whether directly or indirectly, the possibility of exercising influence (as defined in paragraph 43 of the Remedies Notice, footnote 3) over the whole or part of the Divestment Businesses, unless, following the submission of a reasoned request from the Notifying Party showing good cause and accompanied by a report from the Monitoring Trustee (as provided in paragraph 40 of these Commitments), the Commission finds that the structure of the market has changed to such an extent that the absence of influence over the Divestment Businesses is no longer necessary to render the proposed concentration compatible with the internal market.

Structure and definition of the Divestment Businesses

Vaccine Divestment Businesses

5. The Vaccine Divestment Businesses consist of the rights, title and interests in the following products, including the right to develop, improve, manufacture and commercialise:
- (a) the worldwide (excluding U.S.) Circovac branded monovalent porcine circovirus type 2 (*PCV2*) swine vaccine business as described in more detail in Schedule 1 (the *PCV2 Divestment Business*);
 - (b) the worldwide Progressis branded monovalent porcine reproductive and respiratory syndrome (*PRRS*) vaccine business (including [*Conf*]) as described in more detail in Schedule 1 (the *PRRS Divestment Business*);
 - (c) the worldwide Parvovax branded monovalent inactivated porcine parvovirus (*PPV*) vaccine business and the worldwide Parvoruvax branded inactivated multivalent erysipelas and PPV vaccine business as described in more detail in Schedule 1 (the *PPV Divestment Business*); and
 - (d) the worldwide Mucosiffa branded monovalent BVD ruminant vaccine business as described in more detail in Schedule 1 (the *BVD Divestment Business*).

NSAID Divestment Business

6. The NSAID Divestment Business¹ consists of the rights, title and interests in the following products, including the right to develop, improve, manufacture and commercialise:

¹ The Notifying Party commits to divest all NSAID Divestment Products on an EEA-wide basis to solve the Commission's potential competition concerns. However, the Notifying Party intends to divest the NSAID Divestment Products on a worldwide basis, excluding Anafen (Merial's ketofen based multi-

- (a) Merial's injectable NSAIDs for multi-species on a EEA-wide basis, including the brands Ketofen, Romefen, Wellicox, Allevinix, Genixine and Equioxx Injectable, as described in more detail in Schedule 2; and
 - (b) Merial's Equioxx Paste branded oral NSAIDs for horses (including [Conf]) on an EEA-wide basis, as described in more detail in Schedule 2.
7. The legal and functional structure of the Divestment Businesses as operated to date is described in the Schedules. The Divestment Businesses, described in more detail in the Schedules, include all assets and staff that contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Businesses, in particular:
- (a) all tangible and intangible assets (including intellectual property rights);
 - (b) all licences, permits and authorisations issued by any governmental organisation for the benefit of the Divestment Businesses;
 - (c) all contracts, leases, commitments and customer orders of the Divestment Businesses; all customer credit and other records of the Divestment Businesses; and
 - (d) the Personnel to the extent described in Schedules 1 and 2.
8. For the sake of clarity, the Divestment Businesses shall not include any physical production assets or manufacturing units owned or operated by the Parties.
9. The transfer of the Divestment Businesses will include for the Vaccine Divestment Businesses a production transfer to the Purchaser's Phylaxia plant in Hungary and, for the NSAID Divestment Businesses a production transfer to one or several of the Purchaser's existing facilities or a third-party toll manufacturer (*CMO*) (the ***Production Transfer***), combined with transitional supply agreements (*TSA*) with the Purchaser, on the basis of which the Notifying Party will supply to the Purchaser the finished (and/or intermediate) products, and antigens when relevant, pending the completion of the production transfer process, as overseen by the Monitoring Trustee (together with the Technical Expert).
10. To support the transfer of the Divestment Businesses' production process, the Notifying Party commits to provide the support necessary to ensure an effective Production Transfer of the Divestment Businesses to a production location of the Purchaser's choice (***Transfer Support Commitment***).
11. Strict firewall procedures will be adopted so as to ensure that any competitively sensitive information relating to, or arising from such abovementioned arrangements (for example, product roadmaps) will not be shared with, or passed on to, anyone outside of the Divestment Businesses' operations, beyond what is reasonably required for the compliance with the obligations relating to the Production Transfers and TSAs.

species injectable NSAID) in Canada and Merial's Equioxx branded products (injectable and oral, including the [Conf]) in the U.S.

Section C. Related Commitments

Preservation of viability, marketability and competitiveness

12. From the Effective Date until Closing, the Parties shall preserve or procure the preservation of the economic viability, marketability and competitiveness of the Divestment Businesses, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Businesses. In particular the Parties undertake:
- (a) not to carry out any action that might have a significant adverse impact on the value, management or competitiveness of the Divestment Businesses or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of the Divestment Businesses;
 - (b) to make available, or procure to make available, sufficient resources for the development of the Divestment Businesses, on the basis and continuation of the existing business plans;
 - (c) to continue to participate in tender processes in a manner consistent with past practice and ordinary course of business to ensure that the day-to-day operations of the Divestment Businesses are conducted on a “business as usual” basis; and
 - (d) to take all reasonable steps, or procure that all reasonable steps are being taken, including appropriate incentive schemes (based on industry practice), to encourage all Key Personnel to remain with the Divestment Businesses, and not to solicit or move any Key Personnel to the Notifying Party's remaining business. Where, nevertheless, individual members of the Key Personnel exceptionally leave their current position, the Notifying Party shall provide a reasoned proposal to replace the person or persons concerned to the Commission and the Monitoring Trustee. The Notifying Party must be able to demonstrate to the Commission that the replacement is well suited to carry out the functions exercised by those individual members of the Key Personnel. The replacement shall take place under the supervision of the Monitoring Trustee, who shall report to the Commission.

Hold-separate obligations

13. The Notifying Party commits, from the completion of the Concentration until Closing, to keep the Divestment Businesses separate from the businesses it is retaining and to ensure that unless explicitly permitted under these Commitments: (i) management and staff of the businesses retained by the Notifying Party have no involvement in the Divestment Business; (ii) the Key Personnel and Personnel of the Divestment Business have no involvement in any business retained by the Notifying Party and do not report to any individual outside the Divestment Business to the extent reasonably practicable and in any case do not report to any individual having involvement in competing retained businesses. In addition, the Notifying Party commits to take all necessary steps to ensure that the Parties' personnel involved in the transfer of the Divestment Businesses do not use any Confidential Information from the Purchaser other than information strictly required to assist in the transfer of the Divestment Business concerned, and that they only disclose such information to other of the

Notifying Party's personnel to the extent strictly required to assist in the transfer of the Divestment Businesses concerned.

14. Until Closing, the Notifying Party shall assist the Monitoring Trustee in ensuring that the Divestment Business is managed as a distinct and saleable entity separate from the business(es) which the Notifying Party is retaining. Immediately after the adoption of the Decision, the Parties, upon consultation with the Commission and the Monitoring Trustee, shall appoint one or more Hold Separate Managers who shall be responsible for the management of the Divestment Businesses, under the supervision of the Monitoring Trustee. The Hold Separate Manager(s), who shall be part of the Key Personnel, shall manage the Divestment Businesses in the best interest of the businesses with a view to ensuring their continued economic viability, marketability and competitiveness and their independence from the businesses retained by the Notifying Party.
15. The Parties will agree with the Monitoring Trustee and the Hold Separate Manager(s) on the scope of the ring-fencing and hold-separate measures and confidentiality obligations that will apply in the period between Closing and completion of the Production Transfers.
16. The Hold Separate Manager(s) shall closely cooperate with and report to the Monitoring Trustee who will be assisted by the Technical Expert. Any replacement of the Hold Separate Manager(s) shall be subject to the procedure laid down in paragraph 12(d) of these Commitments. The Commission may, after having heard the Notifying Party, require the Notifying Party to replace the Hold Separate Manager(s).

Ring-fencing

17. The Notifying Party, shall, to the extent possible, implement, or procure to implement, all necessary measures to ensure that it does not, from completion of the Concentration, obtain any Confidential Information relating to the Divestment Businesses and that any such Confidential Information obtained by the Notifying Party before the Effective Date will be eliminated and not be used by the Notifying Party. This includes measures vis-à-vis the Notifying Party's appointees on the supervisory board and/or board of directors of the Divestment Businesses. In particular, the participation of the Divestment Businesses in any central information technology network shall be severed to the extent possible, without compromising the viability of the Divestment Businesses. The Parties may obtain or keep information relating to the Divestment Businesses which is reasonably necessary for the divestiture of the Divestment Businesses or the disclosure of which to the Notifying Party is required by law.

Non-solicitation clause

18. To the extent applicable, the Notifying Party undertakes, subject to customary limitations², not to solicit, and to procure that Affiliated Undertakings do not solicit,

² Customary limitations including, but not limited to, general advertising and approach of Personnel out of their own initiative, etc.

the Key Personnel that may be transferred with the Divestment Businesses for a period of 2 years after Closing.

Section D. Monitoring Trustee

I. Appointment procedure

19. The Notifying Party shall appoint a Monitoring Trustee to carry out the functions specified in these Commitments for a Monitoring Trustee. The Notifying Party commits not to close the Concentration before the appointment of a Monitoring Trustee.
20. The Monitoring Trustee shall be assisted by a Technical Expert with regard to all technical questions related to the Divestment Businesses, including technical aspects of the operation of the TSAs. The Technical Expert shall be appointed by and report to the Monitoring Trustee, with the Notifying Party having the right to be heard as to the suitability of the technical expert candidates. The Technical Expert will be independent of the Notifying Party and will not have or be exposed to any conflict of interest. The Notifying Party shall have the right to be heard with any reasoned objections against technical expert candidates, e.g., lack of competence or conflict of interest. In case of controversy between the Notifying Party and the Monitoring Trustee as to the suitability of the technical expert candidate, the Commission will decide on the matter.
21. The Trustee shall:
 - (a) at the time of appointment, be independent of the Notifying Party and its Affiliated Undertakings;
 - (b) possess the necessary qualifications to carry out its mandate, for example have sufficient relevant experience as an investment banker or consultant or auditor; and
 - (c) neither have nor become exposed to a Conflict of Interest.
22. The Trustee and the Technical Expert shall be remunerated by the Notifying Party in a way that does not impede the independent and effective fulfilment of their mandate.

Proposal by the Notifying Party

23. Immediately after the Effective Date, the Notifying Party shall submit the name or names of one or more natural or legal persons whom the Notifying Party proposes to appoint as the Monitoring Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the person or persons proposed as Trustee fulfil the requirements set out in paragraph 21 and shall include:
 - (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments; and
 - (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks.

Approval or rejection by the Commission

24. The Commission shall have the discretion to approve or reject the proposed Trustee and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, the Notifying Party shall appoint or cause to be appointed the person or persons concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Notifying Party shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Notifying Party

25. If all the proposed Trustees are rejected, the Notifying Party shall submit the names of at least two more natural or legal persons within one week of being informed of the rejection, in accordance with paragraphs 19 and 24 of these Commitments.

Trustee nominated by the Commission

26. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom the Notifying Party shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

27. The Trustee shall assume its specified duties and obligations in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or the Notifying Party, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee

28. The Monitoring Trustee shall:
- (a) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision;
 - (b) oversee, in close co-operation with the Hold Separate Manager(s), the on-going management of the Divestment Businesses with a view to ensuring its continued economic viability, marketability and competitiveness and monitor compliance by the Notifying Party with the conditions and obligations attached to the Decision. To that end the Monitoring Trustee shall:
 - (i) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Businesses, and the keeping separate of the Divestment Businesses from the business retained by the Parties, in accordance with paragraphs 12 and 13 of these Commitments;

- (ii) supervise the management of the Divestment Businesses as a distinct and saleable entity, in accordance with paragraph 14 of these Commitments;
- (iii) with respect to Confidential Information:
 - (A) determine all necessary measures to ensure that the Notifying Party does not after the Effective Date obtain any Confidential Information relating to the Divestment Businesses,
 - (B) in particular strive for the severing of the Divestment Businesses' participation in a central information technology network to the extent possible, without compromising the viability of the Divestment Businesses,
 - (C) make sure that any Confidential Information relating to the Divestment Businesses obtained by the Notifying Party before the Effective Date is eliminated and will not be used by the Notifying Party, and
 - (D) decide whether such information may be disclosed to or kept by the Notifying Party as the disclosure is reasonably necessary to allow the Notifying Party to carry out the divestiture or as the disclosure is required by law;
- (iv) monitor the splitting of assets and the allocation of Personnel between the Divestment Businesses and the Notifying Party or Affiliated Undertakings;
- (c) propose to the Notifying Party such measures as the Monitoring Trustee considers necessary to ensure the Notifying Party's compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability or competitiveness of the Divestment Businesses, the holding separate of the Divestment Businesses and the non-disclosure of competitively sensitive information;
- (d) provide to the Commission, sending the Notifying Party a non-confidential copy at the same time, a written report within 15 days after the end of every month until Closing that shall cover the operation and management of the Divestment Businesses as well as the splitting of assets and the allocation of Personnel so that the Commission can assess whether the business is held in a manner consistent with the Commitments;
- (e) provide the Commission, sending the Notifying Party a non-confidential copy at the same time, a written report within 15 days after the end of every quarter during the first year after Closing, and every six months for the next three years, that shall cover the production transfer and the transfer supply agreement of the Divestment Products so that the Commission can assess whether these aspects are executed in a manner consistent with the Commitments;

- (f) promptly report in writing to the Commission, sending the Notifying Party a non-confidential copy at the same time, if it concludes on reasonable grounds that the Notifying Party is failing to comply with these Commitments; and
- (g) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision.

Duties and obligations of the Notifying Party

- 29. The Notifying Party shall provide and shall cause its advisors to provide the Trustee and Technical Expert with all such co-operation, assistance and information as the Trustee and Technical Expert may reasonably require to perform its tasks. The Trustee shall have full and complete access to any of the Notifying Party's or the Divestment Businesses' books, records, documents, management or other personnel, facilities, sites and technical information necessary for fulfilling its duties under the Commitments and the Notifying Party and the Divestment Businesses shall provide the Trustee upon request with copies of any document. The Notifying Party and the Divestment Businesses shall make available to the Trustee and Technical Expert one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of its tasks.
- 30. The Notifying Party shall provide the Monitoring Trustee with all managerial and administrative support that it may reasonably request on behalf of the management of the Divestment Businesses. This shall include all administrative support functions relating to the Divestment Businesses which are currently carried out at headquarters level.
- 31. The Notifying Party shall indemnify the Trustee and its employees and agents (each an "Indemnified Party") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to the Notifying Party for, any liabilities arising out of the performance of the Trustee's and Technical Expert's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee, Technical Expert, or its employees, agents or advisors.
- 32. At the expense of the Notifying Party, the Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to the Notifying Party's approval (this approval not to be unreasonably withheld or delayed) if the Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate, provided that any fees and other expenses incurred by the Trustee are reasonable. Should the Notifying Party refuse to approve the advisors proposed by the Trustee the Commission may approve the appointment of such advisors instead, after having heard the Notifying Party. Only the Trustee shall be entitled to issue instructions to the advisors. Paragraph 31 of these Commitments shall apply *mutatis mutandis*.
- 33. The Notifying Party agrees that the Commission may share Confidential Information proprietary to the Notifying Party with the Trustee. The Trustee shall not disclose such information and the principles contained in Article 17 (1) and (2) of the Merger Regulation apply *mutatis mutandis*.

34. The Notifying Party agrees that the contact details of the Monitoring Trustee are published on the website of the Commission's Directorate-General for Competition and they shall inform interested third parties, in particular any potential purchasers, of the identity and the tasks of the Monitoring Trustee.
35. For a period of 10 years from the Effective Date the Commission may request all information from the Parties that is reasonably necessary to monitor the effective implementation of these Commitments.

III. Replacement, discharge and reappointment of the Trustee

36. If the Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a Conflict of Interest:
 - (a) the Commission may, after hearing the Trustee and the Notifying Party, require the Notifying Party to replace the Trustee; or
 - (b) the Notifying Party may, with the prior approval of the Commission, replace the Trustee.
37. If the Trustee is removed according to paragraph 36 of these Commitments, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in paragraphs 19-26 of these Commitments.
38. Unless removed according to paragraph 36 of these Commitments, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section E. The review clause

39. The Commission may extend the time periods foreseen in the Commitments in response to a request from the Notifying Party or, in appropriate cases, on its own initiative. Where the Notifying Party requests an extension of a time period, it shall submit a reasoned request to the Commission no later than one month before the expiry of that period, showing good cause. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to the Notifying Party. Only in exceptional circumstances shall the Notifying Party be entitled to request an extension within the last month of any period.
40. The Commission may further, in response to a reasoned request from the Notifying Parties showing good cause waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to the Notifying Party. The request shall not have the effect of suspending the application of the undertaking and, in particular,

of suspending the expiry of any time period in which the undertaking has to be complied with.

Section F. Entry into force

41. The Commitments shall take effect upon the date of adoption of the Decision.

SCHEDULE 1

Part A – Vaccine Divestment Businesses

1. The Vaccine Divestment Businesses consist of the rights, title and interests in the following products, including the right to develop, improve, manufacture and commercialise:
 - (a) the worldwide (excluding U.S.) Circovac branded monovalent porcine circovirus type 2 (*PCV2*) swine vaccine business as described in more detail in Part B of Schedule 1 (the *PCV2 Divestment Business*);
 - (b) the worldwide Progressis branded monovalent porcine reproductive and respiratory syndrome (*PRRS Marketed Divestment Business*) vaccine business (including [Conf]) as described in more detail in Part B and C of Schedule 1 (the *PRRS Divestment Business*);
 - (c) the worldwide Parvovax branded monovalent inactivated porcine parvovirus (*PPV*) vaccine business and the worldwide Parvoruvax branded inactivated multivalent erysipelas and PPV vaccine business as described in more detail in Part B of Schedule 1 (the *PPV Divestment Business*); and
 - (d) the worldwide Mucosiffa branded monovalent BVD ruminant vaccine business as described in more detail in Part B of Schedule 1 (the *BVD Divestment Business*).
2. All reference to “exclusively or primarily” in the Commitments text, Schedules and Annexes should be interpreted as relating to the extent to which the relevant assets to be divested are used for the relevant Divestment Products as opposed to retained products. For the avoidance of doubt, even if a Vaccine Divestment Product generates the majority of its turnover outside the divested territory, the assets which relate exclusively or primarily to that product will be transferred to the Purchaser.
3. The tangible or intangible assets and rights that relate exclusively or primarily to the Divestment Businesses will be offered to the Purchaser by means of assignment. The Purchaser will subsequently grant the Notifying Party a licence, sub-licence or otherwise access to those tangible or intangible assets and rights that relate primarily to the Divestment Business but are shared between the Divestment Business and the retained business in view of the commercialisation of products not included in the Vaccine Divestment Businesses, which include Vaccine Divestment Products commercialised in the retained territory (US for the PCV2 Divestment Product) and other products. For the avoidance of doubt, the Notifying Party shall not have the right to sub-license or grant otherwise access in a manner which derogates from the rights granted to the Purchaser to any of the tangible or intangible assets and rights that are made available to the Notifying Party by means of the present provision.
4. Concerning the tangible and intangible assets and rights that are shared between the Divestment Businesses and the retained business but relate primarily to the retained business, the Notifying Party shall grant the Purchaser a licence, sub-licence, or access to such asset or right on a non-exclusive basis.

Part B – Scope of the Vaccine Divestment Businesses

1. The PCV2 Divestment Business, PRRS Marketed Divestment Business, [Conf] PPV Divestment Business and BVD Divestment Businesses as operated to date are not currently stand-alone businesses as they are integrated into a wider operational and commercial organisation; they will therefore be separated from current operations as described below. The PCV2 Divestment Business, PRRS Marketed Divestment Business, PPV Divestment Business and BVD Divestment Business are referred to as "**Marketed Vaccine Divestment Businesses**".
2. The Marketed Vaccine Divestment Businesses include, but are not limited to the transfer of:
 - (a) all biological materials including the master virus/cells seeds (the **Master Seed**) and working seeds except for material necessary to sustain the retained US Circovac business and the monovalent Ruvax business. The Master Seed will transfer partially to the Purchaser promptly upon Closing and will be partially retained by the Notifying Party during the TSA. The remainder of the Master Seed and working seed will be transferred to the Purchaser at the end of the TSA;
 - (b) finished goods inventory, existing lifecycle management projects, pipeline products and product improvements relating to the Vaccine Divestment Businesses, held at the date of Closing;
 - (c) all recipes for the testing media and reagents that are used for the Vaccine Divestment Products and all relevant documentation required to carry out the relevant quality control tests;
 - (d) all available inventory of Vaccine Divestment Products in an intermediate (nude bottled) form, to be replenished on an on-going basis until the Purchaser has complete downstream independence;
 - (e) a [Conf] month antigen inventory stock for Circovac and Progressis to be delivered to the Purchaser as of completion by the Purchaser of its downstream independence,³ to be replenished on a continuous basis and, if required⁴ sufficient antigen inventory stock ([Conf] months) for Parvovax, Parvoruvax and Mucosiffa, to be replenished on an on-going basis until the Purchaser has complete upstream independence;
 - (f) all relevant data, books, records, marketing and advertising/promotional materials, trade-dress, i.e. total image or overall design of appearance of product or its packaging and other documents to the extent exclusively or

³ Should the Purchaser achieve downstream independence before January 2019, the Notifying Party shall transfer the maximum available inventory stock available to the Purchaser, supervised by the Hold Separate Manager and the Monitoring Trustee. Subsequently, the Notifying Party shall increase and replenish the antigen inventory so as to achieve a [Conf] month antigen inventory stock for the production of Circovac and Progressis by January 2019.

⁴ In the event that the downstream and upstream production transfer for Mucosiffa, Parvovax and Parvoruvax cannot be completed simultaneously.

primarily related to or necessary for the operations of the Vaccine Divestment Businesses;

- (g) all know-how for the manufacturing of the Vaccine Divestment Products (including but not limited to the manufacturing of any active ingredient, antigen, reagent, adjuvant or other components of the Vaccine Divestment Products) as well as all know-how required for or associated with obtaining and/or maintaining manufacturing and marketing approvals for the Vaccine Divestment Products in the EEA, including but not limited to stability/reproducibility data (including process capability (**CpK**) data), periodic safety reports, any clinical reports, status reports, yearly product quality review reports;
- (h) with respect to all patent rights exclusively or primarily related to the Vaccine Divestment Businesses, the Notifying Party shall:
 - (i) assign all patent rights that are exclusively owned by Merial; and
 - (ii) use its best efforts, subject to third party rights, to assign the Merial rights under the patents that are jointly owned by Merial with a third party or currently in-licensed by Merial from a third party. Alternatively, the Notifying Party will provide the Purchaser with a licence or a sub-licence for the production and commercialisation of the Vaccine Divestment Products in the EEA territory.
- (i) all trademarks and the registered domain names that are exclusively or primarily used for the commercialisation of Vaccine Divestment Businesses (including the ones listed in **Annex B**);
- (j) all other IP rights (including, for the avoidance of doubt, in relation to the reagents), product formulations, know how, packaging specifications to the extent exclusively or primarily related to the manufacture and/or sale of Vaccine Divestment Businesses;
- (k) all licences, permits and marketing authorisations issued by any governmental organization and held by the Parties or their Affiliated Undertakings, as well as applications for variations in the context of the Production Transfer, that are related to the manufacture and/or sale of the Vaccine Divestment Businesses, including any dossiers relating to current or pending authorisations, to the extent transferrable (including the ones set out in **Annex C**). The transfer and possible updates of the abovementioned permits and authorisations in the EEA will be at the cost of the Notifying Party;
- (l) the Notifying Party will use its Best Efforts to transfer or assign, as appropriate, all customer contracts or relationships (including distribution agreements), and will transfer all available customer lists, customer credit and other records, and any other relevant customer information related to the Vaccine Divestment Businesses;
- (m) if requested by the Purchaser, the Notifying Party will use its Best Efforts to transfer, or assign, as appropriate, all contracts, agreements or relationships (including raw material and reagents supply agreements), leases, commitments and understandings with third-party suppliers of products or services related to

the Vaccine Divestment Businesses (except to the extent required to be retained in order to manufacture for the Purchaser under the TSA);

3. For the avoidance of doubt, in addition to the abovementioned assets, the Marketed Vaccine Divestment Businesses will include all other assets and rights which are used and are necessary for the continued viability and competitiveness of the Marketed Vaccine Divestment Businesses. These assets will be offered to the Purchaser on the following basis:
 - (a) an assignment of all tangible and intangible assets and rights that relate exclusively or primarily to the Marketed Vaccines Divestment Businesses. The Purchaser will subsequently grant the Notifying Party a licence, sub-licence or otherwise access to those tangible or intangible assets and rights that relate primarily to the Marketed Vaccine Divestment Business but are shared between the Marketed Vaccine Divestment Business and the retained business; and
 - (b) a licence, sub-licence, or otherwise access to, on a non-exclusive basis, the shared tangible and intangible assets and rights that are shared between the Marketed Vaccine Divestment Businesses and the retained business but relate primarily to the retained business.

The Monitoring Trustee shall supervise the Notifying Party's performance in this regard.

4. At the option of the Purchaser and subject to applicable employment legislation, the Notifying Party will use its Best Efforts, including appropriate incentive schemes, to transfer to the Purchaser any of the operational/production, industrial/technical, R&D/Regulatory and/or commercial/marketing personnel in the EEA that are necessary to the Vaccine Divestment Businesses, on the following basis:
 - (a) **Key Personnel:**
 - (i) The Notifying Party has identified the following key functions for the Vaccine Divestment Business:
 - [Conf];
 - [Conf];
 - [Conf];
 - [Conf]; and
 - [Conf].
 - (ii) The Key Personnel for each of the abovementioned key functions will be identified by the Parties in consultation with the Hold Separate Manager and the Monitoring Trustee as soon as possible following the Effective Date. During a period of [Conf] months from the Effective Date, the Parties will allow the Purchaser to have access to and make an employment offer to the Key Personnel in the abovementioned key functions. The Parties will take all reasonable steps, or procure that all reasonable steps are being taken, including appropriate incentive

schemes (based on industry practice), to encourage the members of Key Personnel who have received an employment offer from the Purchaser to transfer to the Purchaser, subject to applicable employment legislation.

- (iii) ***Other personnel:*** At the request of the Purchaser, depending on the Purchaser's needs and subject to applicable employment legislation, the Notifying Party will use its Best Efforts, including appropriate incentive schemes, to transfer any other personnel which the Purchaser may reasonably require for the operation of the Vaccine Divestment Business in the EEA. In particular, the Parties will use their Best Efforts (subject to applicable employment legislation), including appropriate incentive schemes, to transfer to the Purchaser the Swine Vaccine Commercial Personnel identified in the Products Asset Purchase Agreement. In the period between the Effective Date and Closing, the Monitoring Trustee will verify that the Purchaser will have the commercial personnel to replicate Merial's existing commercial presence in the EEA, taking into account the Swine Vaccine Commercial Personnel to be transferred to, and the commercial personnel already available to the Purchaser.

5. For the avoidance of doubt, the Notifying Party shall retain:
 - (a) Merial's Circovac business in the US. This shall be effected by means of exclusion of any US-specific assets, and/or a reverse carve-out of US-specific rights, from the items listed in paragraph 2 above.
 - (b) Merial's monovalent Ruvax vaccine business worldwide, including sufficient erysipelas Master Seeds and working seeds. The Notifying Party shall retain the Ruvax business by means of an exclusion of any Ruvax specific assets, and/or reverse carve-out of assets or rights which relate primarily to Ruvax but are shared with the Parvoruvax Divestment Business, from the items listed in paragraph 2 above, whereby the Notifying Party shall grant the Purchaser a licence, sub-licence, or access to such retained assets or rights on a non-exclusive basis in accordance with the general principle set forth in Part A paragraph 4 above.
6. The Parties commit not to use or enable third parties to use any assets that are related to the Vaccine Divestment Products but are retained by the Parties for use in connection with their retained businesses for purposes of development, improvement and manufacture in view to commercialise the Vaccine Divestment Products or biologically identical products in the EEA territory.
7. Following the Production Transfer and the expiry of the TSA, the Purchaser will use its own manufacturing facilities and equipment at one or several sites for manufacturing and packaging of Vaccine Divestment Businesses.
8. For the avoidance of doubt, the Vaccine Divestment Businesses shall not include any right, title and/or interest in:
 - (a) any production assets, manufacturing units, or R&D facilities;

- (b) the patent royalties which Merial is entitled to under the licence agreements it has concluded with BI and/or third parties;
- (c) the Parties' company name, mark, or logo in any form;
- (d) all books and records required to be retained pursuant to any statute, rule, regulation or ordinance, provided that the Notifying Party will provide copies of such documents necessary for the Vaccine Divestment business to the Purchaser, upon request;
- (e) general books of account and books of original entry that comprise the Notifying Party's or any of its Affiliated Undertakings' permanent accounting or tax records provided that the Notifying Party will provide copies of such documents necessary for the Vaccine Divestment Business to the Purchaser, upon request; and
- (f) all books and records subject to the attorney-client or other legally recognised privilege, provided that the Notifying Party will provide copies of such documents necessary for the Vaccine Divestment Business to the Purchaser if the Purchaser and the Notifying Party enter into an arrangement that preserves any such privilege.

Part C – [Conf] Pipeline Divestment Business

1. **[Conf] Pipeline Divestment Business** consists of Merial’s rights to develop and commercialise [Conf] subject to the usual regulatory and technical risks inherent in a vaccine development project.
2. In accordance with paragraph 7 of these Commitments, the **[Conf] Pipeline Divestment Business** includes but is not limited to the transfer of:
 - (a) all biological material already developed by Merial, including available Master Seeds;
 - (b) all relevant data generated during the development project, including all material technical, preclinical, clinical and marketing files, reports, plans, know-how and records in the possession of or under control of Merial existing prior to Closing, which is exclusively or primarily related to or otherwise necessary for the development of commercialisation of the new [Conf] Pipeline Product;
 - (c) all clinical data and studies exclusively or primarily relating to or otherwise necessary to the development of the [Conf] Pipeline Product existing prior to Closing;
 - (d) all correspondence pertaining to regulatory filings and approvals (if any) relating to the commercialisation of the [Conf] Pipeline Product;
 - (e) all recipes for the testing media and reagents that used are for the Vaccine Divestment Products and all relevant documentation required to carry out the relevant quality control tests;
 - (f) any intellectual property rights where available which are primarily or exclusively related to the [Conf] Pipeline Product. These intellectual property rights include product formulations, manufacturing, know-how and other secret know-how, packaging specifications, rights to the trade dress, and all related copyright;
 - (g) relevant data, books, records, and other documents exclusively or primarily related to or necessary for the development and commercialisation of the [Conf] Pipeline Product provided that the Parties redact from such copies any information that does not relate to the [Conf] Pipeline Product; and
 - (h) to the extent applicable,¹ the Notifying Party will use its Best Efforts to transfer to the purchaser any contract or relationships with third party contract development organisations concerning services related to the [Conf] Pipeline Divestment Business (except to the extent required to be retained in order to continue the development of the [Conf] Pipeline Divestment Business according to the plans and projections at the date of these Commitments).

¹ It is currently expected that any studies in relation to the [Conf] Pipeline Product which are being undertaken by third party contract development organisations will have been completed by the time of Closing.

3. For the avoidance of doubt, in addition to the abovementioned assets, the [Conf] Pipeline Divestment Businesses will include all other assets and rights which are used and are necessary for the continued viability and competitiveness of the [Conf] Pipeline Divestment Businesses. These assets will be offered to the Purchaser on the following basis:
 - (a) an assignment of all tangible and intangible assets and rights that relate exclusively or primarily to the [Conf] Pipeline Divestment Businesses. The Purchaser will subsequently grant the Notifying Party a licence, sub-licence or otherwise access to those tangible or intangible assets and rights that relate primarily to the [Conf] Pipeline Divestment Business but are shared between the [Conf] Pipeline Divestment Business and the retained business; and
 - (b) a licence, sub-licence, or otherwise access to, on a non-exclusive basis, the shared tangible and intangible assets and rights that are shared between the [Conf] Pipeline Divestment Businesses and the retained business but relate primarily to the retained business.

The Monitoring Trustee shall supervise the Notifying Party's performance in this regard.

4. The Parties commit not to use or enable third parties to use any assets that are related to the [Conf] Pipeline Divestment Products but are retained by the Parties for use in connection with their retained businesses for purposes of development, improvement and manufacture in view to commercialise the [Conf] Pipeline Divestment Products or biologically identical products in the EEA territory.
5. The [Conf] Pipeline Project will be transferred to the Purchaser at completion of the clinical development with the finalised, written reports. The Notifying Party commits (subject to circumstances entirely outside of its control) to continue the development of the [Conf] Pipeline Divestment Business according to the plans and projections at the date of these Commitments. The Notifying Party commits to update the Hold Separate Manager, the Purchaser, Monitoring Trustee and/or Technical Expert on the progress in the development of the [Conf] Pipeline Product and to grant them access to any relevant information and data regarding the development. Furthermore, the Notifying Party commits to provide assistance in obtaining the relevant marketing authorisation applications.
6. The [Conf] Pipeline Divestment Business will be transferred upon completion of the clinical development phase, according to the plans and projections at the date of these Commitments. Upon completion of the clinical development phase, the Notifying Party commits to separate and transfer the [Conf] Pipeline Divestment Businesses' production process in accordance with the Production Transfer process described in Schedule 1, Part D, paragraphs 1-3.
7. For the avoidance of doubt, the [Conf] Pipeline Divestment Business shall not include any right, title and/or interest in:
 - (a) raw materials, other than any raw materials used to develop the [Conf] Pipeline Product;
 - (b) any production assets, manufacturing units, or R&D facilities;

- (c) the Parties' company name, mark, or logo in any form;
- (d) all books and records required to be retained pursuant to any statute, rule, regulation or ordinance, provided that the Notifying Party will provide copies of such documents necessary for the [Conf] Pipeline Divestment Business to the Purchaser, upon request;
- (e) general books of account and books of original entry that comprise the Notifying Party's or any of its Affiliated Undertakings' permanent accounting or tax records provided that the Notifying Party will provide copies of such documents necessary for the [Conf] Pipeline Divestment Business to the Purchaser, upon request; and
- (f) all books and records subject to the attorney-client or other legally recognised privilege, provided that the Notifying Party will provide copies of such documents necessary for the [Conf] Pipeline Divestment Business to the Purchaser if the Purchaser and the Notifying Party enter into an arrangement that preserves any such privilege.

Part D – Vaccine Production Transfer

1. The Notifying Party commits to separate and transfer the Vaccine Divestment Businesses' production process (the ***Production Transfer***) to the Purchaser's own production facility at one or several sites.
2. The Production Transfer will involve the following:
 - (a) Downstream production process: transfer of the downstream processing, filing and packaging production process for the production of the relevant Vaccine Divestment Product in final form; and
 - (b) Upstream production process: transfer of the relevant upstream Vaccine Divestment Product production process including, but not necessary limited to production of antigen.
3. To ensure the transfer of the production of the Vaccine Divestment Businesses to the location of the Purchaser's choice, the Notifying Party commits to provide the Purchaser with all information and materials to allow the Purchaser to replicate Merial's existing manufacturing equipment and processes in its own manufacturing capabilities, including but not limited to:
 - (a) detailed user requirement specifications for the design (equipment) and construction of a new upstream, and to the extent necessary, downstream facility;
 - (b) detailed specifications of all relevant materials required for the production process;
 - (c) relevant input materials, including reference and/or cell materials and reagents; and
 - (d) detailed standard operating procedures for the execution of all in process controls and final product testing including training employees.

Gerland Antigen Supply

4. At the option of the Purchaser of the Vaccine Divestment Business, as of January 2019, the Notifying Party will dedicate its Gerland (France) production capacity exclusively or primarily to Circovac and Progressis antigen production (***Gerland Antigen Supply***) giving priority to the production of the Circovac and Progressis antigen production over the products of the retained business until the Purchaser has completed its upstream production capability at the Phylaxia plant. The relevant antigen shall be made available to the Purchaser at full manufacturing cost reflecting the current capacity utilization levels at the time of signing the relevant supply agreement, subject to the approval of the Monitoring Trustee and the Technical Expert. The relevant agreement between the Parties and the Purchaser will allow for a yearly revision of the costs of supply, subject to the approval of the Monitoring Trustee and the Technical Expert, in the event of an increase or decrease in the manufacturing cost of [Conf]% or more, it being understood that any increases in the costs of supply can be based on external factors only (e.g. a change requested by the Purchaser resulting in an increase in the manufacturing cost, an increase in the cost of

raw materials or any other justified circumstances outside the control of the Parties resulting in an increase in the manufacturing costs).

5. Should the Purchaser opt for the Gerland Antigen Supply, the Notifying Party will make available the full nominal capacity of the Gerland manufacturing capacity for the production of the relevant Vaccine Divestment Product antigens and the Purchaser shall be granted permanent access and monitoring rights to ensure that the antigen production is undertaken according to product specification. The Purchaser's technicians and operators will be granted access to observe the production process to facilitate the Production Transfer and training process. Additionally, if required, the Notifying Party will guarantee supplies of the Circovac, Progressis and Parvovirus antigen from the Lyon Portes-des-Alpes site, as a back-up supply source under the Gerland Antigen Supply option.

Transfer support commitment

6. To support the transfer of the Vaccine Divestment Businesses' production process, the Parties commit to provide to the Purchaser, at no cost and until six months after the Purchaser has successfully produced three full scale manufacturing batches of the relevant product in its production unit, any support to ensure an effective Production Transfer of the Vaccine Divestment Businesses to the Purchaser's Phylaxia plant.
7. In addition, until the Purchaser has obtained the required variations to the marketing authorizations of the Vaccine Divestment Products, the Parties commit to provide under supervision of the Monitoring Trustee and the Technical Expert, any support which the Purchaser may require to address manufacturing process issues in the production of the Vaccine Divestment Products and to achieve an acceptable robustness level of the relevant production processes of the Vaccine Divestment Products, as reflected in the relevant control charts for the products concerned.
8. The transfer support will at the Purchaser's request be provided either at the Parties' production site(s) or at the Purchaser's site and will include:
 - (a) support for the design, including providing general specifications and supporting the Purchaser in acquiring specific equipment, and the commissioning of a new production facility for the production of the Vaccine Divestment Products or the adjustment of an existing production facility at the Purchaser's premises, on the basis of the know-how and technical documentation included in the Divestment Business;
 - (b) technical training and transfer know-how to the Purchaser's employees in relation to the production of the Vaccine Divestment Products, and any other aspects regarding the operation and maintenance of the relevant production assets, by training at the Purchaser's facility after completion of the Production Transfer at the Notifying Party's own expense;
 - (c) R&D/clinical support by (a) advising on technical issues relating to research; (b) finishing on-going clinical studies; (c) transferring clinical studies, assays and technology; (d) providing assistance for pharmacovigilance and regulatory submissions, (d) support the Purchaser in quality control testing; and (e) train Purchaser's designated personnel; and

- (d) advice on technical knowledge documentation; assistance to the Purchaser to make any necessary regulatory filings and obtain any necessary authorisations; and assist, where necessary in the transfer to the Purchaser of such licences, permits and authorisations concerning the Vaccine Divestment Businesses.
9. The production transfer support will be provided by a team of expert employees of the Parties (*Production Transfer Personnel*), listed at **Annex D**, who will prioritise the effective Production Transfer of the Vaccine Divestment Businesses over their work for the retained businesses and make themselves available according to the requirements for a timely and effective implementation of the Production Transfers. The Parties will implement an appropriate incentive scheme (based on industry practice) to incentivize the Production Transfer Personnel to complete the Production Transfers in a timely and effective manner. The Production Transfer Personnel will be bound by appropriate confidentiality obligations which will be agreed in accordance with paragraph 15 of the Commitments. Where individual members of the Production Transfer Personnel leave their position, the Parties shall replace the person or persons concerned and inform the Monitoring Trustee and the Technical Expert of the replacement.
 10. The Production Transfer Personnel will be assisted by a steering committee, identified at **Annex D**, which will be composed of Merial employees with prior production transfer experience and will oversee/manage and make all necessary strategic decisions in relation to the execution of the Production Transfer of the Vaccine Divestment Products to the Purchaser's Phylaxia plant.
 11. Finally, at the request of the Purchaser, the Parties commit to provide to the Purchaser any support it may require to take over at, or as soon as possible after Closing the distribution of the Divestment Products.

Part E – Vaccine TSA

1. The Notifying Party shall enter into a Transitional Supply Agreement (*TSA*) and supply the products within the scope of Vaccine Divestment Businesses (including the [Conf] Pipeline Divestment Business, if it is completed successfully) until the Production Transfer has been completed. The TSA will be monitored by the Monitoring Trustee (together with the Technical Expert).

Supply of the intermediate or final product:

2. Subject to the requirements of the Purchaser, the Notifying Party shall supply the Vaccine Divestment Products in a finished or intermediate (nude bottled) form at full manufacturing costs on a cost pass-through basis (i.e. no mark-up) to the Purchaser, until the Purchaser has completed the downstream Production Transfer process for the relevant Vaccine Divestment Product or, in any case, for a maximum term of 30 months, extendable with approval of the Monitoring Trustee (together with the Technical Expert), if such extension is required in order to complete the transfer of the downstream production of the relevant Vaccine Divestment Product to the Purchaser's own facilities. Costs will be fixed at the time of signing of the TSA for the duration of the agreement. The TSA will allow for a yearly revision of the costs of supply, subject to the approval of the Monitoring Trustee and the Technical Expert, in the event of an increase or decrease in the manufacturing cost of [Conf]% or more, it being understood that any increases in the costs of supply can be based on external factors only (e.g. a change requested by the Purchaser resulting in an increase in the manufacturing cost, an increase in the cost of raw materials or any other justified circumstances outside the control of the Parties resulting in an increase in the manufacturing costs). .
3. The available inventory of Vaccine Divestment Products in a finished or intermediate (nude bottled) form transferred to the Purchaser upon Closing will be replenished on an on-going basis at least at pre-Transaction announcement level until the Purchaser has complete downstream independence.

Antigen supply:

4. Once the Purchaser has completed the downstream Production Transfer process, the Notifying Party, shall supply the relevant Vaccine Divestment Products antigen at full manufacturing costs on a cost pass-through basis (i.e. no mark-up) to the Purchaser, until the Purchaser has completed the upstream antigen transfer process or, in any case, for a maximum term of 3 years extendable subject to approval of the Monitoring Trustee (together with the Technical Expert), if such extension is required in order to complete the transfer of the antigen production of the Vaccine Divestment Product to the Purchaser's own facilities. Costs will be fixed at the time of signing of the TSA for the duration of the agreement. The TSA will allow for a yearly revision of the costs of supply, subject to the approval of the Monitoring Trustee and the Technical Expert, in the event of an increase or decrease in the manufacturing cost of [Conf]% or more, it being understood that any increases in the costs of supply can be based on external factors only (e.g. a change requested by the Purchaser resulting in an increase in the manufacturing cost, an increase in the cost of raw materials or any other justified circumstances outside the control of the Parties resulting in an increase in the manufacturing costs).

5. The [Conf] month antigen inventory stock for Circovac and Progressis and any antigen inventory stock for Parvovax, Parvoruvax and Mucosiffa to be transferred to the Purchaser upon completion by the Purchaser of downstream independence, will be replenished on an on-going basis at least at pre-Transaction announcement level until the Purchaser has complete upstream independence.

Reagents supply:

6. Subject to the requirements of the Purchaser, the Notifying Party, shall supply any reagents manufactured in-house by Merial necessary for the manufacturing and/or testing of the Vaccine Divestment Products at full manufacturing costs on a cost pass-through basis (i.e. no mark-up) to the Purchaser for the duration of the TSA. Costs will be fixed at the time of signing the TSA for the duration of the agreement. The TSA will allow for a yearly revision of the costs of supply, subject to the approval of the Monitoring Trustee and the Technical Expert, in the event of an increase or decrease in the manufacturing cost of [Conf]% or more, it being understood that any increases in the costs of supply can be based on external factors only (e.g. a change requested by the Purchaser resulting in an increase in the manufacturing cost, an increase in the cost of raw materials or any other justified circumstances outside the control of the Parties resulting in an increase in the manufacturing costs).
7. At the option of the Purchaser, the Notifying Party shall use its Best Efforts to assist the Purchaser to procure the reagents manufactured by third parties necessary for the manufacture and/or testing of any Vaccine Divestment Product for the duration of the TSA . If the Purchaser is not able to source such reagents, the Parties commit to enter, at the option of the Purchaser, into back-to-back supply agreements with reagent suppliers and to make such reagents available to the Purchaser at cost, for such period as required by the Purchaser to establish the Vaccine Divestment Businesses as viable and independent businesses, but not exceeding the duration of the TSA.
8. The TSA will have the following characteristics:
 - (a) Sufficient Master Seed and working seed will be retained by the Notifying Party during the TSA to continue the production of the relevant Vaccine Divestment Products antigen for the Purchaser until the Purchaser has full upstream independency from the Notifying Party;
 - (b) The Purchaser will grant the Notifying Party a temporary licence for the use of the relevant Master Seed, working seed, intellectual property, know-how and technical documentation required for the production of the Vaccine Divestment Products and relevant antigens;
 - (c) The Notifying Party shall manufacture the Vaccine Divestment Products and/or antigen in accordance with specified existing product specifications and it shall continue to manufacture the Vaccine Divestment Products and the relevant antigen at the manufacturing facilities which are currently owned and used by Merial for the production of the relevant vaccines (with the exception of a shift of Circovac/Progressis antigen production to the Gerland site, at the Purchaser's request) to ensure the continued supply of the Vaccine Divestment Products, giving priority to the production of the Vaccine Divestment Products over the products of the retained business should there be technical difficulties or shortage of supply.

- (d) The Vaccine Divestment Product or antigen shall be produced under the same cost structure and of the same quality and consistent with past practice as Merial produced the Vaccine Divestment Product or antigen prior to Closing.
 - (e) The Notifying Party shall supply sufficient volumes of the finished Vaccine Divestment Product and antigen allowing the Purchaser to maintain and expand the existing market position until the Purchaser has established an alternative production capacity, with no limitation to the volume of production subject to Merial's relevant existing manufacturing facilities' capacity.
 - (f) The Notifying Party will provide the Purchaser with assistance in order to implement any changes required to the packaging of the relevant Vaccine Divestment Products.
9. Under the terms of the TSA, the Purchaser will have the right to request on a transitional basis the Parties to assist in the distribution (for example via logistics and supply chain support) of the Vaccine Divestment Products on the Purchaser's behalf in the EEA on a cost basis, until the Purchaser has established commercial independence and in any event for not longer than the duration of the TSA.
10. In the event of a dispute between the Notifying Party and the Purchaser regarding the Production Transfer or the TSA, the matter shall be referred to the Monitoring Trustee (together with the Technical Expert) for resolution.

SCHEDULE 2

Part A – NSAID Divestment Businesses

1. The NSAID Divestment Business consists of the rights, title and interests in the following products, including the right to develop, improve, manufacture and commercialise:
 - (a) Merial’s injectable non-steroidal anti-inflammatory drugs (*NSAIDs*) for multi-species on an EEA-wide basis,² including the brands Ketofen, Wellicox/Allevinix, Genixine and Equioxx Injectable; and
 - (b) Merial’s Equioxx Paste branded oral NSAIDs for horses on an EEA-wide basis (including [*Conf*]) ((a) and (b) the *NSAID Divestment Products*).
2. All reference to “exclusively or primarily” in the Commitments text, Schedules and Annexes should be interpreted as relating to the extent to which the relevant assets to be divested are used for the relevant Divestment Products as opposed to retained products. For the avoidance of doubt, even if a NSAID divested product generates the majority of its turnover outside the divested territory, the assets which relate exclusively or primarily to that product will be transferred to the Purchaser.
3. The tangible or intangible assets and rights that relate exclusively or primarily to the Divestment Businesses will be offered to the Purchaser by means of assignment. The Purchaser will subsequently grant the Notifying Party a licence, sub-licence or otherwise access to those tangible or intangible assets and rights that relate primarily to the Divestment Business but are shared between the Divestment Business and the retained business in view of the commercialisation of products not included in the NSAID Divestment Businesses, which include NSAID Divestment Products commercialised in the retained territory (outside the EEA for the NSAID Divestment Products) and other products. For the avoidance of doubt, the Notifying Party shall not have the right to sub-license or grant otherwise access in a manner which derogates from the rights granted to the Purchaser to any of the tangible or intangible assets and rights that are made available to the Notifying Party by means of the present provision.
4. Concerning the tangible and intangible assets and rights that are shared between the Divestment Businesses and the retained business but relate primarily to the retained business, the Notifying Party shall grant the Purchaser a licence, sub-licence, or access to such asset or right on a non-exclusive basis.

² The Notifying Party commits to divest all NSAID Divestment Products on an EEA-wide basis to solve the Commission’s potential competition concerns. However, the Notifying Party intends to divest the NSAID Divestment Products on a worldwide basis, excluding Anafen (Merial’s ketofen based multi-species injectable NSAID) in Canada and Merial’s Equioxx branded products (including the [*Conf*]) in the U.S.

Part B – Scope of the NSAID Divestment Businesses

1. The NSAID Divestment Business as operated to date is not currently a stand-alone business activity as it is integrated into a wider operational and commercial organisation; it will therefore be separated from current operations as described below.
2. The **NSAID Divestment Business** includes but is not limited to the transfer of:
 - (a) the brands Ketofen, Wellicox/Allevinix, Genixine, Equioxx Injectable and Equioxx Paste in the EEA. For EEA countries where the brands are currently not registered, the Parties commit not to register any of them or oppose to such registration by the Purchaser;
 - (b) finished goods inventory, work in progress, pipelines, product improvements relating to the NSAIDs Divestment Business held at the date of Closing;
 - (c) all relevant clinical reports relating to the NSAID Divestment Business existing prior to Closing;
 - (d) all know-how for the manufacturing of the NSAID Divestment Products as well as all know-how required for or associated with obtaining and/or maintaining manufacturing and marketing approvals for the NSAID Divestment Products in the EEA, including stability/reproducibility data (including process capability (*CpK*) data), periodic safety reports, any clinical reports, status reports, yearly product quality review reports;
 - (e) all relevant data, books, records, marketing and advertising/promotional materials, trade-dress, i.e. total image or overall design of appearance of product or its packaging and other documents to the extent exclusively or primarily related to or necessary for the operation of the NSAID Divestment Business;
 - (f) all trademarks and the registered domain names that are exclusively or primarily used for the commercialisation of the NSAID Divestment Products (including the ones set out in **Annex E**);
 - (g) a licence or sub-licence to Merial's [*Conf*] patent rights on a non-exclusive basis;
 - (h) all other IP rights, product formulations, know-how, packaging specifications to the extent exclusively or primarily related to the manufacture and/or sale of the NSAID Divestment Products;
 - (i) all licences, permits, and marketing authorisations issued by any governmental organization and held by the Parties or their Affiliated Undertakings, as well as to support applications for variations in the context of the Production Transfers, that are related to the NSAID Divestment Products including any dossiers relating to current or pending authorisations, to the extent transferrable (as set out in **Annex F**). The transfer and updates of the abovementioned permits and authorisations will be at the cost of the Notifying Party;

- (j) the Notifying Party will use its Best Efforts to transfer or assign, as appropriate, all customer contracts or relationships (including distribution agreements) and will transfer all available customer lists, customer credit and other records related to the NSAID Divestment Business;
 - (k) if requested by the Purchaser, the Notifying Party will use its Best Efforts to transfer, or assign, as appropriate, all contracts, agreements or relationships (including raw material supply agreements), leases, commitments and understandings with third-party suppliers of products or services related to the NSAID Divestment Business (except to the extent required to be retained in order to manufacture for the Purchaser under the TSA);
 - (l) at the option of the Purchaser, the Parties will use their Best Efforts to transfer (or otherwise provide) to the Purchaser sufficient rights under the agreement currently in place between Merial and [Conf] for Purchaser to obtain supply of [Conf];
 - (m) at the option of the Purchaser, the Parties will use their Best Efforts to reach an arrangement with [Conf] pursuant to which Purchaser could purchase [Conf] directly from [Conf] under the agreement currently in place between Merial and [Conf], through the end of the current term thereof ([Conf]), without the Parties or Purchaser knowing the quantity of [Conf] purchased or forecasted for purchase by the other party.
 - (n) access to any other tangible or intangible assets, with the exception of any physical production assets, which the Purchaser may require to successfully complete and transfer of the NSAID Divestment Business to an alternative production location; and
3. For the avoidance of doubt, in addition to the abovementioned assets, the NSAID Divestment Businesses will include all other assets and rights which are used and are necessary for the continued viability and competitiveness of the NSAID Divestment Businesses. These assets will be offered to the Purchaser on the following basis:
- (a) an assignment of all tangible and intangible assets and rights that relate exclusively or primarily to the NSAID Divestment Businesses. The Purchaser will subsequently grant the Notifying Party a licence, sub-licence or otherwise access to those tangible or intangible assets and rights that relate primarily to the NSAID Divestment Business but are shared between the NSAID Divestment Business and the retained business; and
 - (b) a licence, sub-licence, or otherwise access to, on a non-exclusive basis, the shared tangible and intangible assets and rights that are shared between the NSAID Divestment Businesses and the retained business but relate primarily to the retained business.

The Monitoring Trustee shall supervise the Notifying Party's performance in this regard.

4. At the option of the Purchaser and subject to applicable employment legislation, the Notifying Party will use its Best Efforts, including appropriate incentive schemes to transfer to the Purchaser an employee for each of the key functions identified below:³
 - (i) The Notifying Party has identified the following key functions for the NSAID Divestment Businesses:
 - [Conf];
 - [Conf];
 - [Conf]; and
 - [Conf].
 - (ii) The Key Personnel for each of the abovementioned key functions will be identified by the Parties in consultation with the Hold Separate Manager and the Monitoring Trustee as soon as possible following the Effective Date. During a period of 12 months from the Effective Date, the Parties will allow the Purchaser to have access to and make an employment offer to the Key Personnel in the abovementioned key functions. The Parties will take all reasonable steps, or procure that all reasonable steps are being taken, including appropriate incentive schemes (based on industry practice), to encourage the members of Key Personnel who have received an employment offer from the Purchaser to transfer to the Purchaser, subject to applicable employment legislation.
5. The Parties commit not to use or enable third parties to use any assets that are related to the NSAID Divestment Products but are retained by the Parties for use in connection with their retained businesses for purposes of development, improvement and manufacture in view to commercialise the NSAID Divestment Products or biologically identical products in the EEA territory.
6. Following the Production Transfer and the expiry of the TSA, the Purchaser will either use its own manufacturing facilities and equipment at one or several sites and/or a CMO for manufacturing and packaging of the NSAID Divestment Products.
7. For the avoidance of doubt, the NSAID Divestment Business shall not include any right, title and/or interest in:
 - (a) any production assets, manufacturing units, or R&D facilities;
 - (b) the Parties' company name, mark, or logo in any form;
 - (c) all books and records required to be retained pursuant to any statute, rule, regulation or ordinance, provided that the Notifying Party will provide copies of such documents necessary for the NSAID Divestment Business to the Purchaser, upon request;

³ For the avoidance of doubt, the Key Personnel identified for the key functions described Schedule 1 Part B in relation to vaccines may qualify to fulfil the key functions for the NSAID Divestment Business.

- (d) general books of account and books of original entry that comprise the Notifying Party's or any of its Affiliated Undertakings' permanent accounting or tax records provided that the Notifying Party will provide copies of such documents necessary for the NSAID Divestment Business to the Purchaser, upon request; and
- (e) all books and records subject to the attorney-client or other legally recognized privilege, provided that the Notifying Party will provide copies of such documents necessary for the NSAID Divestment Business to the Purchaser if the Purchaser and the Notifying Party enter into an arrangement that preserves any such privilege.

Part C – [Conf] Pipeline Product

The [Conf] pipeline product ([Conf] *Pipeline Product*)

1. The [Conf] Pipeline Product consists of the rights to develop and commercialise [Conf].
2. In accordance with paragraph 7 of these Commitments, the NSAID Pipeline Product includes but is not limited to the transfer of:
 - (a) pharmaceutical material already developed by Merial in relation to the [Conf] Pipeline Product;
 - (b) all relevant data generated during the development project, including all material technical, preclinical, clinical and marketing files, reports, plans, know-how and records in the possession of or under control of Merial existing prior to Closing in relation to the [Conf] Pipeline Product;
 - (c) all clinical data and studies relating to the development of the [Conf] Pipeline Product, existing prior to Closing;
 - (d) all correspondence pertaining to regulatory filings and approvals (if any) relating to the commercialisation of the [Conf] Pipeline Product;
 - (e) any intellectual property rights which are primarily or exclusively related to the [Conf] Pipeline Product. These intellectual property rights include product formulations, manufacturing, know-how and other secret know-how, packaging specifications, rights to the trade dress, and all related copyright; and
 - (f) the relevant data, books, records, and other documents exclusively or primarily related to or necessary for the development and commercialisation of the [Conf] Pipeline Product provided that the Parties redact from such copies any information that does not relate to the [Conf] Pipeline Product.
3. For the avoidance of doubt, in addition to the abovementioned assets, the [Conf] Pipeline Product will include all other assets and rights which are used and are necessary for the continued viability and competitiveness of the [Conf] Pipeline Product. These assets will be offered to the Purchaser on the following basis:
 - (a) an assignment of all tangible and intangible assets and rights that relate exclusively or primarily to the [Conf] Pipeline Product. The Purchaser will subsequently grant the Notifying Party a licence, sub-licence or otherwise access to those tangible or intangible assets and rights that relate primarily to the [Conf] Pipeline Product but are shared between the [Conf] Pipeline Product and the retained business; and
 - (b) a licence, sub-licence, or otherwise access to, on a non-exclusive basis, the shared tangible and intangible assets and rights that are shared between the [Conf] Pipeline Product and the retained business but relate primarily to the retained business.

The Monitoring Trustee shall supervise the Notifying Party's performance in this regard.

4. The Parties commit not to use or enable third parties to use any assets that are related to the [Conf] Pipeline Product but are retained by the Parties for use in connection with their retained businesses for purposes of development, improvement and manufacture in view to commercialise the [Conf] Pipeline Product or biologically identical products in the EEA territory.
5. The Notifying Party commits (subject to circumstances entirely outside of its control) to continue the development of the [Conf] Pipeline Product project, in the manner in which it is being developed at the date of these Commitments. Furthermore, the Notifying Party commits to provide assistance in obtaining the relevant marketing authorisation applications.
6. The [Conf] Pipeline Divestment Business will be transferred upon completion of the clinical development phase, according to the plans and projections at the date of these Commitments. Upon completion of the clinical development phase, the Notifying Party commits to separate and transfer the [Conf] Pipeline Divestment Businesses' production process in accordance with the Production Transfer process described in Schedule 2, Part D, paragraph 1.
7. For the avoidance of doubt, the [Conf] Pipeline Product shall not include any right, title and/or interest in:
 - (a) any personnel of the Parties;
 - (b) raw materials, other than any raw materials used to develop the [Conf] Pipeline Product;
 - (c) any production assets, manufacturing units, or R&D facilities;
 - (d) the Parties' company name, mark, or logo in any form;
 - (e) all books and records required to be retained pursuant to any statute, rule, regulation or ordinance, provided that the Notifying Party will provide copies of such documents necessary for the [Conf] Divestment Business to the Purchaser, upon request;
 - (f) general books of account and books of original entry that comprise the Notifying Party's or any of its Affiliated Undertakings' permanent accounting or tax records provided that the Notifying Party will provide copies of such documents necessary for the [Conf] Divestment Business to the Purchaser, upon request; and
 - (g) all books and records subject to the attorney-client or other legally recognized privilege, provided that the Notifying Party will provide copies of such documents necessary for the development and commercialization of the [Conf] Pipeline Product to the Purchaser if the Purchaser and the Notifying Party enter into an arrangement that preserves any such privilege.

Part D – NSAID Transfer options

1. The Notifying Party commits to use its Best Efforts to facilitate the transfer to one or several of the Purchaser's existing facilities or to a third party manufacturer of all manufacturing technology, IP and know-how necessary to enable the Purchaser or a third party manufacturer, to manufacture the NSAID Divestment Products.
2. As regards the production of [Conf], the Notifying Party will use its Best Efforts to ensure that the relationship currently in place with [Conf] for the supply of [Conf] is transferred to the Purchaser or to enable the Purchaser to conclude a new agreement. In any event that such arrangements cannot be made, the Notifying Party is prepared to conclude back-to-back supply agreements with the Purchaser.

Transfer support commitments

3. To support the transfer of the NSAID Divestment Business's production process, the Notifying Party commits to provide any support to ensure an effective Production Transfer of the NSAID Divestment Business to the production location of the Purchaser's choice at its own expenses. The Notifying Party envisages that technical assistance could include one or more of the following elements: advising on technical knowledge documentation, supporting the Purchaser in acquiring specific equipment, providing staff with suitable experience and skills to assist and/or advising on technical issues relating to research, assisting in trainings for the Purchaser's staff, providing guidance on regulatory and legal aspects related to the transfer of any licence.
4. At the option of the Purchaser, the Notifying Party commits to support the transfer of the NSAID Divestment Businesses' production process by providing, as required by the Purchaser:
 - (a) for manufacturing, support for the preparation and equipping of the Purchaser's chosen manufacturing site(s) and/or CMO(s); and
 - (b) for R&D/clinical, a transitional service team in order to: (a) finish on-going clinical studies; (b) transfer clinical studies, assays and technology; (c) provide assistance for pharmacovigilance and regulatory submissions, and (d) train the Purchaser's designated personnel.
5. The production transfer support will be provided by a team of expert employees of the Parties (***Production Transfer Personnel***), listed at **Annex D**, who will prioritise the effective Production Transfer of the NSAID Divestment Businesses over their work for the retained businesses and make themselves available according to the requirements for a timely and effective implementation of the Production Transfers. The Parties will implement an appropriate incentive scheme (based on industry practice) to incentivise the Production Transfer Personnel to complete the Production Transfers in a timely and effective manner. The Production Transfer Personnel will be bound by appropriate confidentiality obligations which will be agreed in accordance with paragraph 15 of the Commitments. Where individual members of the Production Transfer Personnel leave their position, the Parties shall replace the person or persons concerned and inform the Monitoring Trustee and the Technical Expert of the replacement.

6. The Production Transfer Personnel will be assisted by a steering committee, identified at **Annex D**, which will be composed of Merial employees with prior production transfer experience and will oversee/manage and make all necessary strategic decisions in relation to the execution of the Production Transfer of the NSAID Divestment Products to the Purchaser's existing facilities or a CMO.
7. At the option of the Purchaser, the Notifying Party shall provide technical assistance to the Purchaser to facilitate the procurement of raw materials necessary for the manufacture of any NSAID Divestment Products. If the Purchaser is not able to source such raw materials, the Notifying Party commits to enter, at the option of the Purchaser, into back-to-back supply agreements with certain raw material suppliers and to make such raw materials available to the Purchaser at cost, for such period as required by the Purchaser to establish the NSAID Divestment Business as a viable and independent business, but not exceeding 2 years from the date of termination of the NSAIDs TSA. Under circumstances outside the control of the Notifying Party, this period can be extended by the Monitoring Trustee until the Purchaser has established the NSAID Divestment Business.

Part E – NSAID TSA

1. The Notifying Party, shall enter into a TSA and supply the NSAID Divestment Products (including [Conf]) (*NSAID TSA*), to the Purchaser, in sufficient volumes allowing the Purchaser to maintain and expand the existing market position of each of the abovementioned NSAID Divestment Products until the Purchaser has established an alternative production capability. The term of the NSAID TSA will be a maximum of 3 years, with the option for the Purchaser to extend the term subject to prior approval of the Monitoring Trustee (together with the Technical Expert). The TSA will be monitored by the Monitoring Trustee (together with the Technical Expert).
2. The NSAID TSA will have the following characteristics:
 - (a) The Purchaser will grant the Notifying Party a temporary licence for the use of the relevant intellectual property, know-how and technical documentation required for the production of the NSAID Divestment Products;
 - (b) The Notifying Party shall manufacture the NSAID Divestment Products (excluding [Conf])⁴ in accordance with specified existing product specifications and it shall continue to manufacture the NSAID Divestment Products (excluding [Conf]) at the manufacturing facilities which are currently owned and used by Merial for the production of the relevant NSAIDs to ensure the continued supply of the NSAID Divestment Products, giving priority to the production of the NSAID Divestment Products over the products of the retained business should there be technical difficulties or shortage of supply;
 - (c) The NSAID Divestment Product (excluding [Conf]) shall be produced under the same cost structure and of the same quality and consistent with past practice as Merial produced the NSAID Divestment Product prior to Closing;
 - (d) In the event that the relationship currently in place with [Conf]: (i) cannot be transferred; or (ii) cannot be renegotiated with the Purchaser to ensure immediate supply of [Conf], the Notifying Party will use its Best Efforts to enter into a back-to-back agreement with [Conf] for the supply of [Conf];
 - (e) The Notifying Party commits to supply the NSAID Divestment Products to the Purchaser at full manufacturing cost on a cost pass-through basis (i.e. no mark-up), that will be fixed at the time of signing the TSA. The TSA will allow for a yearly revision of the costs of supply, subject to the approval of the Monitoring Trustee and the Technical Expert, in the event of an increase or decrease in the manufacturing cost of [Conf]% or more, it being understood that any increases in the costs of supply can be based on external factors only (e.g. a change requested by the Purchaser resulting in an increase in the manufacturing cost, an increase in the cost of raw materials or any other justified circumstances outside the control of the Parties resulting in an increase in the manufacturing costs).

⁴ Produced for Merial by a third-party toll manufacturer.

- (f) The Notifying Party shall make available sufficient volumes of the finished NSAID Divestment Product allowing the Purchaser to maintain and expand the existing market position until the Purchaser has established an alternative production capacity, with no limitation to the volume of production subject to Merial's relevant manufacturing facilities' capacity. The Notifying Party shall replenish on an on-going basis Merial's current stock levels in the hands of the Purchaser;
 - (g) The Notifying Party will provide the Purchaser with assistance in order to implement any changes required to the packaging of the relevant NSAID Divestment Products.
3. Under the terms of the TSA, the Purchaser will have the right to request on a transitional basis the Parties to assist in the distribution (for example via logistics and supply chain support) of the NSAID Divestment Products on the Purchaser's behalf in the EEA on a cost basis, until the Purchaser has established commercial independence and in any event for not longer than the duration of the TSA.
 4. In the event of a dispute between the Notifying Party and the Purchaser regarding the manufacturing costs or the quantities, the matter shall be referred to the Monitoring Trustee (together with the Technical Expert) for resolution.



EUROPEAN COMMISSION
DG Competition

Case M.8744 - DAIMLER / BMW / CAR SHARING JV

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) in conjunction with Art 6(2)
Date: 07/11/2018

***In electronic form on the EUR-Lex website under
document number 32018M8744***



EUROPEAN COMMISSION

Brussels, 7.11.2018
C(2018) 7527 final

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

To the notifying parties:

**Subject: Case M.8744 - DAIMLER / BMW / CAR SHARING JV
Commission decision pursuant to Article 6(1)(b) in conjunction with Article 6(2) of Council Regulation No 139/2004¹ and Article 57 of the Agreement on the European Economic Area²**

Dear Sir or Madam,

- (1) On 17 September 2018, the European Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No. 139/2004³ by which Bayerische Motoren Werke Aktiengesellschaft (“**BMW**”) and Daimler AG (“**Daimler**”) (together, the “Parties”) intend to establish six joint ventures (separately, “the JVs”; all six together, the “JV”), bringing together the Parties' mobility services in five business fields (“the proposed Transaction”). The sixth joint venture will manage the brands and license them out to the other joint ventures. BMW and Daimler will jointly control the JV within the meaning of Articles 3(1)(b) and 3(4) of the Merger Regulation.

¹ OJ L 24, 29.1.2004, p. 1 (the 'Merger Regulation'). With effect from 1 December 2009, the Treaty on the Functioning of the European Union ('TFEU') has introduced certain changes, such as the replacement of 'Community' by 'Union' and 'common market' by 'internal market'. The terminology of the TFEU will be used throughout this decision.

² OJ L 1, 3.1.1994, p. 3 (the 'EEA Agreement').

³ OJ L 24, 29.1.2004, p. 1 (the "Merger Regulation").

1. THE PARTIES

1.1. BMW

- (2) With the trademarks BMW, Rolls Royce and MINI, BMW is a manufacturer ("OEM") of passenger cars and motorcycles worldwide as well as a provider of services in the field of individual mobility, such as (free-floating) car sharing services. BMW is a publicly listed company established under German law which is headquartered in Munich, Germany. Passenger cars include plug-in hybrid vehicles and electric vehicles. With its subsidiary "DriveNow", BMW provides free-floating car sharing services.

1.2. Daimler

- (3) With its divisions Mercedes-Benz Cars, Daimler Trucks, Mercedes-Benz Vans, Daimler Buses and Daimler Financial Services, Daimler is a publicly listed company established under German law with its registered headquarter in Stuttgart, Germany. Daimler is globally active in the development, manufacturing and distribution of automotive products, mainly passenger cars, trucks, vans and buses. The Mercedes-Benz Car division sells passenger cars under the Mercedes-Benz and 'smart' brands. Daimler Financial Services supports the sales of vehicles worldwide. Its product and services portfolio consists of tailored financing and leasing packages for dealers and customers, as well as financial services such as insurance brokerage, investment products, credit cards, and full fleet management and leasing services.
- (4) With its subsidiary "car2go" Daimler provides free-floating car sharing services.

2. THE OPERATION AND THE CONCENTRATION

- (5) The proposed Transaction concerns the acquisition by BMW and Daimler of joint control over six legal entities, bringing together the Parties' mobility services in five business fields, i.e. (i) car sharing services DriveNow and car2go, (ii) ride hailing services, (iii) parking services, (iv) charging services as well as (v) other on-demand mobility services. The sixth joint venture will manage the brands and license them out to the other joint ventures. The Parties will transfer existing business to the JV. The JV will offer its services to commercial customers, public entities and private customers. It is planned that the JV will operate in various countries worldwide. In the EEA, the Parties' activities will overlap in seven cities within the EU, namely in Austria (Vienna), Germany (Berlin, Cologne, Dusseldorf, Hamburg and Munich) and Italy (Milan).
- (6) More specifically, Daimler will contribute to the JV:
- (7) **car2go:** a provider of free-floating car sharing services (www.car2go.com), fully owned by Daimler. Previously Daimler held 75% of the shares in car2go Europe GmbH and [INFORMATION ON TRANSACTION STRUCTURE]. The remaining 25% in car2go Europe GmbH were held by the car rental company Europcar. However, meanwhile Daimler has acquired the entirety of the shares of

and thereby sole control over car2go from Europcar.⁴ Daimler will contribute to the JV all the shares in car2go. [INFORMATION ON TRANSACTION STRUCTURE].

- (8) **mytaxi group (Intelligent Apps GmbH) (“mytaxi”)**: a taxi dispatch service provider (for Europe see under www.de.mytaxi.com). Currently, Daimler holds [INFORMATION ON SHARES]% of the shares in Intelligent Apps GmbH and its subsidiaries with the brands mytaxi, Chauffeur Privé, Beat and Clever taxi. [INFORMATION ON TRANSACTION STRUCTURE]⁵ [INFORMATION ON TRANSACTION STRUCTURE]. The Parties do not, however, offer ride-hailing services in the EEA.
- (9) **moovel**: a multimodal online platform, providing customers with access to a wide range of mobility offerings by enabling in-app searching, booking, ticketing and payment (www.moovel.com). Currently, Daimler holds 100% of the shares in moovel.
- (10) BMW will contribute to the JV:
- (11) **DriveNow**: also a provider of free-floating car sharing services (www.drive-now.com), fully owned by BMW. Previously BMW held 50% of the shares in DriveNow. The remaining 50% were held by the car rental company Sixt. However, meanwhile BMW has acquired the entirety of the shares of and thereby sole control over DriveNow from Sixt.⁶ BMW will contribute to the JV all of the shares in DriveNow.
- (12) **ReachNow**: a provider of car sharing and ride hailing services (www.reachnow.com) in Seattle and Portland (USA). Currently, BMW holds 100% of the shares in ReachNow.
- (13) **Parkmobile/Parknow (“ParkNow”)**: providers of digital cashless parking payment services (de.park-now.com; us.parkmobile.com). Currently, BMW holds 100% of the shares in [INFORMATION ON TRANSACTION STRUCTURE]. BMW will contribute to the JV all its shares in ParkNow.
- (14) **ChargeNow**: a provider of access to charging stations of various charge point operators (www.chargenow.com). Currently, BMW holds 100% of the shares in ChargeNow.

⁴ The acquisition of the remaining 25% of the shares in car2go by Daimler was signed on [DATE OF SIGNING]. The transaction has been notified to the Austrian competition authority (*Bundeswettbewerbsbehörde*) and the German Federal Cartel Office (*Bundeskartellamt*). The acquisition of the remaining car2go shares by Daimler has been cleared by the *Bundeskartellamt* on 8/03/2018 and by the *Bundeswettbewerbsbehörde* on 30/03/2018.

⁵ Annex 5.1(e), paragraph 1 and Annex 3.1(c), paragraph 2.2(a)(i) of the [INFORMATION ON AGREEMENT].

⁶ The acquisition of the remaining 50% of the shares in DriveNow by BMW was signed on [DATE OF SIGNING]. The transaction has been notified to the Austrian competition authority (*Bundeswettbewerbsbehörde*) and the German Federal Cartel Office (*Bundeskartellamt*). The acquisition of the remaining DriveNow shares has been cleared by the *Bundeskartellamt* on 07/02/2018 and by the *Bundeswettbewerbsbehörde* on 28/02/2018.

- (15) The single transactions for each one of the JVs are interdependent as they are conditional upon each other.⁷ In addition, the individual transactions are linked in the following way:
- (16) First, the envisaged transactions are *de jure* inter-conditional. Some structural preparation steps and the contribution of the business fields to the JVs are closing conditions⁸ in the [INFORMATION ON AGREEMENT] are closing actions under the [INFORMATION ON AGREEMENT].⁹ Thus, the Parties will not close the [INFORMATION ON AGREEMENT] without a legal obligation to [INFORMATION ON AGREEMENT].
- (17) The [INFORMATION ON AGREEMENT] states that BMW and Daimler wish to implement their cooperation by setting up the JVs and by establishing a player in the innovative mobility service business through these JVs. According to the above-mentioned agreements, the Parties will not set up one of the JV without the other ones. [INFORMATION ON AGREEMENT].
- (18) Secondly, the single transactions are also *de facto* inter-conditional. All transactions are intended to serve the same purpose: BMW and Daimler have the aim to establish a mobility service provider that offers the whole range of mobility services. It is planned that the offerings of the six JVs will be combined.¹⁰ Moreover, there will be a strategic alignment of the JVs in future¹¹. As a result, also the economic aim of the transactions shows that they will be carried out together and in parallel.

2.1. Joint Control

- (19) Post-closing, the Parties will each hold 50% of the shares and voting rights in all the JVs (and, consequently, in the JV), [INFORMATION ON TRANSACTION STRUCTURE]. Each of the JVs (and, consequently, the JV) will be jointly controlled by BMW and Daimler.¹²
- (20) Each JV will at least have two managing directors (CEO and CFO). Generally, the appointment or dismissal of the directors must be decided by majority vote¹³.

⁷ Paragraph 38 CJN.

⁸ Section 5.1 of the [INFORMATION ON AGREEMENT].

⁹ Section 6.3 of the [INFORMATION ON AGREEMENT] once all merger control approvals have been received.

¹⁰ Section 1.3 of the [INFORMATION ON AGREEMENT] and Section 1.4 of the [INFORMATION ON AGREEMENT].

¹¹ Section 2.4(d) of the [INFORMATION ON AGREEMENT].

¹² [INFORMATION ON TRANSACTION STRUCTURE].

¹³ Section 3.2(e) and Section 3.2(f) of the [INFORMATION ON AGREEMENT].

Thus, BMW and Daimler each have a relevant veto right within the meaning of the CJN.¹⁴ [INFORMATION ON CORPORATE GOVERNANCE].¹⁵

- (21) Corporate planning and the budget must be decided by a qualified majority, i.e. at least 75% of the voting rights.¹⁶ [INFORMATION ON CORPORATE GOVERNANCE].¹⁷
- (22) The above shows that topics which relate to strategic decisions cannot be decided by either BMW or Daimler alone. [INFORMATION ON CORPORATE GOVERNANCE].¹⁸ [INFORMATION ON CORPORATE GOVERNANCE].
- (23) Therefore, BMW and Daimler will have joint control over the JV.

2.2. Full functionality

- (24) The JV will be fully-functional within the meaning of the CJN,¹⁹ as it fulfils all the relevant criteria, namely (i) the assets attributable to the JV already operate on markets and they perform the functions normally carried out by undertakings operating on the same markets; (ii) the JV will not only serve a specific function for the Parties, but will conduct business with third parties and have own access to and presence on markets, (iii) [INFORMATION ON TRANSACTION STRUCTURE]²⁰; (iv) there are no strong sales or purchase relations with the Parties, (v) the JV will be operating on a lasting basis.
- (25) With regard to (iv), the Parties will provide vehicles to the relevant JVs. However, this is in fact not different to the situation today with regard to, on the one hand, BMW and DriveNow and, on the other hand, Daimler and car2go.²¹ [INFORMATION ON CORPORATE GOVERNANCE AND BUSINESS PLANS].²² [INFORMATION ON CORPORATE GOVERNANCE AND BUSINESS PLANS].²³ [INFORMATION ON CORPORATE GOVERNANCE

¹⁴ Paragraph 69 of the CJN.

¹⁵ Section 2.4 [INFORMATION ON AGREEMENT].

¹⁶ Section 6.1 [INFORMATION ON AGREEMENT].

¹⁷ Section 1.5(b) [INFORMATION ON AGREEMENT] and Section 6.1 [INFORMATION ON AGREEMENT].

¹⁸ See Section 3 of the [INFORMATION ON AGREEMENT].

¹⁹ Paragraphs 91 and ff of the CJN.

²⁰ Section 5 of the [INFORMATION ON AGREEMENT].

²¹ Section 7(4) of the [INFORMATION ON AGREEMENT].

²² Section 5.1(f) of the [INFORMATION ON AGREEMENT]. The Parties confirm, in their reply to question 3 of RFI 13 dated 6 November 2018, what stated in paragraphs 134 and ff of the Form CO, i.e. that the supply volume of vehicles to DriveNow and car2go is marginal in comparison to BMW's and Daimler's overall supply volume.

²³ Section 1.7(b) [INFORMATION ON AGREEMENT].

AND BUSINESS PLANS].²⁴ [INFORMATION ON CORPORATE GOVERNANCE AND BUSINESS PLANS]. However, this is only an ancillary function of the JV as its focus lies in providing services to third parties. In conclusion, the Parties estimate that the JV's turnover with the Parties will be less than [INFORMATION ON TURNOVER]% of the JV's total turnover.

- (26) With regard to (v), there is no specific duration in the [INFORMATION ON AGREEMENT AND ON CORPORATE GOVERNANCE].²⁵

3. EU DIMENSION

- (27) The undertakings concerned have a combined aggregate worldwide turnover of more than EUR 5,000 million²⁶. Each of them has an EU-wide turnover in excess of EUR 250 million, but they do not achieve more than two-thirds of their aggregate EU-wide turnover within one and the same Member State.
- (28) The Transaction has therefore an EU dimension according to Article 1(2) of the Merger regulation.

4. MARKET DEFINITION

4.1. Relevant product market

Horizontally Affected Markets

- (29) The stated rationale of the deal is to prepare for a future in which individual car ownership and therefore vehicle sales decrease, and mobility is instead provided as a service; and ultimately, for the age of self-driving vehicles when taxi, ride hailing and car sharing services all collapse into one mobility market. However, a single product market for all mobility solutions seems, at least for the near future, unlikely to be the relevant market.
- (30) In prior decisions, the Commission dealt with the market for (i) all passenger transport services²⁷ and for (ii) short term car rental services including car sharing services.²⁸ However, there are no prior decisions in which the Commission dealt with (iii) car sharing services or (iv) free-floating car sharing services. As a consequence, the Parties submit that the Commission should consider either the

²⁴ Section 7.3 [INFORMATION ON AGREEMENT]. This means that [INFORMATION ON BUSINESS PLANS].

²⁵ [INFORMATION ON CORPORATE GOVERNANCE].

²⁶ Turnover calculated in accordance with Article 5 of the Merger Regulation.

²⁷ See e.g., Cases M.8441 – *Firstgroup/MTR Corporation/South Western Rail Franchise*, para. 14 et seq.; M.7146 – *Govia/Thameslink, Southern and Great Northern Passenger Rail Franchise*, para. 16.

²⁸ See e.g. Cases M.8309 – *Volvo Car Corporation/First Rent A Car*, paragraphs 41 et seq.; M.6333 *BMW/ING Car Lease*, paragraphs 17 et seq.

overall market for all passenger transport services²⁹ or, at least, the market for short term car rental services assessed at national level.

- (31) For the reasons explained in sections 4.1.1, 4.1.2, 4.1.3 below, and in line with the decisional practice of the Commission and considering the number of novel mobility solutions that have been recently realised in various cities across the EEA, it appears appropriate to assess the proposed Transaction under all the market segmentations.

4.1.1. All passengers transport services

4.1.1.1. Commission's practice

- (32) The Commission has considered a product market that comprises all passenger transport services. For example, in one decision, the Commission stated that the relevant product market with regard to railway services could be as wide as all passenger transport services or as narrow as solely rail services.³⁰ In another case, the Commission's market investigation indicated that car sharing services exerted pressure on the transport by bus, especially regarding short and medium distances, and on the transport by personal car.³¹

4.1.1.2. Parties' view

- (33) The Parties submit that it would be accurate to define a market encompassing all passenger means of transport including different options, such as public transport, taxis, cars, scooters and (electric) bicycles for short to medium distances. The Parties argue that the Parties' customers use the services of different providers already today as prices are transparent and there are several transportation options available for a specific trip.³²
- (34) The Parties also refer to the fact that, in their view, smartphones and apps are widely available and that, as a consequence, passengers use different means of transport especially for short and medium distance journeys.³³
- (35) The Parties also refer to the *Zipcar/Streetcar* merger, reviewed by the UK competition authority in 2010³⁴ and to the *Europcar/Buchbinder* merger,

²⁹ The Parties submit that the market for all passenger transport services should include public transport, taxi services together with non-traditional services (such as Uber), car rental (including car sharing activities), motor scooters rental, electric scooters rental, (electric) bicycle rental and private transportation options (e.g. carpooling).

³⁰ See e.g., Cases M.8441 – *Firstgroup/MTR Corporation/South Western Rail Franchise*, para. 14 et seq.; M.7146 – *Govia/Thameslink, Southern and Great Northern Passenger Rail Franchise*, para. 16.

³¹ See e.g. Case M.5741 – *CDC/Veolia Environment/Transdev/Veolia Transport*, paragraph 20.

³² Form CO, paragraph 119.

³³ Form CO, paragraphs 74-75.

³⁴ UK Competition Commission (now CMA), final report of 22 December 2010, *Streetcar/Zipcar*.

reviewed by the *Bundeskartellamt* in 2017³⁵. Whilst the UK competition authority took a narrow car sharing segment as a starting point, it acknowledged in its further assessment that there is in fact a high degree of potential substitution between car sharing and other transport options, such as car rental, taxis and public transport and that these alternatives constrain the prices for car sharing.³⁶ The *Bundeskartellamt*, on the other hand, left the precise market definition open and dealt with car sharing as a minor aspect, given that the merger did not concern car sharing providers.

4.1.1.3. Commission's assessment

- (36) With regard to the supply side, the majority of OEMs that responded to the market investigation did not consider the non-car sharing mobility solutions as substitutable with car sharing. As a consequence, the market investigation did not reveal the market for all passengers transport as being the relevant product market. Rather, station-based car sharing was identified by OEMs that responded to the market investigation as the best alternative to free-floating. In particular, one OEM stated that "*all the other mobility solutions are significantly different, both from a customer perspective and from the operating mode: (i) car sharing requires embedded technology to allow door unlock/lock from a smartphone (or RFID card), [...] (ii) ride hailing and taxi do not offer the same privacy (driver aboard) and pricing as car sharing, (iii) public transport does not offer the same privacy and flexibility since it is based on a fixed route and time schedule, (iv) bike and scooter sharing do not offer the same comfort and luggage capacity, are unpleasant to use with bad weather conditions [...], (v) own car requires a totally different budget for the end user in order to acquire, insure and maintain the vehicle, and afford a parking place [...]*".
- (37) When asked about close substitutes, ride hailing was identified as the closest substitute to free-floating car sharing by OEMs that responded to the market investigation, followed by station-based car sharing and taxi on the one hand, and by public transport and car rental. Another OEM stated that "*scooter and bicycle sharing are less close to car sharing due to comfort and risk perception, [whilst] own car and car rental and taxi are less comparable due to higher costs, ride hailing is less comparable due to customer experience [...]*".
- (38) Amongst other car sharing, scooter sharing, ride-hailing, taxi or other mobility services providers ("mobility service providers"), station-based car sharing was picked up by mobility service providers that responded to the market investigation as the best alternative to free-floating car sharing, followed by peer-to-peer car sharing and taxi and by ride hailing and public transport. Some mobility service providers who responded to the market investigation indicated that free-floating car sharing is only used for spontaneous journeys.
- (39) When asked about close substitutes, station-based car sharing was identified as the closest substitute to free-floating by mobility service providers that responded to the market investigation, whilst taxi and ride-hailing were picked up as close

³⁵ Bundeskartellamt, 26/09/2017, *Europcar/Buchbinder*.

³⁶ Form CO, paragraph 76.

substitutes to free-floating car sharing. One respondent to the market investigation stated that "*although the ease of picking up and dropping off a car using free-floating car sharing services is [more] analogous to car ownership, car ownership is cost prohibitive for many due to the cost of the car, parking, gas, insurance and maintenance, Therefore, for those who don't have free-floating car sharing as an option, station-based car sharing and peer-to-peer car sharing are the most analogous to free-floating car sharing. Ride hailing and taxi are cost prohibitive for longer distances [...] and therefore not competitive, and if bulky items or larger groups (such as family) are being transported, the other options (public transport, scooter sharing, bicycle sharing, etc.) are not competitive*".

- (40) The majority of providers of front-end/back-end and hardware/software car sharing-related technology ("technology providers") who responded to the market investigation indicated station-based car sharing as being part of the same market as free-floating car sharing. A minority of the technology providers who responded to the market investigation indicated that bicycle sharing belongs to the same market as free-floating car sharing. None of the technology providers who responded to the market investigation mentioned other mobility solutions as being part of the same market as (free-floating) car sharing.
- (41) When asked about close substitutes, one technology provider amongst those that responded to the market investigation indicated taxi as being closest substitute to station-based car sharing and public transport and ride-hailing as being close substitutes to station-based car sharing. Another respondent to the market investigation indicated free-floating as being close substitute to ride-hailing.
- (42) On the basis of the results of the market investigation as outlined above, not all of the transport options set out above appear to be closely substitutable with one another. There are stark differences both from a customer perspective and in the positions the various actors on the supply side, as well as very different pricing levels.
- (43) For the purpose of this decision, the Commission considers it more appropriate to assess the proposed Transaction on a market for (free-floating) car sharing services as the narrowest-possible relevant market. However, the Commission will also have due regard to the competitive pressure exerted by some other passengers transport services on (free-floating) car sharing in its competitive assessment below.

4.1.2. *Short term car rental services (including car sharing)*

4.1.2.1. Commission's practice

- (44) In prior decisions, the Commission has considered a market for car rental services. In this framework, the Commission considered that this market could be further segmented into (i) short-term car rental services (e.g. for business trips, leisure trips, tourism) and (ii) long-term car rental services (e.g. with a rental period of more than one year).³⁷ The Commission mentioned further possible

³⁷ See e.g. Cases M.6333 *BMW/ING Car Lease*, paragraph 17; M.4613 *Eurazeo S.A./ApcoaParking Holdings GmbH*, paragraph 16; M.8569 – *Europcar/Goldcar*, paragraph 11.

segmentation of the car rental segment based on customers groups, vehicle category and a possible separate segment for replacement rentals.³⁸ In addition, it has considered whether other mobility solutions such as car sharing form part of short-term car rental services.³⁹

- (45) At national level, the French *Autorité de la Concurrence*, when assessing the merger between France Cars and the Avis Budget Group⁴⁰, examined the market for car rental services, taking into account the Commission's case *BMW/ING Car Lease*⁴¹, where the notifying parties argued that the short-term car rental segment includes car sharing activities.⁴² Finally, the *Autorité de la Concurrence* left the market definition open in this regard.⁴³

4.1.2.2. Parties' view

- (46) In the event the Commission does not accept an all passengers, transport services relevant market, at least a short term car rental segment should be considered, along with car sharing services, as a relevant product market, without further segmentation being appropriate.⁴⁴ In their view, it would not be accurate to separate car sharing from a short term car rental segment, for reasons of demand substitution, supply substitution, potential competition and expansion.⁴⁵
- (47) With regard to demand-side substitutability, according to the Parties, the customer is flexible and can choose a specific car from a number of vehicles offered in order to drive to a destination; he only pays for the concrete use; both options are attractive for a short period of time; pricing flexibility and flexibility in access to the car; and a number of car rental companies has already introduced fully 'counterless' short term car rental services.⁴⁶ With regard to the supply-side

³⁸ See e.g. Case M.4613 – *Eurazeo S.A./Apcoa Parking Holdings GmbH*, paragraph 16.

³⁹ See e.g. Cases M.8309 – *Volvo Car Corporation/First Rent A Car*, paragraphs 41 et seq.; M.6333 *BMW/ING Car Lease*, paragraphs 17 et seq.

⁴⁰ *Autorité de la Concurrence*, Decision of 06/12/2016, *France Cars/A vis Budget Group* (16-DCC-200) (<http://www.autoritedelaconcurrence.fr/pdf7avis/16DCC200versionpublication.pdf>).

⁴¹ *Ibid*, paragraph 7.

⁴² Case M.6333 - *BMW/ING Car Lease*, paragraphs 18 et seq.

⁴³ *Autorité de la Concurrence*, Decision of 6 December 2016, *France Cars/Avis Budget Group* (16-DCC-200), paragraphs 7 and 17.

⁴⁴ Form CO, paragraph 77.

⁴⁵ Form CO, paragraph 112.

⁴⁶ Car rental services where customers do not need to go to a reception counter to rent the car (to pick up the keys and provide the relevant documents). For example, Hertz has launched a new concept (Hertz 24/7) which can currently be used in Europe (in the UK, Germany, France, Portugal, the Netherlands, Italy, Belgium and Spain) and in Australia. The rental process is fully 'counterless': via a smartphone app, the customer can reserve a car at any time. The customer obtains access to the car by using a PIN code. Currently, cars can be picked-up at highly-frequented places (in the UK, for instance, in hundreds of IKEA, B&Q, and Costco stores). The customer is charged by hourly rates.

substitutability, according to the Parties, car rental companies can easily align their offerings to car sharing services in a timely manner insofar as they have not already introduced 'counterless' services, only requiring some minor changes that do not cause substantial costs.

4.1.2.3. Commission's assessment

- (48) Only a minority of OEMs and mobility service providers responding to the market investigation considered car rental to be part of the same market as free-float car sharing. Only two respondents ranked car rental as the closest alternative to or substitute for free-floating car sharing, while three respondents ranked it as second closest alternative, 12 others ranked it as third closest alternative, and the majority of respondents did not even indicate car rental as a substitute for free-floating car sharing.⁴⁷
- (49) Some respondents highlighted the differences between free-floating car sharing and car rental, e.g. the technology used (lock/unlock or RFID card), enrolment services requiring the visit of a reception desk in the case of rental services, and making round trips (as opposed to the flexibility in case of free-floating car sharing) as well as peculiarities in billing (e.g. car rental services do not allow billing based on the number of minutes driven), etc. Others indicated that free-floating car sharing "*can be more flexible than station based car sharing and rental*", and that "*car rental and taxi are less comparable due to higher costs*".⁴⁸
- (50) On this basis, for the purpose of this decision, the Commission does not consider it appropriate to consider a short-term car rental market including (free-floating) car sharing as the relevant product market in this case. As stated above, for the purpose of this decision, the Commission considers it more appropriate to assess the proposed Transaction on a market for (free-floating) car sharing and to look at the competitive pressure exerted by car rental on (free-floating) car sharing in its competitive assessment below.

4.1.3. Car sharing as a whole and station-based vs free-floating

4.1.3.1. Commission's practice

- (51) The Commission has only dealt with car sharing services in a few decisions adopted under the simplified procedure⁴⁹, and there appears to be no settled practice with regard to this possible relevant product market.

4.1.3.2. Parties' view

- (52) As explained above in paragraphs (46) - (47), the Parties only suggested a broad passenger transportation market and (alternatively) a short-term car rental

⁴⁷ Replies to questions 4-5 of questionnaire to OEMs. Replies to questions 6-7 of questionnaire to mobility service providers.

⁴⁸ Replies to questions 4-5 of questionnaire to OEMs.

⁴⁹ See e.g. M.8163 - AC/EYSA/JV and M.6437 – Enterprise Holding / CITER.

segment including car sharing, arguing that a further segmentation is not appropriate.

4.1.3.3. Commission's assessment

- (53) Car sharing is a type of self-service car rental in which cars are picked up and returned by the user without the need to interact with a staff member. It is designed to provide on-demand mobility for people who want to rent cars for short distances and short periods of time. After a one-time registration and authentication process, car sharing users can flexibly search and reserve cars through a dedicated smartphone app. It is usually offered within a certain area of a city and can be further sub-segmented into (i) station-based car sharing, (ii) free-floating car sharing and – to a very small extent – (iii) peer-to-peer car sharing.
- (54) Station-based car sharing – usually used for several hours and longer distances than free-floating car sharing – means that the customer needs to collect and return the car to fixed stations. Usually, the car has to be returned to the same station where it was picked up. Station-based car sharing is only suitable for round trips, it requires prior booking and it is generally for longer durations. Neither of the Parties is active in station-based car sharing.
- (55) Free-floating car sharing – mostly used for short-term trips of around 20 minutes and usually paid per minute – allows customers to pick up and drop off the car anywhere within a certain delimited area of a city using authorised parking spaces (e.g. public parking spots). The car can then be picked up by the next user in the location where the previous user parked it. The car sharing market is a dynamic, young and growing market, which is often (especially in the field of free-floating car sharing) not profitable yet.
- (56) Peer-to-peer (P2P) car sharing involves cars belonging to private individuals. Market players provide an online platform to handle the transaction, offer insurance, and in some cases equip the car with telematic devices to ensure easy access. Users pick up and return the car where the owner has parked it (e.g., in front of her home). For the purpose of this decision, P2P car sharing will not be further discussed as none of the Parties is active in P2P car sharing and it still appears – in relation to free-floating and station-based car sharing – negligible with respect of its size in the cars sharing market.
- (57) In some cities, there is a trend towards convergence of free-floating and station-based car sharing due to the fact that free-floating car sharing suppliers offer schemes which allow for booking of a longer time, e.g. 3, 6, 9 and 24 hours with fixed prices and a maximum number of driven kilometres included, while station-based car sharing suppliers offer shorter renting schemes based on minutes, as is the standard in free-floating. There is also one supplier which has instead of a fixed station certain areas in which the car can be picked up and returned.
- (58) The majority of the OEMs, mobility service providers and technology providers considered that station-based car sharing would belong to the same market as free-floating car sharing. In terms of close substitutes, station-based car sharing was mostly chosen by mobility service providers and technology providers as the closest substitute to free-floating car sharing and by OEMs as one (behind ride hailing) of the close substitutes to free-floating car sharing.

- (59) In addition to the replies to the market investigation, the Commission, in order to delineate the relevant product market, has also considered the results of a July 2018 customer survey in 14 EEA cities by CRA, including the seven overlap cities, which was submitted by the Parties' economic advisers in August 2018.⁵⁰ This survey was conducted in order to better understand the substitution patterns of users of the Parties' car sharing services towards one another and towards other service providers and means of transport.
- (60) On the demand side, the customer survey shows that (i) the market is evolving, (ii) there is a large range of mobility services that are, to varying degrees, seen as substitutes by consumers, including public transport, (iii) the highest diversion ratio goes to competing free-floating car sharing suppliers, narrowly followed by public transport as the only real other alternative.
- (61) Among other, this survey asked users which alternative mobility service they would use for a typical trip if their preferred provider were not available for at least six months. Such diversion questions may allow discerning which services users would be most likely to switch to as an alternative to their preferred provider. Table A below indicates the answer to this question for car2go and DriveNow users as a simple average of overlap cities.

		Diversion from		
Diversion to	car2go	DriveNow	Average	
car2go	./.	[40-50]%	[30-40]%	
DriveNow	[20-30]%	./.		
Public transport	[30-40]%	[20-30]%	[20-30]%	
Own car	[10-20]%	[10-20]%	[10-20]%	
Bike/scooter	[5-10]%	[5-10]%	[5-10]%	
Other free floating	[5-10]%	[5-10]%	[5-10]%	
Taxi/Uber	[5-10]%	[0-5]%	[5-10]%	
Rental/station-based	[0-5]%	[0-5]%	[0-5]%	
Other	[0-5]%	[0-5]%	[0-5]%	
Total	100%	100%	100%	

Table A: Diversion ratios to and from the Parties

⁵⁰ CRA Charles River Associates, Project KITT – analysis of EU survey results, 21/08/2018.

- (62) As shown in the table, users tend to view the respective merging partner as the closest competitor (with on average [30-40]% of customers stating that they would switch to the merger partner as their preferred second option). The difference in the diversion ratios between users of DriveNow and car2go may be explained by the different types of cars on offer. The cars offered by DriveNow are larger and more expensive per minute leading to relatively fewer users of car2go switching to DriveNow.
- (63) Table A also shows, however, that public transport is an equally credible alternative to DriveNow/car2go for a substantial number of users (with on average [20-30]% stating that they consider it their second best option). Finally, customers appear to consider a variety of other means of transport as potential alternatives. Depending on the specific customer and the situation he or she is in, different mobility services may therefore be a substitute to the Parties' car sharing offers.⁵¹
- (64) Given that, as show in Table A, more than [50-60]% of the customers would change to alternative means of transports, especially to public transport and to their own cars, which shows the large heterogeneity of substitution patterns of customers between the different means of transport, the Commission considers that market definition in car sharing and market shares may be less precise indicators of competitive positioning in this case. Therefore, while the Commission will assess this transaction also on both a market for car sharing and in the narrowest plausible market of free-floating car sharing, it will in its competitive assessment also take account of certain out-of-market constraints exerted by, in particular, the public transport services, that are not included in such a market.

4.1.3.4. Conclusion

- (65) Although, on the basis of the results of the market investigation and the above-referred customer survey, it cannot be ruled out that there is a separate market for free-floating car sharing, the precise market definition can be left open as also in a broader market encompassing all types of car sharing (and not just free-floating car sharing services) the assessment would not change.

Vertically Affected Markets

- (66) The Commission also identified several possible vertically affected markets, mostly between the manufacturing of passenger cars and the activities of some of the JVs, including free-floating car sharing. As set out below, these vertical relations do not appear to be of any major concern due to the Parties' moderate share in the market for passenger cars and the presence of several strong competitors in that market.

⁵¹ While a diversion ratio of "only" 36% to the respective merging partner may appear small at first sight, it should be stressed that this is not so. In particular, note that in a hypothetical market where two out of four symmetric firms merge, the diversion ratio from one merging partner to the other would be only 33.3%, even though the combined market share of the merging firms would be 50%. Diversion ratios of 36% are therefore consistent with significant closeness of substitution (see the competitive assessment further below).

4.1.4. Parking

4.1.4.1. Commission's practice

- (67) In *Fortis AG SA/Bernheim-Comofi SA*, the Commission dealt with car parking operators. The notifying parties were of the opinion that a market for the operation of paid public parking facilities (without free parking spaces, residential parking or private or company parking) should be considered.⁵²
- (68) In the case *Eurazeo S.A./Apcoa Parking Holdings GmbH*, the Commission looked at a possible separate market for parking management services.⁵³ The notifying parties argued that a broader market for facility management services should be taken into account.⁵⁴ The Commission's market investigation showed that providers of such services are usually chosen in tender procedures on a long-term basis. They do not mandatorily own the buildings, but manage them under a facilities management contract. The Commission ultimately chose to leave the exact market definition open.⁵⁵ The provision of car park management services "at off-street parking facilities"⁵⁶ in the UK has been examined in the Commission's competitive assessment in the case *Mirael/Ferrovial/NDHI*.⁵⁷

4.1.4.2. Parties' views

- (69) In the Parties' view, the market should comprise all companies that supply hardware which provides access and payment services. This includes suppliers of payment terminals and access equipment, such as (cashless) card payment terminals. According to the Parties, it is not plausible to divide the market for parking (including hardware payment) services into a sub-segment limited to software/mobile technology.⁵⁸

4.1.4.3. Commission's assessment and conclusion

- (70) The Commission considers that the market for parking services has evolved in such a way as to integrate (increasingly) the (hardware) payment services, since customers most often pay at the terminals or with special parking payment cards rather than at the reception desk. Hence, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis

⁵² Case M.2825 - *FORTIS AG SA/BERNHEIM-COMOFI SA*, paragraph 10.

⁵³ Case M.4613 - *Eurazeo S.A./Apcoa Parking Holdings GmbH*.

⁵⁴ Case M.4613 - *Eurazeo S.A./Apcoa Parking Holdings GmbH*, paragraphs 9 and 10.

⁵⁵ Case M.4613 - *Eurazeo S.A./Apcoa Parking Holdings GmbH*, paragraph 10; see also Case M.7398 - *MIRAE/ FERROVIAUNDHI*, paragraph 30.

⁵⁶ These are parking facilities anywhere but on the streets, like garages and lots.

⁵⁷ Case M.7398 - *MIRAE/ FERRO VIAUNDHI*, paragraph 33.

⁵⁸ Form CO, paragraph 215.

below on the market for parking services including hardware payment services as well as on a sub-segment limited to software/mobile technology.

4.1.5. Charging

4.1.5.1. Commission's practice

- (71) In *Verbund/Siemens/E-Mobility Provider Austria*, the Commission dealt with a market for the provision of electric mobility services, i.e. power supply for cars, infrastructure for charging cars and support services for users.⁵⁹ The market investigation conducted by the Commission showed that it could be appropriate to distinguish between these three segments and to further separate the market into private and commercial customers.⁶⁰
- (72) Additionally, the upstream market for the production, supply and installation of charging infrastructure for electric mobility services has been analysed. According to the notifying parties, the market could be segmented into (1) charging hardware, (2) necessary software and (3) additional services. However, the notifying parties also stressed that the market is just developing and that such segmentation could therefore be artificial⁶¹.

4.1.5.2. Parties' views

- (73) In the Parties' view, the operation of charging points and the provision of electric mobility services constitute separate markets. ChargeNow, BMW's access provider to charging stations of various charge point operators, is only active in a potential market for electric mobility services (i.e. a market where drivers are offered an app to allow them finding public charging outlets and easily pay for the charge).
- (74) The Parties are of the opinion that it is not appropriate to segment the potential market for electric mobility services further, e.g. by customer groups. The reason is that practically all electric mobility service providers offer all kinds of services to all type of customers or they are at least in a position to easily expand their product portfolio in that regard within a short period of time.⁶²

4.1.5.3. Commission's assessment and conclusion

- (75) In light of the supply-side substitutability of charging or electric mobility services as explained by the Parties, and taking into account the very limited presence of BMW, through its ChargeNow services, on the market for charging services (more particularly electric mobility services), the Commission considers it

⁵⁹ Case COMP/M.6641 - *Verbund/Siemens/E-Mobility Provider Austria*, para. 13.

⁶⁰ Case COMP/M.6641 - *Verbund/Siemens/E-Mobility Provider Austria*, para. 15 et seq.

⁶¹ Case COMP/M.6641 - *Verbund/Siemens/E-Mobility Provider Austria*, para. 26 et seq.

⁶² Form CO, paragraph 215.

appropriate, for the purpose of this decision, to carry out its vertical competitive analysis below on the market for charging services.

4.1.6. Passenger cars

4.1.6.1. Commission's practice

- (76) The Commission has in previous decisions distinguished between (i) the manufacture and supply of passenger cars and (ii) the distribution of passenger cars, considering both as possible upstream markets for activities such as full fleet management, car rental or car leasing.⁶³
- (77) As regards the manufacture and supply of passenger cars, the Commission has previously considered a segmentation on the basis of car categories: (i) mini cars; (ii) small cars; (iii) medium cars; (iv) large cars; (v) executive cars; (vi) luxury cars; (vii) sport cars; (viii) sport utility vehicles ("SUV"s) and (ix) multipurpose vehicles. For the SUV segment, a further division into (i) small, (ii) medium and (iii) large SUVs has been considered.⁶⁴ Moreover, the Commission has investigated whether electric cars constitute a separate product market and whether this possible market should be further segmented according to (i) technology (electric battery cars and hybrid cars) or (ii) the categories defined for vehicles with combustion engines.⁶⁵ However, the Commission left the market definition open in these cases.
- (78) As regards the distribution of motor vehicles, the Commission has in previous decisions distinguished between the wholesale and retail distribution of motor vehicles.⁶⁶ In its previous decisions, the Commission considered that the distinction between the wholesale distribution of passenger cars and light commercial vehicles was sufficient and that a further segmentation of passenger cars by narrower product segments based on certain categories of cars (e.g. mini cars, small cars, medium cars, etc.) was not appropriate given that *"manufacturers normally distribute a model range which covers different market segments under the same distribution channel"*.⁶⁷

4.1.6.2. Parties' views

- (79) The Parties submit that the relevant market in the case at hand is the wholesale distribution of passenger cars, although the entirety of passenger car sales is channelled both via the wholesale and the retail distribution network of the

⁶³ See e.g. Case M.8309 - *Volvo Car Corporation/First Rent A Car*, paragraph 12; Case M.6333 - *BMW/ING car lease*, paragraph 24; Case M.5568 - *Volkswagen/Fleet Investments/LeasePlan Corporation JV*, paragraph 30.

⁶⁴ Case M.8449 *Peugeot/Opel*, paragraph 12.

⁶⁵ See e.g. Case M.8449 *Peugeot/Opel*, paragraphs 14 et seq.

⁶⁶ See e.g. Case M.6403 - *Volkswagen/KPJ Polska/Skoda auto Polska/VW bank Polska/VW leasing Polska*, paragraph 22.

⁶⁷ See e.g. Case M.6403 - *Volkswagen/KPI Polska/Skoda auto Polska/VW bank Polska/VW leasing Polska*, paragraph 22; Case M. 182 - *Inchcape/IEP*, paragraph 9.

Parties. The Parties explain that large customers, such as car rental and car sharing service providers, however, source passenger cars on the wholesale level and not on the retail level.⁶⁸

- (80) In the Parties' view, the market for manufacture and supply of passenger cars should not be further segmented by categories of cars or into a potential electric segment.⁶⁹

4.1.6.3. Commission's assessment and conclusion

- (81) In line with its previous decisions, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis on the abovementioned segments of the market for the manufacture and supply of passenger cars, i.e. (i) the different categories of cars (mini cars, small cars, medium cars, multipurpose cars, sports cars) and (ii) electric cars, electric battery cars and hybrid cars, because these constitute the narrowest plausible market segments.
- (82) With regard to the distribution of passenger cars, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis below on the overall passenger cars distribution market, since the Parties channel the entirety of their passenger car sales via their wholesale and retail distribution networks, indicating supply-side substitutability between both distribution channels.⁷⁰

4.1.7. *Financial and operational leasing*

4.1.7.1. Commission's practice

- (83) In its previous decisions, the Commission considered a distinction between (i) operational leasing, in which ownership of the relevant asset is typically not transferred to the lessee at the end of the lease and the risk of ownership are retained by the lessor, and (ii) financial leasing, which is generally for a longer period, during which the lessee fully repays the asset cost and in result acquires the ownership of the relevant asset at the end of the lease.⁷¹ The Commission has also considered segmentations of the leasing market (i) according to the types of assets which are leased (cars, office equipment etc.), and (ii) according to the size of customers.⁷² In the end, it was left open whether there is one relevant product market for leasing or whether it should be segmented (i) into operational and

⁶⁸ Form CO, paragraph 126.

⁶⁹ Reply to RFI of 9 October 2018, Annex 1, footnote 1.

⁷⁰ Form CO, paragraph 126.

⁷¹ Case M.8414 – *DNB/Nordea/Luminor Group*, paragraph 54; see also Cases M.5384 – *BNP Paribas/Fortis*, paragraphs 61 et seqq.; M.6763 – *VWFS/PON Holdings B.V./PON Equipment Rental & Lease*, paragraphs 16 et seqq.; and M.6333 – *BMW/ING Car Lease*, paragraphs 14 et seqq. for a distinction.

⁷² Case M.8414 – *DNB/Nordea/Luminor Group*, paragraph 54.

financial leasing, (ii) according to the size of customers (small- and medium-sized enterprises or large corporate customers), and/or (iii) according to the type of assets leased.⁷³

- (84) In particular with regard to the automotive sector, in the *Volvo Car Corporation/First Rent A Car* case, the Commission has identified two types of automotive financing: operational and financial leasing. According to the decision, the primary objective of financial leasing is the acquisition of the car, whereas in the case of operational leasing it is the use of the car. Financial leases function as a loan by the lessor to enable the lessee to purchase a given asset, in this case a car. In essence, the lessee has the obligation to pay all the lease instalments to meet the financing costs of the car, and bears also the operational and residual value risk. With operational leasing, the economic and legal ownership of the car remains with the lessor. Hence, it is the lessor who has to bear all the risks attached to the property (e.g. maintenance, changes to the value of the car and its disposal at the end of the contract).⁷⁴

4.1.7.2. Parties' views

- (85) In the view of the Parties, there is no need to distinguish between financial leasing and operational leasing, leased assets or customer size. There is no generally accepted clear-cut distinction between financial and operational leasing, many suppliers (e.g. banks) offer leasing for a variety of assets and whilst the legal arrangements differ depending on customer size, the available offers as such are not fundamentally different.⁷⁵

4.1.7.3. Commission's assessment and conclusion

- (86) In light of the supply-side substitutability between both leasing services (suppliers offering both) and the similarity of the offers to customers irrespective of the customer size, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis on a market for financial and operational leasing. In any event, the Parties submit that their market shares would not differ significantly from their market shares in the separate financial leasing and operational leasing market segments.

4.1.8. Full fleet leasing and management services

4.1.8.1. Commission's practice

- (87) In its recent decision *Volvo Car Corporation/First Rent A Car*, the Commission left open whether there is a separate market for full fleet leasing and management services, which consists in a combination of operational leasing and related fleet management services, or whether the market could be subdivided as follows:

⁷³ Case M.8553 – *Banco Santander/Banco Popular Group*, paragraph 23 et seq.; Case M.8414 – *DNB/Nordea/Luminor Group*, paragraph 67.

⁷⁴ Case M.8309 – *Volvo Car Corporation/First Rent a Car*, paragraphs 27 et seqq.

⁷⁵ Reply to RFI 10 of 26.10.2018.

- Funded fleet leasing (operational fleet leasing including where offered fleet management) and unfunded fleet leasing (fleet management services provided on a standalone basis);
- Fleet leasing and management for vehicles of up to 3.5 tons (passenger cars and light commercial vehicles) and of more than 3.5 tons (trucks and buses);
- By type (e.g. small, medium, large, executive, sport) or brand of cars (although leasing companies typically offer a range of types and brands; this segmentation does not seem relevant for the market of full fleet management services).⁷⁶ The Commission left the product market definition open.⁷⁷

4.1.8.2. Parties' views

(88) The Parties submit that, for the purpose of the present case, the precise product market definition can be left open since the Proposed Transaction does not raise any concerns on any of these markets.⁷⁸

4.1.8.3. Commission's assessment and conclusion

(89) In light of the limited turnover generated through unfunded fleet leasing (as opposed to funded fleet leasing), the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis below on the market for fleet leasing and management services.

4.1.9. Applications

4.1.9.1. Commission's practice

(90) In the case *Microsoft/Nokia*, the Commission examined whether apps for tablets were comparable in terms of features, functionality and price with those for smartphones⁷⁹ and also considered a separate market for consumer communications apps.⁸⁰

(91) Furthermore, while the Commission considered that mobile productivity apps for corporate users may constitute a separate product market, it left open the question whether the market for mobile productivity apps should be further segmented by functionality and/or operating system.⁸¹

⁷⁶ Case M.8309 - *Volvo Car Corporation/First Rent A Car*, paragraphs 34 et seq.

⁷⁷ Case M.8309 - *Volvo Car Corporation/First Rent A Car*, paragraph 37.

⁷⁸ Form CO, paragraph 157.

⁷⁹ Case M.7047 – *Microsoft/Nokia*, paragraph 33.

⁸⁰ Case M.7047 – *Microsoft/Nokia*, paragraph 45.

⁸¹ Case M.7047 – *Microsoft/Nokia*, paragraph 56.

(92) In the case *Facebook/WhatsApp*, the Commission considered a separate market for consumer communications apps for smartphones and carried out a competitive analysis on this product market.⁸²

(93) In any event, in neither of these two cases did the Commission explicitly distinguish between the development and the sale of smartphone apps.

4.1.9.2. Parties' views

(94) The Parties clarify that development and sale of smartphone apps refers to (i) the development of an app for a third party or (ii) the sale of the final app either to end customers (in the sense that they pay remuneration for downloading the app) or the sale to B2B customers.

(95) With regard to a potential segment for development and/or sale of multimodal apps, the Parties acknowledge that programming business apps might require a different skill set than programming games. However, the Parties do not believe that there are software developers that only program multimodal apps (or any other transportation apps) and are not capable of programming other apps. In their view, it seems that there is a significant amount of supply-side substitutability. Thus, the Parties assume that there is no distinct market for the development and sale of multimodal apps.⁸³

(96) With regard to a potential segment for access to multimodal apps, the Parties are not of the opinion that this is a relevant market pursuant to competition law. The Parties have understood “access to multimodal apps” as transportation service providers (or any other service provider interested) asking to have access to and be shown on a multimodal app. The reason for this view of the Parties is that a multimodal app is only one possible way of offering a transportation service to potential end customers. Most transportation providers rely on a wide variety of means, for example (individual) smartphone apps, homepages, ticket machines etc. The Parties refer to the CRA Study mentioned in paragraph (59) indicating that – even if one looked only at smartphone apps as a way of booking transportation services – multi-homing⁸⁴ is rather common in their view. Thus, there is also no need for a customer to be present on such multimodal app.⁸⁵

4.1.9.3. Commission's assessment and conclusion

(97) In order to conduct a most complete assessment, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis on the narrowest plausible segments of the market for applications (for smartphones), namely on the markets for (i) development/sale of smartphone

⁸² Case M.7217 – *Facebook/WhatsApp*, paragraph 34.

⁸³ Reply to RFI 9.

⁸⁴ Multi-homing is the practice of connecting a host or a computer network to more than one network. Multi-homing in this case would be, for example, the practice of a consumer downloading multiple car sharing applications on his/her device.

⁸⁵ Reply to RFI 9.

applications; (ii) development/sale of multimodal applications and (iii) access to multimodal applications.

4.2. Relevant geographic market

Horizontal

4.2.1. *All passengers transport services*

4.2.1.1. Commission's practice

(98) The Commission has not assessed the geographic scope of the market for an overall market for all (urban) passenger transport services.

4.2.1.2. Parties' view

(99) The Parties submit that, for the purpose of this decision, the geographic market definition could be left open as, even if the narrowest possible geographic market were considered, the proposed Transaction would not give rise to competition concerns.⁸⁶

4.2.1.3. Commission's assessment

(100) The majority of OEMs and mobility service providers indicate that the relevant geographic market is local at city level. The Commission concurs with these results of the market investigation as this is in line with the usage patterns of customers for most of the transport options.

4.2.1.4. Conclusion

(101) For the purpose of this case, the relevant geographic market for an overall market for all (urban) passenger transport services is local at city level.

4.2.2. *Short term car rental services including car sharing*

(102) In prior decisions, the Commission considered the geographic scope of this market to be national.⁸⁷ For short term corporate car rentals, the notifying parties even discussed a possible Europe-wide market.⁸⁸ In *Europcar/Goldcar*, the Commission considered that the market for short term car rental services is either national or local.⁸⁹

⁸⁶ Form CO, paragraph 114.

⁸⁷ See e.g. Case M.8309 - *Volvo Car Corporation/First Rent A Car*, paragraph 45; Case M.5568 - *Volkswagen/Fleet Investments - LeasePlan Corporation JV*, paragraph 20; Case M.3090 - *Volkswagen/Offset/Crescent LeasePlan/JV* paragraph 12.; Case M.1810 - *VW/Europe Car*, paragraph 13.

⁸⁸ Case M.2510- *Cendant/Galileo*, paragraph 20.

⁸⁹ Case M.8569 - *Europcar/Goldcar*, paragraph 42.

4.2.2.1. Parties' view

(103) The Parties consider it appropriate to delineate the market for short term car rental (including car sharing) as national in scope.⁹⁰

4.2.2.2. Commission's assessment

(104) In line with its previous decisions, the Commission considers the market for short term car rental to be national or local.

(105) The market may be considered national in scope due to factors such as differing consumer conduct per country, national preferences (e.g. for national car models), linguistic barriers and difficulties with regard to cross-border transactions.⁹¹

(106) In line with its decision in *Europcar/Goldcar*, the market for short-term car rental services may also be defined as local in scope. In that case, the market investigation confirmed the local features of the market, taking in account the fact that customers (and airport managers) do not consider car rental services offered at airports as interchangeable with car rental services offered downtown.⁹²

(107) The majority of OEMs and mobility service providers indicate that the relevant geographic market is local at city level. The Commission concurs with these results of the market investigation as this is in line with the usage patterns of short term car rental customers.

4.2.2.3. Conclusion

(108) For the purpose of this decision, the relevant geographic scope for a market for short term car rental would be local at city level.

4.2.3. *Car sharing as a whole and station-based vs free-floating*

4.2.3.1. Parties' view

(109) As explained above in paragraphs (33) and (46) *et seq.*, the Parties stated that it is not accurate to separate car sharing from a broad transportation market or, alternatively, the short term car rental segment. Following this line, the Parties stated that it is not appropriate to make a further segmentation.⁹³

⁹⁰ Form CO, paragraph 116.

⁹¹ Case M.8309 - *Volvo Car Corporation/First Rent A Car*, paragraph 45; Case M.5568 - *Volkswagen/Fleet Investments - LeasePlan Corporation JV*, paragraph 20; Case M.3090 - *Volkswagen/Offset/Crescent LeasePlan/JV* paragraph 12.; Case M.1810 - *VW/Europe Car*, paragraph 13.

⁹² Case M.8569 - *Europcar/Goldcar*, paragraphs 41-42.

⁹³ Form CO, paragraph 77.

4.2.3.2. Commission's assessment

- (110) In response to the market investigation, the (large) majority of OEMs and the majority of mobility service providers stated that the geographic market for free-floating car sharing is local on a city level.
- (111) In response to the market investigation, a (large) majority of the OEMs (56%) and 43% of the mobility service providers indicated that the geographic market for free-floating car sharing (including all other mobility services they consider to be substitutes) is local (city level) in scope; 33% of the OEMs and 32% of the mobility service providers indicated an EEA-wide market; none of the OEMs and only 13% of the mobility service providers indicated a national geographic market.⁹⁴
- (112) The criteria taken into account and mentioned by market investigation respondents indicating a local (by city) geographic market are the following: demand-side substitutability, supply-side substitutability and regulatory regulations and requirements.⁹⁵
- (113) One mobility service provider explained that "*[f]rom a demand-side perspective, customers' demand for these services is overwhelmingly local. The average customer wants to make use of their mobility services in the city they live or work in. Their choice as to which provider they use will be driven by the offering of that provider in such a city, not at the national or regional level. Moreover, as a supplier you have to determine whether to be present in a city/local area or not. The network required to provide a compelling offering means that a scattered or light touch spread is not an option. Rather, a supplier could offer a comprehensive network offering in one city but not in the next closest major city. That also affects how a supplier enters a market – they would invariably focus efforts on entry on a local level to get to the necessary level of vehicles. Finally, it is important to note that free floating car sharing services depend totally on the local regulations governing parking in the different cities. This means the supply characteristics vary by city.*"⁹⁶
- (114) This is in line with the fact that free-floating car sharing can only – except for Cologne and Dusseldorf, which can be used as one business area with an extra fee for leaving the car within the other city – be used within a single city. Even though driving outside the business area is possible at any time, the car can only be booked, picked up and left within the relevant city.

4.2.3.3. Conclusion

- (115) The Commission considers the geographic market for (free-floating) car sharing to be local on a city level.

⁹⁴ Replies to Questionnaire to OEMs, question 6. Replies to Questionnaire to mobility service providers, question 8.

⁹⁵ Replies to Questionnaire to OEMs, question 6.1. Replies to Questionnaire to mobility service providers, question 8.1.

⁹⁶ Reply to Questionnaire to mobility service providers, question 8.1.

Vertically related markets

4.2.4. Parking

4.2.4.1. Commission's practice

(116) In *Fortis AG SA/Bernheim-Comofi SA*, a local market was discussed, but the precise market definition was left open.⁹⁷ For the provision of parking management services even an EEA-wide or regional scope has been considered, but the Commission did not decide on the precise market definition.⁹⁸

4.2.4.2. Parties' views

(117) The Parties believe that it is appropriate to define markets on a national basis because market conditions are rather homogenous within each country. In Germany, over 40 cities apply the concept of the so-called *Smart Parking Initiative*, which grants access for every provider of parking services. Thus, companies can rather easily expand their activities. Although in the UK tender processes are used, it is also true that all providers for parking services in the UK compete regularly in these tenders.⁹⁹

4.2.4.3. Commission's assessment and conclusion

(118) In light of the homogenous parking conditions within each country, and in line with its previous decisions, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis with regard to parking services on a national basis.

4.2.5. Charging

4.2.5.1. Commission's practice

(119) Regarding the provision of electric mobility services, different geographical market definitions have been considered by the notifying parties and the participants of the market investigation (regional, national, perhaps wider than national) in the *Verbund/Siemens/E-Mobility Provider Austria* case.¹⁰⁰ The Commission did not finally decide on the market definition in this case.¹⁰¹

(120) As regards the upstream level, i.e. the production, supply and installation of charging infrastructure for electric mobility services, the notifying parties considered an EU- wide or global market, whereas the majority of the participants

⁹⁷ Case M.2825 - *FORTISAG SA/BERNHEIM-COMOFI SA*, paragraph 12.

⁹⁸ Case M.4613 - *Eurazeo S.A./Apcoa Parking Holdings GmbH*, paragraph 18; see also Case M.7398 - *MIRAEEL/FERROVIAUNDHL*, paragraph 30.

⁹⁹ Form CO, paragraph 196.

¹⁰⁰ Case COMP/M.6641 - *Verbund/Siemens/E-Mobility Provider Austria*, para. 19 et seq.

¹⁰¹ Case COMP/M.6641 - *Verbund/Siemens/E-Mobility Provider Austria*, para. 21.

of the market investigation assumed a national, or at most supranational, market.¹⁰²

4.2.5.2. Parties' views

(121) In the Parties' view, the precise geographic market definition for charging services can be left open because the proposed Transaction would not give rise to any competition concerns on any of these markets.¹⁰³

4.2.5.3. Commission's assessment and conclusion

(122) In line with its precedents, the Commission considers, for the purpose of this decision, the geographic market for electric mobility services to be at least national in scope, and will consequently carry out its vertical competitive analysis with regard to charging services at national level, as the narrowest plausible geographic market definition.

4.2.6. *Passenger cars*

4.2.6.1. Commission's practice

(123) In terms of geographic market definition, the Commission has considered the market for passenger cars being EEA-wide or national in scope.¹⁰⁴ The Commission left the market definition open in these cases.

4.2.6.2. Parties' views

(124) In the Parties' view the market for passenger cars is at least EEA-wide in scope.¹⁰⁵

4.2.6.3. Commission's assessment and conclusion

(125) In line with its precedents, the Commission considers, for the purpose of this decision, the geographic market for passenger cars (both (i) manufacture & supply and (ii) distribution) to be at least national in scope, and will consequently carry out its vertical competitive analysis with regard to passenger cars at national level, as the narrowest plausible geographic market definition.

4.2.7. *Financial and operational leasing*

4.2.7.1. Commission's assessment

(126) In its previous decisional practice, the leasing market was considered to be national in scope.¹⁰⁶

¹⁰² Case COMP/M.6641 - *Verbund/Siemens/E-Mobility Provider Austria*, para. 30 et seq.

¹⁰³ Form CO, paragraph 215.

¹⁰⁴ See e.g. Case M.5518 - *Fiat/Chrysler*, paragraph 20; Case M.5518- *Fiat/Chrysler*, paragraph 12; Case M.6403 - *Volkswagen/KPI Polska/Skoda Auto Polska/VW Bank Polska/VW Leasing Polska*, paragraph 19.

¹⁰⁵ Form CO, paragraph 127.

(127) With regard to the automotive sector, in the *Volvo Car Corporation/First Rent A Car* case, the Commission left open whether the geographic market definition for operational and financial leasing is national or EEA-wide in scope.¹⁰⁷

4.2.7.2. Parties' views

(128) With regard to the geographical market, the Parties note that there are examples of cross-border leasing contracts, however, consumer practice, preferences and language barriers point in the direction of national markets, leaving open whether the geographic scope for financial and operational leasing is national or wider than national.¹⁰⁸

4.2.7.3. Commission's assessment and conclusion

(129) In line with its precedents, the Commission considers, for the purpose of this decision, the geographic market for financial and operational leasing to be at least national in scope, and will consequently carry out its vertical competitive analysis with regard to financial and operational leasing at national level, as the narrowest plausible geographic market definition.

4.2.8. *Full fleet leasing and management services*

4.2.8.1. Commission's practice

(130) In its recent decision *Volvo Car Corporation/First Rent A Car*, the Commission left open whether the geographic market is EEA-wide or national in scope.¹⁰⁹

4.2.8.2. Parties' views

(131) In the Parties' view, the precise geographic market definition of the market for full fleet leasing and management services can be left open for the purpose of the present case since the Proposed Transaction does not raise any concerns on any of these markets.¹¹⁰

4.2.8.3. Commission's assessment and conclusion

(132) In line with its precedents, the Commission considers, for the purpose of this decision, the geographic market for full fleet leasing and management to be at least national in scope, and will consequently carry out its vertical competitive analysis with regard to full fleet leasing and management services at national level, as the narrowest plausible geographic market definition.

¹⁰⁶ See e.g. Case M.8414 – *DNB/Nordea/Luminor Group*, paragraph 71.

¹⁰⁷ Case M.8309 – *Volvo Car Corporation/First Rent a Car*, paragraph 33.

¹⁰⁸ Reply to RFI 10 of 26.10.2018.

¹⁰⁹ Case M.8309 - *Volvo Car Corporation/First Rent A Car*, paragraphs 38 et seqq.

¹¹⁰ Form CO, paragraph 157.

4.2.9. Applications

4.2.9.1. Commission's practice

- (133) The geographic scope of the relevant markets for consumer communication services and for mobile productivity apps has been considered to be at least EEA-wide, if not worldwide.¹¹¹
- (134) Also the geographic scope for a separate market for consumer communications apps for smartphones has been considered to be EEA-wide, if not worldwide, in scope.¹¹²

4.2.9.2. Parties' views

- (135) With regard to the development and sale of smartphone apps, the Parties submit that the relevant markets should at least be EEA-wide, if not global. According to them, app developers are located all over the world. It is very common that businesses that do not have in-house development capabilities reach out to such third party developers. There might be some restraints when it comes to finding a suitable developer, depending on budget, experience or project size. But generally speaking, a breadth of developers is available to work for third-party projects. In addition, they do not consider that language barriers are a major obstacle for programming an app, thus they believe the geographic market definition should be at least EEA-wide, if not worldwide.¹¹³

4.2.9.3. Commission's assessment and conclusion

- (136) In line with its precedents, the Commission considers it appropriate, for the purpose of this decision, to carry out its vertical competitive analysis with regard to applications (and its market segments) at EEA-wide level. In addition, the Commission also assessed the applications segments at national level, as the narrowest plausible geographic market definition.

5. COMPETITIVE ASSESSMENT

5.1. Legal framework

- (137) With regard to horizontal effects, according to paragraph 22(a) of the Horizontal Merger Guidelines,¹¹⁴ a concentration could raise competition concerns by eliminating important competitive constraint on one or more firms (non-coordinated effects). There are a number of factors which are considered by the Commission in its assessment of non-coordinated effects in horizontal mergers,

¹¹¹ Case M.7047 – *Microsoft/Nokia*, paragraph 81.

¹¹² Case M.7217 – *Facebook/WhatsApp*, paragraph 44.

¹¹³ Reply to RFI 9 of 26.10.2018.

¹¹⁴ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31, 5 February 2017, p. 5 ("Horizontal Guidelines").

such as (i) merging firms having large market shares, (ii) merging firms being close competitors, (iii) merging entity being able to hinder expansion by competitors.¹¹⁵

- (138) With regard to vertical effects, according to paragraph 15 of the Vertical Merger Guidelines,¹¹⁶ there are certain circumstances in which non-horizontal mergers could raise competition concerns. This is because a non-horizontal merger may change the ability and incentive to compete on the part of the merging entity and their competitors in ways that cause harm to consumers.
- (139) Accordingly, the Commission will first give an overview of the affected markets and second assess the horizontal effects of the proposed Transaction on four plausible markets, namely (i) all passengers transport services, (ii) short term car rental services including car sharing, (iii) car sharing as a whole (including station-based and free-floating) and (iv) free-floating car sharing. The Commission will then analyse the vertical effects of the proposed Transaction on several markets upstream and downstream with respect of (potential) input and/or customer foreclosure.

5.2. Overview of affected markets

- (140) The proposed Transaction gives rise to the following horizontally affected (free-floating) car sharing markets: (i) Berlin, (ii) Cologne, (iii) Dusseldorf, (iv) Hamburg, (v) Munich, (vi) Milan and (vii) Vienna.
- (141) In addition, the proposed Transaction gives rise to the following vertically affected markets: (i) manufacture and supply of passenger cars / (free-floating) car sharing, (ii) manufacture and supply of (pure electric powered cars) passenger cars / parking (including hardware payment services), (iii) manufacture and supply of (pure electric powered cars) passenger cars / charging, (iv) financial and operational leasing / (free-floating) car sharing, (v) full fleet leasing and management services / (free-floating) car sharing, (vi) development and sale of smartphone apps / (free-floating) car sharing, (vii) development and sale of multimodal apps/ (free-floating) car sharing, (viii) access to multimodal apps / (free-floating) car sharing, (ix) charging / (free-floating) car sharing.

5.3. Horizontal effects

Mobility Services

5.3.1. *All passengers transport services*

- (142) On a potential market for all (urban) passengers transport services, according to the Parties' estimates,¹¹⁷ the Parties' combined market share would be [0-5]% in

¹¹⁵ Paragraphs 24-30 and paragraph 36 of the Horizontal Guidelines.

¹¹⁶ Guidelines on the assessment of non-horizontal mergers under the Council regulation on the control of concentrations between undertakings.

¹¹⁷ Form CO, paragraph 254 and reply to Q2 of RFI 6 dated 24 October 2018: these estimates are calculated on the basis of 2017 figures on public transport companies' turnover. The Parties submit that the Parties' combined market share is in fact much lower than the figures provided as (i) the Parties'

Berlin, [0-5]% in Dusseldorf, [0-5]% in Cologne, [0-5]% in Hamburg, [0-5]% in Munich, [0-5]% in Milan and [0-5]% in Vienna.

- (143) As a consequence, in the light of the information provided by the Parties, a potential market for all passengers (urban) transport services would not be affected.

5.3.2. *Short term car rental services including car sharing*

- (144) On a potential short-term car rental market (including car sharing), the Parties' combined market shares would be well below 20%, not giving rise to any affected markets. According to their best estimates, their combined market share would be below 20% under any plausible geographic market definition.¹¹⁸

- (145) In a potential short term car rental segment (including car sharing), there would be many providers, e.g. Sixt, Europcar, Avis, Enterprise, Hertz, Budget, Flinkster, Cambio, book-n-drive, Stadtmobile, Greenwheels and app2drive. All major car rental companies are to a large extent present in the cities in which DriveNow and car2go provide their services. The Parties would continue to face competitive pressure from these car rental services providers post-Transaction.¹¹⁹

- (146) In addition, according to the Parties, new market entries are expected due to the favourable political and regulatory environment and the expected growth of the market. Moreover, the Parties submit that customers are switching between different providers, preventing companies from increasing prices to a significant extent.¹²⁰

5.3.3. *Car sharing as a whole and station based vs free-floating*

Parties' activities on a city level

- (147) The Parties offer (free-floating) car sharing services in a number of countries within the EEA, namely Austria (Vienna), Belgium (Brussels), Germany (Berlin, Cologne, Dusseldorf, Frankfurt/Main, Hamburg, Munich and Stuttgart), Italy (Florence, Milan, Rome and Turin), Netherlands (Amsterdam), Spain (Madrid), Sweden (Stockholm), United Kingdom (London) and additionally – operated via franchises¹²¹ – in Denmark (Copenhagen), Finland (Helsinki) and Portugal

turnover and the turnover of other car sharing providers and (ii) turnover of a number of further competing mobility service providers, other than public transportation companies, e.g. taxi and ride-hailing offerings, would have to be included. These are not included in the figures provided, as the Parties claim that they do not have any concrete figures. That being said, the Parties submit that their combined market share would not differ significantly if such additional services would be included in the market volume. In fact, the Parties claim that the Parties' combined market share would even be lower.

¹¹⁸ Form CO, paragraph 120.

¹¹⁹ Form CO, paragraph 120.

¹²⁰ Form CO, paragraph 120.

¹²¹ [INFORMATION ON AGREEMENT].

(Lisbon). However, on a narrow geographic market definition based on a city level, the Parties only overlap in Austria (Vienna), Germany (Berlin, Cologne, Dusseldorf, Hamburg and Munich) and Italy (Milan).

- (148) The Parties also plan to enter several new cities inside the EEA within the next three years (until the end of 2021). DriveNow has plans to enter [INFORMATION ON BUSINESS PLANS], whereas car2go is planning to enter [INFORMATION ON BUSINESS PLANS].
- (149) These entry plans would result in (direct) potential future overlaps in [INFORMATION ON BUSINESS PLANS]. However, these are plans which are uncertain as to their timing and likelihood. Only Paris (car2go) is confirmed for 2019 by Daimler, and [INFORMATION ON BUSINESS PLANS] (DriveNow) is the most likely entry point for BMW.

Overview of affected markets - implied market shares

- (150) As noted in the section on market definition above (paragraph (59) *et seq.*), the competitive assessment of the proposed Transaction must take proper account of the heterogeneous degrees of closeness of competition between different mobility services, including the potential significance of certain out-of-market constraints.
- (151) Such an assessment of closeness of competition can be conducted on the basis of the diversion ratios between the merging Parties and alternative providers considered by customers. Generally speaking, higher observed diversion ratios between two services mean that those services are closer substitutes towards one another.
- (152) One way of illustrating the competitive positioning of various services from the perspective of customers is to consider which (hypothetical) market shares would be consistent with the observed diversion ratios as shown in Table A. if switching were proportional to market shares. The following table shows these "implied market shares" for the overlap cities Berlin, Cologne, Dusseldorf, Hamburg, Milan, Munich and Vienna.¹²²

¹²² Mathematically, let d_{ij} denote the observed diversion ratio from service i to service j and let s_i denote the implied market share of service i . If diversion between the Parties is proportional to market shares, the diversion ratios between Party 1 and 2 can be expressed as $d_{12} = s_2/(1 - s_1)$ and $d_{21} = s_1/(1 - s_2)$, respectively. Solving these equations for s_1 and s_2 then yields the implied market shares $s_1 = d_{21}(1 - d_{11})/(1 - d_{12}d_{21})$ and $s_2 = d_{12}(1 - d_{21})/(1 - d_{12}d_{21})$. These formulas result in the Parties' share values presented in Table B. The implied shares of other services are presented for illustrative purposes only. They were constructed in proportion to the size of their respective diversion ratios, as a weighted average of the value given in Table A further above.

	Implied market shares							
	Total	BER	COL	DUS	HAM	MIL	MUC	VIE
car2go	[30-40]%	[30-40]%	[30-40]%	[40-50]%	[40-50]%	[30-40]%	[20-30]%	[40-50]%
Drive Now	[10-20]%	[20-30]%	[20-30]%	[10-20]%	[10-20]%	[10-20]%	[20-30]%	[10-20]%
Combined	[50-60]%	[50-60]%	[50-60]%	[50-60]%	[60-70]%	[40-50]%	[50-60]%	[60-70]%
Public transport	[20-30]%	[20-30]%	[20-30]%	[20-30]%	[20-30]%	[10-20]%	[20-30]%	[20-30]%
Own car	[10-20]%	[10-20]%	[10-20]%	[10-20]%	[5-10]%	[5-10]%	[10-20]%	[10-20]%
Bike/scooter	[0-5]%	[5-10]%	[5-10]%	[5-10]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%
Free floating	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[20-30]%	[0-5]%	[0-5]%
Taxi/Uber	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[5-10]%
Rental/station	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%
Other	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%	[0-5]%
Total	100%	100%	100%	100%	100%	100%	100%	100%

Table B: Hypothetical "implied market shares" consistent with observed diversion ratios between the Merging Parties and other means of transport

- (153) As shown in the table, the diversion ratios obtained in the July 2018 customer survey (see paragraph (59)) would be consistent with combined market shares of around [50-60]% on a hypothetical market for all (urban) passenger transport where switching is proportional to market shares. This relatively high market share reflects the fact that customers view the Parties as particularly close substitutes (as noted in the market definition section above, paragraph (59) *et seq.*). It can therefore be concluded that the proposed Transaction would eliminate a particularly important independent constraint for users of the Parties' services. Indeed, while the figures in Table B also reflect a significant degree of competition with various other mobility services, the Parties' implied market shares are appreciably higher than any potential alternative.
- (154) This conclusion is also consistent with the results of the market investigation more generally. While other means of transport do not compete as closely as the

Parties do between each other¹²³, the data shows that they do compete with the Parties and exert non-negligible competitive pressure.

Barriers to entry

- (155) Respondents to the market investigation identified several barriers to entry. Some of them are not related to this Transaction such a local regulation, or would not change materially due to the Transaction such as "access to car telemetry" (for monitoring the car by combining a GPS system with on-board diagnostics). Others, however, are increasing as a consequence of this Transaction. One of these barriers to entry is fleet size required to enter a city and the ensuing financial burden to finance such a fleet. The combined fleet of the merged entity would require higher fleet sizes of new entrants in all overlap cities, a barrier particularly pertinent for small, non-OEM related competitors.
- (156) Another entry barrier named was access to aggregators, which could also increase as a consequence of this Transaction, as the Parties would promote their own aggregator platform "moovel" and could withdraw their must have content from independent aggregator platforms.
- (157) The Commission therefore considers that barriers to entry exist and could become higher as a consequence of this Transaction for at least smaller players. The most important are the capital requirement for a minimum number of cars, which is needed to be visible on the streets, but also access to third aggregator apps, which could also combine different kind of mobility services like car sharing, scooter sharing, car rental and public transport, to be (more) visible online as bookings are usually done either directly via the app of a certain mobility service (car sharing) provider or at least via an third party aggregator's app.
- (158) While the above considerations give rise to serious doubts about the impact of the proposed Transaction on competition in five overlap cities, as will be shown in the assessment of all overlap cities, the Commission also recognizes that the potential competitive damage is attenuated by the following factors: (i) constraint imposed mostly by public transport, (ii) limited entry barriers (except for the need to compete against a much larger provider post-merger, which is addressed via the remedy), (iii) expected entry of Volkswagen and others.

5.3.4. Overlap cities - city by city assessment

5.3.4.1. Berlin

- (159) In Berlin both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹²⁴

¹²³ Note that DriveNow's implied market share is smaller than car2go's in almost all cities. This reflects the fact that DriveNow customers are more likely to switch to car2go than vice versa according (see also Table A further above). Arguably, this is due to the fact that customers tend to view DriveNow as the more valuable (and also more expensive) service. Users of car2go are therefore more likely to "substitute down" towards cheaper means of transport, such as public transport, whereas DriveNow customers are more likely to switch to another provider of free floating car services (in particular, car2go).

- (160) According to the information provided by Parties, there exist another small free-floating car sharing provider, namely Drive by, with a fleet of [INFORMATION ON FLEET] cars, and six more station-based car sharing providers, namely Flinkster ([INFORMATION ON FLEET] cars), Ubeeqo ([INFORMATION ON FLEET] cars), Greenwheels ([INFORMATION ON FLEET] cars), Stadtmobil ([INFORMATION ON FLEET] cars), Cambio ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars).¹²⁵
- (161) Therefore, the total size of Berlin's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [80-90]% for free-floating and station-based car sharing and [90-100]% for (only) free-floating car sharing.
- (162) Focusing on revenues, the Parties estimate market shares of [80-90]% for free-floating and station-based car sharing and [90-100]% for free-floating car sharing only.
- (163) Entry barriers do exist, as mentioned above in paragraph (155) *et seq.* However, parking fees have to be paid on a regular basis and parking permissions are not needed.¹²⁶ There also does not exist a minimum or maximum number of cars for free-floating car sharing.¹²⁷ Therefore, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.
- (164) The market investigation has identified entry plans in the market for car sharing services in Berlin by Volkswagen, which could be considered as timely, likely and sufficient to deter or defeat the anticompetitive effect of the proposed Transaction on the free-floating car sharing market in Berlin.¹²⁸ Volkswagen stated publicly that the Volkswagen brand starts "We Share" e-mobility car sharing in Berlin with 1,500 e-Golf in the second quarter of 2019, with additional 500 e-up! following later.¹²⁹ Furthermore, the market investigation has also identified one additional entry plan, which can be considered at least as timely and likely, and six further entry intentions from several OEMs and other mobility providers, which do have financial resources and/or the expertise for car sharing and related sectors.¹³⁰

¹²⁴ Form CO, Confidential Annex 7.b.

¹²⁵ Form CO, Confidential Annex 7.b.

¹²⁶ Reply Senatsverwaltung Berlin to Questionnaire to local authorities, question 7.

¹²⁷ Reply to Questionnaire to local authorities, questions 10-13.

¹²⁸ Reply to Questionnaire to OEMs, question 18.

¹²⁹ See Press Release published on https://www.volkswagenag.com/en/news/2018/08/VW_Brand_We_Share.html.

¹³⁰ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

(165) In the light of the above, the Commission considers that the proposed Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Berlin as well as on a market definition comprising free-floating and station-based car sharing.

5.3.4.2. Cologne

(166) In Cologne both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹³¹

(167) According to the information provided by Parties, there exists no other free-floating car sharing provider, but four more station-based car sharing providers, namely Cambio ([INFORMATION ON FLEET] cars), Flinkster ([INFORMATION ON FLEET] cars), Mazda Mobil Carsharing ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars), are present in Cologne.¹³²

(168) Therefore, the total size of Cologne's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [50-60]% for free-floating and station-based car sharing and 100% for (only) free-floating car sharing.

(169) Focusing on revenues, the Parties estimate market shares of [50-60]% for free-floating and station-based car sharing and 100% for free-floating car sharing only.

(170) Entry barriers do exist, as mentioned above in paragraph (155) *et seq.* However, parking fees have to be paid on a regular basis (except for electronic vehicles, which are free).¹³³ There also does not exist a minimum or maximum number of cars for free-floating car sharing.¹³⁴ Therefore, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.

(171) The market investigation has identified at least one entry plan which can be considered as timely and likely, but not sufficient, and at least five additional entry intentions in the market for car sharing services in Cologne from several OEMs and other mobility providers, which do have financial resources and/or the

¹³¹ Form CO, Confidential Annex 7.b.

¹³² Form CO, Confidential Annex 7.b.

¹³³ Reply *Stadt Köln* to Questionnaire to local authorities, question 7.

¹³⁴ Reply to Questionnaire to local authorities, questions 10-13.

expertise for car sharing and related sectors.¹³⁵ However, none of them can be considered as timely, likely and sufficient.

- (172) Nevertheless, Volkswagen stated publicly that the Volkswagen brand starts "We Share" e-mobility car sharing in Berlin as of 2019.¹³⁶ Following the launch in Berlin, "We share" will be initially scheduled to roll out in further major cities in Germany. In parallel, as it is stated in above-referred press release of Volkswagen, they have plans to expand in core European markets and selected cities in North America from 2020. The primary focus will be on cities with a population of over one million, which would be theoretically met e.g. in Cologne.
- (173) However, in the light of the above, the Commission considers that the proposed Transaction raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Cologne as well as on a market definition comprising free-floating and station-based car sharing.

5.3.4.3. Dusseldorf

- (174) In Dusseldorf both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹³⁷
- (175) According to the information provided by Parties, there exists no other free-floating car sharing provider, but five more station-based car sharing providers, namely Greenwheels ([INFORMATION ON FLEET] cars), Stadtmobil ([INFORMATION ON FLEET] cars), Flinkster ([INFORMATION ON FLEET] cars), E-carflex ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] car), are present in Dusseldorf.¹³⁸
- (176) Therefore, the total size of Dusseldorf's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [80-90]% for free-floating and station-based car sharing and 100% for (only) free-floating car sharing.
- (177) Focusing on revenues, the Parties estimate market shares of [70-80]% for free-floating and station-based car sharing and 100% for free-floating car sharing only.
- (178) Entry barriers do exist, as mentioned above in paragraph (155) *et seq.* Furthermore, there are also parking permissions needed which have to be paid per

¹³⁵ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

¹³⁶ See Press Release published on https://www.volkswagenag.com/en/news/2018/08/VW_Brand_We_Share.html.

¹³⁷ Form CO, Confidential Annex 7.b.

¹³⁸ Form CO, Confidential Annex 7.b.

car on a yearly basis (less expensive for electronic vehicles).¹³⁹ However, the market investigation made also clear that the number of parking permissions for free-floating car sharing is not yet limited by the municipality and that there also does not exist a minimum or maximum number of cars for free-floating car sharing.¹⁴⁰ Therefore, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.

- (179) The market investigation has identified one entry plan which can be considered as timely, likely and close to sufficient, and at least additional five entry intentions in the market for car sharing services in Dusseldorf from several OEMs and other mobility providers, which do have financial resources and/or the expertise for car sharing and related sectors.¹⁴¹ However, for the purposes of this analysis, none of them can be considered as timely, likely and sufficient because they appear to be in an early stage and no fleet numbers have been disclosed to the Commission.
- (180) In the light of the above, the Commission considers that the proposed Transaction raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Dusseldorf as well as on a market definition comprising free-floating and station-based car sharing.

5.3.4.4. Cologne/Dusseldorf (as one business area)

- (181) The Parties consider Cologne and Dusseldorf as one business area. Only there reserved cars can be picked up in Cologne and parked in Dusseldorf, and vice versa, for an extra fee. The percentage of number of journeys for car2go's vehicles picked up in Cologne and dropped off in Dusseldorf, and vice versa, was approx. [INFORMATION ON PERCENTAGE]% of the total rentals in the Rhineland area in 2017.¹⁴² Approx. [INFORMATION ON PERCENTAGE]% of the total turnover from Cologne and Dusseldorf can be attributed to a drop-off of the cars in the other location. For DriveNow the percentage was approx. [INFORMATION ON PERCENTAGE]% (rentals) and [INFORMATION ON PERCENTAGE]% (turnover).
- (182) In Cologne and Dusseldorf (considered as one business area) both Parties would currently be present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹⁴³
- (183) According to the information provided by Parties, there exists no other free-floating car sharing provider, but seven more station-based car sharing providers, namely Cambio ([INFORMATION ON FLEET] cars), Flinkster

¹³⁹ Reply Landeshauptstadt Düsseldorf to Questionnaire to local authorities, questions 7 and 8.

¹⁴⁰ Reply to Questionnaire to local authorities, questions 10-13.

¹⁴¹ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

¹⁴² See Form CO, paragraph 63.

¹⁴³ Form CO, Confidential Annex 7.b.

([INFORMATION ON FLEET] cars), Stadtmobil ([INFORMATION ON FLEET] cars), Greenwheels ([INFORMATION ON FLEET] cars), Mazda Mobil Carsharing ([INFORMATION ON FLEET] cars), E-carflex ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars), are present in this area.¹⁴⁴

- (184) Therefore, the total size of Cologne/Dusseldorf's car sharing market (free-floating and station-based) would be around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction would be [60-70]% for free-floating and station-based car sharing and 100% for (only) free-floating car sharing.
- (185) Focusing on revenues, the Parties market shares would be [60-70]% for free-floating and station-based car sharing and 100% for free-floating car sharing only.
- (186) Although the market investigation has identified two entry plans which can be considered as timely and likely (and several entry intentions), it could not be considered as sufficient anymore.¹⁴⁵
- (187) Therefore, in the light of the above, the Commission considers that the proposed Transaction also raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Dusseldorf/Cologne as one business area as well as on a market definition comprising free-floating and station-based car sharing.

5.3.4.5. Hamburg

- (188) In Hamburg both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹⁴⁶
- (189) According to the information (mainly) provided by Parties, there exist no other free-floating car sharing provider, but seven more station-based car sharing providers, namely Cambio ([INFORMATION ON FLEET] cars), Oply ([INFORMATION ON FLEET] cars as of 10/10/2018), Greenwheels ([INFORMATION ON FLEET] cars), Ubeeqo ([INFORMATION ON FLEET] cars), share a star car ([INFORMATION ON FLEET] cars), Flinkster ([INFORMATION ON FLEET] cars), app2drive ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars), are present in Hamburg.¹⁴⁷

¹⁴⁴ Form CO, Confidential Annex 7.b.

¹⁴⁵ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

¹⁴⁶ Form CO, Confidential Annex 7.b.

¹⁴⁷ Form CO, Confidential Annex 7.b.

- (190) Therefore, the total size of Hamburg's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [70-80]% for free-floating and station-based car sharing and 100% for (only) free-floating car sharing.
- (191) Focusing on revenues, the Parties estimate market shares of [80-90]% for free-floating and station-based car sharing and 100% for free-floating car sharing only.
- (192) Entry barriers exist, as mentioned above in paragraph (155) *et seq.* However, parking fees have to be paid on a regular basis; parking permissions are not needed.¹⁴⁸ There also does not exist a minimum or maximum number of cars for free-floating car sharing.¹⁴⁹ Therefore, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.
- (193) The market investigation has identified three entry plans which can be considered as timely, but (probably) not sufficient and likely yet. One of these plans was realized by Oply, operating a fleet of 100 cars as of 10 October 2018.¹⁵⁰ Furthermore, there are at least seven additional entry intentions in the market for car sharing services in Hamburg from several OEMs and other mobility providers, which do have financial resources and/or the expertise for car sharing or related sectors.¹⁵¹ However, none of them can be considered as timely, likely and sufficient.
- (194) Therefore, in the light of the above, the Commission considers that the proposed Transaction raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Hamburg as well as on a market definition comprising free-floating and station-based car sharing.

5.3.4.6. Munich

- (195) In Munich both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹⁵²
- (196) According to the information provided by Parties, there exists one more free-floating car sharing provider, namely Flexy with a fleet of [INFORMATION ON FLEET] cars, and five more station-based car sharing providers, namely

¹⁴⁸ Reply Landesbetrieb Verkehr der Hansestadt Hamburg to Questionnaire to local authorities, questions 7 and 8.

¹⁴⁹ Reply to Questionnaire to local authorities, questions 10-13.

¹⁵⁰ See <https://www.carsharing-news.de/oply-kommt-nach-hamburg/>.

¹⁵¹ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

¹⁵² Form CO, Confidential Annex 7.b.

StattAuto ([INFORMATION ON FLEET] cars), Flinkster ([INFORMATION ON FLEET] cars), Oply ([INFORMATION ON FLEET] cars), Audi on demand ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars).¹⁵³

- (197) Therefore, the total size of Munich's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [60-70]% for free-floating and station-based car sharing and [90-100]% for (only) free-floating car sharing.
- (198) Focusing on revenues, the Parties estimate market shares of [60-70]% for free-floating and station-based car sharing and [90-100]% for free-floating car sharing only.
- (199) Entry barriers do exist, as mentioned above in paragraph (155) *et seq.* Furthermore, there are also parking permissions needed which could be paid per car on a yearly basis (except for electronic vehicles, which are free).¹⁵⁴ However, the market investigation made also clear that the number of parking permissions for free-floating car sharing is not yet limited by the municipality and that there also does not exist a minimum or maximum number of cars for free-floating car sharing.¹⁵⁵ Therefore, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.
- (200) The market investigation has identified two entry plans which can be considered at least timely and likely, but (probably) not sufficient yet, and seven additional entry intentions from several OEMs and other mobility providers, which do have financial resources and/or the expertise for car sharing and related sectors.¹⁵⁶ However, none of them can be considered as timely, likely and sufficient.
- (201) Therefore, in the light of the above, the Commission considers that the proposed Transaction raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Munich as well as on a market definition comprising free-floating and station-based car sharing.

¹⁵³ Form CO, Confidential Annex 7.b.

¹⁵⁴ Reply Landeshauptstadt München to Questionnaire to local authorities, question 7 and 8.

¹⁵⁵ Reply Landeshauptstadt München to Questionnaire to local authorities, question 7 and 10-13.

¹⁵⁶ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

5.3.4.7. Milan

- (202) In Milan both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go operates [INFORMATION ON FLEET] cars and DriveNow [INFORMATION ON FLEET] cars.¹⁵⁷
- (203) According to the information provided by Parties, there exist two more free-floating car sharing providers, namely Share'ngo with a fleet of [INFORMATION ON FLEET] cars and Enjoy with a fleet of [INFORMATION ON FLEET] cars. Furthermore, there exist three more station-based car sharing providers, namely Ubeeqo with a fleet of [INFORMATION ON FLEET] cars, E-Vai with a fleet of [INFORMATION ON FLEET] cars and Hertz 24/7 with [INFORMATION ON FLEET] cars.¹⁵⁸
- (204) Therefore, the total size of Milan's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [30-40]% for free-floating and station-based car sharing and [30-40]% for (only) free-floating car sharing. The Parties therefore would be – more or less – at the same level like Share'ngo ([30-40]%) and Enjoy ([20-30]%) on the narrowest market for free-floating car sharing.
- (205) Focusing on revenues, the Parties estimate market shares of [30-40]% for free-floating and station-based car sharing and [30-40]% for free-floating car sharing only.
- (206) Entry barriers do exist, as mentioned above in paragraph (155) *et seq.* There are also parking permissions needed which have to be paid per car on a yearly basis (electric vehicles are for free).¹⁵⁹ Furthermore, a minimum number of 400 cars must be provided for free-floating car sharing.¹⁶⁰ However, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.
- (207) The market investigation has identified five entry intentions from several OEMs and other mobility providers, which do have financial resources and/or the expertise for car sharing and related sectors, which could partially be considered as timely.¹⁶¹ However, none of them can be considered as likely and sufficient.
- (208) Nevertheless, in the light of the above, and especially the strong presence of third free-floating car sharing providers, the Commission considers that the proposed

¹⁵⁷ Form CO, Confidential Annex 7.b.

¹⁵⁸ Form CO, Confidential Annex 7.b.

¹⁵⁹ Reply Municipality of Milan to Questionnaire to local authorities, questions 7 and 8.

¹⁶⁰ Reply Municipality of Milan to Questionnaire to local authorities, questions 11.

¹⁶¹ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Milan as well as on a market definition comprising free-floating and station-based car sharing.

5.3.4.8. Vienna

- (209) In Vienna both Parties are currently present with a fleet of [INFORMATION ON FLEET] cars of which car2go and DriveNow [INFORMATION ON FLEET].¹⁶²
- (210) According to the information provided by Parties, there exist no other free-floating car sharing providers, but five more station-based car sharing providers, namely Stadtauto ([INFORMATION ON FLEET] cars), ÖBB Rail&Drive ([INFORMATION ON FLEET] cars), Sharetoo ([INFORMATION ON FLEET] cars), MO.Point ([INFORMATION ON FLEET] cars) and Elfride ([INFORMATION ON FLEET] car).¹⁶³
- (211) Therefore, the total size of Vienna's car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will be [90-100]% for free-floating and station-based car sharing and 100% for (only) free-floating car sharing.
- (212) Focusing on revenues, the Parties estimate market shares of [90-100]% for free-floating and station-based car sharing and 100% for free-floating car sharing only.
- (213) Entry barriers do exist, as mentioned above in paragraph (155) *et seq.* However, parking permissions are not needed, but parking fees could be paid on a yearly basis.¹⁶⁴ There also does not exist a minimum or maximum number of cars for free-floating car sharing.¹⁶⁵ Therefore, these cannot be considered as entry barriers, as all free-floating car sharing providers are treated in the same way.
- (214) The market investigation has identified one entry plans as timely, but (probably) not sufficient and likely yet, and five additional entry intentions from several OEMs and other mobility providers, which do have financial resources and/or the expertise for car sharing and related sectors.¹⁶⁶ However, none of them can be considered as timely, likely and sufficient.
- (215) Therefore, in the light of the above, the Commission considers that the proposed Transaction raises serious doubts as to its compatibility with the internal market

¹⁶² Form CO, Confidential Annex 7.b.

¹⁶³ Form CO, Confidential Annex 7.b.

¹⁶⁴ Reply *Magistrat der Stadt Wien* to Questionnaire to local authorities, questions 7 and 8.

¹⁶⁵ Reply to Questionnaire to local authorities, questions 10-13.

¹⁶⁶ Replies to Questionnaire to OEMs, question 18. Replies Questionnaire to mobility service providers, question 20.

on a narrow market definition comprising only free-floating car sharing in Vienna as well as on a market definition comprising free-floating and station-based car sharing.

5.3.5. *Potential overlap cities in the future - city by city assessment*

5.3.5.1. Paris

- (216) In July 2018, Paris' biggest free-floating car sharing provider Autolib' stopped operating its fleet of around 4,000 cars due to huge financial losses. As a result of the failure of Autolib', third party providers of free-floating car sharing try to fill the gap, especially Renault, PSA, but also the Parties. On 4 July 2018, Renault publicly announced to offer free-floating car sharing services in Paris with a starting fleet of 120 cars as of September 2018 to be expanded up to 2,000 cars as of the end of 2019.¹⁶⁷ PSA also announced publicly to offer free-floating car sharing services in Paris with a fleet of 500 cars as of the end of 2018.¹⁶⁸
- (217) The Parties are not currently present in Paris. However, car2go is planning to enter as of January 2019 with a fleet of 400 cars, which [INFORMATION ON FLEET].¹⁶⁹ With regard to DriveNow, the Parties stated that [INFORMATION ON BUSINESS PLANS].¹⁷⁰
- (218) According to the information provided by Parties, there will be three more free-floating car sharing providers at the beginning of 2019, namely Renault (operating 120 cars since October 2018¹⁷¹), PSA (500 cars¹⁷²) and Totem mobi ([INFORMATION ON FLEET] cars), and four more station-based car sharing providers, namely Ubeeqo ([INFORMATION ON FLEET] cars), Communauto ([INFORMATION ON FLEET] cars), Zipcar ([INFORMATION ON FLEET] cars) and Zencarx ([INFORMATION ON FLEET] cars).¹⁷³

¹⁶⁷ See Renault's press release of 04/07/2018, published on <https://media.group.renault.com/global/en-gb/groupe-renault/media/pressreleases/21213440/la-ville-de-paris-et-le-groupe-renault-partagent-leur-vision-de-nouveaux-services-urbains-de-mobilit>.

¹⁶⁸ See PSA's press release of 03/07/2018, published on <https://media.groupe-psa.com/en/groupe-psa-finalizes-launch-free2move-paris-sustainable-and-high-quality-carsharing-service>.

¹⁶⁹ Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go. Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018 and Confidential Annex – Car sharing fleets – [INFORMATION ON BUSINESS PLANS].

¹⁷⁰ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018 and Confidential Annex – Car sharing fleets – [INFORMATION ON BUSINESS PLANS].

¹⁷¹ See Renault's press release of 28/09/2018, published on <https://media.group.renault.com/global/en-gb/renault/media/pressreleases/21216518/renault-et-ada-lancement-lapplication-moovinparis-by-renault>.

¹⁷² See PSA's press release of 03/07/2018, published on <https://media.groupe-psa.com/en/groupe-psa-finalizes-launch-free2move-paris-sustainable-and-high-quality-carsharing-service>.

¹⁷³ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018 and Confidential Annex – Car sharing fleets – [INFORMATION ON BUSINESS PLANS].

- (219) Therefore, the total size of Paris's future car sharing market (free-floating and station-based) will be around [INFORMATION ON FLEET] and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction would be [20-30]% for free-floating and station-based car sharing and [30-40]% for (only) free-floating car sharing.
- (220) Focusing at the end of 2019, the total size of Paris's future car sharing market (free-floating and station-based) could be around [INFORMATION ON FLEET] and – focusing on the narrowest possible market for (only) free-floating car sharing – [INFORMATION ON FLEET] cars. In such a scenario, the Parties' market share post-Transaction would fall down to [10-20]% for free-floating and station-based car sharing and [20-30]% for (only) free-floating car sharing.
- (221) Furthermore, the municipality of Paris also stated that the city is open to more carmakers entering the market to help to boost the car sharing service.¹⁷⁴ Renault, BMW, Daimler as well as Volkswagen had expressed their interest, the municipality said.¹⁷⁵
- (222) In the light of the above, the Commission considers that the proposed Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Paris as well as on a market definition comprising free-floating and station-based car sharing.

5.3.5.2. Barcelona

- (223) None of the Parties (but also no third free-floating car sharing provider) are currently present in Barcelona.
- (224) The Parties flagged that they have [INFORMATION ON BUSINESS PLANS].¹⁷⁶ However, these plans could not be considered as timely or likely, as [INFORMATION ON BUSINESS PLANS]. DriveNow currently also considers it [INFORMATION ON BUSINESS PLANS].¹⁷⁷
- (225) In the light of the above, the Commission considers that the proposed Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Barcelona.

¹⁷⁴ See <https://www.bloomberg.com/news/articles/2018-07-04/paris-opens-up-electric-car-sharing-market-after-autolib-failure>.

¹⁷⁵ *Ibidem.*

¹⁷⁶ Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go.

¹⁷⁷ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

5.3.5.3. Madrid

- (226) In Madrid only car2go is currently present with a fleet of [INFORMATION ON FLEET] cars.¹⁷⁸ DriveNow [INFORMATION ON BUSINESS PLANS].¹⁷⁹ However, the Parties stated that it is [INFORMATION ON BUSINESS PLANS].
- (227) According to the information provided by Parties, there exist two more free-floating car sharing providers, namely Emov with a fleet of [INFORMATION ON FLEET] cars and Zity with a fleet of [INFORMATION ON FLEET] cars. Furthermore, three more station-based car sharing providers are present, namely Bluemove ([INFORMATION ON FLEET] cars), Respiro ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars).¹⁸⁰
- (228) Therefore, the total size of Madrid's future car sharing market (free-floating and station-based) will not change and be around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share pre- and post-Transaction will not change ([20-30]% for free-floating and station-based car sharing and [20-30]% for (only) free-floating car sharing).
- (229) Focusing on revenues, the Parties estimate (current) market shares of [20-30]% for free-floating and station-based car sharing and [20-30]% for free-floating car sharing only.
- (230) In light of the above, the Commission considers that the proposed Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Madrid as well as on a market definition comprising free-floating and station-based car sharing.

5.3.5.4. Florence

- (231) In Florence only car2go is currently present with a fleet of [INFORMATION ON FLEET] cars.¹⁸¹ DriveNow [INFORMATION ON BUSINESS PLANS].¹⁸² [INFORMATION ON BUSINESS PLANS].¹⁸³

¹⁷⁸ Form CO, Confidential Annex 7.b.

¹⁷⁹ Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go.

¹⁸⁰ Form CO, Confidential Annex 7.b.

¹⁸¹ Form CO, Confidential Annex 7.b.

¹⁸² Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go. Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

¹⁸³ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

- (232) According to the information provided by Parties, there exist three more free-floating car sharing providers, namely Share'ngo ([INFORMATION ON FLEET] cars), Enjoy ([INFORMATION ON FLEET] cars) and Adduma Car ([INFORMATION ON FLEET] cars). Hertz 24/7 is the only station-based car sharing provider, operating only [INFORMATION ON FLEET] car.¹⁸⁴
- (233) Therefore, the total size of Florence's recent car sharing market (free-floating and station-based) is around [INFORMATION ON FLEET] cars and – focusing on the narrowest possible market for (only) free-floating car sharing – [INFORMATION ON FLEET] cars. The Parties' current market share post-Transaction will not change post-Transaction, being [30-40]% for free-floating and station-based car sharing and [30-40]% for (only) free-floating car sharing, and there exists competitive pressure from three additional free-floating car sharing providers.
- (234) Focusing on revenues, the Parties estimate (current) market shares of [10-20]% for free-floating and station-based car sharing as well as for free-floating car sharing only.
- (235) In the light of the above, the Commission considers that the proposed Transaction does not raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Florence as well as on a market definition comprising free-floating and station-based car sharing.

5.3.5.5. Rome

- (236) In Rome only car2go is currently present with a fleet of [INFORMATION ON FLEET] cars.¹⁸⁵ DriveNow [INFORMATION ON BUSINESS PLANS].¹⁸⁶ [INFORMATION ON BUSINESS PLANS].¹⁸⁷
- (237) According to the information provided by Parties, there exist two more free-floating car sharing providers, namely Share'ngo ([INFORMATION ON FLEET] cars) and Enjoy ([INFORMATION ON FLEET] cars). Furthermore, there exist two more station-based car sharing providers, namely Mobilita Roma Carsharir ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars).¹⁸⁸

¹⁸⁴ Form CO, Confidential Annex 7.b.

¹⁸⁵ Form CO, Confidential Annex 7.b.

¹⁸⁶ Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go. Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

¹⁸⁷ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

¹⁸⁸ Form CO, Confidential Annex 7.b.

- (238) Therefore, the total size of Rome's recent car sharing market (free-floating and station-based) is be around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction will not change immediately post-Transaction, being [20-30]% for free-floating and station-based car sharing and [20-30]% for (only) free-floating car sharing.
- (239) Focusing on revenues, the Parties estimate (current) market shares of [10-20]% for free-floating and station-based car sharing and [20-30]% for free-floating car sharing only.
- (240) In the light of the above, the Commission considers that the proposed Transaction does not raises serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Rome as well as on a market definition comprising free-floating and station-based car sharing.

5.3.5.6. Turin

- (241) In Turin only car2go is currently present with a fleet of [INFORMATION ON FLEET] cars.¹⁸⁹ DriveNow [INFORMATION ON BUSINESS PLANS].¹⁹⁰ [INFORMATION ON BUSINESS PLANS].¹⁹¹ Therefore, DriveNow's entry plan cannot be considered as timely.
- (242) According to the information provided by Parties, there exist another free-floating car sharing provider, namely Enjoy with a fleet of [INFORMATION ON FLEET] cars, and two more station-based car sharing providers, namely BlueTorino ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] cars).¹⁹²
- (243) Therefore, the total size of Turin's recent car sharing market (free-floating and station-based) will be around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share post-Transaction is actually [40-50]% for free-floating and station-based car sharing and [50-60]% for (only) free-floating car sharing.
- (244) Focusing on revenues, the Parties estimate (current) market shares of [30-40]% for free-floating and station-based car sharing and [40-50]% for free-floating car sharing only.

¹⁸⁹ Form CO, Confidential Annex 7.b.

¹⁹⁰ Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go. Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

¹⁹¹ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018.

¹⁹² Form CO, Confidential Annex 7.b.

(245) In the light of the above, the Commission considers that the proposed Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Turin as well as on a market definition comprising free-floating and station-based car sharing.

5.3.5.7. Amsterdam

(246) In Amsterdam only car2go is currently present with a fleet of [INFORMATION ON FLEET] cars.¹⁹³ DriveNow [INFORMATION ON BUSINESS PLANS].¹⁹⁴ However, the Parties stated that it's [INFORMATION ON BUSINESS PLANS].¹⁹⁵

(247) According to the information provided by Parties, there exist another free-floating car sharing provider, namely Ioniq Car Sharing ([INFORMATION ON FLEET] cars), and four more station-based car sharing providers, namely Greenwheels ([INFORMATION ON FLEET] cars), Connect Car ([INFORMATION ON FLEET] cars), mywheels ([INFORMATION ON FLEET] cars) and Hertz 24/7 ([INFORMATION ON FLEET] car).¹⁹⁶

(248) Therefore, the total size of Amsterdam's future car sharing market (free-floating and station-based) will not change and be around [INFORMATION ON FLEET] cars and, focusing on the narrowest possible market for (only) free-floating car sharing, [INFORMATION ON FLEET] cars. The Parties' market share pre- and post-Transaction will be [20-30]% for free-floating and station-based car sharing and [70-80]% for (only) free-floating car sharing.

(249) Focusing on revenues, the Parties estimate (current) market shares of [10-20]% for free-floating and station-based car sharing and [60-70]% for free-floating car sharing only.

(250) In the light of the above, the Commission considers that the proposed Transaction does not raise serious doubts as to its compatibility with the internal market on a narrow market definition comprising only free-floating car sharing in Amsterdam as well as on a market definition comprising free-floating and station-based car sharing.

5.3.6. *Conclusion on horizontal overlap cities*

(251) On the basis of the above, the proposed Transaction would lead to serious doubts on the market for car sharing (and in the market for free-floating car sharing

¹⁹³ Form CO, Confidential Annex 7.b.

¹⁹⁴ Reply of 19/10/2018 to RFIs of 16/10/2018 and 18/10/2018, Confidential Annex 2 – [INFORMATION ON BUSINESS PLANS] – DriveNow and Confidential Annex 3 – [INFORMATION ON BUSINESS PLANS] – car2go.

¹⁹⁵ Reply of 22/10/2018 to RFIs of 16/10/2018 and 18/10/2018 and Confidential Annex – Car sharing fleets – [INFORMATION ON BUSINESS PLANS].

¹⁹⁶ Form CO, Confidential Annex 7.b.

services) in the following five overlap cities: Hamburg, Cologne, Dusseldorf, Munich and Vienna.

- (252) However, as stated above in paragraphs (59) *et seq.* and (150) *et seq.*, the Commission considers that there are also certain out-of-market constraints exerted by, in particular, the public transport services that are not included in the market for car sharing. The Commission will take these into account in its analysis of the (free-floating) car sharing market.
- (253) Moreover, as explained in more detail above, the market investigation confirmed that the car sharing market is in flux with both small (Oply in Hamburg with 100 cars since 10 October 2018) and large [...] entries, and many more planned. However, these entries cannot be considered as likely, timely and sufficient enough to remove serious doubts.
- (254) These two factors (out-of-market constraints and new entries) mitigate the existing serious doubts without eliminating them completely.

5.4. Vertical effects

5.4.1. Manufacture and supply of passenger cars / (free-floating) car sharing

- (255) Both Parties are active in the upstream market for the manufacture and supply of passenger cars in Germany, Austria and Italy and in the downstream market for (free-floating) car sharing in Germany, Austria and Italy.
- (256) The Commission will assess whether the Parties will have the ability or the incentive to foreclose access to passenger cars to their rival (free-floating) car sharing providers or the ability or incentive to foreclose their rival OEMs to a customer base.
- (257) With regard to the upstream market, in line with its previous decisions, the Commission could also consider a market for wholesale/retail distribution of passenger cars. However, the Commission will carry out the assessment of the vertical effects on the market for the manufacture and supply of passenger cars, given that, according to the Parties' best estimates, the Parties' combined market shares in a market for the wholesale/retail distribution of passenger cars will not exceed or at least will not be significantly different from the Parties' market shares in the market for the manufacture or supply of passenger cars.¹⁹⁷ In addition, if a sub-segment for pure electric powered cars were considered, there would be an affected vertical market in Germany and in Italy. However, the same considerations would apply.
- (258) With regard to the downstream market, given that, for the purpose of this decision, the Commission does not consider it appropriate to either consider a market encompassing all passenger transport services or a market for short-term car rental - including (free-floating) car sharing - as the relevant product markets, the assessment of the vertical effects will be carried out on the narrowest-possible relevant market for (free-floating) car sharing.

¹⁹⁷ Annex 2 to the Parties' reply to RFI 6 dated 26 October 2018.

5.4.1.1. Manufacture and supply of passenger cars (*upstream*)

(259) In Germany, the Parties' combined market share post-Transaction is [20-30]% for all cars, [20-30]% for electric cars, [30-40]% for pure electric powered cars, [10-20]% for hybrid cars. In Austria the Parties' combined market shares would be [10-20]% for all cars, [10-20]% for electric cars, [20-30]% for pure electric powered cars, [10-20]% for hybrid cars, and in Italy [5-10]% for all cars, [0-5]% for electric cars, [30-40]% for pure electric powered cars, [0-5]% for hybrid cars.

5.4.1.2. (Free-floating) car sharing (*downstream*)

(260) In Berlin, the Parties' market share post-Transaction will be [80-90]% by number of cars for car sharing as a whole and [90-100]% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [80-90]% for car sharing as a whole and [90-100]% for free-floating car sharing only.

(261) In Cologne, the Parties' market share post-Transaction will be [50-60]% for car sharing as a whole and 100% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [50-60]% for car sharing as a whole and 100% for free-floating car sharing only.

(262) In Dusseldorf, by number of cars the Parties' market share post-Transaction will be [80-90]% for car sharing as a whole and 100% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [70-80]% for car sharing as a whole and 100% for free-floating car sharing only.

(263) In the Cologne/Dusseldorf business area, by number of cars, the Parties' market share post-Transaction would be [60-70]% for car sharing as a whole and 100% for (only) free-floating car sharing. By revenues, the Parties market shares would be [60-70]% for car sharing as a whole and 100% for free-floating car sharing only.

(264) In Hamburg, by number of cars, the Parties' market share post-Transaction will be [70-80]% for car sharing as a whole and 100% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [80-90]% for car sharing as a whole and 100% for free-floating car sharing only.

(265) In Munich, by number of cars, the Parties' market share post-Transaction will be [60-70]% for car sharing as a whole and [90-100]% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [60-70]% for car sharing as a whole and [90-100]% for free-floating car sharing only.

(266) In Milan, by number of cars, the Parties' market share post-Transaction will be [30-40]% for car sharing as a whole and [30-40]% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [30-40]% for car sharing as a whole and [30-40]% for free-floating car sharing only.

(267) In Vienna, by number of cars, the Parties' market share post-Transaction will be [90-100]% for car sharing as a whole and 100% for (only) free-floating car sharing. By revenues, the Parties estimate market shares of [90-100]% for free-floating and station-based car sharing and 100% for free-floating car sharing only.

5.4.1.3. Input foreclosure

- (268) With regard to the ability of the Parties to foreclose access to cars by its rivals, the Parties will have no ability to foreclose rival car sharing providers, as the Parties will not have a degree of upstream market power that would allow them to do so, including in the electric cars segment. Electric cars suited for use in car sharing services are not a scarce resource. Every car manufacturer in Europe has already such cars on offer or is starting to do so as of 2019.
- (269) With regard to their incentive to engage in such foreclosure strategy, the Parties will not have incentive to foreclose rival car sharing providers, as supply to car rental and car sharing companies is a sizeable source of income for the Parties and, moreover, is an important form of non-paid advertisement, causing the respective vehicles and brands to be more visible in the streets. This could even increase sales of electric cars in future. In addition, no competitor in the car sharing segment could be regarded as being dependent on supplies of cars from the Parties.

5.4.1.4. Customer foreclosure

- (270) With regard to ability, the Parties will have no ability to foreclose rival OEMs as each of the Parties is not currently open for the integration of cars by third-party OEMs into their respective fleets. To the contrary, DriveNow's fleet consists exclusively of cars manufactured by BMW and car2go's fleet only of cars manufactured by Daimler. In addition, should the Parties be open, in the future, to integrate cars of third-party OEMs in their own fleet, the number of cars sourced by the Parties would still be too low to have any appreciable effect on the upstream market for the manufacture and supply of passenger cars.

5.4.2. *Manufacture and supply of (pure electric powered cars) passenger cars / Parking (including hardware payment services)*

- (271) Both Parties are active in the upstream market for the manufacture and supply of passenger cars in Germany, Austria and Italy. Only BMW is active in the downstream market for parking in Austria and Germany.
- (272) The Commission will assess whether the Parties will have the ability to foreclose access to passenger cars to their rival parking services providers or the ability to foreclose their rival OEMs to a customer base.

5.4.2.1. *Manufacture and supply of passenger cars (upstream)*

- (273) The market for the manufacture and supply of passenger cars is discussed in section 5.4.1.1. In this case, it would be affected only if the segment of pure electric powered cars in Germany and in Italy is considered.

5.4.2.2. *Parking (downstream)*

- (274) There is no overlap between the Parties in the EEA, as Daimler is not active in the EEA. The Parties were not able to provide reliable market share at city level. However, on a country basis, the Parties' best estimates are the following: less than 5% for Austria and Germany. In a possible sub-segment limited to

software/mobile technology, market share would be between 5 and 10% for Austria and Germany.

5.4.2.3. Input foreclosure

(275) With regard to ability, the Parties will have no ability to foreclose rival parking services providers in Germany and Italy as there are various OEMs in the market and it is not necessary to have access to newly produced passenger cars to offer such services.

5.4.2.4. Customer foreclosure

(276) With regard to ability, the Parties will have no ability to foreclose rival OEMs, as the Parties are not important customers in the market for parking services for any of its OEMs rivals.

5.4.3. *Manufacture and supply of (pure electric powered cars) passenger cars / charging*

(277) Both Parties are active in the upstream market for the manufacture and supply of passenger cars in Germany, Austria and Italy. Only BMW is active in the downstream market for charging in Germany, Austria, Belgium, France and the Netherlands.

(278) The Commission will assess whether the Parties will have the ability to foreclose access to passenger cars to their rival charging services providers or the ability to foreclose their rival OEMs to a customer base.

5.4.3.1. *Manufacture and supply of passenger cars (upstream)*

(279) The market for the manufacture and supply of passenger cars is discussed in section 5.4.1.1. In this case, it would be affected only if the segment of pure electric powered cars in Germany and in Italy is considered.

5.4.3.2. *Charging (downstream)*

(280) BMW offers the ChargeNow services, [INFORMATION ON BUSINESS PLANS]. However, ChargeNow's turnover is marginal (EUR [INFORMATION ON TURNOVER] in the EEA, less than EUR [INFORMATION ON TURNOVER] in Munich, less than EUR [INFORMATION ON TURNOVER] in Berlin, less than [INFORMATION ON TURNOVER] in Hamburg, less than EUR [INFORMATION ON TURNOVER] in Düsseldorf and Cologne in 2017).

5.4.3.3. *Input foreclosure*

(281) With regard to ability, the Parties will have no ability to foreclose rival charging providers in Germany and Italy as there are various OEMs in the market and it is not necessary to have access to newly produced passenger cars to offer such services.

5.4.3.4. Customer foreclosure

(282) With regard to ability, the Parties will have no ability to foreclose rival OEMs as the Parties are not important customers in the market for charging services for any of its OEMs rivals.

5.4.4. *Financial and operational leasing / (free-floating) car sharing*

(283) Both Parties are active in the upstream market for financial and operational leasing in Germany, Austria and Italy and in the downstream market for (free-floating) car sharing.

(284) The Commission will assess whether the Parties will have the ability and incentive to foreclose access to financial and operational leasing to their rival (free-floating) car sharing providers or the ability to foreclose their rival financial and operational leasing providers to a customer base.

5.4.4.1. Financial and operational leasing (*upstream*)

(285) The Parties' combined market share in Germany is [20-30]%¹⁹⁸, in Austria [10-20]%¹⁹⁹ and in Italy [5-10]%²⁰⁰.

5.4.4.2. (Free-floating) car sharing (*downstream*)

(286) The market for (free-floating) car sharing is discussed in section 5.4.1.2. The Parties' combined market share will be high in Berlin, Cologne, Dusseldorf, Munich, Vienna and Milan.

5.4.4.3. Input foreclosure

(287) With regard to ability, the Parties will have no ability to foreclose rival car sharing providers for the following reasons: (i) access to financial and operational leasing is not a pre-condition for offering car sharing services. The Parties estimate that in Germany [INFORMATION ON MARKET ESTIMATES]% of the car sales account for leasing, whilst for Austria the Parties estimate that [INFORMATION ON MARKET ESTIMATES]% account for leasing, (ii) there are other strong providers of financial and operational leasing services in addition to other OEMs, such as banks and car rental companies.

(288) With regard to incentive, the Parties will have no incentive to foreclose rival car sharing providers as financial and operational leasing provided to third parties is a valuable source of income and, for OEMs, there are marketing and advertisement advantages if they supply their cars to car sharing providers.

¹⁹⁸ The Parties submit that there would be no significant difference if (i) financial leasing and (ii) operational leasing were to be distinguished. As explained in Section 4.1.7, for the purpose of this decision, the Commission will therefore assess the impact of the transaction on a market for financial and operational leasing.

¹⁹⁹ See footnote above.

²⁰⁰ See footnote above.

5.4.4.4. Customer foreclosure

(289) With regard to ability, the Parties will have no ability to foreclose rival suppliers of financial and operational leasing services, given that neither of the Parties is a sufficient important customer for third parties. Each of the Parties has only used services from their parent companies in the past.

5.4.5. Full fleet leasing and management services / (free-floating) car sharing

(290) Both Parties are active in the upstream market for full fleet leasing and management services in Germany, Austria and Italy and in the downstream market for (free-floating) car sharing.

(291) The Commission will assess whether the Parties will have the ability and incentive to foreclose access to full fleet leasing and management services to their rival (free-floating) car sharing providers or the ability to foreclose their rival full fleet leasing and management service providers to a customer base.

5.4.5.1. Full fleet leasing and management services (*upstream*)

(292) In Germany, the Parties' combined market share will be [10-20]%²⁰¹, in Austria [0-5]%²⁰² and in Italy [0-5]%²⁰³.

5.4.5.2. (Free-floating) car sharing (*downstream*)

(293) The market for (free-floating) car sharing is discussed in section 5.4.1.2. The Parties' combined market share will be high in Berlin, Cologne, Dusseldorf, Munich, Vienna and Milan.

5.4.5.3. Input foreclosure

(294) With regard to ability, the Parties will have no ability to foreclose rival car sharing providers as (i) full fleet leasing and management services is not a pre-condition for offering car sharing services and (ii) this type of services are widely available in the market.

(295) With regard to incentive, the Parties will have no incentive to foreclose rival car sharing providers given that full fleet leasing and management services provided for third parties is a valuable source of income.

5.4.5.4. Customer foreclosure

(296) With regard to ability, the Parties will have no ability to foreclose rival full fleet leasing and management service providers given that neither of the Parties is a

²⁰¹ The Parties submit that there is no data available for any further segmentation but that, in any event, [INFORMATION ON TURNOVER] (Tables 27-29 Form CO).

²⁰² See footnote above.

²⁰³ See footnote above.

sufficient important customer for third parties. Indeed, neither of the Parties has sourced such type of services from third parties in the past.

5.4.6. *Development and sale of smartphone apps / (Free-floating) car sharing*

- (297) The Parties do not offer and do not intend to offer on their apps online advertising services.
- (298) The Parties do not offer paid smartphone apps at the moment. All smartphone apps relevant for the transaction can be downloaded for free. Only becoming a member of car2go or DriveNow would require the payment of a membership fee. There are also currently no plans to change this business model. The Parties are also no smartphone app developers. They do not offer to programme software for third parties that do not belong to the group of Daimler and BMW respectively.
- (299) In the EEA, the Parties offer the following smartphone apps that will also be transferred to the joint ventures: DriveNow app, car2go app, ChargeNow app, Parkmobile app, moovel and mytaxi apps. All aforementioned smartphone apps aim at mediating contracts, e.g. the car2go smartphone app aims at allowing the user to book rides with car2go vehicles. Turnover is thus not generated directly by selling the smartphone app to potential customers but (leaving the registration fee for car2go or DriveNow aside) by the realisation of contracts for the services offered in the respective smartphone app. Along the same line, “moovel transit” works on a commission basis for each transaction booked on the smartphone app. Both Parties are active in the downstream market for (free-floating) car sharing.
- (300) The Commission will assess whether the Parties will have the ability to foreclose access to smartphone apps to their rival (free-floating) car sharing providers or the ability to foreclose other companies offering smartphone apps to a customer base.

5.4.6.1. *Development / sale of smartphone apps (upstream)*

- (301) At EEA level, according to the Parties' best estimates, the Parties' combined market share would be lower than 30%, whilst in Germany, Italy, Austria the Parties' combined market shares would be below 30% in each territory.

5.4.6.2. *(Free-floating) car sharing (downstream)*

- (302) The market for (free-floating) car sharing is discussed in section 5.4.1.2. The Parties' combined market share will be high in Berlin, Cologne, Dusseldorf, Munich, Vienna and Milan.

5.4.6.3. *Input foreclosure*

- (303) With regard to ability, the Parties will have no ability to foreclose rival car sharing providers as there are several companies that can develop/sell smartphone apps.

5.4.6.4. *Customer foreclosure*

- (304) [...]The Parties will have no ability to foreclose rival developers/suppliers of smartphone apps given that there are several companies that can be considered customers of services involving the development and sale of smartphone apps.

5.4.7. *Development and sale of multimodal apps/ (free-floating) car sharing*

(305) The Parties do not offer paid smartphone apps at the moment. As explained above, turnover is thus not generated directly by selling the smartphone app to potential customers but (leaving the registration fee for car2go or DriveNow aside) by the realisation of contracts for the services offered in the respective smartphone app. That being said, Daimler only offers a multimodal app. Both Parties are active in the downstream market for (free-floating) car sharing.

(306) The Commission will assess whether the Parties will have the ability to foreclose rival (free-floating) car sharing providers or the ability to foreclose companies active in the development/sale of multimodal smartphone apps to a customer base.

5.4.7.1. *Development /sale of multimodal apps (upstream)*

(307) BMW does not offer multimodal apps. As a consequence, at EEA level as well as in Germany, according to the Parties' best estimates, the Parties' combined market share would be lower than 30%.

5.4.7.2. *(Free-floating) car sharing (downstream)*

(308) The market for (free-floating) car sharing is discussed in section 5.4.1.2. The Parties' combined market share will be high in Berlin, Cologne, Dusseldorf, Munich, Vienna and Milan.

5.4.7.3. *Input foreclosure*

(309) With regard to ability, the Parties will have no ability to foreclose rival (free-floating) car sharing providers as there are several companies that can develop and sell multimodal smartphone apps.

5.4.7.4. *Customer foreclosure*

(310) With regard to ability, the Parties will have no ability to foreclose rival companies active in the development/sale of multimodal smartphone apps as software developers are not dependant on the Parties' car sharing services.

5.4.8. *Access to multimodal apps / (free-floating) car sharing*

(311) Daimler operates upstream a multimodal app ("moovel") in some of the overlap cities. Both Parties are active in the downstream market for (free-floating) car sharing. The Commission will assess whether the Parties will have i) the ability and the incentive to foreclose access to multimodal apps to their rival (free-floating) car sharing providers as well as ii) the ability or incentive to foreclose other multimodal apps from access to their API. In addition, the Commission will assess the likely impact on effective competition.

5.4.8.1. *Access to multimodal apps*

(312) Daimler operates the moovel platform which is available in some of the overlap cities. BMW does not offer any multimodal apps in the EEA. As a consequence, at EEA level, as well as in Germany and Austria, according to the Parties' best estimates, the Parties' combined market share would be lower than 30%.

5.4.8.2. (Free-floating) car sharing

(313) The market for (free-floating) car sharing is discussed in section 5.4.1.2. The Parties' combined market share will be high in Berlin, Cologne, Dusseldorf, Munich, Vienna and Milan.

5.4.8.3. Customer foreclosure

(314) With regard to ability, the Parties claim that they will have no ability to foreclose rival car sharing providers given that access to multimodal apps would not be necessary for offering car sharing services as this could be done with individual (provider-owned) apps. However, the Commission considers that, in the light of the fact that multimodal apps are likely to become the gateway to car sharing services, the Parties will have the ability to foreclose rival car sharing providers.

(315) The majority of OEMs and of mobility service providers who responded to the market investigation stated that they are concerned about obtaining access, post-Transaction, to the merged entity's platform for mobility services, i.e. moovel.²⁰⁴ In addition, the majority of mobility service providers who responded to the market investigation stated that their services are included in apps of third party providers, such as independent integrators or apps of competing mobility providers.²⁰⁵

(316) One mobility service provider stated that *"the platform is getting more power against smaller companies to negotiate"*.²⁰⁶ Another mobility service provider stated that *"[w]hen moovel becomes the platform of choice they will be able to allocate bookings to own partners and / or dictate the prices which are charged [...] as well as the commission which moovel might get [...]"*.²⁰⁷ Another mobility service provider stated that *"moovel will push their own providers"*.²⁰⁸

(317) Due to the reasons outlined above, the Commission considers that access to integrators and multimodal apps is important to reach customers. This is likely to increase in the future. As a consequence, the Parties would have the ability to foreclose rival car sharing providers.

(318) With regard to incentive, one mobility service provider that responded to the market investigation stated that *"[...] moovel [...] will become big - therefore it will be difficult for smaller platforms [...]"*.²⁰⁹ In the light of the above, the Commission considers that, due to the fact that access to the most important

²⁰⁴ Replies to question 19 of questionnaire to OEMs and replies to question 24 of the questionnaire to mobility service providers.

²⁰⁵ Replies to question 23 of questionnaire to mobility service providers.

²⁰⁶ Replies to question 24.1 of questionnaire to mobility service providers.

²⁰⁷ Replies to question 24.1 of questionnaire to mobility service providers.

²⁰⁸ Replies to question 24.1 of questionnaire to mobility service providers.

²⁰⁹ Replies to question 24.1 of questionnaire to mobility service providers.

integrator platforms is critical for reaching customers and that the Parties, due to their strong position in free floating car sharing services, could turn moovel into the integrator app of choice, the Parties would have the incentive to foreclose rival car sharing providers from reaching customers by denying them access to their moovel platform.

5.4.8.4. Input foreclosure

- (319) With regard to ability, the Parties claim that the Parties have no ability to foreclose rival multimodal apps, as BMW and Daimler are only present on very few multimodal apps and at least all other transport providers are conceivable as potential customers of any multimodal app. However, the Commission considers that in the light of the fact that, as confirmed by the market test, the Parties' fleet is a must-have for integrator apps, the Commission considers that the Parties will have ability to foreclose rival multimodal apps.
- (320) First, the Parties' combined market share in the downstream market for (free-floating) car sharing is very high in the six overlap cities. Second, the majority of respondents to the market test stated that the Parties' presence on an aggregator app is a must-have.²¹⁰ As one respondent to the market test put it: *"an aggregator app only adds value to the consumer [...] if meaningful mobility providers are being listed and sufficient availability of vehicles is being provided [...]"*²¹¹ Another respondent to the market test stated that *"[...] an aggregator app without [the Parties'] service is not a good selling point for the users and I would not run a shared mobility aggregator without [the Parties] at least in the overlap cities"*.²¹²
- (321) In order to list the Parties' car sharing offering it is necessary for rival integrator apps to have access to Parties' API. Consequently, the Commission considers that the Parties would have the ability to foreclose rival multimodal apps.
- (322) With regard to incentive, the merged entity would benefit from such an input foreclosure strategy in two ways. First, it would fortify its downstream position in car sharing at the expense of rival car sharing providers. Second, it could obtain higher fees from other mobility providers which want to be listed on moovel. Consequently, the Commission considers that the Parties will have incentive to foreclose rival multimodal apps.
- (323) With regard to the likely impact on effective competition, the ability and the incentive of the Parties to foreclose rival multimodal apps is likely to increase barriers to entry in multimodal apps. This is due to the fact that for an integrator app adds value to the consumer if meaningful mobility providers are listed and sufficient availability of vehicles is being provided.

²¹⁰ Replies to question 9 of the Market Test.

²¹¹ Replies to question 9.1 of the Market Test.

²¹² Replies to question 9.1 of the Market Test.

5.4.9. Charging / (free-floating) car sharing

- (324) Only BMW is active in the upstream market for charging in Germany, Austria, Belgium, France and the Netherlands. Both Parties are active in the downstream market for (free-floating) car sharing.
- (325) The Commission will assess whether the Parties will have ability to foreclose access to charging services to rival (free-floating) car sharing providers or ability to foreclose rival charging service providers to a customer base.

5.4.9.1. Charging (*upstream*)

- (326) As stated above, BMW offers the ChargeNow services, [INFORMATION ON BUSINESS PLANS]. However, ChargeNow's turnover is marginal (EUR [INFORMATION ON TURNOVER] in the EEA, less than EUR [INFORMATION ON TURNOVER] in Munich, less than EUR [INFORMATION ON TURNOVER] in Berlin, less than EUR [INFORMATION ON TURNOVER] in Hamburg and less than EUR [INFORMATION ON TURNOVER] in Dusseldorf and Cologne).

5.4.9.2. (Free-floating) car sharing (*downstream*)

- (327) The market for (free-floating) car sharing is discussed in section 5.4.1.2. The Parties' combined market share will be high in Berlin, Cologne, Dusseldorf, Munich, Vienna and Milan.

5.4.9.3. Input foreclosure

- (328) With regard to ability, the Parties will have no ability to foreclose rival car sharing providers as the Parties' presence in the market is limited and, in addition, there are several competitors offering charging services [...], such as emobil, Innogy, Vattenfall, New Motion and plugsurfing.

5.4.9.4. Customer foreclosure

- (329) With regard to ability, the Parties will have no ability to foreclose rival charging providers, given that the Parties' are not important customers for them.

5.5. Conclusion

- (330) For the reasons outlined above, the proposed Transaction would lead to serious doubts as to its compatibility with the internal market on the market for car sharing in the following five overlap cities: Hamburg, Cologne, Dusseldorf, Munich and Vienna. Public transport exerts a certain out-of-market constraint and the market for car sharing is in flux with small and large entries and many more planned which, however, cannot be considered as likely, timely and sufficient enough. Therefore, the Commission considers that these two factors may partially mitigate concerns, but do not remove the existing serious doubts.
- (331) The proposed Transaction would also raise serious doubts in the vertically affected market for access to multimodal apps / (free-floating) car sharing due to the fact that the Parties will have the ability and incentive to foreclose rival providers of multimodal apps and rival car sharing providers. Given that multimodal apps are becoming the gateway to car sharing services and that the

Parties' car sharing fleet is a must-have for competing multimodal apps in the overlap cities, the proposed Transaction would likely raise barriers to entry in the market for car sharing services and for multimodal apps.

6. PROPOSED REMEDIES

6.1. Analytical framework

- (332) Where the Commission considers that a concentration will raise competition concerns, the parties may seek to modify the concentration in order to resolve such competition concerns and thereby gain clearance of their merger.
- (333) In Phase I, commitments offered by the parties can only be accepted where the competition problem is readily identifiable and can easily be remedied. The competition problem therefore needs to be so straightforward and the remedies so clear-cut that it is not necessary to enter into an in-depth investigation and that the commitments are sufficient to clearly rule out serious doubts within the meaning of Article 6(1)(c) of the Merger Regulation. Where the assessment confirms that the proposed commitments remove the grounds for serious doubts on this basis, the Commission clears the merger in Phase I.
- (334) In assessing whether the proposed commitments will likely eliminate the competition concerns identified, the Commission considers all relevant factors including inter alia the type, scale and scope of the proposed commitments, judged by reference to the structure and particular characteristics of the market in which the competition concerns arise, including the position of the parties and other participants on the market.

6.2. Procedure

- (335) In order to render the concentration compatible with the internal market, the Parties have modified the proposed Transaction by entering into the following commitments, submitted on 15 October 2018 and revised on 5 November 2018, which are annexed to this decision and form an integral part thereof.
- (336) After an examination and a market test these commitments are considered suitable to entirely remove the serious doubts identified.
- (337) The commitments notably aim to lower the barriers of entry for third mobility providers in the overlap cities of Berlin, Cologne, Dusseldorf, Hamburg, Munich and Vienna. Furthermore, the commitments secure that the Parties do not terminate or deny contracts with third aggregator apps in order to launch and expand their own app exclusively so that third party aggregator apps would be cut off immediately.
- (338) The Parties commit (i) to remain, under certain conditions, visible on third parties' aggregator platforms and (ii) to allow, under certain conditions, competing mobility service providers to be visible on the Parties' combined Multimodal App ('moovel'). In this spirit, the Parties will (i) grant application programming interface (API) access to third aggregator platforms and (ii) grant access for all interested car sharing providers to their Multimodal App.

- (339) In both cases users will be re-directed to the selected mobility service provider's app; booking a third party mobility service providers' car directly on the Parties' aggregator's platform will not be possible. Both commitments apply for three years after their implementation with a possible extension of two more years if there is no meaningful entry²¹³. They are provided free of charge and on a non-discriminatory basis, but subject to certain conditions. The commitments also include provisions for the appointment of a monitoring trustee and provide for the insertion of an arbitration clause in both the (i) Material Terms Partner-Contract and (ii) Material Terms API Agreement (as Annexes to the commitments).
- (340) On 16 October 2018 the commitments were subjected to a market test, which was launched on that day.
- (341) Overall, the market test provided a positive feedback on the proposed commitments.²¹⁴ Any listing, not only on third party aggregator apps, but also on the Parties' multimodal app, would raise the visibility of car sharing service providers, especially for smaller ones, which could be vital for (smaller) car sharing service providers' chance to enter the market with a smaller fleet, to stay on the market or to expand their business. Furthermore, an aggregator app should cover the most attractive mobility services on their platform to attract as many customers as possible, which would be for the purpose of that case the car sharing services of car2go and DriveNow.
- (342) However, the (old) threshold for meaningful entry (30%) was criticised as being too low, the contract length for anyone entering into an agreement with the Parties later than one year after the implementation of the commitments in the duration period of the Commitments was deemed too short, and a fast track arbitration was also stated as necessary to avoid lengthy procedures.
- (343) After reviewing the market test results, it appeared that the threshold of 30% of the Parties' combined fleet in the previous year in the definition of meaningful entry is not high enough and should be doubled if it is to dispel the serious doubts. Furthermore, a minimum contract term of two years should be granted within the initial duration period of three years, if the individual contracts are signed later than one year after the implementation of the commitments, and the arbitration clause should be fast track.
- (344) On 5 November 2018, the Parties submitted a revised version of the given set of commitments addressing these shortcomings of the first set of the Commitments.

²¹³ Meaningful market entry means that one car sharing provider enters or more car sharing providers enter an overlapping city and reaches/reach more than 60% of the average fleet size of the KITT CS fleet of the preceding calendar year in the respective overlapping city.

²¹⁴ See replies of Market test of Commitments, esp. questions 1 and 2.

7. ASSESSMENT OF THE PROPOSED REMEDIES

- (345) As set out in the Commission Notice on remedies,²¹⁵ the Commission assesses the compatibility of a notified concentration with the internal market on the basis of its effect on the structure of competition in the EU. Where a concentration raises serious doubts which could lead to a significant impediment to effective competition, the parties may seek to modify the concentration so as to resolve the serious doubts identified by the Commission with a view to having the merger cleared²¹⁶.
- (346) The Commission enjoys a broad discretion in assessing whether these remedies constitute a direct and sufficient response capable of dispelling any such doubts.²¹⁷
- (347) In assessing whether or not the remedies will restore effective competition, the Commission considers *inter alia* the type, scale and scope of the remedies by reference to the structure and the particular characteristics of the market in which these serious doubts arise.
- (348) In the present case, the Commission considers that proposed commitments as submitted by the Parties on 15 October 2018 and revised on 5 November 2018 addresses all serious doubts identified in the course of the procedure. As such, the Commission comes to the conclusion that the commitments entered into by the Parties are sufficient to eliminate the serious doubts as to the compatibility of the transaction with the internal market.
- (349) Car sharing, as a relatively new mobility solution in cities, is an evolving market as the proposed Transaction and several entry plans/intentions identified by the market investigation proves. However, not all of them do fully meet the criteria of timely, sufficient and likely, with the exception of Berlin. The Commission acknowledges and takes into account that, as confirmed by the market investigation and the July 2018 customer survey (paragraph (59)), regardless of whether the product market is car sharing (including station-based and free-floating car sharing) or only free-floating car sharing, mostly public transport exerts a certain out-of-market constraint. This out-of-market constraint softens, but does not fully alleviate the competition concerns identified. Consequently, the proposed Transaction would raise, on the narrowest possible market of free-floating car sharing, serious doubts, as there would be only one player in the cities of, at least for a certain period of time. In an overall market for car sharing (i.e. including also station-based), the Transaction would also lead to very high market shares in the same cities, and also for a certain period of time.

²¹⁵ OJ C 267, 22.10.2008, p. 1.

²¹⁶ Article 6.2 of the Merger Regulation.

²¹⁷ Case T-177/04 *easyJet v Commission* [2006] ECR II-1931, paragraph 128 *et seq.*

- (350) The Commission considers that given that the Parties would control a large combined fleet in each of the overlap cities, a new entrant would need to start with a relatively large fleet²¹⁸ itself to become attractive to users. In order to make entry more likely, the proposed remedy would address the likely effects of the merger by lowering the entry barriers for third mobility service providers, especially smaller ones. This would allow them to start (more) easily competing with the Parties (even with a smaller fleet of cars) in all of the five overlap cities of Cologne, Dusseldorf, Hamburg, Munich and Vienna, where the proposed Transaction would lead to serious doubts on the market for (free-floating) car sharing, but also Berlin, where Volkswagen has not entered the market for (free-floating) car sharing yet.

Being visible face-to-face with the Parties on leading third party aggregator apps

- (351) Being visible is one of the keys, not only physically on the streets with a certain number of cars, but also on app(s) as the vehicle can only be searched or identified and reserved through a dedicated smartphone app. This app could either be the (own) app of the car sharing service provider itself, but also – especially for identifying any kind of mobility solutions – a third party (aggregator) app, which combines all kinds of transports.
- (352) The more different kinds of transports (like e.g. public transport, car rental and car sharing), but also the more comparable offers within the same market/segment (like e.g. several fleets of different car sharing service providers being visible online face-to-face on a map) are offered with a certain app, the more attractive the app will be. The more attractive the app is, the more people will download and use it logically.
- (353) Therefore, third party aggregators do have a keen interest in hosting at least the leading car sharing provider on their apps in order to attract their customers. But nevertheless, it could also be helpful for smaller or new car sharing competitors to be hosted face-to-face to the biggest player in town, especially on the currently leading third party aggregator app. Therefore, the remedies are crucial to ensure that the Parties do not (only) built up their own exclusive aggregator app and terminate any existing third parties' contracts.

Being visible face-to-face with the Parties on their combined Multimodal App

- (354) Secondly, due to the fact that the Parties [INFORMATION ON BUSINESS PLANS] and existing contracts with third party aggregators could be terminated, it could be helpful for competing (smaller or new) car sharing providers to be hosted face-to-face on the Parties' app at least for a certain period of time. As the hosting is free of charge and on a non-discriminatory basis, it could be an add on option for smaller (potential) competitors to become more visible online to a major community and to start (more) easily competing with the Parties in all of the five overlap cities of Cologne, Dusseldorf, Hamburg, Munich and Vienna, where the proposed Transaction would lead to serious doubts on the market for (free-floating) car sharing, even with a smaller fleet of cars, but also Berlin, where Volkswagen has not entered the market for (free-floating) car sharing yet.

²¹⁸ Investments would not, however, be insurmountable, for a medium or a large company.

- (355) Furthermore, the commitments secure that the Parties do not terminate or deny contracts with third aggregator apps in order to launch and expand their own app exclusively so that third party aggregator apps would be cut off immediately in order to create the must have app which would become the gatekeeper.
- (356) The Commission's assessment is also reflected in the market test results. As mentioned above in paragraph (341), the market test provided a positive feedback on the proposed commitments. The Commission considers that the proposed commitments would reduce entry barriers especially for smaller players as the enhanced visibility on aggregator apps would allow them to start (more) easily in the overlap cities with a smaller fleet of cars, as in the new mobility world it is essential to be visible not only on the streets with a certain number of cars, but also online via attractive (aggregator) app(s), which is offered by the remedies.

Conclusion

- (357) For the reasons outlined above, the commitments entered into by the undertakings concerned are sufficient to eliminate the serious doubts as to the compatibility of the transaction with the internal market.

8. CONDITIONS AND OBLIGATIONS

- (358) Under the first sentence of the second subparagraph of Article 6(2) of the Merger Regulation, the Commission may attach to its Decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering a notified concentration compatible with the internal market.
- (359) Where a condition is not fulfilled, the Commission's decision declaring the concentration compatible with the internal market no longer stands. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 6(3) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2) and 15(1) of the Merger Regulation.
- (360) In accordance with the distinction described above, the commitments in Section B of the Annex to this Decision constitute conditions attached to this Decision, as only through full compliance therewith can the proposed changes in the relevant markets be achieved. The other commitments set out in the Annex constitute obligations, as they concern the implementing steps which are necessary to achieve the modifications sought in a manner compatible with the internal market.
- (361) The full text of the revised Commitments is attached as Annex to this Decision and forms an integral part of it.

9. CONCLUSION

- (362) For the above reasons, the Commission has decided not to oppose the notified operation as modified by the commitments annexed to the decision and to declare it compatible with the internal market and with the functioning of the EEA Agreement, subject to full compliance with the conditions in section B of the commitments annexed to the present Decision and with the obligations contained in the other sections of the said commitments. This Decision is adopted in application of Article 6(1)(b) in conjunction with Article 6(2) of the Merger Regulation and Article 57 of the EEA Agreement.

For the Commission

(Signed)

Margrethe VESTAGER

Member of the Commission

COMMITMENTS TO THE EUROPEAN COMMISSION

Pursuant to Article 6(2) of Council Regulation (EC) No. 139/2004 (the “**Merger Regulation**”), Bayerische Motoren Werke Aktiengesellschaft (including its subsidiaries “**BMW**”) and Daimler AG (including its subsidiaries “**Daimler**”, and together with BMW the “**Notifying Parties**”) hereby provide the following Commitments (the “**Commitments**”) in order to enable the European Commission (the “**Commission**”) to declare the proposed acquisition of joint control by the Notifying Parties in six joint ventures (all six together the “**JV**”), bringing together the Notifying Parties’ mobility services in five business fields, i.e. car sharing services, ride hailing services, parking services, charging services as well as other (on-demand) mobility services (the “**Proposed Transaction**”), compatible with the internal market and the functioning of the EEA Agreement.

This text shall be interpreted in the light of the Commission’s decision pursuant to Article 6(1)(b) of the Merger Regulation to declare the Proposed Transaction compatible with the internal market and the functioning of the EEA Agreement (the “**Decision**”), in the general framework of European Union law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (the “**Remedies Notice**”).

Section A. Definitions

- (1) For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled by the Notifying Parties, including the six joint venture companies and their subsidiaries, whereby the notion of control shall be interpreted pursuant to Article 3 of the Merger Regulation and in light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (the "**Consolidated Jurisdictional Notice**").

Aggregator Platform(s): any technology platform(s) available on smartphones that establishes a contact between consumers and mobility services like car sharing, ride hailing, public transit ticketing, parking and charging and incorporates at least two different means of transport (e.g. public transport and car sharing).

Car Sharing Vertical or KITT CS: The future car sharing joint venture of the Notifying Parties offering car sharing in the Territory.

Car Sharing Provider(s): any provider(s) of free-floating car sharing services.

Confidential Information: any business secrets, know-how, commercial information, or any other information of a proprietary nature, including but not limited to reports, analyses, compilations, memoranda, summaries, notes, excerpts, intentions, experiences, plans, drawings, designs, findings that is not in the public domain.

Conflict of Interest: any conflict of interest that impairs the Monitoring Trustee's objectivity and independence in discharging its duties under the Commitments.

Control: direct or indirect, sole or joint control pursuant to the Consolidated Jurisdictional Notice and the Merger Regulation.

KITT Multimodal App: the KITT Multimodal App is a technology platform consisting of iOS/Android apps and server components that *inter alia* establishes a contact between consumers and at least two different means of transport (e.g. public transport and car sharing).

Effective Date: the date of adoption of the Decision.

Meaningful Market Entry: one Car Sharing Provider enters or more Car Sharing Providers enter an overlapping city and reaches/reach more than 60% of the average fleet size of the KITT CS fleet of the preceding calendar year in the respective overlapping city.

Monitoring Trustee: one or more natural or legal person(s) who is/are approved by the Commission and appointed by the Notifying Parties, and who has/have the duty to monitor the Notifying Parties' compliance with the conditions and obligations attached to the Decision.

OEM: any original equipment manufacturer that also manufactures passenger cars, regardless of legal form and domicile (e.g. Volkswagen).

Separate Businesses: a Car Sharing Provider or any competing business pursuant to para. (6) in which an OEM directly or indirectly holds a stake that is legally and organizationally separate from the Aggregator Platform in which the same OEM directly or indirectly holds a stake; this is the case if the businesses are located in separate legal entities, have no overlapping directors and senior managers and the sharing of information and business coordination is restricted to the level of businesses without joint ownership (arm's length principle); restricted is therefore, *inter alia*, the sharing of API Access and data related to API Access (including the access credentials), analysis of fleet movements of the Notifying Parties or the provision of tools and information that would allow such analysis either by the Car Sharing Provider and/or the competing business and/or any third party for the Car Sharing Provider and/or the competing business as well as the creation of joint business plans or the conduction of joint strategy meetings.

Territory: the six overlapping cities of Berlin, Cologne, Düsseldorf, Hamburg and Munich (all Germany) and Vienna (Austria).

Section B. Commitments

- (2) In the Notifying Parties' view, the Proposed Transaction does not significantly impede effective competition and is compatible with the Common Market. This is in particular the case because the relevant market should not be limited to free-floating car sharing but also includes further means of transport. Even if such narrow market definition would be applied, due to the market dynamics, the Proposed Transaction does not raise any competitive concerns. However, in order to address the concerns raised by the Commission and to secure a fast clearance in Phase I, the Notifying Parties are willing to offer the following (“**Commitments**”):

1. Grant application programming interface access to Aggregator Platforms

- (3) The Car Sharing Vertical will allow Aggregator Platforms to display certain information by granting access (“**API Access**”) to an application programming interface (“**API**”) for iOS/Android apps under certain premises.
- (4) API Access will be granted in the Territory for a period of three years after closing of the Proposed Transaction.
- (5) The Notifying Parties will establish a closed API approach which will work as follows:
- The Aggregator Platforms must explicitly request API Access, i.e. the API is not open to everyone without request;

- API Access will be granted based on specific access criteria (see below);
- API Access can be rejected and/or revoked if the criteria are not met or violated.

(6) The access criteria are as follows:

- The Aggregator Platform has to sign a standard contract (containing at least the provisions set out in **Annex I**) in order to allow the Notifying Parties to know which Aggregator Platforms are using the API and define the rules for such use;
- For the avoidance of doubt: The Aggregator Platform may not be a scientific institute, as data may only be used for the purpose of car sharing activities and the mediation of transport services (and not for other purposes, e.g. data analytics);
- The API does not need to be made available to large technology companies using data in the area of mobility services (like car sharing and ride hailing) or in the areas of data analytics and/or autonomous driving (this also applies to affiliates and companies in which the large technology company (directly or indirectly) owns a stake).

Aggregator Platforms, directly or indirectly, majority owned by OEM are not excluded from API Access as long as no large technology company has a stake in the Aggregator Platform. Aggregator Platforms are, however, excluded from API Access if the Aggregator Platform and/or an OEM directly or indirectly holding a share in the Aggregator Platform, directly or indirectly, offers car sharing or any service competing with the KITT CS service in the respective overlapping city, irrespective of the brand used. This does not apply in case of Separate Businesses as long as the OEM allows the Notifying Parties to display its car sharing service and/or competing business in the KITT Multimodal App (or any successor thereof) under conditions materially equal to the conditions under the API Access Commitments (“non- discriminatory treatment”).

(7) The Notifying Parties will provide the API Access to the Aggregator Platforms for free. As the remedy should not be used by third parties to develop their business models based on investments by the Notifying Parties, but in order to ensure market entry, the Notifying Parties will not be obliged to make any payments to the Aggregator Platforms (e.g. set-up costs, fees or other kind of remunerations).

(8) An Aggregator Platform which fulfills the criteria described above, will get API Access. The API will provide the following information which the Aggregator Platform may use to display the KITT CS service on its platform:

- Unique identifier to the vehicle;

- Vehicle position (geo coordinates, address);
- Vehicle status (available / not available);
- Vehicle license plate;
- Deep link URL leading to the booking screen for this vehicle in the provider’s app;
- Other relevant vehicle attributes: model, color, fuel type and level.

- (9) The API may be used by the Aggregator Platform for a deep linking. It will make the display of cars possible (car type, location, availability, price, status of fuel/battery). Based on the API, the Aggregator Platform will be able to show the location of available KITT CS cars in the Territory and the features described above on its platform. The customer will have the possibility to click on a KITT CS car and he will be redirected to the KITT CS app(s)¹ for reservation or booking. It is not envisaged that one can login into one’s KITT CS customer account and book the car via the Aggregator Platform. It will also not be possible to open and access cars or to process the payment via the Aggregator Platform.²
- (10) Provided the access criteria are fulfilled, the Notifying Parties will provide access under these Commitments to the API without undue delay and on non-discriminatory basis. The Notifying Parties will treat all Aggregator Platforms – that seek access based on these Commitments and that fulfill the access criteria – equally, regardless of, inter alia, ownership, size or financing, and in a matter and spirit that will allow these Commitments to work effectively.

2. Grant access for all interested Car Sharing Providers to the KITT Multimodal App

- (11) The Notifying Parties will make the KITT Multimodal App available to third party Car Sharing Providers so that they can make visible their car sharing services in the KITT Multimodal App. Access will be made available without a need to pay commissions. Access will be granted in the Territory for a period of three years after closing of the Proposed Transaction.
- (12) There is no right of access in the following cases:
- The Car Sharing Provider is Controlled by an OEM; or

¹ [Details on App implementation].

² It would not be competitively advantageous if the Aggregator Platform would provide more than a deep link solution. If booking via the Aggregator Platform would be possible, the Car Sharing Providers would not have any possibility to show their own app/technical platform and their marketing efforts to the consumer.

- The Car Sharing Provider has a fleet of more than 60% of the average fleet size of the KITT CS fleet of the preceding calendar year in the respective overlapping city.
- (13) The KITT Multimodal App will be owned and operated by an entity jointly Controlled by the Notifying Parties post-closing.
- (14) A third party Car Sharing Provider which does not fall under the exemption above, will be integrated into the KITT Multimodal App after having signed a Partner-Contract (containing at least the provisions set out in **Annex II**). In order to set this up, the third party Car Sharing Provider must transfer data of all vehicles using an API that is defined and provided by the platform. For each vehicle the following information needs to be provided:
 - Unique identifier to the vehicle;
 - Vehicle position (geo coordinates, address);
 - Vehicle status (available / not available);
 - Vehicle license plate;
 - Deep link URL leading to the booking screen for this vehicle in the third party Car Sharing Provider’s app;
 - Other relevant vehicle attributes: e.g. model, color, fuel type and level.
- (15) The third party Car Sharing Provider will be integrated into the KITT Multimodal App with a deep link. The provider’s cars will be displayed (car type, location, availability, price, status of fuel/battery). The consumer can see the cars of the third party Car Sharing Provider on a geographical map. He cannot reserve or book the cars via the KITT Multimodal App. For reservation, booking, opening of the car and payment, the consumer will be redirected to the app of the third party Car Sharing Provider.³
- (16) Presumably in end of January 2019, a so-called “self-service integration API” will be provided by the KITT Multimodal App. This API will allow for seamless deep link integration with minimal setup costs for third party mobility providers. It will offer:
 - Detailed technical documentation on how to integrate with the platform

³ It would not be competitively advantageous if the Notifying Parties would provide more than a deep link solution. If booking via the KITT Multimodal App would be possible, the third party Car Sharing Provider would lose direct customer contact and not have any possibility to show its own app/technical platform and marketing efforts to the consumer. The information exchange could also become problematic.

- Standardized API that allows any third party provider to integrate by:
 - Registering an account;
 - Uploading and configuring own assets that do not change over time (e.g. images, icons, map markers, standard texts); and
 - Sending regular vehicle status updates to the platform.

(17) Provided the access criteria are fulfilled, the Notifying Parties will provide access to the KITT Multimodal App under these Commitments without undue delay and on non-discriminatory basis. The Notifying Parties will treat all Car Sharing Providers that fulfill the access criteria under these Commitments equally, regardless of, inter alia, ownership, size or financing, and in a matter and spirit that will allow these Commitments to work effectively. The Notifying Parties will not treat KITT CS on the KITT Multimodal App differentially solely because they are Controlled by the Notifying Parties. Differential treatment may, however, exist, for example, due to different technical requirements and different ways of integration for KITT CS and third party Car Sharing Providers.

Section C. Reporting

(18) The Notifying Parties will engage a Monitoring Trustee (see under D. below) that will submit a written report to the Commission in English no later than six months after closing of the Proposed Transaction (or at any other time the Commission requests so). The Monitoring Trustee will describe in the report whether the Notifying Parties are in compliance with the Commitments. Thereafter, the Monitoring Trustee will submit compliance reports every six months (or at any other time the Commission requests so) and a final report within two weeks after the Commitments' period expired.

(19) The Notifying Parties are obliged to provide the Monitoring Trustee with all information reasonably necessary to write his reports.

Section D. Monitoring Trustee

(20) The Monitoring Trustee will be responsible for informing the Commission about the implementation of and compliance with the proposed Commitments by the Notifying Parties. If the Commission can conclude that the mechanisms foreseen in the Commitments will allow the Notifying Parties to effectively enforce them in a timely manner, no permanent monitoring of the

Commitments by the Commission is required according to the Commission's Remedies Notice.⁴ The Notifying Parties set-out the relevant procedure below.

I. Appointment procedure

- (21) The Notifying Parties shall appoint a Monitoring Trustee to carry out the functions specified in the Commitments for a Monitoring Trustee. The Notifying Parties commit not to close the Proposed Transaction before the appointment of a Monitoring Trustee.
- (22) The Monitoring Trustee shall:
- (i) at the time of appointment, be independent of the Notifying Parties and their Affiliated Undertakings;
 - (ii) possess the necessary qualifications to carry out its mandate, for example have sufficient relevant experience as an investment banker or consultant or auditor; and
 - (iii) neither have nor become exposed to a Conflict of Interest.
- (23) The Monitoring Trustee shall be remunerated by the Notifying Parties in a way that does not impede the independent and effective fulfillment of its mandate.

Proposal by the Notifying Parties

- (24) No later than four weeks after the Effective Date, the Notifying Parties shall submit the name or names of one or more natural or legal persons whom the Notifying Parties propose to appoint as the Monitoring Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the person or persons proposed as Monitoring Trustee fulfill the requirements set out in para. 22 and shall include:
- (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Monitoring Trustee to fulfill its duties under these Commitments; and
 - (b) the outline of a work plan which describes how the Monitoring Trustee intends to carry out its assigned tasks.

Approval or rejection by the Commission

- (25) The Commission shall have the discretion to approve or reject the proposed Monitoring Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary

⁴ Remedies Notice, para. 66.

for the Monitoring Trustee to fulfil its obligations. If only one name is approved, the Notifying Parties shall appoint or cause to be appointed the person or persons concerned as Monitoring Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, the Notifying Parties shall be free to choose the Monitoring Trustee to be appointed from among the names approved. The Monitoring Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Notifying Parties

- (26) If all the proposed Monitoring Trustees are rejected, the Notifying Parties shall submit the names of at least two more natural or legal persons within one week of being informed of the rejection, in accordance with paras. 21 and 25 of these Commitments.

Monitoring Trustee nominated by the Commission

- (27) If all further proposed Monitoring Trustees are rejected by the Commission, the Commission shall nominate a Monitoring Trustee, whom the Notifying Parties shall appoint, or cause to be appointed, in accordance with a Monitoring Trustee mandate approved by the Commission.

II. Functions of the Monitoring Trustee

- (28) The Monitoring Trustee shall assume its specified duties and obligations in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Monitoring Trustee or the Notifying Parties, give any orders or instructions to the Monitoring Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee

- (29) The Monitoring Trustee shall:
- (i) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision;
 - (ii) propose to the Notifying Parties such measures as the Monitoring Trustee considers necessary to ensure the Notifying Parties' compliance with the conditions and obligations attached to the Decision;
 - (iii) act as a contact point for any requests by third parties in relation to the Commitments;

(iv) promptly report in writing to the Commission, sending the Notifying Parties a non-confidential copy at the same time, if it concludes on reasonable grounds that the Notifying Parties are failing to comply with these Commitments.

III. Duties and obligations of the Parties

- (30) The Notifying Parties shall provide the Monitoring Trustee with all such co-operation, assistance and information as the Monitoring Trustee may reasonably require performing its tasks.
- (31) The Notifying Parties shall indemnify the Monitoring Trustee and its employees and agents (each an “**Indemnified Party**”) and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to the Notifying Parties for, any liabilities arising out of the performance of the Monitoring Trustee’s duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Monitoring Trustee, its employees, agents or advisors.
- (32) At the expense of the Notifying Parties, the Monitoring Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to the Notifying Parties’ approval (this approval not to be unreasonably withheld or delayed) if the Monitoring Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the mandate, provided that any fees and other expenses incurred by the Monitoring Trustee are reasonable. Should the Notifying Parties refuse to approve the advisors proposed by the Monitoring Trustee the Commission may approve the appointment of such advisors instead, after having heard the Notifying Parties. Only the Monitoring Trustee shall be entitled to issue instructions to the advisors.
- (33) The Notifying Parties agree that the Commission may share Confidential Information proprietary to them with the Monitoring Trustee. The Monitoring Trustee shall not disclose such information and the principles contained in Article 17(1) and (2) of the Merger Regulation apply *mutatis mutandis*.
- (34) The Notifying Parties agree that the contact details of the Monitoring Trustee are published on the website of the Commission's Directorate-General for Competition and they shall inform interested third parties of the identity and the tasks of the Monitoring Trustee.
- (35) For a period of 5 years from the Effective Date the Commission may request all information from the Notifying Parties that is reasonably necessary to monitor the effective implementation of these Commitments.

IV. Replacement, discharge and reappointment of the Monitoring Trustee

- (36) If the Monitoring Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Monitoring Trustee to a Conflict of Interest:
- (a) the Commission may, after hearing the Monitoring Trustee and the Notifying Parties, require the Notifying Parties to replace the Monitoring Trustee; or
 - (b) the Notifying Parties may, with the prior approval of the Commission, replace the Monitoring Trustee.
- (37) If the Monitoring Trustee is removed according to para. 36 of these Commitments, the Monitoring Trustee may be required to continue in its function until a new Monitoring Trustee is in place to whom the Monitoring Trustee has effected a full hand over of all relevant information. The new Monitoring Trustee shall be appointed in accordance with the procedure referred to in paras. 21-27 of these Commitments.
- (38) Unless removed according to para. 36 of these Commitments, the Monitoring Trustee shall cease to act as Monitoring Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Monitoring Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section F. Review clause

- (39) The Commission may, prior to the expiry of the Commitments, extend the time period foreseen in (a) the Commitments for granting API Access of the future Car Sharing Vertical to Aggregator Platforms under certain premises and/or (b) the Commitments for granting third party Car Sharing Providers access to the KITT Multimodal App for two years and for individual cities (of the six overlapping cities) only in appropriate cases, on its own initiative. An appropriate case for extension only exists, if within three years no Meaningful Market Entry took place in the respective city.
- (40) The Commission may further, in response to a reasoned request from the Notifying Parties showing good cause waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments. This request shall be accompanied by a report from the Monitoring Trustee, who shall, at the same time send a non-confidential copy of the report to the Notifying Parties.

Section G. Entry into force

The Commitments shall be implemented after closing of the Proposed Transaction without delay.

.....
(Name of the lawyer) (Name of the lawyer) (Name of the lawyer)

duly authorised for and on behalf of

Bayerische Motoren Werke Aktiengesellschaft and Daimler AG

Annex I: Material Terms of the API Agreement

The API Agreement will be a standard contract containing, inter alia, the following material terms:

- Representations by the Aggregator Platform that all access criteria are fulfilled and right of the Car Sharing Vertical to terminate the API Agreement for good cause if the Aggregator Platform (i) breaches these representations or (ii) no longer fulfills the access criteria.
- As long as the API Agreement is entered into during the initial duration period of three years of the Commitments, it will provide at least for a minimum contract term of two years, in which termination without good cause is not permissible. This only applies if the Aggregator Platform and any affiliated undertaking of the Aggregator Platform have not been previously granted API Access under the API Agreement.
- In case the Separate Businesses exemption is evoked, a covenant of the Aggregator Platform and the OEM directly or indirectly holding a stake in the Aggregator Platform that the Separate Businesses exemption is fulfilled and that the safeguards will remain in place during the contract duration, including an audit right for the Monitoring Trustee or an independent third party, and, upon discretion of the Notifying Parties, the requirement to sign a contract materially similar to the API Agreement that allows the Notifying Parties to display the car sharing activities and/or competing business of the OEM in the KITT Multimodal App.
- Covenant of the Aggregator Platform to use the data provided via the API Access only for a display of such data in the app of the Aggregator Platform and, in particular, not for any other purposes, e.g. data analytics.
- Restriction of the API Access to a deep linking where customers wishing to register or book vehicles are directed to the Car Sharing Vertical app and negative covenants for the Aggregator Platform not to undertake, attempt or allow a reservation, booking or access to the vehicles other than through a link to the Car Sharing Vertical App (deep linking).
- Negative covenant of the Aggregator Platform not to access or attempt to obtain access to any data base or IT system of the Car Sharing Vertical other than data that is provided via the API under the API Agreement and in particular not to obtain or try to obtain access to the Car Sharing IT systems in circumvention of applied data security mechanisms.
- Covenant for the Aggregator to use only the official logo files made available by the Car Sharing Vertical to show an integration into the Aggregator Platform app (fleet vehicles, charging stations, parking spots).
- Customary termination rights for cause (e.g. insolvency, breach of material obligations).
- Adequate penalties for the Aggregator Platform in case of a breach of material provisions, in particular, data protection, data security provision or the above covenants (e.g. Separate Businesses exemption).

- The contract includes key tasks and responsibilities of each party, inter alia the provision of data “as is” for to be defined, non-exclusive usage by the aggregator platform, termination rights, and duration of the contract.
- Appropriate data protection, data security provisions and limitations of liability.
- The right of the Car Sharing Vertical to update the API and to change, update and extend the information provided by the API (Aggregator Platforms will be informed timely to ensure that systems can be properly adjusted) for technical (e.g. technical changes or further development of the Car Sharing app(s) or IT systems) or legal reasons always provided that the requirements mentioned in para. 8 of the Commitments will remain to be fulfilled or that information that serves the same purpose will be provided.
- Exceptions to the availability of the API for maintenance of systems, outages, and act of nature beyond control.
- A fast track arbitration clause for potential legal disputes under the API Agreement.

Annex II: Material Terms of the Partner-Contract

The Partner-Contract will be a standard contract containing, inter alia, the following material terms:

- Representations by the third party Car Sharing Provider that the exemptions are not applicable and access should be given and right to terminate the Partner-Contract for good cause if the third party Car Sharing Provider (i) breaches these representations or (ii) the exemption becomes applicable.
- As long as the Partner-Contract is entered into during the initial duration period of three years of the Commitments, the Partner-Contract will provide for a minimum contract term of two years, in which termination without good cause is not permissible. This only applies if the Car Sharing Provider and any affiliated undertaking of the Car Sharing Provider have not been previously granted access to the KITT Multimodal App under the Partner-Contract.
- Key tasks and responsibilities of each party, inter alia permission for the KITT Multimodal App to integrate a deep link to the third party Car Sharing Provider's app for booking requests, termination rights, and its duration.
- Appropriate data protection and data security provisions.
- Provisions about branding: No branding limitations; own brand logo and name can be used; third party logos will be displayed, provided they are available in the region of the activity.
- Customary termination rights for cause (e.g. insolvency, breach of material obligations).
- Adequate penalties for the Aggregator Platform in case of a breach of material provisions, in particular, data protection and data security provisions.
- A fast track arbitration clause for potential legal disputes under the Partner-Contract.



EUROPEAN COMMISSION
DG Competition

CASE M.8788 – APPLE / SHAZAM

(Only the English text is authentic)

MERGER PROCEDURE REGULATION (EC) 139/2004

Article 8(1) Regulation (EC) 139/2004

Date: 06/09/2018

This text is made available for information purposes only. A summary of this decision is published in all EU languages in the Official Journal of the European Union.

Parts of this text have been edited to ensure that confidential information is not disclosed; those parts are enclosed in square brackets.



EUROPEAN
COMMISSION

Brussels, 6.9.2018
C(2018) 5748 final

COMMISSION DECISION

of 6.9.2018

**declaring a concentration to be compatible with the internal market
and the EEA Agreement**

(Case M.8788 – Apple/Shazam)

(Only the English version is authentic)

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to the Agreement on the European Economic Area, and in particular Article 57 thereof,

Having regard to Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings¹, and in particular Article 8(1) thereof,

Having regard to the Commission's decision of 23 April 2018 to initiate proceedings in this case,

Having regard to the opinion of the Advisory Committee on Concentrations²,

Having regard to the final report of the Hearing Officer in this case³,

Whereas:

1. INTRODUCTION

- (1) On 14 March 2018, the Commission received notification of a concentration pursuant to Article 4 of Regulation (EC) No 139/2004 ("the Merger Regulation") that would result from the proposed acquisition by Apple Inc. (United States of America) of sole control of the entire undertaking of Shazam Entertainment Ltd. (United Kingdom) within the meaning of Article 3(1)(b) of the Merger Regulation ("the Transaction").⁴ The undertaking comprising Apple Inc. and its subsidiaries ("Apple" or "the Notifying Party") and the undertaking comprising Shazam Entertainment Ltd. and its subsidiaries ("Shazam") are hereinafter collectively referred to as "the Parties".
- (2) The recitals in this Decision are arranged as follows. Section 2 describes the Parties and explains why the Transaction would result in a concentration within the meaning of the Merger Regulation. Section 3 explains why the Commission acquired jurisdiction to scrutinise the Transaction. Section 4 describes the procedure followed in this case. Section 5 describes the investigation undertaken by the Commission into the Transaction. Section 6 provides an overview of the digital music industry. Section 7 defines the relevant product and geographic markets. Section 8 sets out the Commission's assessment of whether the concentration brought about by the Transaction would significantly impede effective competition in each of the relevant markets. Section 9 contains the Commission's conclusions.

2. THE PARTIES AND THE TRANSACTION

- (3) **Apple** designs, manufactures and sells mobile communication and media devices (such as the "iPhone", the "iPad", the "Apple TV") as well as personal computers (the "Mac"). It also develops a variety of operating systems ("OSs"), which are installed on the hardware of the devices and personal computers ("PCs") it sells

¹ OJ L 24, 29.1.2004, p. 1. With effect from 1 December 2009, the Treaty on the Functioning of the European Union ("TFEU") has introduced certain changes, such as the replacement of "Community" by "Union" and "common market" by "internal market". The terminology of the TFEU will be used throughout this Decision.

In this Decision, [...] and [...] refer to confidential information which has been redacted from the version of this Decision addressed to the Notifying Party.

² OJ C20.. , p....

³ OJ C20.. , p....

⁴ OJ C 106, 21.03.2018, p. 16.

("macOS" for Macs, iOS for smart mobile devices, "watchOS" for smart watches and "tvOS" for smart TVs), as well as other software solutions and mobile application software solutions ("apps"), including for example a virtual assistant software solution ("Siri"). Moreover, Apple sells services, peripherals, networking solutions, and third-party digital content. In particular, Apple sells and delivers digital content online through the "iTunes Store", the "App Store", the "iBook store" and the "Mac App Store", and offers the music and video streaming service through the app "Apple Music".

- (4) **Shazam** is a developer and distributor of music recognition apps for smartphones, tablets and personal computers, branded "Shazam".⁵ It generates revenues from (i) the display of online advertising, (ii) partnerships with third parties, (iii) commissions earned on referrals of users to digital music streaming and download services, such as Apple Music, and (iv) licensing of music data and analytics services.
- (5) Pursuant to a share purchase agreement entered into on 10 December 2017, following completion of the Transaction Apple Inc. will hold the entire issued share capital of Shazam Entertainment Ltd. and will thus acquire sole control of the undertaking comprising Shazam. Therefore, the Transaction would result in a concentration within the meaning of Article 3(1)(b) of the Merger Regulation. The notified concentration that would result from the Transaction is referred to in this Decision as "the Concentration".

3. JURISDICTION OF THE COMMISSION

- (6) The Concentration does not have a Union dimension within the meaning of Article 1 of the Merger Regulation. In the last financial year before notification for which audited accounts are available for Apple (2017), Apple generated an aggregate worldwide turnover of EUR 206.3 billion, of which approximately EUR [...] billion was generated in the Union. In the last financial year before notification for which audited accounts are available for Shazam (2016), Shazam, however, generated an aggregate worldwide turnover of only EUR 45.2 million, of which approximately EUR [...] million was generated in the Union. Therefore, neither the test laid down in paragraph (2) nor the test laid down in paragraph (3) of Article 1 of the Merger Regulation is met.
- (7) On 12 December 2017, the Concentration was notified to the federal competition authority of Austria.
- (8) On 21 December 2017, the Commission received a referral request concerning the Concentration from the federal competition authority of Austria pursuant to Article 22(1) of the Merger Regulation. The national competition authorities of France, Iceland, Italy, Norway, Spain and Sweden subsequently joined the request made by the federal competition authority of Austria. Austria, France, Iceland, Italy, Norway, Spain and Sweden are collectively referred to as "the Referring States".
- (9) On 6 February 2018, the Commission adopted decisions by which it accepted the requests of the Referring States and decided to examine the Concentration pursuant to Article 22(3) of the Merger Regulation ("the Article 22 Decisions").⁶ Therefore,

⁵ Shazam also offers visual recognition services, but, at present, they have no market relevance.

⁶ Commission decision of 6 February 2018 in Case M.8788 – *Apple/Shazam*.

the Commission has acquired jurisdiction to examine the effects of the Concentration with regard to the Referring States.

4. THE PROCEDURE

- (10) On 14 March 2018, the Concentration was notified under Article 4 of the Merger Regulation at the request of the Commission pursuant to the second subparagraph of Article 22(3) of that Regulation.
- (11) After a preliminary examination of the Concentration and based on a first phase market investigation, the Commission decided on 23 April 2018 to initiate proceedings under Article 6(1)(c) of the Merger Regulation (“the Article 6(1)(c) Decision”). In the Article 6(1)(c) Decision, the Commission concluded that the Concentration raised serious doubts as to its compatibility with the internal market and the Agreement on the European Economic Area (“EEA Agreement”) due to non-horizontal non-coordinated effects consisting of:
 - (a) the potential foreclosure of competing providers of automatic content recognition (“ACR”) software solutions, including music recognition apps, in the territory covered by the EEA Agreement (“the EEA”) as a result of conduct such as pre-installing Shazam on iOS or integrating Shazam with iOS or degrading the interoperability of ACR solutions provided by Shazam's competitors on iOS; and
 - (b) the potential foreclosure of competing providers of digital music streaming apps in the EEA as well as in the territories of the Referring States as a result of Apple gaining access to commercially sensitive information on its rivals through the Concentration.
- (12) On 15 May 2018, the Notifying Party submitted its reply to the Article 6(1)(c) Decision (“the Reply to the Article 6(1)(c) Decision”).
- (13) On the same day, the second phase investigation period was extended by ten working days at the request of the Notifying Party pursuant to the first sentence of the second subparagraph of Article 10(3) of the Merger Regulation.
- (14) A state of play meeting between the Parties and the Commission took place on 22 May 2018.
- (15) The Advisory Committee discussed a draft of this Decision on 22 August 2018 and issued a favourable opinion.⁷

5. THE INVESTIGATION

- (16) After issuing the Article 22 Decisions and prior to the notification of the Concentration, the Commission sent four requests for information (“RFIs”) to the Parties. The responses to those RFIs were then included in the notification. The Commission also conducted ten interviews with Shazam, the Parties’ competitors and music labels.
- (17) During the first phase investigation, the Commission sent close to 60 RFIs to the Parties’ competitors and customers, as well as to music labels and the Parties

⁷ At the Advisory Committee all present Member States agreed that that the Transaction must be declared compatible with the internal market and the EEA Agreement in accordance with Article 2(2) and 8(2) of the Merger Regulation and Article 57 of the EEA Agreement.

themselves. The Commission also conducted an interview with a competitor of Shazam and a preliminary reconstruction of the markets for music recognitions apps and digital music streaming apps.

- (18) During the second phase investigation, the Commission sent close to 50 detailed RFIs to the Parties (including targeted internal document requests, resulting in the submission of over 100 000 internal documents of Apple and Shazam) and key market participants in the digital music industry, as well as in the digital platforms space and the online advertising industry, including Google, Inc. (“Google”), Facebook, Inc. (“Facebook”) and Twitter, Inc. (“Twitter”). Further, the Commission conducted several interviews with the Parties’ competitors and the consumer association Bureau Européen des Unions de Consommateurs (“BEUC”) and completed the market reconstruction exercise undertaken in the first phase investigation. Finally, the Commission collected information on the databases maintained by Apple Music, Apple Music's competitors and Shazam's competitors in order to perform a benchmarking exercise of Shazam’s data against comparable databases under several metrics, as further detailed in Section 8.

6. OVERVIEW OF THE DIGITAL MUSIC INDUSTRY

- (19) The industry sector on which the Commission has assessed the impact of the Concentration on competition is the digital music sector, where both Parties are active players, albeit with different roles (as further explained in the following sub-sections).

6.1. The digital music distribution value chain

- (20) Music publishers oversee all activities related to the preparation and issuing of musical works by authors. Upstream, they are active in the supply of publishing services to authors. These services include signing authors and providing them with financial, marketing and career support in exchange for the rights to their musical work or an economic interest in their musical work (that is, the right of publishers to obtain a certain portion of the royalties collected). Downstream, music publishers are active in the exploitation of works of authors who are under contract and for a certain period of time following expiration of their contracts (the so-called retention period). To this end, they either directly grant licences to rights users in exchange for the payment of royalties or they receive a part of the royalties collected by collecting societies⁸ (for licences issued by societies) for the exploitation of an author's work.
- (21) The following types of publishing rights exist:
- (a) mechanical rights: the right to reproduce a work in a sound recording (for example compact disks);
 - (b) performance rights: the right for commercial users, such as broadcasters (TV or radio stations), concert halls, theatres, night clubs or restaurants, to divulge a work to the public;
 - (c) synchronisation: the right for commercial users, such as advertising agencies or film companies, to synchronise music with a visual image;
 - (d) print rights: the right to reproduce a work in sheet music; and

⁸ Collective management organisations, also known as collecting societies, are entities which manage copyrights in musical works, see Commission decision of 15 June 2015 in case M.6800 - *PRRfM/STIM/GEMA/JV*, recital 4.

- (e) online rights: a combination of mechanical and performance rights for online applications, such as music downloading and/or streaming services.⁹
- (22) Record companies give concrete and material (physical or digital) shape to musical works, which are then brought to end consumers. To do so, record companies need, among other things, to have mechanical rights licensed to them from publishers and/or collecting societies. Like music publishers, record companies also operate both upstream vis-à-vis authors and downstream vis-à-vis distributors. In particular, upstream, record companies provide a number of services to authors and performing artists, including discovering, developing and promoting recording artists, as well as the recording of their music (so-called "A&R", which stands for "artists and repertoire"), whereas downstream, they sell recorded music in physical or digital form to wholesalers and/or retailers (bricks and mortar shops or online platforms, such as iTunes) and license the recording rights over their catalogue to audio or video streaming digital service providers (such as Apple Music).
- (23) Publishing rights differ from recording rights. Publishing rights are rights to the notes and lyrics of a song and are usually transferred to a publisher by the author. Recording rights are rights to the particular rendition of that song, as recorded by a performing artist (who is often different from the author).
- (24) Digital music distributors have mechanical and performance rights licensed to them from collecting societies and/or music publishers and rights to actual recordings licensed to them from record companies. They then offer the musical works to consumers. There are a variety of digital music distribution channels available to consumers, who typically access music in a number of different ways.¹⁰
- (25) The main retail models for digital music distribution services are music streaming and music download.¹¹ Download involves the purchase and storage of a digital copy of a musical work on one or more personal computers or media devices. Typical examples of download platforms are Apple's iTunes apps and the MP3 service¹² of Amazon.com, Inc., ("Amazon"). With a streaming service, the user does not download music files and no permanent copy is stored on the user's personal

⁹ See Commission Decision of 22 May 2007 in Case M.4044 – *Universal/BMG Music Publishing*, recitals 18-25; Commission decision of 19 April 2012 in Case M.6459 - *Sony/Mubadala/EMI Music Publishing*, paragraph 19.

The exploitation of online rights constitutes the main area of interest for the purpose of assessing the Concentration and it is also the one which has experienced an exceptional development in the last decade, as demonstrated by the data on royalties collections reported by the International Confederation of Societies of Authors and Composers ("CISAC"). Indeed, according to the CISAC's 2017 report, available at <http://www.cisac.org/CISAC-University/Library/Global-Collections-Reports/Global-Collections-Report-2017> (accessed on 1 August 2018), although digital royalty collections are still a relatively small segment, they dominate worldwide growth across all regions. In 2016, global digital music revenues streams were around EUR 945 million, with a 51.9% growth rate from 2015, while in Europe (comprising, for the purpose of the market study at stake, Belgium, Denmark, Netherlands, Sweden, United Kingdom, France, Spain, Italy, Germany, Switzerland, Czech Republic and Turkey) digital collections for music were around EUR 526 million, with a 40.8% compared to previous year and had nearly tripled in the precedent five years, driven by explosive growth in streaming music and video platforms services.

¹⁰ Reportedly, consumers each listen on average to music on 4 different licensed ways, International Federation of the Phonographic Industry ("IFPI"), *Music Consumer Insight Report 2017*, available at <http://www.ifpi.org/downloads/Music-Consumer-Insight-Report-2017.pdf> (accessed on 1 August 2018).

¹¹ Commission decision of 15 June 2015 in case M.6800 - *PRRfM/STIM/GEMA/JV*, recital 113 and footnote 85.

¹² An MP3 service is a media device that stores and plays songs in a computer format (called MP3) for creating sound files that are much smaller than standard sound files.

computer or media device. Instead, the audio file is delivered in small data packets over the Internet and playback commences as soon as the streaming service (for example, an app or web-based solution) is initiated.

- (26) Streaming services can comprise basic ad-sponsored services, available free of charge, and premium, paid-for services. Premium services are typically ad-free, offer additional functionalities (for instance, unlimited plays of songs, a larger music library or support of smart mobile devices) and may grant users the possibility to download and store tracks in order to listen to them offline during the period of the subscription (so-called “tethered downloads”).¹³ Music streaming can be played on PCs, smart mobile devices, home entertainment systems, car entertainment systems, gaming consoles and similar devices, both online and offline. Music streaming services are available on different OSs, although commonly used most on Android by Google and iOS.

6.2. Competitive dynamics, key metrics and trends

- (27) In the last 20 years, the recorded music industry has undergone continuous and substantial transformation with a significant impact on the way music is distributed. Distribution has indeed shifted from physical to digital and, within digital, from download to streaming and from “ownership” to “access”.¹⁴
- (28) After more than a decade of declining revenues in music distribution, the global recorded music industry has in recent years recovered and experienced continuous growth, with total revenues rising from USD 14.2 billion in 2013 to USD 17.3 billion in 2017. This growth was largely driven by digital music streaming services, whose revenues surpassed those of digital music downloads in 2016.¹⁵ In 2017, more than half of all revenues (54%) in the recorded music industry were generated by distribution of digital music and, in particular, by 176 million users of premium streaming services.¹⁶ Notwithstanding the exceptional growth in recent years, digital music revenues are expected to continue to increase in the coming years, given that digital music is still mainly conveyed by free, ad-supported music services.¹⁷ With

¹³ A tethered download is a song file downloaded from a music subscription service that can be played only on personal computers or media device registered to an account of the relevant music subscription service, as opposed to untethered downloads which can be played on compatible devices, regardless of whether it is registered to an account of the music subscription service.

¹⁴ IFPI, *Global Music Report 2017*, p.7, available at: <http://www.ifpi.org/downloads/GMR2017.pdf> (accessed on 1 August 2018).

¹⁵ IFPI, *Global Music Report 2018: State of the Industry*, p. 11, available at <http://www.ifpi.org/downloads/GMR2018.pdf> (accessed on 1 August 2018).

¹⁶ According to IFPI, *Global Music Report 2018: State of the Industry*, p. 10, available at <http://www.ifpi.org/downloads/GMR2018.pdf> (accessed on 1 August 2018), global recorded music revenues (reported at wholesale prices) grew for the third consecutive year to reach around EUR 15.344 billion in 2017. The 8.1% growth was the highest percentage rate increase from a previous year in the past 20 years. Specifically, streaming revenues made up 38% of total global revenues; digital revenues (excluding streaming) made up 16%; physical unit revenues made up 30%; performance rights' revenues made up 14%; and synchronization revenues made up 2%. Moreover, record-company income deriving from digital formats and services grew by 19.1%, increasing from some EUR 7 billion to EUR 8.33 billion. Three Member States are among the top nine digital markets globally: Germany and the United Kingdom hold each 8% of the global market and France, one of the Referring States, holds 5%.

¹⁷ Form CO, paragraph 232; MIDiA, *State of the Streaming Nation 2 Report*, May 2017, Annex 6.3.III.B(a) to Form CO; and Statista worldwide and Europe data on the size of the music streaming services market, Annexes 6.3.III.B(b) and (c) to Form CO; Reply to the Article 6(1)(c) Decision, Section 2.A. In this vein also: [...]’s response to RFI [...]; agreed minutes of the conference call with Deezer, of 30 May 2018, paragraph 14, and [...] and Spotify’s IPO prospectus, Form F-1, available at:

respect to the EEA, this has been confirmed by the results of the Commission's market investigation.¹⁸

- (29) Furthermore, benefiting from increasing Internet and mobile device penetration, the growth in music streaming services is expected to continue in Europe over the next few years.¹⁹
- (30) In order to sustain their growth, music streaming service providers operate on the basis of a variety of different business models. As mentioned in Section 6.2, some providers operate so-called freemium models whereby they offer a basic, free and ad-supported service to attract users, while additional features are offered in a premium service to which users can subscribe in exchange for the payment of a monthly fee. For such business models, conversion of free users into paid subscribers is important.
- (31) When developers of music streaming apps offer their app in the app stores available on the different OSs, they may be required to use the in-app purchase or billing mechanism of the OS provider as a method of payment to process customer transactions related to the purchase of premium subscriptions. Depending on the developer terms for the app store, the developers may have to pay a fee to the OS provider on the value of transactions processed.
- (32) In particular, Apple requires third party developers (including digital music streaming providers) which sell digital content to users via apps on iOS devices to use Apple's In-App Purchase Mechanism ("IAP") for the relevant payments²⁰ and charges a fee equal to 30% of the subscription price.²¹ While a subscription outside the app (for example, on the service provider's website) with an alternative payment mechanism remains possible, Apple's App Store Review Guidelines²² limit the ability of competitors to Apple Music to promote this possibility to iOS users.²³
- (33) As regards Android, Google does not require music streaming service providers to use its in-app billing as a method of payment as long as the content may (also) be consumed outside of the app itself.²⁴ In such cases, music streaming service providers do not have to pay any transaction fees to Google.²⁵
- (34) Music streaming service providers use a number of methods in order to engage music enthusiasts, promote their services, acquire customers and retain existing users. In this respect, the results of the market investigation indicate that promotional campaigns (for example, specific offers for a limited time) and in-app advertisement in digital music streaming apps to customers which are not yet premium subscribers are generally considered to be the most effective methods to grow the subscriber base of music streaming services. Thus organic growth customer acquisition channels are

<https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm>, (accessed on 1 August 2018), page 2 and following.

¹⁸ See Section 8.4.2.1(c)(iv).

¹⁹ See: <https://www.statista.com/outlook/202/102/digital-music/europe> (accessed on 1 August 2018).

²⁰ See section 3.1.1. of Apple's App Store Review Guidelines, available at: <https://developer.apple.com/app-store/review/guidelines/> (accessed on 1 August 2018).

²¹ This is reduced to 15% after a subscriber accumulates one year of a paid service, available at <https://developer.apple.com/app-store/subscriptions/> (accessed on 1 August 2018).

²² See section 3.1.3 (b) of Apple's App Store Review Guidelines, available at <https://developer.apple.com/app-store/review/guidelines/> (accessed on 1 August 2018).

²³ For example, [...]

²⁴ See Developer Policy Center, Monetization and Ads, available at: <https://play.google.com/about/monetization-ads/> (accessed on 1 August 2018).

²⁵ This is different for the distribution of games.

of primary importance. These are followed, in order of importance, by paid online search advertising, marketing on social network sites and partnerships with mobile network/telecoms operators,²⁶ e-mail campaigns to current or former customers and referrals from other apps.²⁷

- (35) In this respect, a provider of music streaming services, SoundCloud, explained that “[c]urrently, [its] most effective customer acquisition method is [its] Customer Relationship Management program (“CRM”) that communicates via email, push and in-app notifications to [its] base of free tier listeners. [It uses] CRM to communicate about new releases, product updates and to upsell users to the paid subscriptions, sometimes incorporating promotional discounts.”²⁸ In the same vein, [...]”²⁹
- (36) Music streaming service providers typically compete for new customers who have not yet subscribed to any music streaming service provider, rather than for subscribers of competing services. As Spotify’s Director of Economics put it in 2017: “The key development in the market at the moment is competition. What is especially key is that it is competition based around market growing, not market stealing. There are more big players - and arguably more sustainable players - than have come and gone in the past, and it’s all about making new audiences aware of streaming and expanding the market. At the moment, we are growing, Apple’s growing, Amazon’s growing, and other services are coming on board, and we’re not stealing each other’s lunch.”³⁰
- (37) During the market investigation, several market respondents, such as [...]”³¹ and [...]”³², explained that at this stage of the market, growth typically comes from first-time subscribers to music streaming services rather than users who were previously subscribers of competing music streaming services. Also [...] considered that its main strategic focus was acquiring new users rather than attracting competitors’ users to its service.³³
- (38) Customers that use streaming services for free are more likely to switch to alternative service providers than paying subscribers, as the latter are typically less price sensitive and more engaged users (for example, by using additional features such as creating their own playlists).³⁴ Relatively low churn rates for premium subscribers

²⁶ The importance of partnerships with mobile network/telecoms operators is suggested by [...]. The importance of this mode of generating new subscribers is demonstrated by comments made by digital music distributors. For example, the Form CO, paragraph 246, reports that the former CEO of Deezer stated that “mobile operators are the only ones who can contribute to the critical mass” required for the success of a service” (available at: <https://www.mobileworldlive.com/interview-deezer-ceo>), while Spotify’s global head of telco partnerships has stated that such partnerships give Spotify a degree of marketing and promotion “on a scale we’d never be able to afford on our own”, increased average revenue per user and help “get people into the paid funnel and keeping them in the paid funnel”, with around 80% of paid users remaining after the end of the bundle period (available at: https://www.youtube.com/watch?v=M1rFSVdbS_I).

²⁷ Apple’s response to RFI 36, question 3 b); Soundcloud’s response to RFI 22, question 2; Deezer’s response to RFI 19, question 2; Spotify’s response to RFI, question 2; [...].

²⁸ SoundCloud’s response to RFI 22, question 3.

²⁹ [...].

³⁰ IFPI, *Global Music Report 2017*, p. 17, available at: <http://www.ifpi.org/downloads/GMR2017.pdf> (accessed on 1 August 2018).

³¹ [...].

³² [...].

³³ [...].

³⁴ [...].

confirm relatively limited switching by paid subscribers.³⁵ Younger users³⁶ and free users³⁷ are more likely to "multi-home" by using two or more apps for streaming music.

6.3. Digital music streaming services in the EEA

- (39) In the EEA, the offer of subscription-based or ad-funded music streaming services, excluding video streaming, is concentrated in just a few retailers, namely Spotify Technology S.A. ("Spotify"), Apple Music, Deezer S.A. ("Deezer"), Amazon and Google.
- (40) Spotify launched its music streaming services in 2008 and is the market leader in the EEA. The company was recently publicly listed (April 2018) and, in May 2018, it reached over 160 million monthly active users, including 75 million paying subscribers ("Premium Subscribers") and 90 million ad-funded users ("Freemium Subscribers") across 65 countries.³⁸ This growth has also been sustained by a commercial offering of Spotify's services to mobile operators who resell Spotify services or, more often, bundle them with, for example, TV and/or broadband services for a fixed monthly fee.
- (41) Apple Music, launched in 2015, has very rapidly become the second largest provider of music streaming services in the EEA, with a fast growing subscriber base of 50 million users worldwide at the beginning of 2018, of which around 8 million users are on a free trial and over 40 million are paying subscribers.³⁹ Apple Music adopts a paying-for music streaming model with the possibility of a limited free trial to encourage customers to become paying subscribers. Apple has few limited partnerships with telecoms operators in the EEA. Apple Music is pre-installed on the iOS devices and offered on a standalone basis via an app on Android devices.
- (42) Deezer launched the first streaming service in the EEA in 2007, with a relatively small catalogue. Until 2011, Deezer was available only in a limited number of countries in the EEA (France, Belgium and the United Kingdom). Since then, it has expanded its services worldwide to reach 180 countries, with a catalogue of 53 million songs and, in 2018, 14 million active users.⁴⁰ Similar to Spotify, Deezer has a premium as well as a freemium offer, and has supported its user base's growth in the EEA by bundling its music streaming service with mobile services (in particular, in partnership with Orange S.A.). Deezer also integrates in its apps a technology ("Songcatcher") which enables it to offer music recognition functionalities to its customers.

³⁵ Spotify reported in its IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018), that its churn rate in the fourth quarter of 2017 was 5.1 %, meaning that 5.1 % of paid subscribers cancelled their subscription in the fourth quarter of 2017.

³⁶ See "Younger consumers use two or more apps for streaming music, mobile messaging, says Nielsen", available at: <https://techcrunch.com/2017/08/21/younger-consumers-use-two-or-more-apps-for-streaming-music-mobile-messaging-says-nielsen/?guccounter=1> (accessed on 1 August 2018).

³⁷ [...].

³⁸ See "Spotify Technology S.A. Announces Financial Results for First Quarter 2018": <https://investors.spotify.com/financials/press-release-details/2018/Spotify-Technology-SA-Announces-Financial-Results-for-First-Quarter-2018/default.aspx> (accessed on 1 August 2018).

³⁹ See "Apple CEO Says He Told Trump Tariffs Are Wrong Approach to China": <https://www.bloomberg.com/news/articles/2018-05-15/apple-ceo-says-he-told-trump-tariffs-are-wrong-approach-to-china> (accessed on 1 August 2018).

⁴⁰ See: <https://www.deezer.com/it/company/about> (accessed on 1 August 2018).

- (43) Amazon, which launched a premium, ad-free music streaming service, “Amazon Music Unlimited”, at the end of 2016, is the most recent entrant in the music streaming business. The service is also available as part of the “Amazon Prime” offer to its registered customers (over 100 million in 2018), although in a “lighter” form which allows access only to a restricted part of the catalogue (2 million tracks instead of 50 million) and for a limited period of time (40 hours maximum per month instead of unlimited access). Amazon Music's subscriber base is estimated in 2017 as being over 16 million, across Amazon Prime Music and Amazon Music Unlimited, over 30 countries.
- (44) Google also offers an on demand music streaming service, “Google Play Music”, which was originally launched in 2011 as a paid download service. Google Play Music is preinstalled on the Android OS and offered on a standalone basis via an app on iOS devices. Google's Play Music's catalogue is comparable to those of other players, with 40 million tracks and is available worldwide upon subscription. In May 2018, Google announced the launch of another music streaming service, YouTube Music, which would replace Google Play Music by 2019.

6.4. The interaction between ACR software solutions and the digital music industry: music recognition software solutions

- (45) ACR software solutions are based on audio identification technologies, which use a device's microphone to recognize (audio or video) content based on two different methodologies, so called "fingerprinting" and "watermarking".
- (46) Fingerprinting is based on the generation of unique fingerprints from the content itself which is then stored in a reference database. Audio signals captured by a media device containing ACR support (typically a smartphone or a tablet) are matched with the reference database to identify the captured content. The core of the technology lies in the quality of the algorithms aimed at extracting recognizable data points from the audio signal. The reference database (and associated business processes) is built and engineered to maximize the number of audio samples gathered (for example, for a given song).
- (47) Conversely, watermarking requires inserting digital tags containing specific information about the content into the content file itself prior to its distribution. Watermarking thus adds information, embedding it, within a video or an audio signal. Devices containing ACR support read the watermarks instead of actually recognising the played content by matching it with a reference database. Watermarking requires a technological infrastructure aimed at adding the watermark at the source of content creation. The core of the technology lies in the quality of the algorithms aimed at inserting data into the audio signal. The back-end database is typically smaller and much easier to search than the reference database needed for the fingerprinting methodology.
- (48) Music recognition software solutions are part of the broader category of ACR software solutions and are specifically used to identify music content. Music recognition software solutions based on fingerprinting technology recognise music by matching music fingerprints generated on users' devices with a reference database of fingerprints. In order to have a music catalogue that is representative of what users may seek to identify, providers of music recognition software solutions need first to

source fingerprints corresponding to popular music which are provided by music labels and music streaming or download service providers and music aggregators.⁴¹

- (49) ACR software solutions, including music recognition software solutions, are used on different platforms having an enabled microphone.
- (50) ACR software solutions, including music recognition software solutions, developed in app format ("ACR apps" and "music recognition apps") for smart mobile devices, smart TV and smart watches, enable users to obtain additional information about the content they have just experienced without any user based input or search efforts.
- (51) Apps providing music recognition functionalities either rely on their own ACR software solution, such as the solution provided by SoundHound, Inc. ("SoundHound") or Shazam, or they are powered by third party providers (for example, Deezer, MusixMatch S.p.A. ("Musixmatch") and Genius Media Group, Inc. ("Genius") apps rely on the software solution provided by ACRCLOUD Limited ("ACRCLOUD")).

6.5. ACR software solution providers in the EEA

- (52) Several providers of ACR software solutions, based on both fingerprinting and/or watermarking methodologies, are active in the EEA.
- (53) Shazam is available as apps for smartphones, tablets and personal computers whose core functionality is to allow consumers to recognize music based on fingerprinting.⁴² Shazam's users are predominantly using [...] to access its services. Shazam's technology also powers music recognition functionalities of third parties (including, in particular, Apple's virtual assistant Siri and Snapchat's music recognition functionalities within the Snapchat social network services).⁴³
- (54) Gracenote, Inc. ("Gracenote"), controlled by the global information and data group Nielsen, provides music, video and sports metadata based on fingerprinting ACR technology to entertainment services and companies, worldwide. Its main service offerings include: (i) music recognition services, to enable third party apps and software solutions to identify songs;⁴⁴ (ii) music data, providing a collection of music data; (iii) services for TV and over-the-top providers. Moreover, Nielsen connects Gracenote viewership data to a wide spectrum of Nielsen, first- and third-party consumer data for person-level consumer insights, as well as hundreds of integrated paid and owned media platforms for marketing activation.⁴⁵

⁴¹ White label providers or music aggregators are platforms that provide access to an existing large and diverse digital music catalogue and perform the clearing of rights (obtaining licences from the record labels to sell the music catalogue digitally), the settling of technological issues, including digital rights management systems, the creation of online music storefronts, secure billing systems and delivery networks. The main white label providers include 7 Digital, Nokia/OD2 and MusicLoad. These white label providers service many of the music services operated by Internet Service Providers and specialist bricks-and-mortar retailers. There are music aggregators that collect rights from a range of rights holders and supply them to digital music stores, as well as specialized digital distributors that retail and market music via online and mobile channels. See Commission decision of 19 April 2012 in Case M.6459 - *Sony/Mubadala/EMI Music Publishing*, paragraph 78.

⁴² [...]. See Form CO, paragraph 85, as well as Apple's White Paper on ACR technology of 19 June 2018, paragraph 5.

⁴³ Apple does not offer music recognition functionalities as part of a standalone product.

⁴⁴ Gracenote does not offer apps or software solutions for consumers.

⁴⁵ See: <http://www.nielsen.com/us/en/press-room/2017/nielsen-launches-first-person-level-tv-dmp-powered-by-gracenote-smart-tv-viewership-data.print.html> (accessed on 1 August 2018).

- (55) ACRCLOUD is a Chinese company which develops ACR software solutions based on fingerprinting technology. ACRCLOUD relies on a database of over 40 million music fingerprints. Its main service offerings includes: (i) music recognition services, to enable third party apps and software solutions to identify songs;⁴⁶ (ii) broadcast monitoring services, which are designed for media monitoring and analysis agencies, labels, broadcasters, media operators, content owners to monitor and measure content's performance and to protect copyright; (iii) second screen synchronization solutions to boost second screen viewing experiences of recorded content for broadcasters, content owners, advertisers and app developers.⁴⁷
- (56) Audible Magic Corporation ("Audible Magic") is a provider of ACR software solutions based on fingerprinting technology. It provides content identification for major customers such as Facebook, SoundCloud, the streaming video services Twitch and Vimeo and the telecommunications operator Verizon Wireless.⁴⁸ Its ACR software solution is also used to provide copyright complacency services.⁴⁹
- (57) SoundHound is an audio and speech recognition software provider, whose products are based on fingerprint ACR technology. Its main products are "Houndify" (a voice-AI developer platform), "Hound" (a voice-enabled digital assistant), and "SoundHound" (a music recognition mobile app for consumers).⁵⁰
- (58) Information.io GmbH ("Tonio") is an Austrian company which develops and distributes apps based on watermarking ACR technology to allow broadcasters (for example, TV channels and radio stations) to send program-associated messages and information which can be "read" through the Tonio app.
- (59) Digimarc Corporation ("Digimarc") is a global technology company which develops ACR software solutions based on the watermarking technology.⁵¹
- (60) MusicTrace GmbH ("MusicTrace") is a German company which develops ACR software solutions based on watermarking technology.⁵²
- (61) Google search app for iOS, Windows and Android offers Voice Search among other functions to search the web. The Google search app can perform music recognition functionalities. In late 2017, Google released the Pixel 2 phone running the Android OS. Google introduced the "Now Playing" feature with the Google Pixel 2 launch, which allows a user to ask the Pixel 2 to identify automatically a song playing in the user's physical environment.
- (62) MusixMatch is an Italian company maintaining the catalogue of song lyrics and lyric translations. It has expanded into music recognition, by providing an app, powered by ACRCLOUD's music recognition technology. The MusixMatch app allows for the identification of music and provides users with associated content, in particular displaying lyrics of the recognized songs.
- (63) Finally, Genius is also the provider of an app embedding as ACR software solution powered by ACRCLOUD.

⁴⁶ ACRCLOUD does not offer apps or software solutions for consumers.

⁴⁷ See: <https://www.acrcloud.com/> (accessed on 1 August 2018).

⁴⁸ Audible Magic does not offer apps or software solutions for consumers.

⁴⁹ See: <https://www.audiblemagic.com/about/> (accessed on 1 August 2018).

⁵⁰ See <https://www.soundhound.com/about> (accessed on 1 August 2018).

⁵¹ See: <http://www2.digimarc.com/1/7182/2013-06-20/18g75> (accessed on 1 August 2018).

⁵² See: <https://www.musictrace.de/index.php/about-us> (accessed on 1 August 2018).

6.6. The role of data in the digital music industry

- (64) As described in Section 6.2, the music industry is undergoing a significant change with a shift from physical to digital distribution. In this environment, user data already plays an important role today and that role is likely to grow in the future in the music industry. Such data may include: (i) device data (for example, unique device identifier, device language, operating system), (ii) demographic data (for example, name, gender, age); and (iii) behavioural data (for example, user's clicks in app, the time users spend in various screens, microphone volume level, track titles, artists, time and location of when a song has been played, the reason why a song stopped playing, social media activity).
- (65) The user data gathered by the players in the music industry has several different uses, including but not limited to: (i) development of new methods for delivering music to consumers; (ii) generation of data analytics; (iii) helping artists to understand their performance; (iv) identification of new music trends and prediction of future music hits; (v) understanding the music tastes of listeners in order to offer personalised playlists and provide music recommendations; and (vi) targeting advertising.
- (66) In the past, in order to gather similar data and generate useful insights, the music industry relied primarily on more traditional sources of information, such as physical sales data and how often songs were played on the radio. Today, with the transformation brought by digitisation, there are more players active at different levels of the music industry value chain and more data is available. In fact, the industry can rely on more precise information not only on what people are listening to, but also on where, when and through which device they are listening to it.
- (67) Further, digital distribution, and in particular music streaming, increase accessibility and convenience for users and allow for more personalization of the music experience.
- (68) Similarly to other players active in the industry, each of Shazam and Apple collect data on their users and their activity through their respective apps and services.
- (69) Shazam currently collects (i) a set of information regarding the user's identity, which varies depending on whether the individual user opts to be anonymous⁵³ or to access the Shazam app through a registered account;⁵⁴ (ii) [...];⁵⁵ (iii) the user's recognition activity performed through the Shazam app which includes, for each song recognized by the user, the track title, the artist, the time at which the song was recognized, and the location where the app was used (if the user has given this permission, otherwise only information on the country where the song was recognized is collected) (the data collected on the user's recognition activity is referred to in this Decision as "Shazam's User Behavioural Data"); and (iv) which buttons or features within the

⁵³ The Parties estimates that [...] % of the daily active users of the Shazam app are not registered users, that is the users have installed the Shazam app and use it without creating a Shazam account. For such users, Shazam creates an identifier, consisting of an arbitrary sequence of digits, to tie the user's information to a single area in the Shazam database so that, for example, the Shazam history is available for the individual user; see Form CO, paragraph 306.

⁵⁴ The Parties estimates that, for the [...] % of users which have created a Shazam account, Shazam has the following information: (i) if the user has signed up for registration through email, the user's email address; (ii) if the user has signed up through Facebook logging in service and his/her privacy settings allows the exchange of information, the user's Facebook identifier, email address, birthday, Facebook Friends List and current city; see Form CO, paragraph 310 and response to RFI12, question 2.b.

⁵⁵ In this respect, see in further detail Section 8.4.2.1.

Shazam app itself the user clicks on.⁵⁶ In this Decision, the data described in (i) to (iv) is referred to as "Shazam User Data".

- (70) On the basis of Shazam's User Behavioural Data, Shazam publishes and offers for free on its website and apps music data charts identifying songs and artists that are showing strong positive momentum within the Shazam app in a certain geographic territory ("music discovery charts"). Shazam also licenses music data charts in customised format and the raw music data used to compile its music discovery charts. Shazam further offers the "Shazam for Artists" programme, which includes access to music discovery charts in a standardised format to artists and music labels.
- (71) When consumers use Apple Music,⁵⁷ notably by playing video and audio content, Apple collects information on: title and artist of the video and audio played on the app; [...]; content the users "love", comment, or share; the time at which the song was played, and the time at which the song stopped playing; [...]; where in Apple Music the song was played; device level information (for example [...]), the user's Apple identifier, and the user's Internet protocol ("IP") address.⁵⁸ Similar information is collected by Apple on [...].
- (72) Such information is used by Apple in order to produce personalized musical recommendations for its own subscribers, as well as to offer data products similar to those offered by Shazam to the general public. Notably, Apple displays for free on its websites and apps music charts based on its iTunes sales data ("music consumption charts"). Such data can provide useful insights to music labels and artists on the performance and "trendiness" of their repertoire. Moreover, in January 2018 Apple has launched "Apple Music for Artists", which includes a dashboard giving artists access to a database on consumers' listening and buying habits.
- (73) Similar music databases are compiled by digital music distributors, including digital music streaming providers such as Amazon, Spotify and Deezer.⁵⁹
- (74) Finally, both Parties use third party music data to perform their activities. This includes in particular: digital music master recording files, [...], and music tracks metadata, such as the publishing information (name of the track, artist, producer, album, songwriter etc.). Music labels and music aggregators provide this data on a non-exclusive basis to the various players active in the music industry.⁶⁰

7. RELEVANT MARKETS

- (75) For the assessment of the Concentration, the following business activities of the Parties are relevant: (1) Apple develops OSs for its smart mobile devices (tablets and smartphones), PCs, smart watches and smart TVs, for which third parties can

⁵⁶ [...], see Form CO, paragraph 316.

⁵⁷ Apple Music's subscribers can create a profile comprised of their user handle, display name, and, if desired, a profile photo, biography, and other information which can appear alongside comments a user posts and activity a user shares on Apple Music, see Form CO, paragraph 327.

⁵⁸ If a subscriber of Apple Music has signed up for registration through a mobile network carrier, the user's phone number will be sent to Apple and will be associated with the playback activity, see Form CO, paragraph 328.

⁵⁹ In this respect, see in more detail Section 8.4.2.2(c)(v).

⁶⁰ No concern has been raised in the market investigation with respect to the effects of the Concentration in the markets for the acquisition of this data. Notably data providers, which replied to the market investigation, did not raise any concerns about the possible increase of buyer power on the part of Apple vis-à-vis them as a result of the Concentration. Thus, in this Decision the Commission will not further assess the effects of the Concentration with respect to the acquisition of music data.

develop software solutions and apps; (2) Shazam is active in the provision of ACR software solutions, including music recognition apps; (3) Apple is active in the provision of digital music distribution services, which are offered through apps; (4) both Parties are active in the licensing of music data; and (5) both Parties are active in the provision of online advertising services.

7.1. Legal framework

(76) Market definition is a tool to identify and define the boundaries of competition between firms.⁶¹ It has both a product and a geographic dimension.

(77) A relevant product market comprises all those products and services which are regarded as interchangeable or substitutable, by reason of the products' characteristics, their prices and their intended use.⁶² In determining the relevant product market, the Commission assesses demand substitution by determining the range of products which are viewed as substitutes by the consumers.⁶³ Demand-side substitutability is the focus of the Commission's assessment when defining the relevant markets. The Commission may also take into account supply-side substitutability, namely when its effects are equivalent to those of demand substitution in terms of effectiveness and immediacy.⁶⁴ This is the case when suppliers are able to switch production to the relevant products and market them in the short term without incurring significant additional costs or risks in response to small and permanent changes in relative prices.

(78) The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those areas.⁶⁵

7.2. Software solutions platforms

7.2.1. Product market definition

(79) As explained in Section 2 and in recital (75), Apple develops OSs for different types of devices, that is macOS for PCs, iOS for the smartphones “iPhone” and the tablets “iPad”, tvOS for Apple TV and watchOS for Apple Watch.⁶⁶ For the purposes of assessing the Concentration, those OSs are relevant to the extent that third parties develop software solutions and apps, including, among others, music recognition app developers such as Shazam, for those OSs in order to reach end-users of Apple's devices. For this reason, the Commission has analysed OSs as platforms for software solutions and/or apps.

⁶¹ Commission Notice on the definition of relevant market for the purposes of Community competition law (“Market Definition Notice”), OJ C 372, 09.12.1997, paragraph 2.

Given that Apple does not license its OSs to third parties, the existence of any potential markets for licensable OSs is not discussed in this Decision.

⁶² Market Definition Notice, paragraph 7.

⁶³ Market Definition Notice, paragraph 15.

⁶⁴ Market Definition Notice, paragraph 20.

⁶⁵ Market Definition Notice, paragraph 7.

⁶⁶ OSs are system software products that control the basic functions of computing devices such as servers, PCs, smart mobile devices and enable the user to use the device and run application software on it. See Commission decision of 6 December 2016 in Case M.8124 – *Microsoft/LinkedIn*, paragraph 8.

Given that Apple does not license its OSs to third parties, the existence of any potential markets for licensable OSs is not discussed in this Decision.

7.2.1.1. The Notifying Party's view

- (80) In the Form CO, the Notifying Party did not take a firm view on the relevant product market for OSs.
- (81) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not contest the Commission's findings in the Article 6(1)(c) Decision with regards to OSs for PCs, OSs for smart mobile devices and OSs for smart TVs. The Notifying Party noted that OSs for smart watches should not be considered a relevant market in itself and that smart wearables other than smart watches should be included in the same product market as OSs for smart watches.⁶⁷

7.2.1.2. Commission's assessment

- (82) In previous decisions, the Commission has not considered specifically software solutions and/or apps platforms and, in particular, whether a segmentation by device type would be relevant in that respect (that is, between PCs, smart mobile devices, smart TVs, smart watches and/or smart wearables).
- (83) Nonetheless, in *Google/Motorola Mobility*, while leaving the exact market definition open, the Commission took the view that OSs for PCs and OSs for smart mobile devices belong to separate product markets, given that both used different hardware and had different performance capacities.⁶⁸ A similar approach was adopted in *Microsoft/Nokia*⁶⁹ and in *Microsoft/LinkedIn*.⁷⁰ In *Google/Motorola Mobility* the Commission considered that OSs for smartphones and tablets were likely to belong to the same market as OSs for smart mobile devices, in view of their similar functionalities, but it left the market definition open.⁷¹
- (84) The evidence in the Commission's file has not provided any indication which would suggest that, in defining the relevant product market for software solutions and/or apps platforms, it would be appropriate to depart from its previous practice in relation to the definition of the relevant product market for OSs for PCs and OSs for smart mobile devices. The evidence in the Commission's file was also not conclusive on the question as to whether software solutions and/or apps platforms for smart mobile devices constitutes a separate market from software solutions and/or apps platforms for other smart wearables, although it indicates that software solutions and/or apps platforms for smart TVs could be considered a separate market.
- (85) Nonetheless, for the purposes of assessing the Concentration the Commission considers that the exact scope of the relevant product markets for software solutions and/or apps platforms can be left open as the Concentration would not significantly impede effective competition under any plausible market definition.

7.2.2. Geographic market definition

7.2.2.1. The Notifying Party's view

- (86) In the Form CO, the Notifying Party considered that a potential market for OSs for smart mobile devices is at least EEA-wide, if not global.

⁶⁷ Reply to the Article 6(1)(c) Decision, paragraph 152.

⁶⁸ Commission decision of 13 February 2012 in Case M.6381 – *Google/Motorola Mobility*, paragraphs 26 and 29-30.

⁶⁹ Commission decision of 4 December 2013 in Case M.7047 – *Microsoft/Nokia*, paragraph 27.

⁷⁰ Commission decision of 6 December 2016 in Case M.8124 – *Microsoft/LinkedIn*, paragraphs 11-15.

⁷¹ Commission decision of 13 February 2012 in Case M.6381 – *Google/Motorola Mobility*, paragraph 29.

(87) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards geographic market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.2.2.2. Commission's assessment

(88) As mentioned in recital (82), in previous decisions, the Commission has not considered the geographic scope of the relevant product market for software solutions and/or apps platforms, or sub-segments thereof.

(89) Nonetheless, in its previous decisional practice, the Commission has considered the market for OSs for smart mobile devices to be EEA-wide, or even worldwide, but it has ultimately left the exact geographic market definition open.⁷² With regard to the geographic market definition for OSs for PCs, the Commission found in *Microsoft* that the relevant geographic market for client PC OSs was worldwide.⁷³ In *Microsoft/LinkedIn* the Commission considered that the relevant geographic market for OSs for PCs was EEA-wide.⁷⁴

(90) The evidence in the Commission's file has not provided any indication which would suggest that, in defining the relevant product market for software solutions and/or apps platforms (and sub-segments thereof), it would be appropriate to deviate from its previous decisional practice in relation to OSs for PCs and smart mobile devices. The evidence in the Commission's file was also not conclusive on the question as to whether the relevant geographic markets for software solutions and/or apps platforms for smart TVs and smart wearables (including smart watches) and smart watches are EEA-wide or worldwide in scope.

(91) Nonetheless, for the purposes of assessing the Concentration, the Commission considers that the exact geographic scope of the relevant product markets for software solutions and/or apps platforms (and sub-segments thereof) can be left open as the Concentration would not significantly impede effective competition under any plausible market definition.

7.3. Digital music distribution services

7.3.1. Product market definition

7.3.1.1. The Notifying Party's view

(92) In the Form CO, the Notifying Party submitted that the question whether the digital music market should be further segmented into downloading and streaming services could be left open. According to the Notifying Party, no segmentation between digital music distribution apps according to OSs would be relevant.⁷⁵

(93) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards product market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.3.1.2. Commission's assessment

(94) In its previous decisional practice, the Commission has analysed the market for digital music distribution and, while leaving the market definition open, it has found

⁷² Commission decision of 13 February 2012 in Case M.6381 – *Google/Motorola Mobility*, paragraphs 33-35; Commission decision of 4 December 2013 in Case M.7047 – *Microsoft/Nokia*, paragraphs 74-77.

⁷³ Commission decision of 24 March 2014 in case C3/37.792 – *Microsoft*, recital 324-330.

⁷⁴ Commission decision of 6 December 2016 in Case M.8124 – *Microsoft/LinkedIn*, paragraph 18.

⁷⁵ Response to RFI 10, question 15.

evidence that the boundaries between streaming and downloading services were becoming blurred.⁷⁶ The Commission has not specifically assessed previously whether further segmentations, based on the type of software solution or the nature of the service, would be appropriate.

- (95) The market investigation in this case did not provide a conclusive finding as to whether music downloading services and music streaming activities form part of the same product market. That said, the market investigation results indicated that some music streaming providers would not consider themselves to be in a position to start offering digital music downloading services in the short term or without incurring significant investments.⁷⁷
- (96) The market investigation was also not conclusive with regard to the need for further segmentation based on the type of software solution offered to distribute digital music, be it a dedicated app for smartphone and/or tablet, apps that perform digital distribution functionalities next to other services (such as video streaming or other non-music distribution related services), or websites that offer music distribution functionalities. The market investigation results indicated, however, that digital music distribution software solutions for PCs or websites offering music distribution functionalities only exert a limited competitive constraint on dedicated apps for digital music distribution. Further, a segmentation by OSs does not appear to be relevant.⁷⁸
- (97) The Commission notes that, during the market investigation, concerns were raised with respect to the effects of the Concentration only in relation to the possible product market for digital music streaming apps. Moreover, as further explained in Section 8.4.2.2(a), the Commission notes that a possible product market for such apps is the only one for which a relevant link exists between the activities of Apple and the activities of Shazam, namely the “referrals” to certain digital music streaming apps on both iOS and Android, including for example Apple Music.
- (98) As regards digital music downloading services, the Commission notes that pre-Transaction, Shazam has referral partnerships [...]. iTunes is not available on Android smart mobile devices. Therefore, even if Apple were to engage in any of the practices discussed in Section 8.4.2.2., no anticompetitive effect could arise.
- (99) Therefore, it is not necessary in this case to analyse further the market for digital music downloading services. For the purposes of assessing the effects of the Concentration, the Commission considers that the narrowest relevant product market is the one for digital music streaming services for smart mobile devices, excluding video streaming services,⁷⁹ and the competitive assessment should therefore be carried out on that basis.

7.3.2. *Geographic market definition*

7.3.2.1. The Notifying Party's view

- (100) In the Form CO, the Notifying Party submitted that digital music services are readily available online in many countries with little difference in the service or features offered. Moreover, licensing deals for music are typically entered into globally by

⁷⁶ See Commission decision of 25 July 2014 in Case M.7290 - *Apple/Beats*, paragraphs 18-19.

⁷⁷ Responses to questionnaire to digital music distributors - Q6, question 32.

⁷⁸ Responses to questionnaire to digital music distributors - Q6, questions 14 and 15.

⁷⁹ In the following any reference to "digital music streaming apps" refers to such dedicated music streaming services, excluding video streaming services, for smart mobile devices .

digital music service providers and not on a country-by-country basis. Therefore, the relevant product market should no longer be considered national in scope, but rather global. Ultimately, the Notifying Party argued that the geographic market definition could be left open.

- (101) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards geographic market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.3.2.2. Commission's assessment

- (102) As regards the geographic scope, the question whether the market for digital music distribution services is national or EEA-wide has been left open by the Commission in its previous decisional practice.⁸⁰ The Commission has not analysed the geographic scope of a (narrower) market limited to digital music streaming apps.
- (103) The market investigation was not conclusive as to whether prevailing differences in customer demand and expectations for digital music distribution apps in each EEA country continue to warrant a geographic market definition based on national markets.⁸¹
- (104) For the purposes of assessing the Concentration, the question as to whether the geographic scope of the relevant product market for digital music streaming apps on smart mobile devices is EEA-wide or national can be left open as the Concentration would not significantly impede effective competition under any plausible geographic market definition.

7.4. ACR software solutions, including music recognition apps

7.4.1. Product market definition

7.4.1.1. The Notifying Party's view

- (105) In the Form CO, the Notifying Party submitted that all methods of recognising music, including but not limited to manual searches, and the provision of ACR technology are part of the same relevant product market. In particular, the Notifying Party submitted that the relevant market encompasses not only music recognition apps, such as the Shazam app, but also web-based solutions offering music recognition, as well as other software solutions offering music recognition functionality. According to the Notifying Party, the market of music recognition services should not be further segmented according to the technology used, the functionalities offered, the device or the OS. The Notifying Party argued that, in any event, even a narrower market definition of music recognition services would not lead to any competition issues and, as such, the exact market definition could be left open.
- (106) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards product market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.4.1.2. Commission's assessment

- (107) In previous decisions, the Commission has not specifically assessed ACR or music recognition software solutions or, more narrowly, ACR and music recognition apps.

⁸⁰ Commission decision of 25 July 2014 in Case M.7290 - *Apple/Beats*, paragraphs 20-21.

⁸¹ Responses to questionnaire to digital music distributors - Q6, questions 34 and 35.

- (108) Overall, the market investigation did not provide a conclusive finding as to whether the relevant product market is limited to dedicated stand-alone music recognition apps for a specific device type (that is, smart mobile devices, TVs, PCs, smart watches) that only perform music recognition functionalities, or whether it has to be defined as a broader market covering also apps or software solutions for all device types as well as web-based solutions that perform music recognition as part of a broader offering, or even a market encompassing all ACR software solutions.⁸²
- (109) The market investigation, nonetheless, provided some indications that apps that perform music recognition functionalities as part of a broader offering are likely to be a viable alternative for users of dedicated music recognition apps, whereas desktop-based or web-based software solutions appear to exert only limited constraints on dedicated music recognition apps for smart mobile devices.⁸³
- (110) From the market investigation it also appears that, from a user perspective, both technologies used to perform ACR functionalities, namely fingerprinting and watermarking, serve the same purpose. This would suggest that software solutions and apps based on both technologies are part of the same relevant product market.⁸⁴ From the supply-side perspective, as described in Section 6.4, the two technologies have significant differences, in particular in terms of the data and algorithms required.
- (111) The Commission notes that Shazam's market position would be significantly less relevant in a market including ACR and music recognition software solutions for other devices than smart mobile devices, music recognition software solutions which perform music recognition as part of a broader offering, web-based solutions or even a market encompassing all ACR software solutions.
- (112) Moreover, as further explained in Section 8.4.2.2(a), the Commission notes that, in the course of the market investigation, complaints have been made in relation to the leveraging of Shazam's market position in the provision of music recognition apps on smart mobile devices.
- (113) Finally, as further explained in Section 8.4.3, the Commission notes that, in the course of the market investigation, it received a complaint in relation to the effects of the Concentration in the market for ACR software solutions and, in particular, ACR apps for PCs, smart mobile devices, smart watches and smart TVs. Those effects would be the result of leveraging Apple's market position in software solutions platforms for PCs, smart mobile devices, smart watches and smart TVs.
- (114) Therefore, for the purposes of assessing the Concentration, the Commission considers that the effects of the Concentration should be assessed on the narrowest relevant product market for the provision of dedicated stand-alone music recognition apps for smart mobile devices, as well as on the broader possible markets for ACR software solutions for each of PCs, smart mobile devices, smart wearables (including smart watches), smart watches and smart TVs. The question as to whether a segmentation of the relevant product market should also be made according to the underlying technology (watermarking or fingerprinting) should be left open.

⁸² Responses to questionnaire to providers of music recognition software solutions - Q5, questions 9 to 24.

⁸³ Responses to questionnaire to providers of music recognition software solutions - Q5, question 9, 19 and 23.

⁸⁴ Tonio's written submission of 28 March 2018.

7.4.2. *Geographic market definition*

7.4.2.1. The Notifying Party's view

(115) In the Form CO, the Notifying Party submitted that the geographic market for music recognition services is worldwide, or at least EEA-wide, given that the same solutions are typically available in multiple countries throughout the world, with only minor adaptations.

(116) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards geographic market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.4.2.2. Commission's assessment

(117) Respondents to the market investigation considered that there were generally no differences in customer demand and requirements for software solutions offering ACR software solutions, including music recognition software solutions, across the various countries of the EEA.⁸⁵

(118) Therefore, the Commission considers that, for the purposes of assessing the Concentration, the geographic scope of the relevant product market is at least EEA-wide.

7.5. Licensing of music data

7.5.1. *Product market definition*

(119) As explained in Section 6.6, both Parties license music charts data. No overlap arises in relation to the Parties' user behavioural data, which is not licensed by the Parties to third parties.⁸⁶

7.5.1.1. The Notifying Party's view

(120) During the first phase investigation, the Notifying Party submitted that the publication of music data charts and similar music data analytics does not correspond to a specific activity belonging to a relevant product market, but is instead an ancillary feature of the core business of music streaming or voice recognition.⁸⁷ However, if a market existed for the collection of data on individuals' music tastes and the analytics of such data, such a market should, according to the Notifying Party, not be limited to data collected in the digital music industry, but should cover all data compiled relating to music preferences, including data gathered by undertakings active in the wider field of online social networks, such as LinkedIn, Facebook, WhatsApp or Google which collect the same type of data on their users, and even additional and more valuable information.⁸⁸

(121) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards product market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

⁸⁵ Responses to questionnaire to providers of music recognition software solutions - Q5, question 25 and 25.1.

⁸⁶ In relation to Shazam's User Data as possible competitive advantage, to improve existing functionalities, or offer additional functionalities, on digital music streaming apps (regardless of whether it constitutes a relevant product market or segment), see Section 8.4.2.2(c)(v).

⁸⁷ Response to RFI 10, question 28, p. 29.

⁸⁸ Form CO, paragraphs 169-170.

7.5.1.2. Commission's assessment

- (122) The Commission has not considered the market for the licensing of music data in previous decisions.
- (123) In the market investigation, the Commission has investigated the degree of substitutability (or complementarity) between the Parties' different data products, notably their music data charts. In this respect, the majority of the respondents to the market investigation indicated that Shazam's charts are complementary to rather than substitutable for Apple's charts because the music charts compiled by Shazam may give an indication of the popularity of certain music tracks, as well as of future music trends (music "discovery") while Apple's charts reflect estimates of Apple's own music sales and/or usage patterns (music "consumption").⁸⁹
- (124) For the purposes of assessing the Concentration, the Commission considers that it is not necessary to conclude whether Shazam's music discovery charts and Apple's music consumption charts belong to the same product market as the Concentration would not significantly impede effective competition in respect of the licensing of music data under any plausible market definition.

7.5.2. *Geographic market definition*

7.5.2.1. The Notifying Party's view

- (125) During the first phase investigation, the Notifying Party submitted that the geographic market for the licensing of music data is at least EEA-wide, and it could possibly be worldwide, in scope. According to the Notifying Party, it does not seem that there are any differences between collecting this data in one country compared with collecting it in another. Furthermore, the relevant companies active in this space are generally active on a global basis. At any rate, according to the Notifying Party, the exact geographic market definition can be left open as, irrespective of the exact market definition adopted, the Concentration will not have any adverse effect on competition.
- (126) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards geographic market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.5.2.2. Commission's assessment

- (127) The results of the market investigation were not conclusive on the geographic scope of the licensing of music data as the undertakings offering such services are generally active both in the EEA and worldwide, although a few local providers also exist (especially, for data on music popularity).⁹⁰
- (128) Nonetheless, the Commission considers that, for the purposes of assessing the effects of the Concentration, even in a scenario where the licensing of music data by the Parties is part of the same product market, the geographic scope of the relevant product market can be left open as the Concentration would not significantly impede effective competition under any plausible market definition.

⁸⁹ Responses to questionnaire to recorded music companies and music aggregators – Q8, question C.1.1., responses to questionnaire to digital music distributors - Q6, question g.51.1, and responses to questionnaire to providers of music recognition software solutions - Q5, question 35.

⁹⁰ Response to questionnaire to digital music distributors - Q6, question 51.1.

7.6. Online advertising

7.6.1. Product market definition

(129) Shazam is offering online advertisement mainly through displaying ads in the Shazam app (for example, [...]). [...] complemented by brand-specific audio or visual content in the Shazam app (for example, an in-app commercial) [...].⁹¹ The brand-specific advertising product is marketed under the name "Shazam for Brands".

(130) Apple does not offer online advertising services on Apple Music or iTunes. It is only active in the online advertising space in a limited way through its Apple News service. The Apple News app is a news aggregator launched by Apple in 2015 and, so far, is available in the EEA only to users in the United Kingdom.

7.6.1.1. The Notifying Party's view

(131) In the Form CO, the Notifying Party submitted that the Concentration could be analysed on the basis of a market consisting of online advertising services. According to the Notifying Party no separate market for online advertising for music enthusiasts would exist and, in any event, in such market the Parties' activities would not overlap.

(132) In the Reply to the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards product market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.6.1.2. Commission's assessment

(133) In past decisions, the Commission considered the market for online advertising to be separate from the market for offline advertising. It also considered possible further segmentations between search and non-search advertising or on the basis of the platform (PCs, smart mobile devices), but it ultimately left the market definition open.⁹²

(134) The evidence in the Commission's file has not provided any indication which would suggest that, for the purposes of assessing the Concentration, it would be appropriate to deviate from its prior decisional practice. The same evidence has not provided conclusive indications as to whether it would be possible to identify a separate market or segment for online advertising for music enthusiasts, where only Shazam would be active and there would be no overlap between the Parties' activities.

(135) In any event, the Commission considers that, for the purposes of assessing the Concentration, the product market definition can be left open as the Concentration would not significantly impede effective competition in relation to online advertising under any plausible market definition.

7.6.2. Geographic market definition

7.6.2.1. The Notifying Party's view

(136) In the Form CO, the Notifying Party submitted that the exact geographic market definition could be left open.

⁹¹ Response to RFI 12.

⁹² See Commission decision of 21 December 2016 in Case M.8180 – *Verizon/Yahoo*, paragraphs 22-25; Commission decision of 6 December 2016 in Case M.8124 – *Microsoft/LinkedIn*, paragraphs 159-161; Commission decision of 3 October 2014 in Case M.7217 – *Facebook/WhatsApp*, paragraphs 74-79.

- (137) In the Reply to o the Article 6(1)(c) Decision, the Notifying Party did not bring forward any additional argument as regards geographic market definition, nor did it contest the Commission's findings in the Article 6(1)(c) Decision.

7.6.2.2. Commission's assessment

- (138) With reference to the geographic scope of the online advertising market and its possible sub-segments, in previous cases the Commission noted that they should be defined as national in scope or alongside linguistic borders within the EEA.⁹³
- (139) The evidence in the Commission's file has not provided any indication which would suggest that, for the purposes of assessing the Concentration, it would be appropriate to deviate from its previous decisional practice.
- (140) For the purposes of assessing the Concentration, the Commission therefore concludes that the market for online advertising and its possible sub-segments should be defined as national in scope or alongside linguistic borders within the EEA.

8. COMPETITIVE ASSESSMENT

8.1. Introduction

- (141) Shazam was incorporated and listed in the early 2000s. It launched its first music recognition app (for iPhones) in 2008. [...].
- (142) [...].⁹⁴
- (143) The Notifying Party submitted that, by acquiring Shazam, Apple would have the opportunity to make better use of Shazam's recognition services with Apple's products and services by joining Apple's technological knowhow with that of Shazam's. According to the Notifying Party, the Concentration "*will thereby make the existing and future functionality available to Apple's user base in a faster way, while at the same time enriching the quality of Apple's product offering incorporating Shazam's recognition services beyond which each firm could achieve separately.*"⁹⁵
- (144) In this context the Commission notes that the Concentration mainly combines Apple's and Shazam's complementary services (software solutions platforms and digital music streaming services for Apple and ACR software solutions, and in particular music recognition apps, for Shazam). While both Apple and Shazam are active in licensing music data and both provide some online advertising services, these activities are not their core business. Hence, the Concentration only gives rise to limited horizontal overlaps while, at the same time, giving rise to some non-horizontal relationships.

⁹³ See Commission decision of 21 December 2016 in Case M.8180 – *Verizon/Yahoo*, paragraphs 27-28; Commission decision of 6 December 2016 in Case M.8124 – *Microsoft/LinkedIn*, paragraphs 163-164; Commission decision of 3 October 2014 in Case M.7217 – *Facebook/WhatsApp*, paragraphs 44 and 83; Commission decision of 4 September 2012 in Case M.6314 – *Telefónica UK/Vodafone UK/Everything Everywhere/JV*, recitals 226-229; Commission decision of 18 February 2010 in Case M.5727 – *Microsoft/Yahoo! Search Business*, paragraphs 91-93; Commission decision of 11 March 2008 in Case M.4731 – *Google/DoubleClick*, recitals 83-84.

⁹⁴ For example, Facebook's 2012 acquisition of Instagram for USD 1 billion, Microsoft's acquisition of Skype for USD 8.5 billion, Facebook's 2014 acquisition of WhatsApp for USD 19 billion or Microsoft's 2016 acquisition of LinkedIn for USD 26 billion.

⁹⁵ Form CO, paragraph 11.

- (145) After having illustrated the Parties' market position in the relevant markets in Section 8.2, the horizontal and non-horizontal effects of the Concentration are assessed in Sections 8.3 and 8.4 respectively.

8.2. Market shares

- (146) According to the Horizontal Merger Guidelines and the Non-Horizontal Merger Guidelines,⁹⁶ in the assessment of the effects of a merger, market shares constitute a useful first indication of the structure of the markets at stake and of the competitive importance of the relevant market players.

8.2.1. Software solutions platforms

- (147) As explained at recital (79), third parties develop software solutions and apps for Apple's OSs in order to reach end-users of Apple's devices. Therefore, the Commission considers Apple's share of shipments for each type of device to be the best proxy for calculating Apple's position as a software solutions platform in the EEA and worldwide.⁹⁷
- (148) With respect to **PCs**, based on IDC⁹⁸ data, the Notifying Party estimates that Apple had a share by shipment of approximately [5-10]% in the EEA in 2017.⁹⁹
- (149) With respect to **smart mobile devices**, based on IDC data, the Notifying Party estimates that Apple had a worldwide share by shipment of approximately [10-20]% and a share of approximately [20-30]% in the EEA in 2016.¹⁰⁰
- (150) With respect to **smart wearables including smart watches**, based on IDC data, the Notifying Party estimates that Apple had a share by shipment of approximately [20-30]% in the EEA in 2017.¹⁰¹ With respect to **smart watches** market segments, based on IDC data, Apple had a share by shipment of approximately [50-60]% in the EEA in 2017.¹⁰²
- (151) With respect to **smart TVs**, the Notifying Party was not able to provide any shares at EEA level. Based on the estimate provided by the Notifying Party, Apple would have a share by shipment of [10-20]% at worldwide level.¹⁰³

8.2.2. Digital music streaming apps

- (152) The Notifying Party claimed that, to the best of its knowledge, there is no reliable source of information that would allow market shares in the field of digital music distribution to be quantified accurately. According to the Notifying Party, estimating market shares in this field is difficult due to the lack of reliable publicly available

⁹⁶ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings ("Horizontal Merger Guidelines"), OJ C 31, 05.02.2004, paragraph 14; Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings ("Non-Horizontal Merger Guidelines"), OJ C 265, 18.10.2008, paragraph 24.

⁹⁷ The Commission considers that there is no need to calculate Apple's market shares for the narrowest possible markets since Apple's software solutions platforms are the only ones available on Apple's devices.

⁹⁸ International Data Corporation ("IDC") is a market intelligence company, see: <https://www.idc.com/about> (accessed on 1 August 2018).

⁹⁹ Form CO, paragraph 298.

¹⁰⁰ Form CO, paragraph 290. Separate shares by shipments for smartphones (iPhones) and tablets (iPads) have not been provided.

¹⁰¹ Response to RFI 36, question 10.

¹⁰² Response to RFI 12, question 15.f.

¹⁰³ [...]; see Response to RFI 12, question 15.g.

information and the lack of comparable data between digital streaming distributors and digital downloading distributors on the one hand, and among the various market players in the field of digital streaming on the other hand.¹⁰⁴

- (153) Nevertheless, the Notifying Party estimated that Apple Music's market share in the provision of digital music streaming apps services was [10-20]% in the EEA in 2017 based on revenues and [5-10]% based on subscribers.¹⁰⁵ Moreover, the Notifying Party estimated that, in 2018, Apple Music's market share in the provision of digital music streaming apps services, based on revenues, was [20-30]% in Austria, [10-20]% in France, [10-20]% in Italy, [10-20]% in Spain, [0-5]% in Sweden and [5-10]% in Norway.¹⁰⁶ The Notifying Party submits that Apple Music is not active in Iceland [...].
- (154) The Notifying Party only provided market shares for its main rivals (Spotify, Deezer, Amazon Music and Pandora) at the worldwide level, based on revenues and users in 2017.¹⁰⁷ On the basis of this data, which does not correspond, however, to any plausible market definition, Spotify would be the market leader with a share of [50-60]% based on revenues, but Apple Music (which was launched only in 2015) would have already gained second position, albeit at some distance, with a market share of [20-30]%.
- (155) During the market investigation, the Commission has conducted a market reconstruction collecting confidential data on the total number of subscribers, premium subscribers, revenues and revenues from subscription of digital music streaming apps¹⁰⁸ in the EEA in the years 2015, 2016 and 2017.¹⁰⁹ While the results of the market reconstruction indicate that the Notifying Party's estimates on Apple Music's market share by subscriber are conservative (especially if considering the premium customer group), they are in line with the revenue shares provided by the Notifying Party and confirm that Spotify is still the leading digital music streaming service in the EEA.
- (156) The results of the market reconstruction in the EEA market for the years 2015, 2016 and 2017 show that, by either metric used by the Commission, [...]. Moreover, [...].¹¹⁰
- (157) The results of the market reconstruction in the EEA market for the year 2017 are illustrated in Figure 1.

¹⁰⁴ Form CO, paragraph 234.

¹⁰⁵ Form CO, Tables 7 and 8.

¹⁰⁶ Response to RFI 10, question 15.

¹⁰⁷ Form CO, Tables 22 and 23.

¹⁰⁸ Data have been provided by Apple Music as well as Amazon, SoundCloud, Google Play, Spotify and Deezer, that is five out of the nine competitors in digital music streaming identified by the Parties in the Form CO, Annex 6.3IIIB.(e). Of the remaining four companies, Vevo provided data, but they have not been included in the market reconstruction given the different nature of the service offered by Vevo (that is, music video streaming): however, even if included, the data provided by Vevo does not have a material impact on the results of the market reconstruction. Tidal, Napster and Pandora did not provide a response. However, the Commission considers the market reconstruction as representatives: in fact Pandora ([...]) is only available in the United States (<https://www.pandora.com/restricted> (accessed on 1 August 2018)), while Tidal and Napster appear to be extremely small even when considering data on downloads of their respective digital music streaming apps on iOS for the years 2015 to 2017 in the EEA (see Annex Q16.3 to the response to RFI 10) and on Android (see number of installs for each of these apps at <https://play.google.com/store/apps> (accessed on 1 August 2018)).

¹⁰⁹ Responses to questionnaire to digital music distributors - Q6 and responses to RFIs 18, 19, 20, 21 and 22.

¹¹⁰ [...].

Figure 1: Market shares in provision of digital music streaming apps in the EEA (2017)

Providers	Total subscribers		Premium subscribers		Revenues		Subscription fees	
	Number	%	Number	%	EUR	%	EUR	%
Apple Music	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Amazon	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Sound Cloud	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Google Play	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Spotify	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Total	[...]	100%	[...]	100%	[...]	100%	[...]	100%

Source: Commission's market reconstruction.

(158) Based on the evidence collected during the market investigation, the Commission considers that Apple's position at national level in the Referring States as estimated by the Notifying Party is likely to be a reliable proxy for its market position in those countries.

8.2.3. *ACR software solutions, including music recognition apps*

(159) With respect to the broader markets for **ACR software solutions** for each of PCs, smart mobile devices, smart wearables (including smart watches), smart watches and smart TVs, the Notifying Party was not able to provide an estimate of Shazam's position. Based on public information, the Commission notes that ACR software solutions market size was estimated at around USD 900 million in 2016.¹¹¹ In the same year Shazam's revenue from technology licensing was less than USD [...] million¹¹², whereas its overall revenue was USD 54 million. Therefore, even in a scenario where all of Shazam's revenue was obtained through its proprietary ACR technology, Shazam would have a market share of only approximately [5-10]% in the market for ACR software solutions at worldwide level.

(160) With respect to the narrowest product market for the supply of **dedicated music recognition apps for smart mobile devices**, the Notifying Party submits that, to the best of its knowledge, there is no reliable source of information that would allow market shares in the field of music recognition services to be quantified, nor is it aware of third-party sources which track this information. As is the case for digital music streaming apps, according to the Notifying Party, estimating reliable market shares is very difficult given the large number of competitors and the lack of

¹¹¹ See <https://www.marketsandmarkets.com/Market-Reports/automatic-content-recognition-market-148131627.html> (accessed on 1 August 2018).

See also: <https://www.businesswire.com/news/home/20160718005570/en/Automatic-Content-Recognition-Market---Global-Forecast> (accessed on 1 August 2018).

¹¹² Form CO, Table 1.

comparable data among the many music recognition service providers. Moreover, the Notifying Party submits that market shares are a poor proxy for measuring market power in a dynamic market such as the music recognition space.¹¹³

- (161) Nevertheless, the Notifying Party estimates that in the EEA the Shazam app is used by approximately [10-20]% of smart device users ([0-5]% worldwide).¹¹⁴ The Notifying Party estimates that Shazam's market share would remain well below 30% (at approximately [20-30]%) worldwide even using more conservative figures on monthly active users and it considers that there is no reason to believe that Shazam's market share in the EEA would be materially different. The Notifying Party nonetheless considers that these figures are incomplete and that Shazam's market share estimate could be lower since not all music recognition services are included, notably SongCatcher, a functionality recently launched by Deezer on its streaming app, as well as services provided by numerous other companies.¹¹⁵
- (162) The Commission acknowledges that market shares may not be a perfect proxy for measuring market power in recent and fast-growing sectors characterised by frequent market entry and short innovation cycles.¹¹⁶ Nonetheless, the Commission notes that, as acknowledged by the Parties, Shazam is not a start-up company but rather a mature company which has been active on the market for dedicated music recognition services for nearly 20 years¹¹⁷ and launched its first app for smart mobile devices back in 2008.
- (163) The market investigation did not provide any indications of recent disruptive entry or innovation in the market for dedicated music recognition apps for smart mobile devices. On the contrary, during the market investigation, the vast majority of respondents named Shazam as an established player in the supply of music recognition apps for smart mobile devices, with a customer base and a brand image superior to those of the undertakings identified by the Notifying Party in the Form CO as Shazam's competitors.¹¹⁸ Moreover, based on different publicly available rankings, Shazam is consistently the number one free app for the provision of music recognition services on both Android and iOS in all Member States.¹¹⁹ On the basis of this qualitative evidence, the Commission considers that the market shares provided by the Parties are likely to underestimate Shazam's position in the EEA.

¹¹³ Form CO, paragraphs 188-190.

¹¹⁴ Form CO, paragraph 194.

¹¹⁵ Form CO, paragraphs 203-204. In the Form CO, paragraph 116, the Notifying Party identified as main providers of a stand-alone app for music recognition, Shazam, SoundHound, MusicID, Radio Scout, DS Music Recognition, Music Identifier, Beatfind and MusicDNA ID, while as main providers of a stand-alone app not fully dedicated to music recognition but which includes music recognition functionalities it indicated Musixmatch, Genius, Lyrics Mania, Google Sound Search, Google Assistant (in its standalone app format), Hound (in its standalone app format) and Deezer (beta of upcoming version which includes a music recognition functionality). Contrary to the Notifying Party's submission, Spotify does not offer integrated music recognition functionalities (response to questionnaire to digital music distributors - Q6, question 39.1).

¹¹⁶ Commission decision of 3 October 2014 in Case M.7217 – *Facebook/WhatsApp*, paragraph 99. See also Case T-79/12 *Cisco Systems Inc v Commission*, EU:T:2013:635, paragraph 69.

¹¹⁷ Form CO, paragraph 506.

¹¹⁸ Responses to questionnaire to providers of music recognition software solutions - Q5, questions 13 and 30. See also agreed minutes of conference call with Audible Magic of 7 March 2018, para 13.

¹¹⁹ See <https://apptopia.com/store-insights/top-charts/google-play/music-audio/austria> (accessed on 1 August 2018); <https://www.applyzer.com/?mmenu=worldcharts> (accessed on 1 August 2018); <https://www.appannie.com/en/apps/ios/top/italy/music/iphone/> (accessed on 1 August 2018). This finding is based on a review of these rankings considering only music recognition services.

- (164) During the market investigation, the Commission therefore conducted a market reconstruction collecting confidential data on daily and monthly active users of providers of music recognition apps for smart mobile devices¹²⁰ worldwide and in the EEA for the year 2017.¹²¹ The scope of this exercise was limited to the reconstruction of market shares for the narrowest product market for the provision of music recognition apps for smart mobile devices. This is because of the relevance of that product market in assessing the potential anticompetitive effects of the Concentration through the leveraging of Shazam's position. It was on those effects that the Commission received complaints. They are discussed in Section 8.4.2.2.
- (165) The results of the market reconstruction indicate that Shazam is the leading provider of music recognition apps in the EEA as well as worldwide, with a market share well in excess of 30% in the potential market for dedicated music recognition apps for smart mobile devices (in other words, excluding data for the Google Search app from the dataset), and in excess of 30% even in a broader market for apps for smart mobile devices including a music recognition functionality as part of a larger offering (in other words, [...]). Notably, the results of the market reconstruction indicate that Shazam's 2017 EEA market share, based on either monthly or daily active users, would be above [...] in even the broader market for apps for smart mobile devices including a music recognition functionality, and above [...] at worldwide level, as illustrated in Figure 2.

¹²⁰ Data have been provided by Shazam as well as Musixmatch, SoundHound, Deezer and Google, that is four out of the 14 competitors in music recognition identified by the Notifying Party in the Form CO, paragraph 116 and Annex 6.3IIIA.(b) (see footnote 115). The other companies, instead, did not provide an answer to the market investigation. However, the Commission considers the market reconstruction as representative: first, in the market investigation SoundHound has been identified as the main competitor of Shazam by the large majority of respondents, followed by Google (responses to questionnaire to digital music distributors - Q6, questions 5-7, and to questionnaire to providers of music recognition software solutions - Q5, question 3); second, as regards the companies not included in the market reconstruction, they appear to be extremely small even when considering data on downloads on iOS for the years 2015 to 2017 in the EEA (see Annex Q16.3 to the response to RFI 10) and on Android (see number of installs for each of these apps at <https://play.google.com/store/apps> (accessed on 1 August 2018)).

As regards the other companies also indicated as providers of music recognition technology in Annex 6.3IIIA.(b) of the Form CO, the Commission notes that ACRCLOUD and Audible Magic replied to the market investigation but indicated not to be active in the provision of music recognition apps, but only to offer music recognition software solutions to businesses.

¹²¹ Responses to questionnaire to providers of music recognition software solutions - Q5 and responses to RFI 15.

Figure 2: Market shares in provision of music recognition apps in the EEA (2017)

Providers	Daily active users				Monthly active users			
	EEA		Worldwide		EEA		Worldwide	
	000	%	000	%	000	%	000	%
Dedicated music recognition apps for smart mobile devices								
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
MusixMatch	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Shazam	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Sound Hound	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Total	[...]	100%	[...]	100%	[...]	100%	[...]	100%
Music recognition apps for smart mobile devices (including non-dedicated apps)								
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Google	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
MusixMatch	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Shazam	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
SoundHound	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Total	[...]	100%	[...]	100%	[...]	100%	[...]	100%

Source: Commission's market reconstruction.

8.2.4. Licensing of music charts data

(166) The Parties have not been able to provide any market shares or other information on value or volumes with regard to the licensing of music data and, particularly, music charts data. The Notifying Party maintained that many undertakings exchange such data for free, or publish them for free to the general public and that it would therefore be difficult to find adequate metrics to evaluate the market size and the positions of the Parties on such market.

(167) The market investigation has provided indications confirming the Parties' claims that there is a large number of sources of music chart data and on the difficulties of estimating market shares in that respect.¹²²

8.2.5. Online advertising

(168) No overlap arises between the Parties' activities in the national markets, or in markets defined along linguistic borders within the EEA, of any of the Referring

¹²² Responses to questionnaire to recorded music companies and music aggregators – Q8, question C.2, and to questionnaire to advertisers - Q7, question C.1.

States, and Shazam's market share in any of those markets would be, according to the Notifying Party, [0-5]%.¹²³

- (169) The Parties were not able to provide estimates on Shazam's market share in a hypothetical market for online advertising for music enthusiasts. The market investigation has nonetheless provided indications confirming the Parties' claims that other large providers would be active in such a hypothetical market, including Google and Facebook.

8.3. Assessment of horizontal effects

8.3.1. Legal framework

- (170) Under Article 2(2) and (3) of the Merger Regulation, the Commission must assess whether a proposed concentration would significantly impede effective competition in the internal market or in a substantial part of it, in particular through the creation or strengthening of a dominant position.
- (171) The Horizontal Merger Guidelines distinguish between two main ways in which mergers between actual or potential competitors on the same relevant market may significantly impede effective competition, namely non-coordinated and coordinated effects.
- (172) The Horizontal Merger Guidelines describe horizontal non-coordinated effects as follows: "*A merger may significantly impede effective competition in a market by removing important competitive constraints on one or more sellers who consequently have increased market power. The most direct effect of the merger will be the loss of competition between the merging firms. For example, if prior to the merger one of the merging firms had raised its price, it would have lost some sales to the other merging firm. The merger removes this particular constraint. Non-merging firms in the same market can also benefit from the reduction of competitive pressure that results from the merger, since the merging firms' price increase may switch some demand to the rival firms, which, in turn, may find it profitable to increase their prices. The reduction in these competitive constraints could lead to significant price increases in the relevant market.*"¹²⁴
- (173) The Horizontal Merger Guidelines list a number of factors which may influence whether or not significant horizontal non-coordinated effects are likely to result from a merger, such as the large market shares of the merging firms, the fact that the merging firms are close competitors, the limited possibilities for customers to switch suppliers, or the fact that the merger would eliminate an important competitive force. Furthermore, not all of these factors need to be present to make significant non-coordinated effects likely, and it is not an exhaustive list.¹²⁵ Finally, the Horizontal Merger Guidelines describe a number of factors which could counteract the harmful effects of the merger on competition, including the likelihood of buyer power, entry and efficiencies.

¹²³ In the EEA, in 2017 Shazam generated revenues in the field of online advertising services of approximately EUR [...] million in the EEA (Form CO, paragraph 279.), whilst Apple generated revenues of approximately EUR [...] million in the United Kingdom in the field of online advertising services through its Apple News service. Based on these figures, the Notifying Party estimates that each of Shazam's and Apple's market share in an hypothetical EEA narrowest product market or segment for provision of mobile non-search advertising would be below [0-5] % based on value in 2016 (with data for 2017 not being available).

¹²⁴ Horizontal Merger Guidelines, paragraph 24.

¹²⁵ Horizontal Merger Guidelines, paragraph 26.

(174) To assess whether a concentration constitutes a significant impediment of effective competition pursuant Article 2(3) of the Merger Regulation, the Commission must compare the competitive conditions that would result from the concentration with the conditions that would have prevailed without the concentration.¹²⁶ While normally the competitive conditions existing at the time of the merger constitute the relevant comparison for evaluating the effects of a merger, in some circumstances the Commission may take into account future changes to the market that can "*be reasonably predicted*".¹²⁷ On the basis of paragraph 9 of the Horizontal Merger Guidelines it is for the Commission to show the existence of a significant impediment to effective competition in the market considering reasonably predictable future changes.

8.3.2. *Licensing of music charts data*

8.3.2.1. The Notifying Party's view

(175) According to the Notifying Party, irrespective of the market definition adopted, the Concentration will not have any negative impact on competition as Shazam does not possess a very rich or unique dataset. In particular, other companies, notably digital music distributors, possess more significant data covering music consumption (sales and streams) patterns, in other words musical works that customers actually listen to and not just songs that they seek to recognise. According to the Notifying Party, the former is a more accurate and direct indication of music preferences.¹²⁸ In addition, many data companies provide analytical tools specific to the music industry that offer their customers the ability to derive insights about trends in the music industry, very similar to what Shazam could offer, but often with more sophisticated metrics.¹²⁹

(176) The fact that there is a lot of music data available and that Shazam's music charts data set has little commercial value is demonstrated by [...].¹³⁰ [...].¹³¹

8.3.2.2. Commission's assessment

(177) As described in recitals (70) to (72), Shazam offers music discovery charts while Apple provides mainly music consumption charts.

(178) The Commission notes that an overlap between the Parties' activities would arise only in a hypothetical overall market encompassing both the music charts data licensed by Shazam and the music charts compiled by Apple, which, as explained in Section 7.5.1.2, is not warranted based on the results of the market investigation.

(179) Nonetheless, the Commission considers that, even in such a broader market and regardless of its geographic scope, the Concentration would not significantly impede effective competition. Indeed, based on the responses of the majority of the participants in the market investigation, even in such a broader product market, the music charts data offered by Shazam and Apple would be complementary rather than close competitors.¹³² Further, the majority of respondents to the market investigation

¹²⁶ Horizontal Merger Guidelines, paragraph 9.

¹²⁷ Horizontal Merger Guidelines, paragraph 9.

¹²⁸ Form CO, paragraph 300 and Annex 6.3.III.F(a).

¹²⁹ Form CO, paragraph 342.

¹³⁰ Form CO, paragraph 301 and Annex 6.3.III.A(d) Shazam's "Go Forward Plan".

¹³¹ Form CO, paragraph 321.

¹³² Responses to questionnaire to recorded music companies and music aggregators – Q8, question C.2.2., to questionnaire to advertisers - Q7, question C.2.2, to questionnaire to digital music distributors - Q6,

took the view that there are plenty of sources for music charts data in the music industry.¹³³ Finally, based on the results of the market investigation, it appears that in such a heterogeneous competitive landscape, none of the music charts data sets offered in the market, including the data sets offered by Shazam or Apple, is considered "unique" or, in any event, of any particular value compared with other data available on the market.¹³⁴

- (180) Therefore, the Commission considers that the Concentration would not significantly impede effective competition in relation to the licensing of music charts data.

8.3.3. *Online advertising*

8.3.3.1. The Notifying Party's view

- (181) According to the Notifying Party, irrespective of the market definition adopted, the Concentration will not have any negative impact on competition as Apple and Shazam have a very limited position in the online advertising market and, moreover, alternative significant operators would remain active in the market.

8.3.3.2. Commission's assessment

- (182) As illustrated in Section 8.2.5, while the Parties are both active in online non-search advertising, no reportable market exists in relation either to the supply of online advertising or to any sub-segments of it. Irrespective of that, the Commission further notes that respondents to the market investigation considered that the Concentration is unlikely to raise concerns with respect to online advertising.¹³⁵
- (183) The Commission has also considered whether any concern could arise in narrower sub-segments of the market for online advertising, such as the market segment for online advertising for music enthusiasts.¹³⁶ The Commission notes that, in a narrowly defined market or segment like that, Apple is not active and there would be no overlap between the Parties' activities.
- (184) The Commission further considers that even if post-Transaction Apple were to use some of its assets (in particular, its user data) to strengthen Shazam's position in the market/segment for online advertising for music enthusiasts, this would not significantly impede effective competition. Indeed, a number of major companies offering online advertising services on inventories far larger than Shazam, including Google and Facebook, allow advertisers to target specific audiences based on their interest and also allow the targeting of music enthusiasts. Further, as discussed in Section 8.4.2.2.(c)(v), other digital music streaming players collect and have available databases on music enthusiasts similar to Apple Music and could

question 53, and to questionnaire to providers of music recognition software solutions - Q5, question 35.2.

¹³³ Responses to questionnaire to recorded music companies and music aggregators – Q8, question C.2, and to questionnaire to advertisers - Q7, question C.1. See also agreed minutes of the conference calls with Universal Music Group of 7 March 2018 and with Warner Music Group of 6 March 2018.

¹³⁴ Responses to questionnaire to recorded music companies and music aggregators – Q8, question C.3., to questionnaire to advertisers - Q7, question C.1., and agreed minutes of the conference calls with Universal Music Group of 7 March 2018, with Warner Music Group of 6 March 2018, with Deezer of 7 March 2018 and with Google of 8 March 2018.

¹³⁵ See responses to questionnaire to advertisers - Q7, question D.1.
In relation to the possible use of Shazam as advertising tool for digital music streaming apps, see Section 8.4.2.2(c)(iii).

¹³⁶ See Commission decision of 6 December 2016 in case M.8124 – *Microsoft / LinkedIn*, and Commission decision of 3 October 2014 in case M.7217 – *Facebook/ WhatsApp*.

potentially partner with providers of advertising services, should this data asset be needed to compete in the music enthusiast segment. In particular, the Commission notes that Google, which also controls YouTube and Google Play Music, would remain one of the main channels for targeting music enthusiasts to online advertisers.¹³⁷

- (185) Therefore, the Commission considers that the Concentration would not significantly impede effective competition in respect of online advertising, and possible sub-segments thereof.

8.4. Assessment of non-horizontal effects

8.4.1. Legal framework

8.4.1.1. Vertical non-coordinated effects

- (186) According to the Non-Horizontal Guidelines, non-coordinated effects may significantly impede effective competition as a result of a vertical merger if such merger gives rise to foreclosure. Foreclosure occurs where actual or potential competitors' access to supplies or markets is hampered or eliminated as a result of the merger, thereby reducing those companies' ability and/or incentive to compete.¹³⁸ Such foreclosure may discourage entry or expansion of competitors or encourage their exit.¹³⁹

- (187) The Non-Horizontal Guidelines distinguish between two forms of foreclosure. Input foreclosure occurs where the merger is likely to raise the costs of downstream competitors by restricting their access to an important input. Customer foreclosure occurs where the merger is likely to foreclose upstream competitors by restricting their access to a sufficient customer base.¹⁴⁰

- (188) In assessing the likelihood of an anticompetitive foreclosure scenario, the Commission examines, first, whether the merged entity would have, post-merger, the ability to substantially foreclose access to inputs or customers, second, whether it would have the incentive to do so, and third, whether a foreclosure strategy would have a significant detrimental effect on competition.¹⁴¹

8.4.1.2. Conglomerate non-coordinated effects

- (189) According to the Non-Horizontal Guidelines, in the majority of circumstances, conglomerate mergers will not lead to any competition problems.¹⁴² However, foreclosure effects may arise when the combination of products in related markets may confer on the merged entity the ability and incentive to leverage a strong market position from one market to another closely related market by means of tying or bundling or other exclusionary practices. While tying and bundling have often no anticompetitive consequences, in certain circumstances such practices may lead to a

¹³⁷ 1.5 billion logged in viewers visit Youtube every single month. See, "Updates from VidCon: more users, more products, more shows and much more", available at: <https://youtube.googleblog.com/2017/06/updates-from-vidcon-more-users-more.html> (accessed on 1 August 2018).

¹³⁸ Non-Horizontal Guidelines, paragraph 18.

¹³⁹ Non-Horizontal Guidelines, paragraph 29.

¹⁴⁰ Non-Horizontal Guidelines, paragraph 30.

¹⁴¹ Non-Horizontal Guidelines, paragraph 32.

¹⁴² Non-Horizontal Guidelines, paragraph 92.

reduction in actual or potential competitors' ability or incentive to compete. This may reduce the competitive pressure on the merged entity allowing it to increase prices.¹⁴³

- (190) In assessing the likelihood of anticompetitive foreclosure effects, the Commission examines, first, whether the merged firm would have the ability to foreclose its actual or potential competitors, second, whether it would have the economic incentive to do so and, third, whether a foreclosure strategy would have a significant detrimental effect on competition, thus causing harm to consumers.¹⁴⁴

8.4.1.3. Other non-coordinated effects

- (191) Finally, according to the Non-Horizontal Merger Guidelines, non-horizontal non-coordinated effects can arise also when the merged entity may, by vertically integrating, gain access to commercially sensitive information regarding the upstream or downstream activities of rivals. For instance, by becoming the supplier of a downstream competitor, a company may obtain critical information, which allows it to price less aggressively in the downstream market to the detriment of consumers. It may also put competitors at a competitive disadvantage, thereby dissuading them to enter or expand in the market.¹⁴⁵

- (192) In this context, for a competitive concern to arise, as a result of a merger the merged entity should gain access to commercially sensitive information on its rivals in upstream or downstream markets, which can allow the merged entity to undertake conducts which would put competitors at a competitive disadvantage.

- (193) Such possible theory of harm differs from the vertical non-coordinated effects discussed in paragraphs 29 to 77 of the Non-Horizontal Merger Guidelines in so far as it does not require the merged entity to directly foreclose access of its actual or potential rivals to supplies (input foreclosure) or markets (customer foreclosure). The qualifying element of the potentially anticompetitive conduct is in fact linked to the intelligence underlying that conduct, that is commercially sensitive information on the merged entity's rivals acquired through the vertical integration brought about by the merger. However, the conduct must also be liable to negatively affect competition, for instance because the merged entity can price less aggressively to the detriment of consumers or because it can put competitors at a competitive disadvantage.

8.4.2. *Possible foreclosure of competing providers of digital music streaming apps*

- (194) In the Article 6(1)(c) Decision, the Commission considered that the Concentration raised serious doubts as to its compatibility with the internal market and the EEA Agreement due to potential foreclosure of competing providers of digital music streaming apps in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway, as a result of Apple gaining access to commercially sensitive information on its rivals through the Concentration.

- (195) The Article 6(1)(c) Decision also considered that the foreclosure effects potentially arising from the theory of harm described in recital (194) could be compounded by two possible groups of practices that Apple could undertake post-Transaction, that is denial or degradation of access of Apple Music's rivals to (i) Shazam's referrals as customer acquisition channel and/or (ii) Shazam as user engagement tool and/or (iii)

¹⁴³ Non-Horizontal Guidelines, paragraphs 91 and 93.

¹⁴⁴ Non-Horizontal Guidelines, paragraph 94.

¹⁴⁵ See Non-Horizontal Merger Guidelines, paragraph 78.

Shazam User Data as an input to improve existing functionalities, or offering additional functionalities, on music streaming services.

8.4.2.1. Access to commercially sensitive information

(a) *Introduction*

- (196) The Commission notes that Shazam currently collects certain data on users of third party's apps, and in particular digital music streaming apps, installed on the same smart mobile devices where the Shazam app is installed (for both Android and iOS devices) which corresponds to categories (i) and (ii) described in recital (69).
- (197) In particular, the Shazam app currently collects information as to the presence of certain apps, including digital music streaming apps, on the mobile device of the Shazam user. [...].¹⁴⁶ The digital music streaming apps for which this information is collected are, on iOS devices, [...]. On Android devices, in addition to those apps, information is also collected for [...].¹⁴⁷
- (198) Moreover, based on the Application Program Interfaces ("APIs") published by Spotify, the Shazam app allows those of its users who are also users of Spotify to connect their Shazam account (anonymous or registered) to their Spotify account (freemium or premium). If a Shazam user has connected its Shazam account to a Spotify account, Shazam is able to gain access to some additional pieces of information on Spotify users, in particular Spotify premium users, in addition to information on the mere presence of the Spotify app on the device, for example it can gain access to playlist names. In this respect, [...].¹⁴⁸
- (199) Finally, the Shazam app currently collects some user data that allows its users to be identified, for example the email address or Facebook identifier for registered Shazam users and the advertising identifier for anonymous Shazam users.¹⁴⁹
- (200) In this context the Commission has assessed whether, through the acquisition of control over the Shazam app and Shazam's database, Apple could gain access to certain data on its competitors, and in particular on Spotify, in the markets for digital music streaming apps in the EEA and in the Referring States and whether this could lead to any non-horizontal non-coordinated anticompetitive effects.

(b) *The Notifying Party's view*

- (201) In Apple's Observations of 3 April 2018, in an economic submission of 10 April 2018 as well as in the Reply to the Article 6(1)(c) Decision, the Notifying Party

¹⁴⁶ The Form CO, at paragraph 308, [...]. However, in the response to question 4.a. of RFI 12, [...].

¹⁴⁷ Response to question 4.a. of RFI 12.

¹⁴⁸ Form CO, paragraph 350, and response to question 21 of RFI 10. It cannot be excluded that the information currently stored only on the users' devices could not be transferred also on Shazam's servers.

As noted on Spotify's developer website, Spotify's user data available through its APIs include the user's display name, information about the user's followers, and the user's Spotify identifier, as well as (subject to the user's consent) the user's birthdate, country of the user, the user's email address, the user's account type (freemium or premium), the user's top artists and tracks, and the user's currently playing track. Further information on Spotify's API is available at <https://developer.spotify.com/documentation/web-api/reference/> (accessed on 1 August 2018), while the full list of information requiring authorization are listed on Spotify's developer website: <https://developer.spotify.com/documentation/general/guides/scopes/#overview> (accessed on 1 August 2018).

[...], see Reply to the Article 6(1)(c), paragraph 101.

¹⁴⁹ Form CO, paragraph 350, and response to question 21 of RFI 10.

argued that the Concentration will not give Apple Music access to commercially sensitive information on its competitors and in any event it would not give rise to anticompetitive foreclosure to the disadvantage of its rivals' customers.

- (202) First, the Notifying Party claimed that the data collected by Shazam is not commercially sensitive.
- (203) Second, the Notifying Party claimed that any increase in the ability of Apple Music to target rivals' customers by using the data collected through Shazam would be not material because (i) Apple is already able to determine which apps are installed by users on iOS, and (ii) it is already possible even today to do targeted advertising campaigns via services offered by Facebook, Google and others (including ad networks offering services based on apps installed on a user's device).
- (204) Third, the Notifying Party also claimed that, for the more accurate data on Spotify's connected users, Spotify has control of the information that Shazam could gather as it could stop allowing the use of its APIs.
- (205) Fourth, according to the Notifying Party, it would not be clear that the merged entity would have an incentive to target advertising or competitive initiatives at rivals' customers, rather than at consumers that have yet to select a music streaming service.
- (206) Fifth, the Notifying Party argued that, even if the merged entity were to target advertising or price discounts at rivals' customers, there is no prospect that this could give rise to anticompetitive effects that harm consumers. In particular, it would be highly unlikely that any targeting of rivals' customers by Apple would materially reduce the ability or incentive of such rivals to compete for users with Apple Music. Indeed, the most likely response to any aggressive advertising or pricing initiative by Apple Music would be for rivals to respond with their own competitive initiatives, which would benefit consumers.
- (207) Sixth, the Notifying Party claimed that even if the merged entity were to target advertising or price discounts at rivals' customers, the number of users Apple could target through data collected by Shazam would be too small to have any material impact on Apple Music's rivals' ability and incentives to compete.
- (208) Finally, the Notifying Party stated that, in any event, it plans to change Shazam's data collection practices to bring them in line with Apple's industry leading-positions on privacy and to update the Shazam app for OSs other than Apple's OSs so it will not send to Apple information concerning the presence of non-Apple music streaming services on the user's device, unless the music streaming service provider of that user agrees to allow this information to be sent.

(c) *Commission's assessment*

- (209) The Commission has assessed, first, whether the information to which Apple would gain access as result of the Concentration is commercially sensitive information (Section 8.4.2.1(c)(i)). Then, it has assessed the competitive disadvantage that Apple Music's competitors could suffer as a result of Apple potentially making use of that information. In this context, applying by analogy paragraph 32 of the Non-Horizontal Merger Guidelines, the Commission has examined whether Apple would have the ability (Section 8.4.2.1(c)(ii)) and incentives (Section 8.4.2.1(c)(iii)) to use the commercially sensitive information acquired through the Concentration to put competing digital music streaming apps at a competitive disadvantage, and what overall impact such a strategy would have on effective competition (Section 8.4.2.1(c)(iv)).

(i) *Commercially sensitive information*

(210) In this case the Concentration would allow Apple to gain access to certain information on Apple Music's rivals. As explained in recitals (196) to (199), the Shazam app currently collects:

- (a) information about the presence of non pre-installed digital music streaming apps on the mobile device where the Shazam is installed: in the EEA this currently relates to approximately [...] million monthly active users of the Shazam app on Android devices and [...] million users on iOS devices;¹⁵⁰
- (b) with respect to Spotify's users who have connected their account with the Shazam app, information about the fact that the user has connected the Shazam account to his/her Spotify account and potentially other, more granular pieces of information, based on Spotify's API.¹⁵¹ In the EEA this currently relates to approximately [...] million monthly active users of the Shazam app on Android devices and [...] million users on iOS devices.

(211) The information collected by the Shazam app as described in the preceding recital (referred to as "Customer App Information") can be combined with other information collected by Shazam about its users, allowing those Shazam users who are (or are not) already customers of digital music streaming apps competing with Apple Music to be identified.

(212) More precisely, based on the information in the Commission's file, the identification exercise could be performed:

- (a) through the user's email address, for approximately [...] million EEA monthly active users of Shazam who have registered on Shazam providing their email address ([...] million on iOS devices and [...] million on Android devices). Of these [...] million EEA monthly active users, around [...] million are Spotify customers connected with Shazam ([...] million on iOS devices and [...] million on Android devices);
- (b) through the user's Facebook identifier, for approximately [...] million EEA monthly active users of Shazam who have registered on Shazam without providing their email address ([...] million on iOS devices and [...] million on Android devices). Of these [...] million EEA monthly active users, around [...] million are Spotify customers connected with Shazam ([...] on iOS devices and [...] on Android devices);
- (c) through the mobile device's advertising ID, for the remaining EEA anonymous users of Shazam, approximately [...] million EEA monthly active users ([...] million on iOS devices and [...] million on Android devices). Of these [...] million EEA monthly active users, around [...] million are Spotify customers connected with Shazam ([...] on iOS devices and [...] on Android devices).¹⁵²

(213) Nonetheless it cannot be excluded that the identification could be currently, or in the near future, performed through technical means other than the advertising ID.

¹⁵⁰ See Form CO, Table 6.

¹⁵¹ See footnote 148. This could include Spotify's users email address and information on the account types (freemium or premium).

¹⁵² Response to question 1 of RFI 12.

As explained at footnote 148, based on Spotify's APIs, Shazam could acquire (subject to the user's consent) the Spotify's user's email address, even for anonymous users of Shazam.

- (214) By combining the Customer App Information with the information mentioned at recital (212), Apple could thus derive a list of customers of Apple Music's rivals, including identifiers. Such information is referred to in this Decision as "the Customer Information".
- (215) The Customer Information could be used by Apple to improve the performance of its customer acquisition effects, by performing more targeted advertising or marketing campaigns aimed at customers of rival music streaming app service providers (in particular Spotify's freemium customers). This customer group could arguably be more prone to switching and take an Apple Music's subscription, compared to the universe of all other potential addresses of Apple's targeted advertising or marketing campaigns, which may be not be a music enthusiast. In turn, this could undermine the growth of Apple Music's rivals, in particular those operating on the basis of a business model whereby the conversion of free users into paid subscribers is important.¹⁵³
- (216) Whilst the Non-Horizontal Merger Guidelines do not provide a definition of "commercially sensitive information", the Commission notes that customer lists are indicated as constituting business secrets of an undertaking, together with quantities produced and sold, cost and price structure and sales strategy, that is information whose disclosure could result in a serious harm to an undertaking, in the Commission Notice on the rules for access to the Commission file.¹⁵⁴
- (217) In the Reply to the Article 6(1)(c) Decision, the Notifying Party argues that neither the Customer Information would amount to commercially sensitive information in light of the precedents of the Commission and the case law of the General Court and the European Court of Justice,¹⁵⁵ which, in the Notifying Party's view, tend to consider information relating to future prices, pricing intentions, demand or capacity information as commercially sensitive. Further the Notifying Party argues that the reference to the Commission Notice on the rules for access to the Commission file would not be relevant for the application of paragraph 78 of the Non-Horizontal Merger Guidelines. This would be because the protection of confidential information in competition proceedings does not hinge on there being a negative impact on competition, but it only requires that there is a risk of harm to the information provider, should the information be disclosed.
- (218) In this respect, the Commission considers that, first, the reason why the Commission has not considered customer lists as commercially sensitive in the previous cases recalled by the Notifying Party is not connected to the nature of the information at stake, but rather to the fact that in those cases the question of the qualification of customer lists was not relevant.

¹⁵³ See Section 6.2.

¹⁵⁴ Commission Notice on the rules for access to the Commission file in cases pursuant to Articles 81 and 82 of the EC Treaty, Articles 53, 54 and 57 of the EEA Agreement and Council Regulation (EC) No 139/2004, OJ C 325, 22.12.2005, p. 7-15, paragraph 18.

¹⁵⁵ Cases M.1879 - Boeing/Hughes, M.2510 - Cendant/Galileo, M.2738 - Gees/Unison, M.2822 - ENBW/ENI/GVS, M.2925 - Charterhouse/CDC/Telediffusion de France, M.3440 - EDP/ENL/GDP, M.3653 - Siemens/VA Tech, as well as AT.39904 Rechargeable Batteries; Case C-7/95 P, John Deere Ltd v. Commission, upholding Case T-35/92, J. Deere vs. Commission, Case T-16/98, Wirtschaftsvereinigung Stahl a.o. v Commission, Case C-40/73, Suiker Unie a.o. v Commission, Case 172/80, Gerhard Züchner v. Bayerische Vereinsbank AG, Case C-89/85, Ahlström a.o. v Commission, and Case C-49/92 P, Commission v Anic.

- (219) Second, the Commission agrees with the Notifying Party that, for a finding of anticompetitive effects pursuant to paragraph 78 of the Non-Horizontal Merger Guidelines, it is not sufficient to demonstrate that, through a merger, the merged entity would gain access to commercially sensitive information on its rivals, but that it is also necessary to show that access to that information could have a negative impact on competition. This, however, is a second successive step of the assessment.
- (220) Thus, the Commission considers that the Customer Information constitutes commercially sensitive information on Apple Music's rivals in the market for digital music streaming apps in the EEA and in the Referring States within the meaning of paragraph 78 of the Non-Horizontal Merger Guidelines.
- (ii) *Ability to use the Customer Information to put competitors at a competitive disadvantage*
- (221) The Commission considers that it is unclear whether the merged entity would be able to put competing providers of digital music streaming apps at a competitive disadvantage by using the Customer Information acquired through the Concentration to perform more targeted advertising or marketing campaigns.
- (222) In this respect the Commission notes that, from a technical point of view, post-Transaction Apple would be able to access the Customer Information and to use it.
- (223) Indeed, first, the Customer Information, and in particular the Customer App Information, is (or could be stored)¹⁵⁶ [...],¹⁵⁷ so that no technical change would be required to centrally collect the data (should this be needed to perform the practices at stake, such as targeted advertising).
- (224) Second, while already pre-Transaction, Shazam has deleted certain user data as part of its broader strategy to comply with the General Data Protection Regulation ("GDPR"),¹⁵⁸ this does not exclude in itself the possibility that Apple would be able to use the Customer Information. Indeed, at the date of adoption of this Decision, Shazam has [...]. According to the Notifying Party, the latter is significant because it means that Shazam [...]. Nonetheless, the Commission notes that, [...], based on the information in its file, the possibility cannot be excluded that, even for those users that Shazam can currently identify only through the advertising ID, other technical solutions or data collected by the Shazam app could be used for the purposes of user identification and ad serving. Further, nothing technically prevents Apple from starting to collect the Customer Information again post-Transaction, including the more granular pieces of information on Spotify's users as compared with the information collected pre-Transaction by Shazam through Spotify's APIs.
- (225) Nonetheless, the Commission notes that there appears to be certain legal and/or contractual limitations on the use of the Customer Information by Apple post-Transaction.

¹⁵⁶ See footnote 148.

¹⁵⁷ Response to RFI 12, question 4.b.

¹⁵⁸ Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation)(OJ L 119, 4.5.2016, p. 1).

The GDPR does not require the deletion of user data. See question 2.c, RFI12. The Parties submit that there is no specific provision of the GDPR which was over-riding in Shazam's considerations, but that Article 32 of the GDPR establishes a general obligation on companies to design for privacy which was an important factor.

- (226) First, the Commission notes that the processing of personal data, including the transmission of Customer Information to the Notifying Party and its subsequent processing, is subject to the applicable European rules dealing with data protection, notably the GDPR.¹⁵⁹ On the basis of the evidence in its file, the Commission notes that [...].
- (227) Those rules apply to personal data, that is "*any information relating to an identified or identifiable natural person ('data subject'); an identifiable natural person is one who can be identified, directly or indirectly, in particular by reference to an identifier such as a name, an identification number, location data, an online identifier or to one or more factors specific to the physical, physiological, genetic, mental, economic, cultural or social identity of that natural person*".¹⁶⁰
- (228) In this respect, the Commission notes that, to the extent that the combination of the Customer App Information with other pieces of information allows for identification of those Shazam's users which are (or are not) already customers of digital music streaming apps competing with Apple Music,¹⁶¹ the Customer Information could qualify as personal data and would be thus subject to the GDPR.
- (229) Pursuant to Article 5(1)(b) of the GDPR, personal data which has been collected for specified, explicit and legitimate purposes may not be further processed in a manner that is incompatible with those purposes. Data which qualifies as personal data under the GDPR can be processed by a third party only to the extent that there exists a contractual legal basis for the transmission to the third party and a legal basis for the processing by that third party.
- (230) In this respect, the Commission notes that, under Shazam's current terms of service and privacy policy, the Customer Information could be used in particular "*(i) to provide [the user] with services including, but not limited to, the display of customized content, integration with [Shazam's] partner apps, and targeted advertising both on websites and other apps/websites that [Shazam] advertise through; [and] (ii) to communicate with [the user] about Shazam products and services, including sending marketing communications that [Shazam] believe[s] may be of interest to [the user], through electronic communications with [the user's] consent or where otherwise permitted by applicable law, and to provide assistance with customer service issues*". Customer Information could also be shared "*with third parties including advertisers and partners, some of whom may use [the user's] data for the purposes of interest-based advertising, including demographic, behavioral, and geographic ad targeting or to provide localized services (with [the user's] prior permission or where otherwise permitted by applicable law*" and could in particular be transferred to a third party in "*the event that ownership of Shazam or an operator of one or more of the sites changes as a result of a merger, acquisition, or transfer to another company.*" In the latter case, however, if "*such a transfer results in a material change in the use of [the user] personal data, then Shazam will provide [the user] with appropriate notice.*"¹⁶²

¹⁵⁹ In this Decision the Commission discusses these rules only for the purposes of the assessment the Concentration under the Merger Regulation. The discussion from recital (226) onwards is therefore without any prejudice to the relevant administrative or legal procedures where the Parties' compliance with those rules may be assessed.

¹⁶⁰ GDPR, Article 4.

¹⁶¹ See recitals (211) to (214).

¹⁶² See Shazam's terms of service and privacy policy at https://www.shazam.com/terms#privacy_policy (accessed on 1 August 2018).

- (231) Without prejudice to the assessment of the matter by the competent data protection authorities, the Commission notes that Shazam's terms of service and privacy notice appear to inform on processing of the Customer Information collected by Shazam. Such terms of service and privacy notice appear to describe the purpose of the data processing and, based on the evidence in the Commission's file, it appears that such purpose has been specified and made manifest to Shazam's users.
- (232) The GDPR requires that individuals concerned by the processing must be informed in a transparent manner on all relevant circumstances of the processing, including on the identity of each controller and the purposes of the processing. Shazam (and Apple post-Transaction) are accountable to implement appropriate technical and organisational measures to ensure and to be able to demonstrate that processing is performed in accordance with the GDPR. In particular, they must ensure the lawfulness of the processing of personal data collected by Shazam and transmitted to Apple and comply with the principles relating to the processing of personal data, including the principles of purpose limitation, fairness and transparency.
- (233) In addition, the Commission notes that Union rules dealing with privacy and the protection of the confidentiality of communications, notably the e-Privacy Directive,¹⁶³ may also pose some limitations as to the transmission of the Customer Information to the Notifying Party and its subsequent use.
- (234) Article 5(3) of the e-Privacy Directive requires that Member States ensure that the storing of information or gaining access to information already stored in the terminal equipment of a subscriber or user is only allowed on condition that the subscriber or user concerned has given his or her consent, having been provided with clear and comprehensive information, in accordance with the GDPR, inter alia, about the purposes of the processing. This does not prevent any technical storage or access for the sole purpose of carrying out the transmission of a communication over an electronic communications network, or as strictly necessary for the provider of an information society service explicitly requested by the subscriber or user to provide the service.
- (235) Thus, Apple would be able to store the Customer Information or access the Customer Information already stored in the terminal equipment of a subscriber or a user to the extent allowed under the e-Privacy Directive.
- (236) Second, with regard to the Customer App Information, the Commission notes that Shazam is able to access data about which apps are installed on a user's Android device because the Android Developer Guidelines allow it to do so.¹⁶⁴ This situation could change at any point in time in the future and is not controlled by Apple.

¹⁶³ Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector ("Directive on privacy and electronic communications" or "e-Privacy Directive") OJ L 201, 31.7.2002, p.37-47.

In this Decision the Commission discusses these rules only for the purposes of the assessment the Concentration under the Merger Regulation. The discussion in recitals (234) and following is therefore without any prejudice to the relevant administrative or legal procedures where the Parties' compliance with those rules may be assessed.

¹⁶⁴ In fact, Google recommends that an app checks third party app presence when the app allows for linking or integration with other apps on Android, as this would prevent the app's malfunction when trying to link a non-existing app. See <https://developer.android.com/training/basics/intents/sending#Verify> (accessed on 1 August 2018).

- (237) Finally, in relation to the specific data on Spotify's users, the Commission notes that Shazam has access to this data through Spotify's public APIs and access to that data is governed by Spotify's developer terms and conditions of service, which restrict the use of Spotify's user data by app developers and can be enforced by Spotify. Notably, those terms of service include, amongst others, obligations for developers to: (i) only request from Spotify users the data they need to operate their app; (ii) not to email Spotify users without explicit consent; and (iii) completely and accurately disclose the privacy practices and policies they apply on their app or website. Further, Spotify's terms of service (section I, points f and h) prevent the use of Spotify's user data "*in any manner to compete with Spotify*".¹⁶⁵ Thus, post-Transaction, on the one hand, Apple would be contractually prevented from using the data Shazam collects through Spotify's public APIs "*in any manner to compete with Spotify*" and, on the other hand, Spotify could undertake a defensive conduct and stop the exchange of data. Finally, the same considerations made at recitals (226) to (232) on the legal restrictions stemming from applicable European data protection rules apply also to Spotify's user data.
- (238) Thus, in this Decision, the Commission, while mindful that legal and/or contractual constraints may limit Apple's possible future use of the Customer Information, will assess the effects of the Concentration on the assumption that such use could be achieved in a lawful manner.
- (iii) *Incentives to use the Customer Information to put competitors at a competitive disadvantage*
- (239) The Commission considers that it is unclear whether the merged entity would have the incentive to use the Customer Information to harm put Apple Music's competitors at a competitive disadvantage.
- (240) In this respect, the Commission notes that, Apple's internal documents show that [...].¹⁶⁶
- (241) Nonetheless, the Commission also notes that, first, (while this is not alone a ground for excluding concerns), the internal document review confirmed Apple's submission that [...]. This seems to be in line with the market practice of targeting marketing efforts to new subscribers, not switchers.¹⁶⁷
- (242) Second, while Apple Music user base is currently concentrated [...].¹⁶⁸ [...].
- (243) In this respect, the Commission notes that Apple's internal documents and analysis show that Apple Music's [...] on Android [...].¹⁶⁹
- (244) This seems to be in line with Apple's general customer acquisition strategy for Apple Music, which appears to be focussed on organic growth exploiting Apple's long experience as download service provider, having launched iTunes back in 2001, and

¹⁶⁵ Spotify's Developer Terms and Conditions of Service, available at: <https://developer.spotify.com/terms/> (accessed on 1 August 2018).

¹⁶⁶ For example see Annex Q37.15 to RFI 10.

¹⁶⁷ See Section 6.2.

¹⁶⁹ For example, Apple's internal documents, APL-SHZ_000018943 and APL-SHZ_000173026, the latter being a document on [...] where [...].

its large installed base of iPhone users (over 700 million users worldwide in 2017).¹⁷⁰ [...].¹⁷¹

(245) Third, the Commission notes that, in response to an RFI pursuant to Article 11(2) of the Merger Regulation, Apple has stated its plans to change Shazam's data collection practices to bring them in line with Apple's industry leading-positions on privacy and, thus, to update the Shazam app for OSs other than Apple's OSs so that it will not send to Apple the Customer App Information, unless the music streaming service of that user agrees to allow this information to be sent to Apple.¹⁷²

(iv) *Impact on competition*

(246) Most importantly, on the basis of the evidence in its file, the Commission considers that, even if the merged entity were to have the ability and incentives to put competing providers of digital music streaming apps at a competitive disadvantage by using the Customer Information, the related practices, such as targeted advertising, are unlikely to have a negative impact on effective competition in the market for digital music streaming apps in the EEA, Austria, France, Iceland, Italy, Norway, Spain and Sweden.

(247) First, the ability to access the Customer App Information on Android, and thus to derive the Customer Information, is not limited to Shazam and would not be limited to Apple post-Transaction. Indeed, any app that is installed on an Android device is allowed by the Android Developer Guidelines to access the Customer App Information. Although arguably Shazam's installed base allows it to gather the Customer App Information for a very high number of (music enthusiast) users, the same would be true for Facebook and Twitter, for example, which also collect information on their users' interest.

(248) In fact, even if Apple were to gain access to the Customer Information, its ability to target subscribers of competing music streaming services post-Transaction is not set to increase materially. Indeed, the market investigation confirmed the Notifying Party's claim that there exist several providers, including, but not limited to Facebook, Google and Twitter, which allow for the targeting of "music enthusiast" audiences (including some players allowing targeting of audiences of users of digital music streaming distributors, such as "Spotify app users") which Apple could rely upon to target such users already pre-Transaction.¹⁷³ Further, the ability to target subscribers of competing music streaming services post-Transaction would not be limited to Apple, as Apple Music's rivals could also rely on the same third party services post-Transaction (as well as pre-Transaction).

(249) In this respect SoundCloud explained that it prospects "*potential users through "look-a-like modeling", which entails defining the attributes and behaviors of [its] most likely customers and identifying new audiences who've taken similar actions and exhibited similar behavior. [...]*".¹⁷⁴

¹⁷⁰ See: <https://www.statista.com/statistics/755625/iphones-in-use-in-us-china-and-rest-of-the-world/> (accessed on 1 August 2018).

¹⁷¹ Form CO, paragraph 246.

¹⁷² Response to RFI 46, question 1.

¹⁷³ Facebook's response to RFI 30; Twitter's response of RFI 29. [...] and [...] explained that they offer their customers the possibility to target users that have a specific app installed on a device (for example, the Spotify app), see responses to, respectively, RFI 33 and RFI 34.

¹⁷⁴ SoundCloud's response to RFI 22, question 5.

(250) Second, the market investigation clearly indicated that the digital music streaming service market in the EEA (and in the Referring States, including Iceland where Apple Music is active) has been growing considerably, as illustrated by Figure 3, based on data on new subscribers (gross adds) acquired by providers of music streaming apps in the period 2015-2017, as well as estimates from 2018 based on data on the first quarter of 2018.

Figure 3: Music streaming apps' gross adds in the EEA and Referring States (2015-2018)

[...]

Source: Commission's market reconstruction.

(251) Not only the market growth rate in the EEA has been considerable, but also market projections appear to show similar trends for the next few years. In this respect Statista estimates a continuous increase of the number of users and revenues of digital music streaming services until 2022, as shown in Figure 4.

Figure 4: Evolution of digital music streaming market in Europe (by revenues and subscribers, 2016-2022)



Source: Statista, September 2017, provided as Annex 6.3.III.B(c) to the Form CO.

- (252) In the course of the market investigation, similar market growth estimates by revenues at EEA level, illustrated in Figure 5, have been provided by Spotify, based on Goldman Sachs data.¹⁷⁵

**Figure 5: Market growth of digital music streaming market in the EEA
(by gross revenues, 2018-2023)**

2018	2019	2020	2021	2022	2023
31%	25%	21%	19%	14%	15%

Source: Goldman Sachs data provided by Spotify.

- (253) Statista also estimates a continuous increase of the number of users and revenues of digital music streaming services until 2022 in France, Italy, Spain, Sweden and Norway.¹⁷⁶ With respect to Austria, albeit user penetration and total market size by subscribers are projected to be stable, still Statista estimates an annual growth rate in the period 2018-2022 of 1.8%.¹⁷⁷ Statista does not elaborate estimates for Iceland.
- (254) Further, respondents to the market investigation, including [...],¹⁷⁸ confirmed that growth comes mainly through subscription of new customers rather than win-back of competitors' customers: competition is for new users and not for switchers. In this vein, [...],¹⁷⁹ while [...].¹⁸⁰ [...].¹⁸¹
- (255) In this context, any target advertising or marketing campaign aimed at persuading existing customers to churn would have very limited, if any, anticompetitive effects. This is in particular the case as, today, Apple Music is not the leader in the market for music streaming services in the EEA as well as in the Referring States, where Spotify continues to be the leading player, not only in terms of subscriber market shares (which provide a static picture of the current competitive constraint exerted by a player),¹⁸² but also in terms of [...] market shares (which provide a dynamic picture of the projected competitive constraint of a market player). This is illustrated by Figure 6 which contains shares of [...] for music streaming services in the EEA and in the Referring States since the launch of Apple Music in 2015, as reconstructed by the Commission's in the market investigation.

¹⁷⁵ Agreed minutes of the meeting with Spotify of 29 May 2018, paragraph 11.

¹⁷⁶ See for France: <https://www.statista.com/outlook/209/136/music-streaming/france#>;
for Italy: <https://www.statista.com/outlook/209/141/music-streaming/italy>;
for Spain: <https://www.statista.com/outlook/209/153/music-streaming/spain>;
for Sweden: <https://www.statista.com/outlook/209/154/music-streaming/sweden>;
for Norway: <https://www.statista.com/outlook/209/145/music-streaming/norway#> (accessed on 1 August 2018).

¹⁷⁷ See <https://www.statista.com/outlook/209/128/music-streaming/austria#> (accessed on 1 August 2018).

¹⁷⁸ [...].

¹⁷⁹ [...].

¹⁸⁰ [...].

¹⁸¹ [...].

¹⁸² See also Statista, Spotify Is Pulling Away From Apple Music, 27 July 2018 <https://www.statista.com/chart/8399/spotify-apple-music-paid-subscribers/> (accessed on 1 August 2018).

**Figure 6: Shares of [...] for music streaming services
in the EEA and in the Referring States (2015 to first quarter (Q1) 2018)**

Providers	EEA				Austria			
	Q1 2018	2017	2016	2015	Q1 2018	2017	2016	2015
Apple Music	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Amazon	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
SoundCloud	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Google Play	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Spotify	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Providers	France				Italy			
	Q1 2018	2017	2016	2015	Q1 2018	2017	2016	2015
Apple Music	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Amazon	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
SoundCloud	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Google Play	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Spotify	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Providers	Spain				Sweden			
	Q1 2018	2017	2016	2015	Q1 2018	2017	2016	2015
Apple Music	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Amazon	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
SoundCloud	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Google Play	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Spotify	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Providers	Iceland				Norway			
	Q1 2018	2017	2016	2015	Q1 2018	2017	2016	2015
Apple Music	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Amazon	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
SoundCloud	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Google Play	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Spotify	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Deezer	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Source: Commission's market reconstruction.

Note: [...]).

- (256) To the contrary, in line with the Notifying Party's submission, it is likely that any target advertising or marketing campaign by Apple aimed at persuading existing customers to churn would prompt Apple's digital music streaming rivals to react by engaging in similar practices.¹⁸³
- (257) Third, the Commission notes that the Notifying Party's internal documents containing best estimates for Apple Music's customer acquisition opportunities generated by the Concentration overall (that is, not limited to [...]) measure the effects of those opportunities in a total of [...] new Apple Music's subscribers over the next five years worldwide,¹⁸⁴ that is around [...] new Apple Music's subscribers

¹⁸³ See SoundCloud's response to RFI 22, question 10; [...].

¹⁸⁴ Apple's internal documents, Form CO, Annex 5.4(a).1.

per year. This equals to around [...] % of Apple Music's gross adds in 2017 and projected gross adds in 2018 in the EEA alone and less than [...] of the 2017 aggregated gross adds, and 2018 aggregated estimated gross adds, of all digital music streaming app providers in the EEA based on the Commission's market reconstruction. Such small percentages suggest that the impact of the Concentration overall in the markets for digital music streaming apps in the EEA and in the Referring States is likely to be limited. In this context, the possible effects of the use of the Customer Information are likely to be negligible.

(258) In light of the above, it is unlikely that the data increment brought by Shazam could provide a significant competitive advantage to Apple which could lead to non-horizontal non-coordinated anticompetitive effects, by reducing the ability and incentives to compete of competing digital music streaming providers.

(v) *Conclusion*

(259) In light of the above, the Commission considers that the Concentration would not significantly impede effective competition as a result of non-coordinated effects in respect of digital music streaming apps in the EEA or in any of Austria, France, Italy, Spain, Sweden, Iceland and Norway due to access to commercially sensitive information.

8.4.2.2. Other non-coordinated effects to the detriment of competing providers of digital music streaming apps

(a) *Introduction*

(260) Music recognition apps offer a functionality, which is of interest and is used by the same users of digital music distribution apps. In fact, music recognition functionalities are integrated in some digital music streaming apps, as is the case of SongCatcher in Deezer. As a result, music recognition apps and digital music streaming apps can be considered complementary or at least closely related products within the meaning of paragraph 91 of the Non-Horizontal Merger Guidelines.

(261) Moreover, after the user has "shazammed" or tagged a song for recognition, Shazam provides the user with information on the song (title and artist) and various other features to enrich its experience, including links to digital music distribution apps. If the user makes use of one of these links, that user will be referred to the platform of the digital music download app (iTunes on iOS and Google Play on Android) or to the digital music streaming app of her/his choice between Apple Music, Spotify, Deezer, Google Play and, in some countries, Amazon Music.¹⁸⁵ These links constitute the so called "mechanism of referral", which constitutes one of the various tools for customer acquisition ("referrals to registration", [...]) and engagement available to providers of digital music streaming apps ("referrals to streaming", [...])¹⁸⁶. Similar links are offered by competing providers of music recognition apps, such as SoundHound. Also in light of these links, music recognition apps and digital music streaming apps can be considered complementary or at least closely related products within the meaning of paragraph 91 of the Non-Horizontal Merger Guidelines.

(262) Furthermore, data collected by music recognition apps, and in particular by Shazam, could be used to improve existing functionalities, or offer additional functionalities,

¹⁸⁵ Shazam result page contains, in a separate tab, also a link to the video streaming service YouTube.

¹⁸⁶ [...]. Google Play is however also the preinstalled digital music download app on Android devices, a link to which is also included in the Shazam result page.

on digital music streaming apps. In this context, user data collected by Shazam could be considered as an important input within the meaning of paragraph 30 and 34 of the Non-Horizontal Merger Guidelines for providers of digital music streaming apps.

- (263) In their referral requests, the Referring States identified possible foreclosure concerns arising from both the conglomerate and vertical relationships existing between the Parties' products.¹⁸⁷ Likewise, in the market investigation both competing providers of digital music streaming apps, the independent music companies association "Impala" and BEUC expressed concerns with respect to the potential foreclosure effects of the Concentration in the market for digital music streaming apps.
- (264) In the Article 6(1)(c) Decision the Commission found that, by leveraging Shazam's market position, Apple could have engaged in some restricting and exclusionary practices, which in combination with the effects of the conducts related to access to commercially sensitive information, might have reduced the ability or incentives to compete of Apple Music's rival providers of digital music streaming apps in the EEA, Austria, France, Iceland, Italy, Norway, Spain and Sweden.
- (265) Since, as described in Section 8.4.2.1, the Concentration would not significantly impede effective competition due to access to commercially sensitive information, in the following recitals, the Commission explains why, already in the Article 6(1)(c) Decision, it considered that those practices leveraging Shazam's market position are equally unlikely to give rise to non-horizontal non-coordinated effects through foreclosure of competing providers of digital music streaming services in the EEA, Austria, France, Iceland, Italy, Norway, Spain and Sweden.
- (b) *The Notifying Party's view*
- (266) According to the Notifying Party, while it plans to generate a total of [...] new Apple Music's subscribers over the next five years as a result of the Concentration, this cannot give rise to any foreclosure effects to the detriment of competing providers of digital music streaming apps. This is because of the following reasons put forward by the Notifying Party in particular in the Form CO and in the Reply to the Article 6(1)(c) Decision.
- (267) First, if Shazam was so valuable to other music streaming providers, it would be inconceivable that Apple would be able to purchase Shazam for less than EUR [...] million in a market currently valued by the market leader (which is not Apple) at USD 10 billion.
- (268) Second, the market for digital music streaming apps is growing very fast and Shazam is an insignificant source of customer acquisition: the Notifying Party claims that Shazam's total referrals accounted in 2017 for [...]%) of net new users at worldwide level. Thus, it is inconceivable that competing providers of music streaming services would suffer any anticompetitive foreclosure effect if they no longer were to have access to this single source of new users.

¹⁸⁷

In the Article 22 Decisions, based on the submission of the Referring States, the Commission considered that two types of adverse effects were likely to be brought about by the Concentration, that is:

(a) Potential foreclosure of competing digital music distributors, leveraging on Shazam's market position, through either (i) denial or degradation of access to Shazam as an important entry point, or (ii) denial or degradation of access to Shazam's software/technology to power integrated or connected with music recognition services; and

(b) Potential increased barriers to entry and expansion in the markets for (i) digital music distribution and (ii) online advertising, as a result of the combination of Shazam's data with Apple's data.

- (269) Third, users only have a very limited interaction with Shazam and Shazam therefore is not a source of significant user engagement which would meaningfully enriches the experience of customers of digital music streaming apps. In particular, the average user spends less than [...] per month using Shazam, with each session typically lasting less than [...], and the average Shazam monthly active user tags less than [...] songs in a month and takes no further action in approximately [...]of those tags. In contrast, an average Spotify user spends approximately 25 hours per month on the Spotify app which corresponds to approximately 375 songs listened per monthly active user.
- (270) Fourth, [...] post-Transaction providers of those apps will continue to have a number of potential technology partners available should they wish to develop a music recognition offering.
- (271) Finally, Shazam’s data on user music discovery is not a key asset and is not unique. Shazam’s User Behavioural Data [...]. In the music industry, the most potentially valuable data relates to actual music consumption (that is, sales, streams) because that is most representative of the correlation across multiple songs a user may like. As a result, the most interesting and valuable data to offer digital music streaming services is held by music streaming providers themselves.
- (c) *Commission's assessment*
- (272) Shazam's market share in the EEA and worldwide markets for music recognition apps (regardless of whether such market includes only dedicated music recognition apps or also other apps with embedded music recognition functionalities) is well in excess of the 30% threshold set forth in paragraph 25 of the Non-Horizontal Merger Guidelines.¹⁸⁸ Nonetheless, based on the evidence in its file, the Commission notes that, so far, Shazam's high market shares have not translated into a significant degree of market power within the meaning of paragraphs 23 of the Non-Horizontal Merger Guidelines in the provision of music recognition apps. Indeed, Shazam [does not extract significant revenues] from users of the Shazam app ([...])¹⁸⁹ [...].
- (273) Nonetheless, assuming that Shazam's market shares were indicative of a significant degree of market power within the meaning of paragraphs 23 of the Non-Horizontal Merger Guidelines, the Commission investigated whether, after the Concentration, the merged entity could give raise to non-horizontal non-coordinated effects through foreclosure of competing digital music streaming apps.
- (274) On the basis of the submissions from the Referring States and from respondents to the market investigation, the Commission has identified the following groups of possible practices through which the merged entity could potentially be able to foreclose competing providers of digital music streaming apps:
- (a) exclusionary practices leveraging the merged entity's market position from music recognition apps to the markets for digital music streaming apps, which in turn consist of:
- denying or degrading access of competing providers of digital music streaming apps to Shazam's referral mechanism as customer acquisition channel, and at the same time directing all referrals to Apple Music or

¹⁸⁸ See Section 8.2.3.

¹⁸⁹ See recital (69) on the data collected by Shazam.

giving more prominence to referrals to Apple Music (assessed in Section 8.4.2.2.(i));

- denying or degrading access of competing providers of digital music streaming apps to Shazam's referral mechanism as functionality, which boosts user engagement or enriches user experience on digital music streaming apps, and at the same time directing all referrals to Apple Music or giving more prominence to referrals to Apple Music (assessed in Section 8.4.2.2.(ii));

- (b) practices restricting access of competing providers of digital music streaming apps to the Shazam app as advertising tool, and at the same time restriction of the use of the Shazam app as advertising tool only to Apple Music (assessed in Section 8.4.2.2.(iii));¹⁹⁰
- (c) integration of Shazam's music recognition functionalities within the Apple Music apps, and at the same time denial of similar levels of integration to competing providers of digital music streaming apps (assessed in Section 8.4.2.2.(iv)); and
- (d) practices restricting access of competing providers of digital music streaming apps to Shazam User Data as an important input to improve existing functionalities, or offer additional functionalities, on digital music streaming apps (assessed in Section 8.4.2.2.(v)).

(275) The Commission's assessment on each of those practices in the light of the results of the in-depth investigation is set out in the following recitals. For this purpose, consistent with paragraphs 32 and 94 of the Non-Horizontal Merger Guidelines, in relation to each of these practice the Commission examines (i) whether the merged entity would have the ability to foreclose competing providers of digital music streaming apps; (ii) whether it would have the economic incentive to do so; and (iii) what overall impact such a foreclosure strategy would have on effective competition.

(i) *Shazam as customer acquisition channel*

(276) The Commission considers that the merged entity is likely to have the **ability** to engage in the denial or degradation of access to Shazam's referral mechanism as customer acquisition channel.

(277) In this respect, the Commission notes that, first, from a technical point of view, the referral tiles are designed as a hyperlink, which, when clicked, in the absence of the digital music streaming app on the mobile device of the Shazam user, directs the user to the app store of the relevant OS so that s/he can download the app. Such hyperlink is added on the results page of the Shazam app and does not interfere with the music track recognition. The removal of referral tiles to competing digital music streaming apps appears to be technically fairly simple and not to degrade to a meaningful extent the experience of Shazam users.

(278) Second, the Commission notes that Apple's internal documents [...].¹⁹¹

(279) Moreover, the Commission considers that the merged entity is likely to have the **incentives** to engage in the denial or degradation of access to Shazam's referral

¹⁹⁰ This practice was not identified in the Article 6(1)(c) Decision and analysed by the Commission in the second phase investigation.

¹⁹¹ See Form CO, Annex 5.4(a)8 [...].

mechanism as customer acquisition channel. This is demonstrated by Apple's internal documents, [...].¹⁹² In its internal documents Apple estimates that this strategy would bring up to [...] additional users on Apple Music over five years, corresponding to USD [...] revenues,¹⁹³ [...].

- (280) However, the Commission considers that, even if the merged entity were to have the technical ability and the incentives to engage in the denial or degradation of access to Shazam's referral mechanism as customer acquisition channel, it is unlikely that post-Transaction the merged entity would have the ability to foreclose competing providers of digital music streaming apps and that such conducts would have a negative **impact on competition**, in particular with regard to prices and choice in the markets for digital music streaming apps in the EEA and in the Referring States.
- (281) First, the evidence in the Commission's file indicates that, albeit Shazam has a significant market share in the market for music recognition apps and its competitors do not appear to have the same strength in particular in terms of brand recognition and attractiveness to users in the EEA,¹⁹⁴ this does not appear to have translated in a significant degree of market power, including vis-à-vis providers of digital music streaming apps. Indeed, the revenues generated by Shazam from the partnership with digital music streaming apps are very limited.
- (282) Second, and more importantly, the effects of denial or degradation of access of competing providers of digital music streaming apps to Shazam's referral mechanism are unlikely to be enough to reduce their ability or incentives to compete.
- (283) In this respect the Commission notes that, while it is theoretically conceivable that competing providers of digital music streaming apps could be negatively impacted by a denial or degradation of access to Shazam's referral mechanism, and [...], no Apple Music's rival to date provided any quantitative or qualitative evidence showing that access to Shazam was important for them to thrive as providers of digital music services. To the contrary, the evidence in the Commission's file confirms the Notifying Party's claim on the insignificant relevance of Shazam as customer acquisition channel for digital music streaming apps in the EEA, as well as in the Referring States. During the market investigation the Commission has conducted a market reconstruction collecting confidential data on digital music streaming apps' new subscribers acquired in the EEA in the years 2015, 2016 and 2017 and in the Referring States in 2017, overall (gross adds) and through Shazam's referrals to registration. The results of the market reconstruction indicate that the relevance of Shazam's referrals as customer acquisition channel in the EEA and in the Referring States is in line with the Notifying Party's estimate for the worldwide market. In fact, Shazam's referrals only account for [...] of the new users of digital music streaming services in the EEA, as shown in Figure 7 and [...] at national level depending on the Referring Member State.

¹⁹² See footnote 191.

¹⁹³ See Form CO, Annex 5.4(a)1 [...].

¹⁹⁴ Responses to questionnaire to digital music distributors - Q6, question 13, and responses to questionnaire to providers of music recognition software solutions - Q5, question 30. See also responses to questionnaire to digital music distributors - Q6, questions 40 and 41 on the relative importance of the Shazam app in terms of customer acquisition channel compared to other music recognition apps.

Figure 7: Shazam referrals's contribution to gross adds growth in the EEA (2015-2018)

[...]

Source: Commission's market reconstruction.

- (284) In this context, referral to registration via Shazam appears to be merely one out of the large number of different customer acquisition channels for digital music streaming apps described in Section 6.2 (and a rather unimportant one accounting, for example, for [...] of new subscribers for both Spotify and Deezer in the EEA¹⁹⁵). Other customer acquisition channels (such as search advertising or on social networks) will remain available post-Transaction, so that competing digital music streaming apps will not be prevented from engaging in effective customer approaches.
- (285) The Commission further notes that:
- (a) although Spotify had no referral agreement between mid-2015 and mid-2016, it managed to expand its customer base at a very high rate.¹⁹⁶ [...];¹⁹⁷
 - (b) Amazon Music has rapidly grown its subscribers with no or negligible contribution by Shazam's referrals.¹⁹⁸ [...].
 - (c) [...].¹⁹⁹
- (286) Therefore, given the small fraction of new users that Shazam's referrals account for in the EEA and in the Referring States and the availability of other customer acquisition channels, the Commission considers that, even if the merged entity were to stop referrals from Shazam to competitors of Apple Music, it is unlikely that the reduction of sales prospects faced by digital music streaming apps, which would not benefit anymore of Shazam's referrals to registration, could reduce their ability or incentives to compete. Neither does the Commission consider that the merged entity's foreclosure strategy at stake could deter entry by potential competitors in the market for digital music streaming apps, given the limited number of customers over which Apple Music would have an acquisition advantage thanks to Shazam's referrals to registration.²⁰⁰ This is in particular because of the exponential growth that

¹⁹⁵

[...].

¹⁹⁶

Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018). Based on the market reconstruction undertaken by the Commission, Spotify's new subscribers grew b [...] from 2015 to 2016.

¹⁹⁷

Shazam's internal documents, [...]

¹⁹⁸

Data provided by Shazam in the Form CO, Tables 10, 11, 12 and 25, referrals to Amazon in 2017 accounted for [...]. Based on the market reconstruction undertaken by the Commission, referrals to registration accounted in 2017 for [...] of Amazon's new subscribers, while its new subscribers have grown by [...].

¹⁹⁹

Apple's Observations on the Commission's Preliminary Questions, paragraph 19 iii.

²⁰⁰

The Commission also notes that [...] of Shazam active user base is on iOS devices and on such devices already pre-Transaction the referral tile to Apple Music has a more prominent position. Moreover, already pre-Transaction around a [...] of the referrals to registration of (both iOS and Android) users in the EEA from the Shazam app to digital music streaming apps goes to Apple Music: Apple Music is the [...] receiver by number of referrals to registration from Shazam, [...].

the market for digital music streaming apps in experiencing at worldwide and EEA levels as well as in the Referring States.²⁰¹

- (287) Thus, the Commission considers that the Concentration would not significantly impede effective competition as a result of conglomerate foreclosure effects in the markets for digital music streaming apps though denial or degradation of access to Shazam's referral mechanism as customer acquisition channel in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway.
- (ii) *Shazam's referral mechanism as functionality which boosts user engagement or enriches user experience on digital music streaming apps*
- (288) The Commission considers that the merged entity is likely to have the **ability** to engage in the denial or degradation of access to Shazam's referral mechanism as functionality, which boosts user engagement or enriches user experience on digital music streaming apps.
- (289) In this respect the Commission notes that, from a technical point of view, the same tiles on the Shazam results page allow both referrals to streaming and referrals to registration. The difference is that, when the user has already installed on her/his mobile device the digital music streaming app, a click on the tile directs the user to the digital music streaming app, and not to the app store. Once on the digital music streaming app premium subscribers of the digital music streaming app (or also free trial subscribers, depending on the app) can listen to the full track they have tagged with Shazam. Therefore, for the same reasons explained in recital (277), the Commission considers that the removal of referral tiles to competing digital music streaming apps appears to be technically fairly simple and not to degrade to a meaningful extent the experience of Shazam users.
- (290) However, the Commission considers that, even if the merged entity were to have the technical ability to engage in the denial or degradation of access to Shazam's referral mechanism as an engagement functionality, it is unlikely to have the ability and the incentives to foreclose rivals in the market for digital music streaming apps and that such conducts would have a negative **impact on competition**, in particular with regard to prices and choice in the markets for digital music streaming apps in the EEA and in the Referring States.
- (291) First, the evidence in the Commission's file indicates that, albeit Shazam has a significant market share in the market for music recognition apps and its competitors do not appear to have the same strength in particular in terms of brand recognition and attractiveness to users in the EEA,²⁰² this does not appear to have translated in a

²⁰¹ Form CO, Annex 6.3.III.B(b) and Form CO, Annex 6.3.III.B(c). Statista forecasts that the market will grow from approximately USD 8 billion to USD 12 billion from 2017 to 2022 worldwide and from USD 2.3 billion to USD 3.5 billion on a European basis.

See also, Reply to the Article 6(1)(C), Annex II.A. Goldman Sachs industry report shows an expected growth of the worldwide paid streaming market by USD 8.9 billion (from USD 5.1 billion to USD 14 billion) between 2017 and 2022

See also, Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018), page 2 and following where it is indicated that "*streaming is growing globally*" and that "*the streaming market is still in its infancy*".

²⁰² Responses to questionnaire to digital music distributors - Q6, question 13 and responses to questionnaire to providers of music recognition software solutions - Q5, question 30. See also responses to questionnaire to digital music distributors - Q6, questions 44 and 45 on the relative importance of the Shazam app in terms of customer engagement.

significant degree of market power, including vis-à-vis providers of digital music streaming apps. [...].²⁰³ Likewise, the Commission notes that [...],²⁰⁴ while, in the market investigation, [...].²⁰⁵ All these elements provide an indication of limited economic relevance of referrals to streaming for boosting user engagement or enriching user experience on digital music streaming apps.

(292) Second, the effects of such practice are unlikely to be enough to reduce the ability or incentives to compete of competing providers of digital music streaming apps.

(a) First, the Commission notes that the evidence in the Commission's file indicates that the relevance of referrals to streaming as functionality, which boosts user engagement or enriches user experience on digital music streaming apps is very limited. The Commission has benchmarked the number of referrals to streaming in the EEA with the number of total subscribers and premium subscribers of digital music streaming apps in the EEA:²⁰⁶ the result of this exercise shows that the number of referrals to streaming per subscriber as well as per premium subscriber is negligible in the EEA. The Commission also tried to estimate the proportion of users of digital music streaming apps in the EEA for which referrals to streaming may be an important functionality. For this purpose, assuming that all referrals to streaming were performed by the same users and that these users would click once per week on the referral tile, the Commission has divided the total number of clicks to streaming in the months of December 2017 and January 2018 by the number of weeks per month and benchmarked the result with the user basis of digital music streaming providers. Also on the basis of this conservative metric referrals to streaming appear to have a limited importance in terms of user engagement on digital music streaming apps: indeed the proportion of these customers out of the total number of subscribers or premium subscribers of digital music streaming apps in the EEA would be small. Assuming that users, for which referrals to streaming are particularly important in terms of engagement and user experience, would click more than once per week on the referral tile, the share of demand represented by these customers would be even smaller.

(b) Second, the Commission notes that Shazam is used for only [...] per month by its users,²⁰⁷ which is a minimal if compared to several hours of use of music streaming apps ([...] ²⁰⁸, [...] ²⁰⁹). This means that the user exposure to the brand of the music streaming apps within Shazam is very marginal.

(c) Third, the Commission notes that, rather than boosting user engagement or enriching user experience on digital music streaming apps, referrals to

²⁰³ [...], see footnote 186.

²⁰⁴ See, for example, responses to questionnaire to digital music distributors - Q6; agreed minutes of the [...], and agreed minutes of the [...].

²⁰⁵ [...].

²⁰⁶ [...]; subscriber data provided in response to providers of digital music distributors - Q6, questions 4 and 5.

²⁰⁷ Form CO, paragraph 266.

²⁰⁸ Commission's calculation based on information provided by third parties

²⁰⁹ See Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018).

streaming may at best (if at all)²¹⁰ serve this purpose for Shazam. In this respect, the Commission notes that, in fact, [...].²¹¹

- (d) Fourth, already pre-Transaction the referral tile to Apple Music has a more prominent position on iOS devices, where around [...] of Shazam active user base is and [...] of referrals to streaming are performed. Moreover, already pre-Transaction around a [...] of the referrals to streaming of iOS users in the EEA from the Shazam app to digital music streaming apps goes to Apple Music: Apple Music is the [...] receiver by number of referrals from Shazam, the [...].²¹²
 - (e) Fourth, the removal of a link to competing digital music streaming apps would not as such stop users of such services from shazamming songs and then listening to those songs on rival digital music streaming apps. This can be done by simply opening the respective digital music streaming app and looking for the recognised song.
- (293) The market investigation has not provided any indication that the effects of the denial or degradation of access to Shazam's referral mechanism as engagement functionality would be different in any of the national markets for digital music streaming apps in the Referring States.
- (294) Thus, the Commission considers that the Concentration would not significantly impede effective competition as a result of conglomerate foreclosure effects in the markets for digital music streaming apps though denial or degradation of access to Shazam's referral mechanism as functionality in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway.
- (295) A functionality to boost user engagement or enrich user experience on digital music streaming apps, much more useful than Shazam's referrals, appears to be offering embedded music recognition functionalities, as Deezer has recently done.²¹³ As discussed in Section 8.4.2.2.(iv), the Commission considers that the Concentration is unlikely to give rise to anticompetitive effects in relation to the ability of competing providers of digital music streaming apps to access music recognition software solutions to offer such embedded functionalities.
- (iii) *The Shazam app as advertising tool*
- (296) The Commission considers that the merged entity is likely to have the **ability** to engage in practices restricting access to the Shazam app as advertising tool for competing digital music streaming apps.
- (297) In this respect the Commission notes that, all what is required to perform this conduct is to use the advertising space on the Shazam app to promote exclusively Apple Music. Further, Apple could redesign the Shazam app so to display push notifications promoting Apple Music on Android devices²¹⁴ (regardless of whether

²¹⁰ [...] (Form CO, Tables 11, 12 and 25, and response to RFI 10, question 39).

²¹¹ In an internal document attached to the Form CO as Annex 5.4(a)8, Apple states that, post-Transaction, [...]. See footnote 191.

²¹² Response to RFI 10, question 39, as well as Form CO, Tables 11, 12 and 25.

²¹³ Deezer's response to questionnaire to digital music distributors – Q6, question 47: "the best option for increasing the customer retention is the integration of a music recognition feature in our services".

²¹⁴ On iOS devices Apple already has the ability to send push notifications pre-Transaction.

the device has installed a music streaming app) and thus growing its user base on a platform [...].²¹⁵

- (298) Moreover, the Commission considers that the merged entity is likely to have the **incentives** to engage at least in the first of these practices. This is demonstrated by [...].²¹⁶ To the contrary, with respect to the possibility of sending push notifications, [...],²¹⁷ so that the Commission considers it unclear whether Apple would have the incentive to introduce a feature which could reduce the value of the company/assets it is acquiring.
- (299) However, the Commission considers that, even if the merged entity were to have the technical ability to engage in practices restricting access to the Shazam app as advertising tool, it is unlikely to have the ability and the incentives to foreclose rivals in the markets for digital music streaming apps and that such conducts would have a negative **impact on competition**, in particular with regard to prices and choice in the markets for digital music streaming apps in the EEA and in the Referring States.
- (300) First, the Commission notes that the potential of this strategy would reflect nothing, but Shazam's strength in the advertising market. As explained in Section 8.2.5, Shazam appears to be a relatively small player in online advertising. As such Shazam does not have significant degree of market power within the meaning of paragraph 61 of the Non-Horizontal Merger Guidelines in the market for online advertising nor in the possible sub-segment for online advertising for music enthusiasts.
- (301) Even considering the potential market segment for online advertising for music enthusiasts, the Commission notes that, as explained in Section 8.3.3.2., a number of major companies offering online advertising services on inventories far larger than Shazam, including Google and Facebook, allow advertisers to target music enthusiasts and would remain available to competitors of Apple Music post-Transaction.
- (302) Further, as explained in Section 6.2., after promotional campaigns and in-app advertisement in digital music streaming apps, the most effective advertising tools for digital music streaming apps appear to be paid online search advertising, marketing on social network sites and partnerships with mobile network/telecoms operators, e-mail campaigns and referrals from other apps. Thus, non-search advertising on platform others than social networks, including on the Shazam app, does not appear to be among the most effective advertising tools for digital music streaming apps. In particular the Commission notes that, when asked about the important/effective customer acquisition channels, [...].²¹⁸ In the same vein [...].²¹⁹
- (303) In addition, the Commission note that the Shazam app is used for only [...] per month by its users, which is minimal if compared to several hours of use of other non-search advertising platforms.²²⁰ This means that the user exposure to the brand of the music streaming apps within the Shazam app is very marginal.
- (304) Thus, it appears that, for digital music streaming players, having their service featured on the Shazam app is only one of the many different ways (and clearly not

²¹⁵ The practice of push notifications is indicated as customer acquisition tool by SoundCloud in its response to RFI 22, question 3.

²¹⁶ In Form CO, Annex 5.4(a)2 and Annex 5.4(a)9, [...]. In Form CO, Annex 5.4(a)2, [...].

²¹⁷ Shazam's internal documents, [Doc IDs 795-43224; 795-14539; 795-1720].

²¹⁸ [...].

²¹⁹ [...].

²²⁰ Form CO, paragraph 266.

one of the most important ways), in which they attempt to build/market their brand and to promote their services. Therefore, even if the merged entity were to restrict Shazam as advertising tool exclusively to Apple Music, the impact on the ability or incentives to compete of its rivals would be negligible.

- (305) With specific reference to the use of push notifications on Android, the Commission notes that such use is regulated by Android's developer guidelines. These guidelines provide for the user's ability to accept or suppress push notifications and an app developer cannot simply decide to send push notifications to all users who have the app. Consequently, post-Transaction any push notifications would only be sent to a subset of the Shazam users on Android.
- (306) Further, the Commission notes that, even if the merged entity were to start sending such push notifications, the effects of such practice are unlikely to be enough to reduce the ability or incentives to compete of other providers of digital music streaming apps on Android devices. First, the growth of competing digital music streaming apps has not been supported by Shazam push notifications pre-Transaction and there is no evidence that this would have changed absent the Transaction. Second, even if the use of push notifications were to attract the attention of Android users to Apple Music (despite the draw-backs mentioned at recital (298), [...]²²¹).
- (307) Thus, the Commission considers that the Concentration would not significantly impede effective competition as a result of conglomerate foreclosure effects in the markets for digital music streaming apps though restricting access to the Shazam app as advertising tool in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway.
- (iv) *Shazam as provider of software solutions to power music recognition functionalities*
- (308) The Commission considers that the merged entity is likely to have the **ability** and the **incentive** to integrate Shazam's music recognition functionalities within the Apple Music apps and to deny similar levels of integration to competing digital music streaming apps. In particular, based on Apple's internal documents, [...]²²²[...].²²³
- (309) However, the Commission considers that, even if the merged entity would have the technical ability and the incentives to integrate Shazam's music recognition functionalities within the Apple Music apps and to deny similar levels of integration to competing digital music streaming apps, it is unlikely that post-Transaction the merged entity would have the ability to foreclose competing providers of digital music streaming apps and that such conducts would have a negative **impact on effective competition**, in particular with regard to prices and choice in the markets for the digital music streaming apps in the EEA and in the Referring Membr States.
- (310) Importantly, post-Transaction, several alternative providers of music recognition technology, such as Tonio, Gracenote and ACRCLOUD, would remain active in the market which could partner with digital music streaming app providers to provide music recognition functionalities to end-users. In this vein, in the market investigation, Musixmatch noted that, in order to provide music recognition functionality it is possible to use providers like ACRCLOUD or Gracenote.²²⁴ More

²²¹ In this respect see Section 8.4.2.1(c).

²²² Form CO, Annex 5.4(a)10. [...]

²²³ Form CO, Annex 5.4(a)2 and Annex 5.4(a)9. [...]

²²⁴ Response to questionnaire to providers of music recognition software solutions Q5, question 24. In particular, Musixmatch integrates ACRCLOUD's music recognition online service and customized offline

generally, most of competing providers of ACR software solutions and apps responding to the market investigation considered that the Concentration would have a neutral or positive impact on the market for ACR and music recognition software solutions in the EEA.²²⁵ In this respect, another competitor, Audible Magic noted that the Concentration may be positive since it may encourage digital music distributors to partner with providers of music recognition technology.²²⁶

- (311) Moreover, already pre-Transaction, those alternative providers were offering their music recognition technology to digital music streaming apps. For example, ACRCLOUD is the provider of the music recognition technology used by Deezer in its newly-launched in-app music recognition functionality "Songcatcher"²²⁷, while Gracenote has a partnership with Amazon Music.²²⁸ The viability and competitiveness of the offering of those alternative providers is confirmed in an internal discussion [...].²²⁹
- (312) Thus, the Commission considers that the Concentration would not significantly impede effective competition as a result of conglomerate foreclosure effects in the markets for digital music streaming apps though the integration of Shazam's technology into Apple Music in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway.
- (v) *Shazam as provider of user data to improve existing functionalities, or offer additional functionalities, on digital music streaming apps*
- (313) The Commission considers that the merged entity is likely to have the technical **ability** and the **incentive** to use the Shazam User Data²³⁰ to improve its digital music streaming. [...].²³¹
- (314) Nonetheless, the Commission notes that applicable European rules dealing with data protection, privacy and the protection of the confidentiality of communications, notably the GDPR and the e-Privacy Directive, may pose some limitations as to the transmission of personal data of Shazam's users to the Notifying Party and its subsequent use. In this respect, the same considerations made in Section 8.4.2.1(c)(ii) apply.
- (315) Nonetheless, the Commission considers that, even if the merged entity were to have the ability and the incentive to use the Shazam User Data, it is unlikely that post-Transaction the merged entity would have the ability to foreclose competing providers of digital music streaming apps and that such conduct would have a negative **impact on competition**, in particular with regard to prices and choice in the markets for the digital music streaming apps in the EEA and in the Referring States.

recognition technology, available at: <https://www.acrcloud.com/music-recognition> (accessed on 1 August 2018).

²²⁵ Responses to questionnaire to providers of music recognition software solutions - Q5, question 36.

²²⁶ See agreed minutes of the conference call with Audible Magic of 7 March 2018.

²²⁷ New Deezer SongCatcher Feature Brings Music Closer to the Fans, available at: <http://www.deezer-blog.com/press/new-deezer-songcatcher-feature-brings-music-closer-to-the-fans/> (accessed on 1 August 2018).

²²⁸ New Deezer SongCatcher Feature Brings Music Closer to the Fans, available at: <http://www.deezer-blog.com/press/new-deezer-songcatcher-feature-brings-music-closer-to-the-fans/> (accessed on 1 August 2018).

²²⁹ Shazam internal document, [...], [Doc ID 795-43758].

²³⁰ See recital (69).

²³¹ Form CO, Annex 5.4(a)1.

- (316) First, the market investigation provided mixed results on whether Shazam User Data should be considered as important to offer music streaming services.²³² In fact, some digital music streaming providers indicated that Shazam User Data could be relevant and complementary to the one on their users. Nonetheless, the Commission notes that, currently, [...]. As described in recital (70), Shazam licenses [...] music data charts in customised format and the raw music data used to compile music charts to third parties and, among digital music streaming providers, [...].²³³ Thus Shazam User Data does not appear to be an important input to improve existing functionalities, or offer additional functionalities, on digital music streaming apps.
- (317) Second, the Commission notes that it is unlikely that, should Shazam User Data, or a subset thereof, were to be used exclusively by Apple Music, this would affect a sufficiently important proportion of Apple Music's competitors to result in a significant price increase or reduction of market incentives to innovate. This is because Shazam User Data does not appear to be unique and, thus, be able to confer a significant "data advantage" to Apple post-Transaction and Apple Music's competitors would have the opportunity to access to similar database. In this respect the Commission has compared the Shazam User Data to other dataset available on users of digital music services using four relevant metrics: that is the variety of data composing the dataset; the speed at which the data are collected (velocity); the size of the data set (volume); and the economic relevance (value). These metrics, the so-called "Four Vs"²³⁴, comprise the four key parameters that are increasingly used to assess the commercial and thus competitive relevance of large datasets.
- (318) With regard to the **variety** of data, the Commission notes that, based on the responses to the market investigation, both providers of digital music streaming apps and music recognition services collect similar type of device data (for example, device language, operating system), demographic data (for example, name, gender, age), and behavioural data (for example, user's clicks in app) on their users as the one encompassed in the Shazam User Data.²³⁵
- (319) Further, several respondents have indicated that they collect and do have access to music tag data. Therefore, the same type of data could be available from other sources. Importantly, Deezer has recently launched a music recognition functionality within its digital music streaming app, which would enable it to collect music tag activity about its own users to complement the data on music streaming activity and, thus, further enriching the variety of data it maintains on its users. A similar strategy is available to other music streaming apps, due to the presence of several providers of music recognition technology on the market.²³⁶

²³² Responses to questionnaire to digital music distributors – Q6, questions 51 and 54.

²³³ The effect of the Concentration in relation to the licensing of music charts data has been already discussed in Section 8.3.2.

²³⁴ See "Competition Law and Data", 10 May 2016, joint report of the *Bundeskartellamt* the German National Competition Authority ("NCA") and the *Autorité de la concurrence* French NCA, available at <http://www.autoritedelaconcurrence.fr/doc/reportcompetitionlawanddatafinal.pdf> (accessed on 1 August 2018).

See also, German Monopolies Commission (Monopolkommission), Special Report N.68: Competition policy: The challenge of digital markets", 2015, available at http://www.monopolkommission.de/images/PDF/SG/s68_fulltext_eng.pdf. (accessed on 1 August 2018).

²³⁵ Responses to questionnaire to providers of music recognition software solutions - Q5, question 5. See also, responses to questionnaire to providers of music recognition software solutions – Q6, question 9.

²³⁶ See Section 8.4.2.2.(c)(iv).

- (320) Moreover, the Commission considers that for the purposes of providing recommendations and personalised suggestions to users based on their tastes, several datasets are needed and used in the market. Currently all music streaming players offer such functionality based on their own user consumption data (that is data on the music that users stream) as well as discovery data (that is data collected through various market intelligence sources on popularity of certain music tracks and future music trends). For example, Spotify compiles a database of music discovery data, albeit based on different sources than music tag activity, and it has been very successful in providing personalized experience to their user through recommendations without the use of Shazam data.²³⁷
- (321) Shazam collects only music discovery data based on one possible (even if arguably important) source that is music tag activity (data on which songs a given user has "shazamed" in a given location at a given point in time). Therefore, Shazam User Data seems to be one of the several data points that allow market players (artists, recorded music companies, digital music services) to understand which songs are trending in a given area. However, the variety of data collected by Shazam appears to be more limited compared to data sets collected by other industry players, given that Shazam does not have access to music consumption data.
- (322) With regard to the **velocity** of data, using the average time spent by users each month on the app as a proxy of the speed at which new data is generated and the data previously collected become outdated, it appears that Shazam collects users' data at lower speed compared to providers of music streaming apps. In particular, the Shazam app is used for approximately [...] per month per user,²³⁸ which is significantly lower compared to the time spent by users on Spotify (25 hours per month),²³⁹ on Apple Music ([...] per month)²⁴⁰ or other music streaming apps (on average [...] hours per month).²⁴¹
- (323) With regard to the **volume** of data, while Shazam has access on data on over [...] active users in the EEA, Apple Music's competitors in the EEA, in aggregate, have access to [...] monthly active users with a significantly higher app engagement (in terms of time spent on the app)²⁴² which would result in a significantly higher volume of data compared to Shazam. For example, Spotify publicly stated that it maintains a large and diversified data set of more than 200 petabytes, which provides significant insights into content consumption and user behaviour, including discovery data.²⁴³

²³⁷ Spotify provides recommendations playlists such as Discover Weekly, Release Radar, and Daily Mix. Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018).

²³⁸ Form CO, paragraph 266.
²³⁹ Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018).

²⁴⁰ RFI 36, question 11.

²⁴¹ Commission's calculations based on responses to questionnaire to digital music distributors - Q6, question 8.3.

²⁴² See recital (322).

²⁴³ See Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018).

- (324) With regard to the **value** of data, Shazam User Data does not appear to be a key asset and is not unique. The limited relevance of Shazam User Data is confirmed by [...]Shazam [...] was able to generate [...] EUR [...] worldwide and EUR [...] in the EEA in 2017.²⁴⁴ [...].²⁴⁵
- (325) In the music industry, the most potentially valuable data appears to relate to actual music consumption, as that is the most representative of the correlation across multiple songs a user may like. As a result, the most interesting and valuable data to offer digital music streaming services is typically held by music streaming providers themselves.²⁴⁶
- (326) In particular, Shazam User Data does not appear to be a key element of success of digital music streaming apps. In this respect, the Commission notes in an internal document Shazam itself notes that [...].²⁴⁷ Further, in the market investigation the Commission has asked to Apple's digital music streaming competitors to provide any analysis, study, report (made internally or provided by third party such as external advisors/consultants) they may have undertaken on Shazam User Data, [...]: this suggests that Shazam User Data has no relevance for digital music streaming apps.²⁴⁸
- (327) Thus, it appears that the addition of the Shazam User Data would not allow Apple to materially improve its services by offering even more targeted music suggestions to users. In this respect, in some internal documents, Apple defines Shazam's data as [...] in the market for digital music streaming.²⁴⁹
- (328) In this context, even if the merged entity were to deny access to Shazam User data to competitors of Apple Music, the impact on the ability to compete of those rivals would likely be negligible. Therefore, the Commission considers that Shazam User Data, cannot be qualified as an important input within the meaning of paragraph 34 of the Non-Horizontal Guidelines with respect to the provision of digital music streaming services in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway.
- (329) Thus, the Commission considers that the Concentration is unlikely to lead to a significant impediment of effective competition as a result of input foreclosure effects to the detriment of providers of digital music streaming apps in the EEA and in Austria, France, Italy, Spain, Sweden, Iceland and Norway.
- (vi) *Conclusion*
- (330) In light of the above, the Commission considers that the Concentration would not significantly impede effective competition in the EEA or in any of Austria, France, Italy, Spain, Sweden, Iceland and Norway as a result of non-horizontal foreclosure effects in respect of digital music streaming apps through the practices discussed in

²⁴⁴ Form CO, Table 1.

²⁴⁵ Shazam's submission and internal documents on Shazam's sale process of 26 February 2018.

²⁴⁶ For example, Spotify claims that its programmed "playlists have become a key discovery tool for users" and that Spotify is "an essential partner to both aspiring and established artists by enabling their music to be discovered". In particular, as a result of its programmed playlist, listening diversity is increasing with users being encouraged to discover new artists. Spotify's IPO prospectus, Form F-1, available at: <https://www.sec.gov/Archives/edgar/data/1639920/000119312518063434/d494294df1.htm> (accessed on 1 August 2018). See also, "Listening Diversity Increases Nearly 40 Percent on Spotify", available at: <https://insights.spotify.com/us/2017/11/02/listening-diversity-spotify/> (accessed on 1 August 2018).

²⁴⁷ Shazam internal document, [...], [Doc ID 795-43758].

²⁴⁸ Shazam internal documents, [...], Doc ID:795-42061.

²⁴⁹ [...].

Section 8.4.1.2(c)(i) to Sections 8.4.1.2(c)(iv), including to the extent that these effects would compound the non-horizontal non-coordinated effects of the Concentration stemming from the conduct discussed in Section 8.4.2.1.

8.4.3. *Possible foreclosure of competing providers of ACR software solutions, including music recognition apps*

- (331) ACR software solutions offer a functionality, which is of interest and is also used by the same users of PCs, smart TVs, smart mobile devices and smart wearables. In fact, ACR software solutions are integrated into music recognition solutions which are available on PCs, TVs, smart mobile devices and smart wearables, as is the case for the Shazam app which is available on several platforms. As a result, ACR software solutions and software solutions and/or apps platforms for PCs, smart TVs, smart mobile devices and smart wearables (including smart watches) and smart watches can be considered complementary or at least closely related products within the meaning of paragraph 91 of the Non-Horizontal Merger Guidelines.
- (332) During the market investigation a concern has been raised whereby Apple could increase Shazam's market position in the market for ACR software solutions by leveraging its OS position.²⁵⁰
- (333) In the Article 6(1)(c) Decision, the Commission considered that the Concentration raised serious doubts as to its compatibility with the internal market and the EEA Agreement due to potential foreclosure of competing providers of ACR software solutions in the EEA.
- (334) Accordingly, the Commission analyses whether the Concentration could give rise to non-horizontal non-coordinated effects through foreclosure of competing providers of ACR software solutions in the EEA.

8.4.3.1. The Notifying Party's view

- (335) The Notifying Party submitted that the Concentration would not have any impact on competition on the market for ACR software solutions and narrower potential segments, such as the provision of music recognition apps in the EEA. This is because of the following reasons put forward by the Notifying Party in particular in the Form CO and in the Reply to the Article 6(1)(c) Decision. First, Apple has limited shares of device shipment in the EEA. Second, Apple would not have the ability to foreclose Shazam's competitors since many different platforms would remain available to other providers of ACR software solutions post-Transaction. Third, Apple already pre-Transaction has a deeper integration with Shazam and therefore the Concentration would only result in Apple internalizing a current technology provider: such internalization will not impact Shazam's position on the market. Finally, Apple would not have the incentives to limit access to third party providers of ACR software solutions and music recognition apps since its strategy is to provide a wide range of high quality apps to attract customers. For example, Apple's App Store includes apps that compete with Apple owned-apps such as music streaming services (for example, Spotify's), messenger services (for example, WhatsApp's) and productivity software (such as, Google's).

²⁵⁰ Tonio's written submission of 28 March 2018. See also agreed minutes of the call with Tonio of 15 May 2018 and of 8 March 2018. In the market investigation, no similar concern has been put forward in relation to music recognition apps.

8.4.3.2. Commission's assessment

- (336) On the basis of a complaint received in the market investigation, the Commission has identified some potential practices through which the merged entity could potentially be able to foreclose competing providers of ACR software solutions, including music recognition apps. Post-Transaction, Apple could (i) pre-install the Shazam app on Apple's PCs, smart mobile devices and other platforms; (ii) provide a deeper integration to the Shazam app on Apple's products and services for PCs, smart mobile devices and other platforms; and (iii) reduce the interoperability between Apple's products and services (and, specifically, Apple devices' microphone) and third parties ACR apps and software solution.²⁵¹ As a result, competing providers of ACR software solutions could be potentially be marginalized.
- (337) The Commission's assessment of those practices, in light of the results of the market investigation, is set out in the following recitals. For this purpose, consistent with paragraph 94 of the Non-Horizontal Merger Guidelines, in relation to each of these practice the Commission examines: (i) whether the merged entity would have the ability to foreclose competing providers of ACR software solutions; (ii) whether it would have the economic incentive to do so; and (iii) what overall impact such a foreclosure strategy would have on competition.
- (338) The Commission considers that the merged entity is likely to have the **ability** to pre-install the Shazam apps, to deeply integrate Shazam's technology with its products and services (such as Apple's OSs) and/or to reduce interoperability between Apple's products and services and third parties' ACR software solutions. In this respect, the Commission notes that, first, being a vertically integrated operator in the development of software solutions and/or apps platforms, the merged entity would be capable of integrating the Shazam app or Shazam's ACR software solutions on its devices without incurring significant cost or investments. Second, for the merged entity, it would also be possible to enhance the integration with Shazam's offering and/or to reduce interoperability with third party ACR software solutions since, based on Apple's Developer Program, Apple may revoke or remove access to third parties to its API "*at any time in its sole discretion*".²⁵²

²⁵¹ See agreed minutes of the conference call with Tonio of 15 May 2018. More precisely, in relation to this conduct, Tonio explained that, in the near future, the use of microphones installed in smartphones will change. Audio input will be widely exploited to transmit information from media sources around the user into his/her smartphones. The ACR function will be permanently switched on and will keep on recording all audio input in the surroundings of the user (so called "Always On Strategy"). According to Tonio, the Concentration will provide Apple with the necessary ACR technology to successfully establish on an emerging market for metadata on media consumption, in particular digital music consumption.

In this respect, the Commission notes that, already pre-Transaction, Apple has access to Shazam's technology: thus, if it wanted it could agree with Shazam to undertake the Always On Strategy already pre-Transaction. Moreover, the Commission notes that in response to an RFI pursuant to Article 11(2) of the Merger Regulation, Apple stated that it has no plans, and no intention, of integrating the Shazam music recognition technology into any Apple OSs, or functionality offered on any Apple devices, in order to collect what music the user is playing from a competing music streaming service on an Apple device without the user's consent (response to RFI 46, question 2). Finally, the Commission notes that, should the merged entity decide to undertake the Always On Strategy, it should abide to applicable European rules dealing with data protection, privacy and the protection of the confidentiality of communications, notably the GDPR and the e-Privacy Directive. In this respect, the same considerations made in Section 8.4.2.1(c)(ii) apply in relation to the limitations to the ability to collect and use the data.

²⁵² Annex Q9, RFI12.

- (339) The Commission considers that it is unclear whether the merged entity would have the **incentive** to engage in the practices described at recital (336). On the one hand, Apple is likely to have the incentive to enhance its integration with Shazam’s ACR software solutions and provide more visibility to the Shazam app on its products and services.²⁵³ In particular, as described in recital (308), [...]. On the other hand, it does not seem likely that Apple would reduce its integration with third party music recognition apps and ACR software solutions. In this respect, the Commission notes that, should Apple “grant exclusive access to [its] products’ microphones to Shazam, i.e. [should] only Shazam [be]able to “receive” data via microphone” on Apple’s devices,²⁵⁴ post-Transaction, such conduct may harm the competitiveness of Apple’s core device business. Indeed, this could undermine the attractiveness of Apple’s devices by reducing availability of software solutions and apps that require access to the microphone to operate, but also deprives Apple from the revenues it generates from distributing third party apps,²⁵⁵ in the effort to drive customers to use Shazam, a free app [...].²⁵⁶
- (340) Moreover, the Commission considers that, even if the merged entity were to have the incentive to engage in the practices described at recital (336), it is unlikely that post-Transaction the merged entity would have the ability to foreclose competing providers of ACR software solutions, including music recognition apps, or that such conduct would have a negative **impact on competition**, in particular with regard to prices and choice, in the market for ACR software solutions in the EEA.
- (341) First, as regards the software solutions and/or apps platforms, the Commission notes that Apple has at least a strong position in relation to smart watches, where it had a share of [50-60]% by shipment in the EEA in 2017. In relation to PCs, smart TVs and smart mobile devices, smart wearables (including smart watches), as described in Section 8.2.1, Apple's share of the market is currently more limited in each case. Nonetheless, the Commission further notes that even Apple’s smart watches do not appear to constitute a particularly significant channel for providers of ACR software, and in particular music recognition apps. In this respect the Commission notes that, for example, only [...] % of Shazam’s monthly active users are on Apple’s smartwatches²⁵⁷ and Shazam's monthly active users on smart watches relates to only [...] % of the total number of smart watches shipped worldwide in 2017.²⁵⁸
- (342) Second, the concern at stake does not seem to be merger-specific. Already pre-Transaction, as of mid-2014²⁵⁹ Shazam and Apple had an ongoing partnership pursuant to which Shazam outsourced its technology, including its ACR software solution, to Apple for integration into Apple’s virtual assistant, Siri. Therefore, Apple's choice to partner with Shazam and to refuse integration with competing providers of ACR software solutions and apps is a business choice independent of the Transaction. Moreover, the same complainant, Tonio, in its submission, also

²⁵³ Annex 5.4.(a).1, Form CO.

²⁵⁴ Tonio’s submission, page 13.

²⁵⁵ Apple generated approximately USD [...] revenue from the distribution of third party apps in 2017. See, Annex 37.3 to RFI 10, slide 101.

²⁵⁶ Shazam internal document, [...] [Doc ID 795-53297].

²⁵⁷ Shazam has approximately [...] monthly active users worldwide on Apple Watches, in comparison with Shazam’s total monthly active users worldwide which were [...] as of December 2017; see Reply to Article 6(1)c Decision, paragraph 157.

²⁵⁸ 18 million smart watches have been shipped in 2017. See: <https://techcrunch.com/2018/02/06/apple-watch-shipments-jumped-in-2017-according-to-analysts/?guccounter=1> (accessed on 1 August 2018).

²⁵⁹ Annex 6.3.I Form CO.

noted that its request to access Siri's audio domain had been ignored by Apple long before the Transaction was announced.²⁶⁰

- (343) Furthermore, post-Transaction Apple would still lack an ACR software solution based on watermarking technology which is a different technology from the one developed by Shazam based on fingerprinting.²⁶¹ Thus, Apple's incentives as regards the potential foreclosure of providers of ACR software solutions based on watermarking technology are not likely to be affected by the Concentration as it does not change Apple's market position as regards the ownership of such technology.
- (344) Third, the majority of competing providers of ACR software solutions, including music recognition apps, responding to the market investigation considered that the Concentration would have a neutral or positive impact on the market for ACR software solutions in the EEA (or worldwide).²⁶² In this vein, Audible Magic noted that the Concentration might be positive since it might encourage other digital music distributors to partner with providers of music recognition technology.²⁶³ Musixmatch noted that the Concentration would be really positive for its business.²⁶⁴ Finally, [...].²⁶⁵
- (345) Moreover, one of the main providers of ACR software solutions, ACRCLOUD, noted that the Concentration would not have any impact on its business since even pre-Transaction it did not have any collaboration with Apple.²⁶⁶ Likewise, while some respondents to the market investigation indicated that Apple is a relevant channel, they also noted that only a minority of their revenue is generated from presence on Apple's devices.²⁶⁷
- (346) Further, several respondents expressed the view that several other software solutions platforms would remain available post-Transaction, including but not limited to Android.²⁶⁸ In fact, the Commission notes that, as explained in Section 6.4, ACR software solutions are not specifically developed for smart watches or smart mobile devices, but for a wider range of platforms including smart TVs, PCs and other services aimed at recognising audio content,²⁶⁹ which would not be controlled by Apple post-Transaction.

²⁶⁰ Tonio's written submission of 28 March 2018.

²⁶¹ See Section 6.4.

²⁶² Responses to questionnaire to providers of music recognition software solutions - Q5 2018, question 36.

²⁶³ Agreed minutes of the conference call with Audible Magic of 7 March 2018.

²⁶⁴ Responses to questionnaire to providers of music recognition software solutions - Q5 2018, question 36.
²⁶⁵ [...].

²⁶⁶ Agreed minutes of the conference call with ACRCLOUD of 6 March 2018.

²⁶⁷ Responses to questionnaire to ACR providers - Q37 questions 2, 6, 7 and 8.

²⁶⁸ Responses to questionnaire to ACR providers - Q37, question 7.

²⁶⁹ For example ACR software solutions are used to provide media monitoring services, enabling copyright owner to identify copyrighted music for compliance and royalty management.

(347) Finally, the Commission considers it unlikely that any deeper integration of the Shazam technology with, or pre-installation of the Shazam app within, Apple's devices would lead to the anti-competitive foreclosure of competing ACR software solutions providers. Shazam's current integration with Apple has not prevented other providers of ACR software solutions and music recognition apps to compete²⁷⁰ or enter the market.²⁷¹ In this regard, the Commission notes that, first, as described in Section 8.3.3, even based on an over-estimate Shazam's position in the market, Shazam has only a limited market share of approximately [5-10]% in the market for ACR software solutions at worldwide level. Second, with regard to music recognition apps, being integrated on the pre-installed virtual assistant Siri has not boosted Shazam's usage pre-Transaction, since the number of music tags through Siri accounted for only approximately [...] % of the total volume of music tags by Shazam users in the EEA in 2017.²⁷² Third, the evidence in the Commission's file has not provided any indication that use of the Shazam app on Apple's devices would significantly increase post-Transaction.

8.4.3.3. Conclusion

(348) In light of the above, the Commission considers that the Concentration would not significantly impede effective competition as a result of conglomerate foreclosure effects in the market for ACR software solutions, or in any possible sub-segments of that market including music recognition apps, either in the EEA or worldwide.

9. CONCLUSION

(349) For the reasons set out in Section 8, the Commission finds that the Concentration would not significantly impede effective competition in respect of the provision of any of the following: (i) the licensing of music charts data at worldwide level, in the EEA or in any of the Referring States; (ii) online advertising services in any of the Referring States; (iii) digital music streaming apps in the EEA or in any of the Referring States; and (iv) ACR software solutions at worldwide level or in the EEA,

HAS ADOPTED THIS DECISION:

Article 1

The notified concentration resulting from the transaction whereby Apple, Inc. acquires control, within the meaning of Article 3(1)(b) of the Regulation (EC) No 139/2004, of the entire undertaking of Shazam Entertainment Ltd. is declared compatible with the internal market and the Agreement on the European Economic Area.

²⁷⁰ For example, ACRCLOUD has launched a partnership with Deezer in order to provide in-app music recognition functionalities. See, "New Deezer SongCatcher Feature Brings Music Closer to the Fans", available at: <http://www.deezer-blog.com/press/new-deezer-songcatcher-feature-brings-music-closer-to-the-fans/> (accessed on 1 August 2018).

²⁷¹ For example, Tonio App has been released in October 2014 when the integration agreement between Apple and Shazam was already in place.

²⁷² Form CO, Table 12.

Article 2

This Decision is addressed to:

Apple, Inc.

1 Infinite Loop

CA 95014 - Cupertino

United States of America

Done at Brussels,

For the Commission

(Signed)

Margrethe VESTAGER

Member of the Commission



EUROPEAN COMMISSION
DG Competition

*Case M.8861 -
COMCAST / SKY*

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(1)(b) NON-OPPOSITION
Date: 15/06/2018

*In electronic form on the EUR-Lex website under
document number 32018M8861*



Brussels, 15.6.2018
C(2018) 3923 final

In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

To the notifying party

**Subject: Case M.8861 - Comcast/Sky
Commission decision pursuant to Article 6(1)(b) of Council
Regulation No 139/2004¹ and Article 57 of the Agreement on the
European Economic Area²**

Dear Sir or Madam,

- (1) On 7 May 2018, the European Commission received notification of a proposed concentration pursuant to Article 4 of the Merger Regulation by which Comcast Corporation ("Comcast" or the "Notifying Party", United States) proposes to acquire within the meaning of Article 3(1)(b) of the Merger Regulation sole control of the whole of Sky plc ("Sky", United Kingdom and the "Proposed Transaction"). Comcast and Sky are collectively referred to as the "Parties".³

1. THE OPERATION

- (2) Comcast is a US listed global media, technology and entertainment company, with two primary businesses: Comcast Cable and NBCUniversal ("NBCU"). Comcast is present in Europe almost entirely through NBCU, which is active in Europe in: (i) production, sales and distribution of film and television content; (ii) wholesale supply of TV channels and on-demand services; (iii) CNBC, a business news service, as well as NBC News; (iv) the provision of television content to end users through NBCU's video on demand service; (v) the licensing of its

¹ OJ L 24, 29.1.2004, p. 1 (the 'Merger Regulation'). With effect from 1 December 2009, the Treaty on the Functioning of the European Union ('TFEU') has introduced certain changes, such as the replacement of 'Community' by 'Union' and 'common market' by 'internal market'. The terminology of the TFEU will be used throughout this decision.

² OJ L 1, 3.1.1994, p. 3 (the 'EEA Agreement').

³ Publication in the Official Journal of the European Union No C 170, 17.05.2018, p. 9.

intellectual property to manufacturers and distributors of consumer products; (vi) minor golf-related digital businesses; and (vii) minor direct to consumer DVD, Blu-ray and music disk sales.⁴

- (3) Sky is a UK public company whose shares are listed on the London Stock Exchange. Sky is the holding company of a number of subsidiaries carrying on business in a variety of sectors predominantly in the UK, Ireland, Germany, Austria and Italy, including: (i) licensing/acquisition of audiovisual programming; (ii) TV channel wholesale supply in the UK and Ireland; (iii) retailing of audiovisual programming to subscribers; (iv) provision of technical platform services to broadcasters on Sky's DTH platforms in the UK, Ireland, Germany and Austria; (v) sale of TV advertising; (vi) in the UK and Ireland, the provision of fixed-line retail telephony and broadband services; (vii) in the UK, the provision of mobile communications services; and (viii) in the UK, provision of access to public Wi-Fi hotspots. Sky also recently launched its over-the-top ("OTT") subscription service ("Now TV") in Spain.

2. THE CONCENTRATION

- (4) On 25 April 2018, Comcast published its announcement for a pre-conditional cash offer for the entire issued and to be issued share capital of Sky, under Rule 2.7 of the UK City Code on Takeovers and Mergers. This constitutes the announcement of the intention to launch a public bid in terms of Article 4(1) of the EUMR.
- (5) Comcast intends to implement its offer to acquire the entire issued and to be issued share capital of Sky by way of a takeover offer pursuant to the relevant provisions of Part 28 of the UK Companies Act 2006. Whilst Comcast's objective is to achieve 100% ownership in Sky, under these circumstances, the offer will be conditional upon the receipt of valid acceptances in respect of Sky shares which, together with Sky shares that Comcast has acquired or may agree to acquire (pursuant to the offer or otherwise), carry in aggregate more than 50% of the voting rights normally exercisable at a general meeting of Sky. The offer will thus be conditional on a minimum acceptance condition of 50 per cent, plus one share. The Proposed Transaction therefore constitutes a concentration pursuant to Article 3(1)(b) of the Merger Regulation.
- (6) The Commission notes that, by decision of 7 April 2017 in case M.8354 – *Fox/Sky*, it unconditionally approved the proposed acquisition by Twenty-First Century Fox, Inc. of the remaining shares that it does not currently own in Sky.

⁴ In the US, Comcast is also active as a broadband and cable TV provider. In the course of the market investigation, the Commission received third party submissions alleging that the as a result of the Proposed Transaction, Comcast would engage in anticompetitive foreclosure of third party content over Sky's broadband network. First, the Commission notes that there is no overlap between the Parties for the provision of broadband anywhere in the EEA and as a result, the Parties' market power will not change as a result of the Transaction. Second, Sky's market share for the provision of broadband services in the UK and Ireland is significantly below 30% and a number of other providers will continue to be active post-transaction. As a result, the Commission has not considered these submissions further.

That transaction has not been completed yet. The current transaction in case M.8861 - *Comcast/Sky* constitutes a competing bid for Sky.

3. EU DIMENSION

- (7) The undertakings concerned have a combined aggregate world-wide turnover of more than EUR 5 000 million⁵ (Comcast: EUR 74 437 million; Sky: EUR 15 186 million). Each of them has an EU-wide turnover in excess of EUR 250 million (Comcast: EUR [turnover]; Sky: EUR [turnover]), but they do not achieve more than two-thirds of their aggregate EU-wide turnover within one and the same Member State. The notified operation therefore has an EU dimension pursuant to Article 1(2) of the Merger Regulation.

4. RELEVANT MARKETS

- (8) The Proposed Transaction relates to all the levels of the TV value chain. Section 4.1 first provides an overview of the TV value chain and the Parties activities at each level of the chain. Section 4.2 onward then discusses the product and geographic market definition for each level of the TV value chain.

4.1. Introduction: the TV value chain and the Parties' activities

- (9) Audiovisual ("AV") content for television (TV content) comprises all products (films, sports, series, shows, live events, documentaries, etc.) that are broadcast via TV.⁶ In previous decisions, the Commission has identified different activities in the TV value chain, namely: (i) the production and supply of TV content (including the supply of pre-produced TV content and commissioned TV content); (ii) the wholesale supply of TV channels; and (iii) the retail provision of TV services to end customers.⁷ As a part of its analysis of the Parties' activities, the Commission also considers the Parties' activities in the area of advertising (section 4.1.4).
- (10) Sections 4.1.1 to 4.1.3 further describe these levels of the TV value chain as well as provide an overview of the Parties' activities at each level in the UK, Ireland, Germany, Austria, Italy and Spain.

4.1.1. Production, supply and acquisition of TV content

- (11) This upstream level of the value chain concerns the production of new TV content. TV production companies produce TV content for either: (i) internal use on their own TV channels or retail TV services if they are vertically integrated in the wholesale supply of TV channels and/or in the retail provision of TV services (that is to say, captive TV production); or (ii) supply to third-party customers (that is to say, non-captive TV production).

⁵ Turnover calculated in accordance with Article 5 of the Merger Regulation and the Commission Consolidated Jurisdictional Notice (OJ C 95, 16.4.2008, p. 1).

⁶ Commission decision of 25 June 2008 in case M.5121 *News Corp/Premiere*, recital 28.

⁷ Commission decision of 25 June 2008 in case M.5121 *News Corp/Premiere*, recital 28; Commission decision of 7 April 2017 in case M.8354 – *Fox/Sky*, recital 29.

- (12) Third-party customers are typically: (i) TV channel suppliers (TV broadcasters), which then incorporate the TV content into linear TV channels, or (ii) content platform operators, which then retail the TV content to end users on a non-linear basis (that is to say, Pay-Per-View ("PPV") or video on demand ("VOD")), including non-traditional platforms, that is to say internet or so-called Over-The-Top ("OTT") platforms.
- (13) TV broadcasters and TV distributors who source TV content for their TV channels or retail TV services generally have a choice between a number of sourcing models, which can be broadly categorised as follows:
- a. Obtaining TV content produced on an 'ad hoc' basis (that is to say tailor-made), by:
 - i. Commissioning TV content from a TV production company (which owns the relevant TV format);
 - ii. Hiring a TV production company to provide the technical means and deliver the finished TV content based on a format owned by the broadcaster; or
 - iii. Producing the content themselves by relying on their in-house facilities (captive TV production); or
 - b. Acquiring broadcasting rights from TV production companies for pre-produced TV content (pre-produced TV content, sometimes referred to as off-the-shelf or tape sales).
- (14) As regards commissioned TV content, in most cases, TV production companies produce TV content tailored to the needs of their customers on the basis of original TV formats⁸ that they develop themselves or that they acquire from right holders (commissioned production). However, in some instances, TV production companies are hired by TV broadcasters or content platform operators to simply provide the technical production means and deliver the finished programme based on a TV format owned or acquired by the hiring company (production-for-hire or supply of TV production services).
- (15) The production costs are usually borne entirely or almost entirely by the TV broadcasters or content platform operators. As regards ownership of the various rights relating to the TV content (for example, primary TV broadcast rights, 'catch-up', VOD, etc.), the extent to which those rights are retained by the production company – as opposed to the acquirer of TV content – may vary based on a number of factors, such as national regulation in the country concerned, the type of broadcasting, the outcome of the commercial negotiations between the parties, etc. Producers or the acquirers of TV content may then achieve secondary revenues by further licensing/distributing the TV content or the TV format to third parties.
- (16) As regards pre-produced TV content, this upstream level of the value chain concerns the licensing of broadcasting rights relating to pre-existing TV content –

⁸ Commission decision of 25 June 2008 in case M.5121 *News Corp/Premiere*, recital 28.

that is to say TV content that has been previously produced and is subsequently made available ‘off-the-shelf’ by the rights holder (so-called pre-produced TV content) – and broadcasting rights relating to sports events.

- (17) The broadcasting rights relating to TV content can belong to one or more of the following: (i) the holder of the rights to the TV format; (ii) the production company that produced the TV content; and (iii) the company that commissioned the production of the TV content. In addition, the broadcasting rights can belong to a third-party distributor, to which they were licensed by the original owner, with a right to sub-license.
- (18) As regards the supply-side of the market:
 - a. Sky licenses small amounts of both commissioned and pre-produced TV content through its distribution arm, Sky Vision. It has also minimal activities through its Vision Distribution joint venture⁹ and Sky Cinema Original Films initiative¹⁰.
 - b. Comcast licenses both commissioned and pre-produced TV content via several NBCU companies (e.g. Universal Studios, Carnival Films and others).
- (19) As regards the demand-side of the market:
 - a. Sky acquires some TV content from third party content owners and distributors to include in its own channels and for its content platforms;
 - b. Comcast has a minor presence in acquisition of TV content in the EEA to include in its own channels.

4.1.2. Wholesale supply and acquisition of TV channels

- (20) TV broadcasters use the TV content that they have acquired or produced in-house in order to package it into linear TV channels. (Linear) TV channels are broadcast to end users either on a free-to-air ("FTA") basis or on a pay-TV basis.
- (21) At a very general level, FTA channels are TV channels that are available to viewers free of charge. Pay-TV channels are channels for which the viewer must pay a subscription fee in order to watch. Traditionally, FTA channels finance their operations via advertising revenues (with the exception of the publicly-owned TV channels in a number of Member States which are subject to advertising limitations), while pay-TV channels generate revenues through subscription fees.
- (22) The Commission notes that TV broadcasters are increasingly complementing their traditional linear TV channel offering with non-linear services such as VOD services.¹¹

⁹ Vision Distribution is a joint venture with five Italian independent producers (Cattleya, Wildside, Lucisano, Palomar, and Indian Production), focused on Italian films.

¹⁰ The initiative was launched in 2018.

¹¹ VOD services can be further differentiated into three types. First, Subscription VOD ("SVOD") designates a service whereby the end user obtains the right to watch multiple titles during a

- (23) Some TV broadcasters are vertically integrated as they are also active as retail TV operators (TV distributors) in the market for the retail provision of TV services to end users. Other TV broadcasters are not vertically integrated and rely on third party TV distributors to distribute their TV channels at the retail level.
- (24) As regards the supply-side of the market:
- a. Sky supplies channels to TV distributors and also holds a 50% stake in channel provider A&E Networks UK, a joint venture with A&E Networks. Sky does not supply channels on a wholesale basis in Italy and Austria, and only to very limited extent in Germany;
 - b. NBCU supplies a range of basic pay-TV channels on a wholesale basis, including 13th Street, Universal Channel, SyFy, E!, CNBC and Movies24.
- (25) As regards the demand-side of the market:
- a. Sky enters into agreements with TV broadcasters for the distribution of TV channels in the UK, Ireland, Germany, Austria and Italy;
 - b. Comcast does not acquire TV channels.

4.1.3. Retail provision of TV services to end users

- (26) TV distributors either limit themselves to carrying TV channels and making them available to end users, or also act as channel aggregators, which ‘package’ TV channels. The TV services supplied by TV distributors to end users consist of: (i) packages of linear TV channels (which they have either acquired or produced themselves); and (ii) content aggregated in non-linear services, such as VOD, SVOD, TVOD and PPV. TV content can be delivered to end users through a number of technical means including cable, satellite and IPTV.¹² OTT players deliver channels and content in both a linear and non-linear fashion through the use of the internet.
- (27) The content offered by the TV distributor is presented in an electronic programme guide ("EPG"), which is an application used on television sets to list current and scheduled programmes that are or will be available on each channel and a short summary or commentary for each programme. Each channel broadcast on the TV platform receives an EPG position, which is usually agreed between the TV broadcaster and the TV distributor. Traditional EPGs are not always used with

designated time period, for instance one month, through a single payment. Second, Transactional VOD ("TVOD") designates a service whereby the end user obtains the right to watch a single selected title within a designated time frame, for instance within 24 hours, through a single payment. Third, pay per view ("PPV") designates a service whereby the end user makes a payment to watch a single title that is being broadcast at a specific time, which is the same for all viewers. In the case of TVOD and SVOD, viewers can select, purchase and view the titles at times of their own preference, whereas in the case of a title available for PPV, viewers purchase the right to watch that title at the given time it is broadcast, which is the same for everyone (for instance, the right to watch the live broadcast of a football match can be purchased for PPV).

¹² IPTV is the abbreviation for Internet Protocol TV; it is a system through which television services are delivered using the Internet protocol over a packet-switched network such as the internet, instead of being delivered through traditional terrestrial, satellite signal and cable television formats.

regard to online content platforms and other non-linear methods of supplying content, or may form only part of a TV distributor's customer interface.

(28) In the retail provision of TV services to end users:

(a) Sky offers retail services in the UK, Ireland, Germany, Austria and Italy, retailing its own and third party linear pay-TV channels and VOD programming via DTH satellite, OTT and mobile technologies to end customers. Sky also broadcasts a limited number of FTA channels: Sky News International (available across much of Europe); in the UK and Ireland, Sky News, Sky News Arabia, Challenge, Pick and the Sky Intro channel; and in Italy, Cielo and TV8. Sky's TV services on an OTT basis include NowTV in the UK, Ireland¹³ and Italy, "Sky Ticket" in Germany and Austria, Sky Go (which is an OTT service available to DTH subscribers) and services operated under the Sky brand in Spain, which enable the end user to access Sky TV content in a linear and/or non-linear manner on big screen and small screen mobile devices without requiring a cable or satellite connection with Sky.

(b) NBCU supplies on demand service *hayu* in the UK and Ireland. It also offers limited direct sales to clients from licensing the CNBC linear channel in the UK, Ireland, Germany, Austria and Italy.

4.1.4. Advertising

(29) Advertising space can be provided through various media, including newspapers, TV airtime, radio or online advertising.

(30) When it comes to online advertising, the online advertising value chain has, on the supply side, ad publishers (including broadcasters and website owners); and on the demand side, advertisers, media buyers and advertising agencies. The ad publishers have advertising inventory available (i.e. "spaces" on their websites, videos or other digital assets) that they seek to monetise. The demand-side players seek these spaces on which to display their advertisements. Intermediaries, ad networks and ad exchanges sometimes operate in between those two markets.

(31) Once advertising space has been sold by a publisher to an advertiser, either directly or through an intermediary, both parties need to ensure that the correct ad actually appears (i.e. is served) onto the publisher website space at the right place at the right time. This step is undertaken by the ad serving tools.

(32) Both Parties are active in the supply of TV advertising airtime. Sky is also active in selling online advertising space, including targeted advertising (through Sky AdSmart) and multiplatform advertising (through Sky Advance). Apart from that, Comcast provides online display ad serving technology (through FreeWheel).

¹³ A difference between standard Sky retail TV services and NowTV is the method of distribution. NowTV customers also have more limited access to content compared to regular Sky TV customers. NowTV customers gain access to content via subscriptions to "passes" which allows them to view pre-defined blocks of linear TV channels and on-demand content.

4.2. Production, supply and acquisition of TV content

4.2.1. Product market definition

4.2.1.1. Commission precedents

- (33) With regard to the market for the supply of TV content, in previous decisions the Commission has concluded that there are separate markets for the: (i) production and supply of commissioned TV content; and (ii) licencing of broadcasting rights for pre-produced TV content.¹⁴
- (34) With regard to the market for licencing of broadcasting rights for TV content, the Commission has considered that it could be subdivided by content type, in particular: (i) films; (ii) sports; and (iii) other TV content (i.e. all non-sport, non-film content); and potential sub-segments within these content types. Ultimately, the Commission left the exact scope of the product market open.¹⁵
- (35) The Commission has also considered further sub-dividing the market for the licensing of broadcasting rights for TV content by exhibition window: (i) subscription video on demand ("SVOD"); (ii) transactional video on demand ("TVOD"); (iii) pay-per-view ("PPV"); (iv) first pay-TV window; (v) second pay-TV window; and (vi) FTA; but left the market definition open.¹⁶

4.2.1.2. Notifying Party's view

- (36) The Notifying party submits that, notwithstanding potential sub-divisions of TV content, if a company is only active in the production of one type of content (in particular, film content) it would be able to start producing sports content and/or other TV content within a short timeframe and without incurring significant additional costs. Moreover, there is no material difference from a demand-side perspective between US films and non-US films since both types compete to attract the same viewing audience in the EEA. Accordingly, it is the Notifying Party's view that the distinction in the Commission's decisional practice by

¹⁴ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 69. See also Commission decision of 16 September 2014 in case M.7282 *Liberty Global/Discovery/All3Media*, recital 41 and Commission decision of 9 October 2014 in case M.7360 *21st Century Fox/Apollo/JV*, recital 40.

¹⁵ Commission decision of 7 April 2017 in case M.8354 – *Fox/Sky*, recital 67; Commission decision of 21 December 2011 in case M.6369 *HBO/Ziggo/HBO Nederland* and Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 69; Commission decision of 21 December 2011 in case M.6369 *HBO/Ziggo/HBO Nederland*, recitals 18–20; Commission decision of 15 April 2013 in case M.6880 *Liberty Global/Virgin Media*, recital 19. Moreover, as regards sports, the Commission has also previously considered a distinction between football and other sports and further distinctions within football, for example between regular football events and football events that are played more intermittently (Commission decision of 18 January 2007 in case M.4519 *Lagardère/Sportfive*, recital 10). As regards films, the Commission has considered distinguishing between US-produced films and other films (Commission decision of 2 April 2003 in case M.2876 *News Corp/Telepiù*, recitals 58 and 61).

¹⁶ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 69; Commission decision of 21 December 2011 in case M.6369 *HBO/Ziggo/HBO Nederland*, recital 18; Commission decision of 16 September 2014 in case M.7282 *Liberty Global/Discovery/All3Media*, recitals 46–48; Commission decision of 9 October 2014 in case M.7360 *21st Century Fox/Apollo/JV*, recitals 45–47, Commission decision of 10 October 2014 in case M.7000 *Liberty Global/Ziggo*, recitals 38–44.

content type may not necessarily reflect conditions of competition from a supply or demand side perspective.

- (37) Moreover, the Notifying Party does not believe that it is necessary formally to distinguish the licensing of broadcasting rights by exhibition window (SVOD, TVOD, PPV, first pay-TV window, second pay-TV window or FTA) for the purpose of market definition since suppliers of TV content do not produce different types of TV content designed for different exhibition windows, and the content licensed in each window is broadly substitutable from a demand side perspective.

4.2.1.3. The Commission's assessment

- (38) The results of the market investigation indicate that, although content providers did not provide definitive views, most broadcasters and retail providers of audiovisual services consider the segmentations adopted in prior Commission decisions (by content type and exhibition window as indicated above) still relevant.¹⁷
- (39) In any event, for the purpose of this decision, the exact product market definition for the production and supply of TV content can be left open, as the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market regardless of whether the market is segmented on the basis of content type or exhibition window.

4.2.2. *Geographic market definition*

4.2.2.1. Commission precedents

- (40) In past decisions, the Commission has defined the market for the production and supply of TV content, including production of TV content and the licensing of broadcasting rights for TV content to be either national or regional, based on linguistically homogeneous areas.¹⁸

4.2.2.2. Notifying Party's view

- (41) Comcast submits that the relevant geographic market for the production and supply of TV content, including any narrower segmentation thereof, is national in scope. This delineation reflects the nature of the typical licensing relationship between the supplier of the TV content and the licensee. In particular, Comcast considers that the majority of licensing relationships are concluded at the national level, with some exceptions in which the licensee obtains broadcasting rights to multiple countries/regions with a common language. Moreover, in many cases, supranational considerations are not relevant given many broadcasters (particularly FTA broadcasters) are only active in one Member State.

¹⁷ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, part B; Replies to Questionnaire Q3 to TV distributors of 7 May 2018, part B.

¹⁸ Commission decision of 7 April 2017 in case M.8354 – *Fox/Sky*, recital 74; Commission decision of 21 December 2010 in case M.5932 *News Corp/BSkyB*, recitals 73–75; Commission decision of 15 April 2013 in case M.6880 *Liberty Global/Virgin Media*, recital 24. Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recitals 73-76.

Accordingly, it is more appropriate to delineate the geographic scope of the market based on national, rather than linguistic, boundaries.

4.2.2.3. The Commission's assessment

- (42) The results of the market investigation show that most of the respondents among TV broadcasters and distributors purchase content nationally or for certain linguistic regions. Broadcasters sometimes also purchase content on an EEA or worldwide basis.¹⁹
- (43) In any event, for the purpose of this decision, the exact geographic market definition for the production and supply of TV content can be left open, as the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market regardless of whether the market is considered to be national or by linguistic region.

4.3. Wholesale supply and acquisition of TV channels

- (44) TV broadcasters package the TV content that they have acquired or produced in-house into linear TV channels. Linear TV channels are broadcast to end users either on a FTA basis or on a pay-TV basis. This wholesale level is an intermediate activity between upstream production and licensing of content, and the downstream retail provision of TV services to customers.

4.3.1. Product market definition

4.3.1.1. Commission precedents

- (45) In previous decisions, the Commission has identified a wholesale market for the supply of TV channels. Within that market, the Commission has further identified two separate product markets for: (i) FTA TV channels; and (ii) pay-TV channels.²⁰ The Commission has further concluded that within the pay-TV channel market, there are separate markets for: (i) premium pay-TV channels; and (ii) basic pay-TV channels. For the purposes of its assessment, the Commission has considered FTA channels to be in the market for basic pay-TV channels.²¹
- (46) In previous decisions, the Commission also examined a number of other potential segmentations, including: (i) genre or thematic content (such as films, sports, general entertainment, news, youth, and others);²² (ii) linear channels vs non-

¹⁹ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question B4.

²⁰ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 91. Commission decision of 18 July 2007 in case M.4504 *SFR/Télé 2 France*, recitals 37–40; Commission decision of 18 July 2007 in case M.4504 *SFR/Télé 2 France*, recital 40; Commission decision of 21 December 2010 in case M.5932 *News Corp/BskyB*, recitals 80, 83 and 85; Commission decision of 21 December 2011 in case M.6369 *HBO/Ziggo/HBO Nederland*, recital 24; Commission decision of 15 April 2013 in case M.6880 *Liberty Global/Virgin Media*, recital 37.

²¹ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 101.

²² Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 92. Commission decision of 2 April 2003 in case M.2876 *Newscorp/Telepiù*, 2 April 2003, recital 76; Commission decision of 18 July 2007 in case M.4504 *SFR/Télé 2 France*, recitals 41–42; Commission decision of 26 August 2008 in case M.5121 *News Corp/Premiere*,

linear services (VOD, PPV);²³ and (iii) the different means of infrastructure used for the delivery to the viewer (cable, satellite, terrestrial TV and IPTV).²⁴ It has ultimately left the market definition open in all these regards.

4.3.1.2. Notifying Party's view

- (47) The Notifying Party considers that basic pay-TV channels and FTA TV channels are broadly substitutable, since any differences in terms of content, pricing and licensing rights are insufficient to create a meaningful distinction. In this respect, Comcast notes that a programme produced for pay-TV could just as easily play on a FTA platform, and is not inherently of a different type. Within basic pay-TV channels, as mentioned above, Comcast considers that it is not necessary to distinguish between channels on the basis of genres for the purposes of product market definition, since each of the above mentioned genres are broadly substitutable with one another from the consumer's perspective.
- (48) In particular, the Notifying Party considers that a distinction between FTA and pay-TV does not make sense with respect to news channels. Several channels providing news content, for example the BBC and Sky News in the UK and Ireland, are available on both a FTA basis and through the EPG for retail pay-TV services in the five Member States where Sky is primarily active. Further, within these Member States, the majority of news viewing tends to be undertaken on channels available on a FTA basis, even on pay-TV platforms. Consequently, FTA news channels (such as the BBC and Sky News in the UK) are in direct competition with the (generally much smaller) news channels which are only available on a pay-TV basis (e.g. Euronews in the UK). The lack of any practical distinction between FTA and pay-TV news channels is also demonstrated by the fact that many news channels – including CNBC in the UK, Ireland and Italy – are available both FTA and via pay-TV platforms. The lack of relevance of a distinction between FTA and pay-TV in the news genre is further illustrated through the choice of several media regulatory agencies to analyse news consumption at the level of “all TV” when reporting on news consumption and competitive dynamics within their Member State.

4.3.1.3. The Commission's assessment

- (49) According to broadcasters, the distinctions drawn between FTA and pay-TV channels as well as between basic and premium pay-TV are still relevant in the UK, Ireland, Germany, Austria and Italy. However, the market investigation did not provide definitive views on whether thematic channels are only substitutable with other channels that broadcast the same specific content.²⁵

recital 35; Commission decision of 21 December 2010 in case M.5932 *News Corp/BskyB*, recital 81; Commission decision of 10 October 2014 in case M.7000 *Liberty Global/Ziggo*, recital 89.

²³ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 94. Commission decision of 18 July 2007 in case M.4504 *SFR/Télé 2 France*, recital 43; Commission decision of 26 August 2008 in case M.5121 *News Corp/Premiere*, recital 21.

²⁴ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 98. Commission decision of 18 July 2007 in case M.4504 *SFR/Télé 2 France*, recital 44; Commission decision of 26 August 2008 in case M.5121 *News Corp/Premiere*, recital 22.

²⁵ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, part B.

- (50) In any event, for the purpose of this decision, the exact product market definition in relation of the wholesale supply of TV channels can be left open, as the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market regardless of whether the market is segmented on the basis of channel type or exhibition window.

4.3.2. *Geographic market definition*

4.3.2.1. Commission precedents

- (51) In previous decisions, the Commission found the market for the wholesale supply of TV channels to be either national in scope,²⁶ sub-national,²⁷ or by linguistic region encompassing more than one Member State.²⁸

4.3.2.2. Notifying Party's view

- (52) Comcast considers that the appropriate geographic market is national in scope, given that the majority of wholesale supply relationships are concluded at the national level, with some exceptions in which the retailer obtains broadcasting rights to multiple countries/regions with a common language.

4.3.2.3. The Commission's assessment

- (53) The results of the market investigation show that the majority of agreements between TV broadcasters and retail TV distributors for the wholesale supply of TV channels are negotiated on either a national basis, although they are also sometimes negotiated on a linguistic basis. Exceptionally, agreements are also made on a sub-national or worldwide basis.²⁹
- (54) In any event, for the purpose of this decision, the exact geographic market definition for wholesale supply of TV channels can be left open, as the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market regardless of whether the market is considered as national, sub-national or by linguistic region.

4.4. **Retail provision of TV services**

4.4.1. *Product market definition*

4.4.1.1. Commission precedents

- (55) In previous cases the Commission has split the retail supply of television services in two separate markets: (i) FTA and pay-TV.³⁰ The Commission also considered

²⁶ Commission decision of 21 December 2011 in case M.6369 *HBO/Ziggo/HBO Nederland*, recital 39; Commission decision of 15 April 2013 in case M.6880 *Liberty Global/Virgin Media*, recital 41; Commission decision of 10 October 2014 in case M.7000 *Liberty Global/Ziggo*, recital 98.

²⁷ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*.

²⁸ Commission decision of 21 December 2010 in case M.5932 *News Corp/BskyB*, recitals 86–88; Commission decision of 15 April 2013 in case M.6880 *Liberty Global/Virgin Media*.

²⁹ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question B4.

³⁰ See for instance the Commission decisions of 18 July 2007 in case M.4504 *SFR/Télé 2 France*, recital 40, and of 25 June 2008 in case M.5121 *News Corp / Premiere*, recital 20. In other cases this

whether pay-TV can be segmented further according to: (ii) linear vs non-linear pay-TV services;³¹ (iii) according to distribution technologies (e.g. cable, satellite, or terrestrial);³² and (iv) premium vs basic pay-TV services.³³ In recent cases, the Commission has left open the market definition with regard to each of these potential sub-segments.³⁴

4.4.1.2. Notifying Party's view

- (56) Sky considers that there is a single, albeit differentiated, market for the provision of all audiovisual services (comprising pay and FTA, basic and premium) to end users.

4.4.1.3. The Commission's assessment

- (57) A number of respondents to the market investigation doubted the relevance of the distinction between basic and premium pay-TV. In addition, respondents were divided as to whether the provision of retail services could be segmented by genre.³⁵
- (58) The results of the market investigation indicated that most distributors provide both linear and non-linear services. However, they did not provide definitive views as to whether the broadcasting rights for linear and non-linear services are always acquired separately or together. A majority of distributors did not consider VOD services offered by OTT providers substitutable to pay-TV services.³⁶
- (59) In any event, for the purpose of this decision, the exact product market definition in relation of the retail supply of TV services can be left open, as the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market regardless of whether the market is further segmented or not.

question has instead been left open (see for instance the Commission decisions of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 119-120, of 25 June 2008 in case M.5121 *News Corp/Premiere*, recitals 15 and 21, and of 10 October 2014 in case M.7000 *Liberty Global/Ziggo*, recital 108).

³¹ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 124. Commission decision of 25 June 2008 in case M.5121 *News Corp/Premiere*, recital 21. Commission decision of 10 October 2014 in case M.7000 *Liberty Global/Ziggo*, recitals 109–110.

³² Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 127. Commission decision of 25 June 2008 in case M.5121 *News Corp/Premiere*, recital 22; Commission decision of 21 December 2010 in case M.5932 *News Corp/BskyB*, recital 105. Commission decision of 10 October 2014 in case M.7000 *Liberty Global/Ziggo*, recital 113.

³³ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*, recital 119.

³⁴ Commission decision of 7 April 2017 in case M.8354 – *Fox/Sky*.

³⁵ Replies to Questionnaire Q3 to TV distributors of 7 May 2018, part B.

³⁶ Replies to Questionnaire Q3 to TV distributors of 7 May 2018, part B.

4.4.2. *Geographic market definition*

4.4.2.1. Commission precedents

- (60) The Commission has previously considered that the market for the retail provision of TV services is either national, or limited to the geographic coverage of a supplier's cable network.³⁷

4.4.2.2. Notifying Party's view

- (61) Comcast considers that the geographic scope of the market for the retail provision of TV services is national, but submits that the analysis would not be materially different if the markets were combined into linguistic regions (or considered on a sub-national basis).

4.4.2.3. The Commission's assessment

- (62) Nothing in the market investigation contradicts the Commission's previous findings that the market is either national, or limited to the geographic coverage of a supplier's cable network.
- (63) In any event, the Commission considers the exact geographic market definition for the retail provision of TV services can be left open, as the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market on any geographic basis.

4.5. Advertising

4.5.1. *Product market definition*

4.5.1.1. Commission precedents

- (64) The Commission has previously defined separate product markets for the sale of advertising space in national newspapers and TV broadcasting.³⁸ The Commission has also drawn a distinction between online and offline advertising, due to each channel's specificity and different pricing mechanisms.³⁹
- (65) With respect to TV advertising, the Commission has not previously distinguished between advertising space on FTA channels and pay-TV channels.⁴⁰
- (66) With respect to online advertising, the Commission has previously distinguished between the market from the provision of advertising space and the market for the provision of online display ad technology.⁴¹ Within the market for the provision of advertising space, the Commission has considered that: (i) there may be

³⁷ Commission decision of 24 February 2015 in case M.7194 *Liberty Global / Corelio / W&W / De Vijver Media*.

³⁸ Commission decision of 21 December 2010 in case M.5932 *News Corp/BskyB*, recital 267.

³⁹ Commission decision of 9 September 2014 in case M.7288 *Viacom/Channel 5 Broadcasting*, recital 35.

⁴⁰ *News Corp/BskyB*, recital 267, *Viacom/Channel 5 Broadcasting*, recital 38.

⁴¹ Commission decision of 11 March 2008 in case M.4731 *Google/DoubleClick*, recital 56.

different markets for search and non-search advertising but left the market open;⁴² and (ii) intermediation is likely part of the market.⁴³

4.5.1.2. Notifying Party's view

- (67) The Notifying Party notes that advertisers typically use TV advertising airtime to reach a mass audience, while also seeking to reach particular audience demographics that might be delivered by advertising on particular channels or programmes. Moreover, in view of the increasing consumption of TV services (particularly non-linear services) online, online advertising exercises an increasing competitive constraint on TV advertising. Comcast considers that the precise definition of the relevant market can be left open, as the Proposed Transaction does not raise any competition concerns under any plausible product market definition.
- (68) The Notifying Party considers that the relevant market comprises the supply of online display ad serving technology, in line with previous Commission precedent.

4.5.1.3. The Commission's assessment

- (69) Nothing in the market investigation contradicts the Commission's previous findings regarding the advertising markets.
- (70) In any event, the Commission considers that the precise definition of the relevant market can be left open, as the Proposed Transaction does not raise any competition concerns under any plausible product market definition.

4.5.2. *Geographic market definition*

4.5.2.1. Commission precedents

- (71) Previous Commission decisions have taken the view that the markets for TV advertising are national in scope.⁴⁴
- (72) As regards the geographic market definition for online display ad serving technology services, the Commission has previously considered the geographic market for these services to be at least EEA-wide in scope.⁴⁵

4.5.2.2. Notifying Party's view

- (73) The Notifying Party considers that there is no need to precisely delineate the scope of these markets as the Proposed Transaction does not raise concerns under any approach to geographic market definition. It does not offer a position on the geographic scope of online display ad serving technology services market.

⁴² Commission decision of 11 March 2008 in case M.4731 *Google/DoubleClick*, recital 73.

⁴³ Commission decision of 11 March 2008 in case M.4731 *Google/DoubleClick*, recital 81.

⁴⁴ Commission decision of 7 March 2008 in the case M.5051 - *APW/GMG/EMAP*; Commission decision of 21 December 2010 in case M.5932 *News Corp/BskyB*; and Commission decision date 9 September 2014 in case M.7288 *Viacom/Channel 5 Broadcasting*.

⁴⁵ *Google/DoubleClick*, recital 91.

4.5.2.3. The Commission's assessment

- (74) Nothing in the market investigation contradicts the Commission's previous findings that the markets for TV advertising are national in scope and that the market for online display ad serving technology services is at least EEA in scope.
- (75) Accordingly, in line with previous decisions, the Commission takes the view that the markets for advertising TV space and newspaper advertising are national in scope. The Commission also considers the geographic market for online display ad serving technology services to be at least EEA-wide but leaves the precise geographic market definition open.

5. COMPETITIVE ASSESSMENT – HORIZONTALLY AFFECTED MARKETS

- (76) The Proposed Transaction results in a number of horizontal overlaps at different levels of the distribution chain.
- (77) Upstream, the Parties' activities overlap with regard to the supply of TV content. Comcast is active with regard to the production and supply of commissioned TV content, as well as licensing pre-produced film and other TV content.⁴⁶ While Sky has some marginal activities with regard to licensing pre-produced and commissioned TV content and sports content, its presence upstream is negligible, leading to no horizontally affected markets in relation to the production or supply of TV content.
- (78) The Parties' activities also overlap with regard to the acquisition of TV content which: (i) Sky includes in its TV channels (which are incorporated into its retail TV offering and/or wholesales to third parties) as well as for supply via its PPV/TVOD services; and (ii) Comcast includes in its TV channels which are wholesaled to third parties. This overlap results in a number of horizontally affected markets in the UK, Ireland, Germany, Austria and Italy, which are discussed further below in Sections 5.1, 5.2 and 5.3.
- (79) Both Parties supply TV channels on a wholesale basis to third parties in a number of Member States. Sky supplies a range of channels including sports, movie and other channels to third parties, in particular those under the Sky brand. Comcast has a more limited number of TV channels, including 13th Street, Universal Channel, Syfy, E!, CNBC and Movies24. Horizontally affected markets arise in the UK and Ireland which are discussed further below in Sections 5.4 and 5.5 respectively.
- (80) In Germany, Austria and Italy, Sky's has a "self-retail" business model: in addition to retailing TV channels on its own platform, Sky's service is available on the platform of cable network and IPTV providers who transmit the programs' signal to end customers and perform certain marketing and distribution services for Sky. Sky, however, enters into direct contractual relationships with subscribers, controls subscriber data, deploys its own subscriber management system and retains the rights to determine the service packaging and pricing. Sky

⁴⁶ NBCU also has limited licencing activities for sports content.

is therefore not active with regard to the wholesale distribution of TV channels in Germany, Austria and Italy and no affected markets arise.

- (81) Sky is active as a retail supplier of TV services in the UK, Ireland, Germany, Austria and Italy. Comcast is also active in those Member States with the overlap resulting in an affected market in United Kingdom, Ireland, and Italy which is discussed further below in Section 5.6.
- (82) For the sake of completeness, the Commission notes that Sky also expanded its OTT offering by launching a retail TV service in Spain on 11 September 2017 under the Sky brand via NOW TV.⁴⁷ Sky's retail offering in Spain does not currently include any of Sky's own TV channels, but rather broadcasts third party TV channels supplied by wholesale TV channel suppliers such as Twenty First Century Fox ("21CF"), Turner, NBCU and Viacom. However, no horizontally affected markets arise.
- (83) Finally, the Parties' activities also overlap with regard to the supply of TV advertising airtime on their TV channels. However no horizontally affected markets arise on any plausible market definition.
- (84) In the course of the market investigation the Commission received a third party submission alleging possible adverse effects on competition arising from the Proposed Transaction in the market for premium video advertising technology services. Comcast is active in the provision of online display ad serving technology services (FreeWheel), while Sky provides targeted and multi-platform advertising services (Sky AdSmart and Sky AdVance).
- (85) While reserving an opinion on the precise delineation of the product market, the Commission considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market in relation to video advertising technology services. Sky's services are not an online ad serving technology,⁴⁸ and Sky requires ad serving technology from third-party providers for its on demand adverts. The Transaction therefore does not lead to any overlap in this respect. In addition, Comcast's position in the relevant market is limited (even on the narrowest market definition, Comcast's market share will amount to [5-10] – [10-20]%) and there are other competitors present, for example Google DoubleClick, Ooyala, AppNexus or SpotX.

5.1. Acquisition of TV content - UK & Ireland

- (86) In the UK and Ireland, both NBCU and Sky acquire distribution rights for TV content for inclusion in their TV channels and in their non-linear service

⁴⁷ The Service comprises 16 non-exclusive, non-premium linear channels and over 3,000 hours of video-on-demand programming priced at EUR 10 a month with no contract. The linear channels available on Sky's OTT service include (inter alia): FOX, FOX Life, TNT, Historia, Syfy, Disney Junior, Nickelodeon, TCM, Comedy Central, Calle 13, Disney XD and National Geographic. On demand content accessible via the OTT service includes boxset TV series and movies such as *How I Met Your Mother*, *Grey's Anatomy*, and *Guardians of the Galaxy*. Catch-up content from the available linear channels is also made available to subscribers on-demand.

⁴⁸ The online ad serving technology market has been considered in *Google/DoubleClick*; Ad serving tools ensure that the correct ad actually appears (i.e. is served) onto the publisher website space at the right place at the right time.

offerings. Table 1 below shows the segments where the Parties' overlapping activities result in horizontally affected markets, namely: (i) acquisition of all TV content, and (ii) acquisition of all film content. There are no affected markets when considering a segment of all other TV content, or when considering only pre-produced content.

Table 1 - Market shares for the acquisition of TV content – UK & Ireland -2017

	All TV content (%)	All film content (%)
NBCU	[0-5]	[0-5]
Sky	[40-50]	[50-60]
Combined	[40-50]	[50-60]

Source: Form CO, table 7.

- (87) Table 1 shows that when considering the market for the acquisition for all TV content, the Parties combined market share is [40-50]%. However, the increment brought about by the Proposed Transaction is limited as while Sky has a market share of [40-50]%, Comcast's share is less than [0-5]%. When considering the segment for the acquisition of film content, the position is similar. The Parties have a combined market share of [50-60]% with an increment of just [0-5]%. The market shares do not materially change when considering the UK and Ireland separately although for the acquisition of film content in Ireland, there would not be an overlap as Comcast [*business secret regarding business strategy of Notifying Party*] film content in Ireland.
- (88) Whilst Sky has a material share for the acquisition of all TV content and film content in the UK and Ireland, the Proposed Transaction does not materially change the competitive landscape in those segments and is unlikely to significantly increase Sky's market power because of the limited increment.
- (89) Moreover, in each of the UK and Ireland there are also a number of other players present in the segment for the acquisition of film content, including the BBC, ITV and Channel 4, as well as OTT players such as Netflix and Amazon.
- (90) Consequently, the Commission considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market with regard to the acquisition of TV content in the UK and Ireland, whether the Member States are considered together or separately.

5.2. Acquisition of TV content – Germany & Austria

- (91) In Germany and Austria both NBCU and Sky acquire distribution rights for TV content for inclusion in their TV channels. Table 2 shows the Parties' market share for the segment for all film content. No affected market arises when considering the market for the acquisition of all film content.

Table 2 - Market shares for the acquisition of TV content – Germany and Austria - 2017

	All film content (%)
NBCU	[0-5]
Sky	[20-30]
Combined	[20-30]

Source: Form CO, table 7.

- (92) Table 2 shows that the Parties combined share is [20-30]% (Sky: [20-30]%; Comcast: [0-5]%). The market shares do not materially change when considering Germany and Austria separately.
- (93) Given the minimal NBCU's acquisition activities in Germany and Austria, the increment share arising from the Proposed Transaction would be negligible. With limited increment, the Proposed Transaction could not be expected to materially increase Sky's market power in this regard.
- (94) Moreover, in each of Germany and Austria there are also a number of other players present in the segment for the acquisition of film content, including ARD, ZDF, PS71 and RTL as well as OTT players such as Netflix and Amazon.
- (95) Consequently, the Commission considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market with regard to the acquisition of TV content in Germany and Austria, whether the Member States are considered separately or together.

5.3. Acquisition of TV content – Italy

- (96) In Italy both NBCU and Sky acquire distribution rights for TV content for inclusion in their TV channels. Table 3 below shows the segments where the Parties' overlapping activities result in horizontally affected markets, namely: (i) acquisition of all TV content, and (ii) acquisition of all film content.

Table 3 - Market shares for the acquisition of TV content – Italy - 2017

	All TV content (%)	All film content (%)
NBCU	[0-5]	[0-5]
Sky	[20-30]	[30-40]
Combined	[20-30]	[30-40]

Source: Form CO, table 7.

- (97) Table 3 shows that when considering the market for the acquisition for all TV content, the Parties combined market share is [20-30]% however, the increment brought about by the Proposed Transaction is limited as while Sky has a market share of [20-30]%, Comcast's share is less than [0-5]%. When considering the

segment for the acquisition of film content, the position is similar. The Parties have a combined market share of [30-40]% with an increment of [0-5]%.

- (98) As in the case of other markets on which the Parties' are both active, the increment brought about by the Proposed Transaction is minimal. The Proposed Transaction could not be expected to materially increase Sky's market power in this regard.
- (99) Moreover, there are also a number of other players in the Italian market that are active with regard to the acquisition of TV content, including film content. With regard to the acquisition of film rights RAI and Mediaset occupy a similar position as the biggest competitors of the merged entity with [20-30]% and [20-30]% market share respectively and OTT players such as Netflix and Amazon are also active.
- (100) Consequently, the Commission considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market with regard to the acquisition of TV content in Italy.

5.4. Wholesale supply of TV channels – UK

- (101) Both Sky and Comcast are active in the wholesale supply of TV channels in the UK. Comcast wholesales five channels to distributors: Universal Channel, SyFy, E! Entertainment Television, CNBC and Movies24. Sky licenses a wide range of channels including sports, movie and "other" TV channels.⁴⁹ The Parties' activities give rise to affected markets in the overall market for the wholesale supply of TV channels and its possible segmentations of news channels, pay-TV channels, basic pay-TV channels and the basic general entertainment channels segment. No overlap arises in respect of premium pay-TV channels category, since Comcast is not active in that area.
- (102) The Parties' market shares on the basis of revenue and audience shares in the affected markets (or market segments) can be seen below in Table 4. The Parties' combined market share in the pay-TV basic channel market is the same by revenue and by audience and amounts to [20-30]%.

**Table 4 - Market shares for the wholesale supply of basic pay-TV channels – UK
2017**

	By revenue (%)	By audience (%)
NBCU	[5-10]	[5-10]
Sky (including AETN)	[20-30]	[20-30]
Combined	[30-40]	[30-40]

Source: Form CO, Table 9 and 10, response to RFI 5.

⁴⁹ Sky's channels include: Challenge, Pick, Sky 1, Sky 2, Sky Living, Sky Atlantic, Sky Arts, Sky Intro, Sky Cinema channels, Sky News, Sky Sports channels (1-5, Box Office, F1, Mix, Sports News HQ).

- (103) The Commission considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market in this market in for the following reasons: (i) the limited increment brought about by the Proposed Transaction; (ii) the presence of multiple competing TV channel providers that will continue to constrain the merged entity post-transaction; and (iii) the fact that generally the Parties are not close competitors.
- (104) First, the overall increment brought about by the Proposed Transaction is limited or does not lead to significant market shares. When looking at the segment of news channels, Comcast's presence on that market is minimal, so the increment brought about by the transaction is negligible. On the basic pay-TV channels market, Sky has a wide range of pay-TV channels but Comcast only wholesales five channels in the UK and does not license any sports channels. While Sky may already have a material market position, given the limited extent of NBCU's offering, the Commission does not consider that the Proposed Transaction will have a significant effect on the competitive landscape in the UK or materially increase Sky's existing market power with regard to the wholesale supply of TV channels.
- (105) Second, a large number of TV channel suppliers will continue to compete with the merged entity post-Transaction, in particular UKTV ([10-20]% by revenue and [10-20]% by audience), Discovery ([5-10]% by revenue, [5-10]% by audience), Fox ([5-10]% by revenue and [5-10]% by audience), Viacom ([10-20]% by revenue, [10-20]% by audience), Disney ([5-10]% by revenue, [5-10]% by audience) and Time Warner ([0-5]% by revenue, [0-5]% by audience). These broadcasters each supply a range of basic pay-TV channels to third parties and will continue to place a competitive constraint on the merged entity.
- (106) Third, the results of the market investigation indicate that Sky and Comcast's channels do not closely compete. The majority of respondents to the market investigation noted the wide range of channels offered by the Parties and the limited overlapping content of the channels, considering each of the Parties' portfolios to be complementary given Sky's focus on sports and premium channels and Comcast's more limited portfolio focussed on general entertainment non-premium movie content.
- (107) There were however a number of respondents to the market investigation that indicated that certain channels offered by the Parties' do compete closely in the general entertainment segment, in particular Sky 1, Sky Atlantic and Sky Living were identified by some respondents as close competitors to Comcast's Universal and SyFy channels.
- (108) When considering the narrower general entertainment segment of basic pay-TV channels, the Parties have a combined market share of [50-60]% by revenue and [30-40]% by audience share (Sky, including AETN: [40-50]% by revenue, and [20-30]% by audience; Comcast: [5-10]% by revenue, and [10-20]% by audience). By channel, Comcast's Universal channel has a [5-10]% share by revenue and [5-10]% by audience and SyFy has a share of [0-5]% by revenue and by audience.
- (109) The Commission notes that Sky Atlantic is exclusive to Sky and not currently wholesaled to third parties. It therefore does not contribute to Sky's position on the wholesale market. With regard to the reported closeness between Sky One and

Sky Living on the one hand and Universal and SyFy on the other, the Commission considers that there are a sufficient number of other closely competing channels, some of which are larger than the Comcast channels, that will remain post-Transaction and continue to place a constraint on the merged entity. In particular, UKTV's GOLD ([5-10]% by revenue and [5-10]% by audience) and Alibi ([0-5]% by revenue and [5-10]% audience) channels and Fox's FOX channel ([5-10]% by revenue and [5-10]% by audience) were all also identified as being close competitors to the Comcast channels. Furthermore, several distributors have indicated that the entry of new channels could not be excluded.

- (110) The Commission therefore considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the wholesale provision of TV channels in the UK.

5.5. Wholesale supply of TV channels – Ireland

(111) Both Sky and Comcast are active in the wholesale supply of TV channels in Ireland. Comcast wholesales five channels to downstream customers: Universal Channel, SyFy, E! Entertainment Television, CNBC and Movies24. Sky licenses a wide range of channels including sports, movie and “other” TV channels.⁵⁰ The Parties’ activities give rise to affected markets in the overall market for the wholesale supply of TV channels and its possible segmentations of news channels, pay-TV channels, and within that basic pay-TV channels and basic pay-TV general entertainment channels. No overlap arises in respect of the premium pay-TV channels category, since Comcast is not active in that area.

(112) The Parties’ market shares on the basis of revenue and audience shares in the affected market are shown below in Table 5. By revenues, the Parties have a combined market share of [10-20]% (Sky: [10-20]%; Comcast: [0-5]%), the audience based market shares are higher: [20-30]% (Sky: [10-20]%; Comcast: [5-10]%). An affected market only arises when considering the market on the basis of audience shares.

Table 5 - Market shares for the wholesale supply of basic pay-TV channels – Ireland 2017

	By revenue	By audience
NBCU	[0-5]%	[5-10]%
Sky (including AETN)	[10-20]%	[10-20]%
Combined	[10-20]%	[20-30]%

Source: Form CO, Table 11, response to RFI 5.

⁵⁰ Challenge, Pick, Sky 1, Sky 2, Sky Living, Real Lives, Sky Arts, Sky Cinema channels, Sky News, Sky Sports channels (Main Event, Premier League, Football, Cricket, Golf, Action, Arena F1, Mix, Sports News).

- (113) The Commission considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market in this market for the following reasons: (i) the limited increment brought about by the Proposed Transaction; (ii) the presence of multiple competing TV channel providers that will continue to constrain the merged entity post-transaction; and (iii) the fact that generally the Parties are not close competitors.
- (114) First, the overall increment brought about by the Proposed Transaction is limited. When looking at the segment of news channels, Comcast's presence on that market is minimal, so the increment brought about by the transaction is negligible. On the basic pay-TV channels market, the Parties' combined market share ([20-30]%) does not give rise to competition concerns.
- (115) Second, a large number of TV channel suppliers will continue to compete with the merged entity post-Transaction, in particular Viacom ([10-20]% by revenue, [20-30]% by audience), Discovery ([5-10]% by revenue, [10-20]% by audience), UKTV ([10-20]% by revenue, [5-10]% by audience), Disney ([5-10]% by revenue and by audience), and Fox ([5-10]% by revenue, [5-10]% by audience). These broadcasters each supply a range of basic pay-TV channels to third parties and will continue to place a competitive constraint on the merged entity.
- (116) Third, as described above in paragraph (106) in relation to the UK, the results of the market investigation indicate that Sky and Comcast's channels do not closely compete in the UK and Ireland. The majority of respondents to the market investigation noted the wide range of channels offered by the Parties and the limited overlapping content of the channels, considering each of the Parties' portfolios to be complementary given Sky's focus on sports and premium channels and Comcast's more limited portfolio focussed on general entertainment non-premium movie content.
- (117) There were however a number of respondents to the market investigation that indicated that certain channels offered by the Parties' do compete closely in the general entertainment segment, in particular Sky 1, Sky Atlantic and Sky Living were identified by some respondents as close competitors to Comcast's Universal and SyFy channels.
- (118) When considering the narrower general entertainment segment of basic pay-TV channels in Ireland, the Parties have a combined market share of [20-30]% by revenue and [40-50]% by audience share (Sky, including AETN: [20-30]% by revenue, and [30-40]% by audience; Comcast: [0-5]% by revenue, and [10-20]% by audience). By channel, Comcast's Universal channel has a [0-5]% share by revenue and [5-10]% by audience and SyFy has a share of [0-5]% by revenue and [0-5]% by audience.
- (119) The Commission notes that Sky Atlantic is exclusive to Sky and not currently wholesaled to third parties. With regard to the reported closeness between Sky One and Sky Living on the one hand and Universal and SyFy on the other, the Commission considers that there are a sufficient number of other closely competing channels, some of which are larger than the Comcast channels, that will remain post-Transaction and continue to place a constraint on the merged entity. In particular, UKTV's GOLD ([5-10]% by revenue and [5-10]% by audience) and Alibi ([5-10]% by revenue and [0-5]% audience) channels and Fox's FOX channel ([5-10]% by revenue and [5-10]% by audience) were all also

identified as being close competitors to the Comcast channels. Furthermore, several distributors have indicated that the entry of new channels could not be excluded.

- (120) The Commission therefore considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the wholesale provision of TV channels in Ireland.

5.6. Retail provision of TV services

- (121) In the UK and Ireland, Comcast offers one non-linear service, *hayu*, direct to end-users, and licenses the CNBC linear channel to hotels and financial services firms. In Italy, Comcast's retail activities are limited to licensing the CNBC linear channel to hotels and financial services firms. In these countries, the overlap with Sky's own retail TV services leads to technically affected markets given Sky's retail market shares.⁵¹

- (122) However, Comcast's retail activities are *de minimis*. As of 5 April 2018, *hayu* has [redacted] direct subscribers in the UK and [redacted] direct subscribers in Ireland and Comcast's share does not exceed [0-5]% of the potential sub-segment for the retail provision of non-linear pay TV services. Similarly, Comcast's position resulting from direct sales of CNBC account for a negligible share of the retail market for pay TV services or potential linear pay TV sub-segment.

- (123) Accordingly, the Proposed Transaction will not lead to a material increment in the merged entity's market share in the retail provision of pay TV services.

- (124) The Commission therefore considers that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market with respect to the retail provision of TV services in the UK, Ireland and Italy given the negligible overlap and Comcast's minimal presence on these markets.

6. COMPETITIVE ASSESSMENT – VERTICALLY AFFECTED MARKETS.

- (125) As noted above: (i) both Parties are active with regard to the supply of TV content; (ii) both Parties supply TV channels on a wholesale basis to third parties in the UK and Ireland; and (iii) Sky is active as a TV distributor for retail TV services in the UK, Ireland, Germany, Austria and Italy and Comcast is active in the UK, Ireland and Italy. The Proposed Transaction therefore results in a number of vertical relationships.

- (126) These activities at various levels of the value chain give rise to the following vertically affected markets in various Member States:

(a) Comcast's and Sky's upstream activities as suppliers of TV content and their respective downstream activities in the wholesale supply of TV channels; and,

⁵¹ Sky's share of retail pay TV services by revenue amounts to [60-70]% in the UK, [60-70]% in Ireland and [70-80]% in Italy. These market shares will not be materially increased as a result of the Proposed Transaction.

(b) Comcast's and Sky's upstream activities as wholesale suppliers of TV channels and Sky's downstream activities as a TV retailer.

- (127) Where there are vertically affected markets, two possible forms of foreclosure arise. The first is where the merger is likely to raise the costs of downstream rivals by restricting their access to an important input (input foreclosure). The second is where the merger is likely to foreclose upstream rivals by restricting their access to a sufficient customer base (customer foreclosure).
- (128) Section 6.1 discusses the possible input foreclosure concerns arising from the Proposed Transaction with regard to TV markets; Section 6.2 discusses the possible customer foreclosure concerns arising from the Proposed Transaction with regard to TV markets.
- (129) For the sake of completeness, the Commission notes that it found no vertically affected markets in relation to advertising markets.

6.1. Input foreclosure – TV markets

6.1.1. Introduction

- (130) The Proposed Transaction will bring about a vertical relationship with regard to the licensing of broadcasting rights. Sky operates as a purchaser of broadcasting rights (to assemble TV channels to be provided to TV retailers or to use in a self-retail model) and TV channels (which it integrates in its TV retail offers) while Comcast is active at the wholesale level as a licensor of TV content (such as films and TV series) and provider of TV channels (such as 13th Street or SyFy).
- (131) In a merger between companies which operate at different levels of the supply chain, anti-competitive effects may arise when the merged entity's behaviour could limit or eliminate competitor's access to supplies – input foreclosure.
- (132) In assessing the likelihood of an anticompetitive input foreclosure scenario, the Commission examines: (i) whether the merged entity would have post-merger the ability to substantially foreclose access to input; (ii) whether the merged entity would have the incentive to do so; and (iii) whether a foreclosure strategy would have a significant detrimental impact on effective competition downstream.⁵²
- (133) In the course of the market investigation the Commission received a third party submission with regards to a possible input foreclosure strategy in relation to video ad technology services.⁵³ The Commission does not consider that the Proposed Transaction gives rise to serious doubts with regard to its compatibility with the internal market as a result of input foreclosure effects in relation to online display/video ad technology services for lack of ability to foreclose access to input. Even on the narrowest market definition, Comcast's limited market shares ([5-10] – [10-20]%) do not give rise to a significant degree of market power. The merged entity's share in the acquisition of online display ad serving technology services is estimated well below 30%, such that there are not

⁵² See Guidelines on the assessment of non-horizontal mergers under the Council Regulation on the control of concentrations between undertakings ("Non-Horizontal Merger Guidelines"), OJ C 265, 18.10.2008, p. 11, paragraph 32.

⁵³ See also paragraph (84) in relation to horizontal concerns.

vertically affected markets in relation to these services. Regardless, on both the advertiser-side and publisher-side there exist other significant competitors, including Google, Ooyala, AppNexus, and SpotX. In addition, video ad serving technology services are not a necessary input into the supply of digital advertising, either for publishers or advertising sales houses.

- (134) The following sections examine any possible input foreclosure with respect to the supply of TV content and TV channels in the UK, Ireland, Germany, Austria and Italy.

6.1.2. Supply of TV content

6.1.2.1. Notifying Party's view

- (135) The Notifying Party submits that it would not have the ability to engage in input foreclosure post-merger as: (i) it does not have market power in any product or geographic segment of the upstream market for licensing of TV content; (ii) multi-year contractual relationships with downstream customers would hamper the merged entity's ability to restrict the supply of TV content or otherwise degrade the terms on which it supplies content to third parties; (iii) Sky already licenses content from NBCU on an exclusive basis.
- (136) The Notifying Party submits that it would equally have no incentive to engage in input foreclosure given: (i) its strategy to license its content [*Business Secrets redacted regarding sales strategy*], (ii) that using NBCU content exclusively or otherwise to degrade the conditions on which it provides access to NBCU content would result in significant lost licensing revenues that the merged entity would have no prospect of recovering downstream.
- (137) Finally, it submits that in any event, such strategy would not have any impact on competition as there would be no change in the current position with regard to access to NBCU content for third parties (*Confidential information redacted regarding Comcast's current licensing arrangements*), and the existence of several other providers of film content which would continue to be accessible by competing channel suppliers.

6.1.2.2. Commission's assessment

(a) Ability to engage in input foreclosure

- (138) In the UK and Ireland, the merged entity's share in the upstream market is between [10-20]% and [20-30]% in all market segments, except for the narrower segment of licensing of US film content in the first pay-TV window in which NBCU has a [20-30]% market share in 2017. Post-transaction the other major Hollywood studios will also have significant market shares licensing of US film content in the first pay-TV window: Disney ([20-30]%), Fox ([10-20]%), Warner ([10-20]%), Sony ([10-20]%), Paramount ([0-5]%) and will continue to place a competitive constraint on the merged entity.

- (139) In Germany and Austria, the merged entity's market shares are below 20% in all vertically affected segments.⁵⁴
- (140) In Italy, merged entity's market shares in the upstream market are below [10-20]% in the TVOD/PPV and first pay-TV window segments and [20-30]% in the overall all film content category. In the US film first pay-TV window Comcast held a [20-30]% market share in 2016, but its share fell to [10-20]% in 2017. Post-transaction the other major Hollywood studios will have superior to similar market shares: Warner ([30-40]%), Disney ([20-30]%), Fox ([10-20]%) and will continue to place a competitive constraint on the merged entity.
- (141) Given the merged entity's limited market position with regard to the licensing of content, the Commission considers that it would not have the ability to foreclose its downstream rivals.

(b) Incentive to engage in input foreclosure

- (142) Several respondents to the market investigation consider that the merged entity may have the incentive to exclusively supply some of its TV content to Sky and not to other TV channel suppliers/TV services retailers, or to otherwise degrade the terms and conditions on which it provides access.⁵⁵
- (143) On the other hand, the Commission notes that [redacted] of Comcast's licensing revenue is accounted for acquirers other than Sky. Existing contractual arrangements for the provision of content could also disincentive the merged entity from foreclosing its inputs. Furthermore, given the significant position of alternative content suppliers, foreclosing access to Comcast's content would not significantly impact the merged entity's downstream revenues.
- (144) In any event, given the lack of ability to foreclose, it is not necessary to conclude as to whether the merged entity will have the incentive to foreclose competing TV channel suppliers and/or TV services retailers from its content in the relevant Member States.

(c) Impact on effective competition

- (145) Regardless of whether the merged entity has either the ability or the incentive to foreclose competing downstream rivals with regard to the supply of TV content, the Commission does not consider that such strategy would have an impact on competition.
- (146) The market shares presented above indicate that several providers of TV content would remain active in the market in each of the UK, Ireland, Germany, Austria and Italy and so competing TV channel suppliers and providers of TV retail services would continue to have access to TV content that competes with the content supplied by Comcast today.

⁵⁴ Data for 2017, response to RFI4 Table 10.1. In 2016, NBCU's market shares in the licensing of US film first pay-TV window was [20-30]%.

⁵⁵ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question C5; Replies to Questionnaire Q3 to TV distributors of 7 May 2018, question D7.

(d) Conclusion

- (147) In light of the above, the Commission considers that the Proposed Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of input foreclosure effects to the detriment of either competing TV broadcasters or providers of TV retail services in the UK, Ireland, Germany, Austria or Italy.

6.1.3. Wholesale supply of TV channels

6.1.3.1. Introduction

- (148) The Proposed Transaction increases Sky's pre-existing vertical integration by adding Comcast's channels to Sky's existing portfolio. The Commission has therefore assessed the risk of input foreclosure with regard to TV channels as a result of the transaction. The Commission notes, in this regard, that Comcast broadcasts general entertainment channels and CNBC, a business news channel. CNBC is available on an FTA basis in the UK, Ireland and Italy. In Germany and Austria, CNBC's audience share is negligible⁵⁶, such that input foreclosure can be excluded at the outset. The below analysis will therefore focus on input foreclosure in relation to general entertainment channels.

6.1.3.2. The Notifying Party's view

- (149) The Notifying Party submits that the merged entity would lack the ability to engage in input foreclosure. It argues that the Parties' combined share is limited in all Member States where Sky is active and considers that none of Comcast's channels can be considered to constitute important inputs to downstream competitors. The Notifying Party also indicates that there will remain a sufficient number of wholesale competitors for downstream rivals to have access to alternative inputs, especially in the general entertainment segment where major broadcasters like Fox, Time Warner, UKTV, Viacom and Discovery will continue to compete after the Transaction.
- (150) In addition, the Notifying Party indicates that the merged entity would lack the incentive to cease making Comcast's channels available to downstream competitors. It argues that the limited increment brought about by the Transaction would not suffice to modify the merged entity's incentives. The Notifying Party indicates that Comcast's current incentive to [*Business secret redacted regarding Comcast's sales policy*] will remain unchanged by the Transaction. Moreover, it notes that, despite already being vertically integrated, Sky has not foreclosed its downstream rivals' access to its wholesale TV channels in the UK and Ireland, and its incentive in that regard will not change as a result of the Proposed Transaction.
- (151) Finally, the Notifying Party considers that Comcast's channels do not just compete with other general entertainment channels, but also with channels broadcasting different thematic content. Because the merged entity's position in

⁵⁶ The Notifying Party has only provided market share estimates for all pay-TV channels and were unable to provide market share estimates limited to pay TV-only news channels, due to the limited size of this market in Germany and Austria. However, no respondent to the market investigation identified any input foreclosure risk in relation to CNBC.

other genres would remain unaffected by the Transaction, the Notifying Party argues that any hypothetical customer diversion as a result of input foreclosure can be expected to be very limited. As a result, according to the Notifying Party, the merged entity's incentives would not be changed by the Transaction and any putative impact on competition would be immaterial.

6.1.3.3. The Commission's assessment - UK and Ireland

(a) Ability to engage in input foreclosure

- (152) As set out above in Tables 4 and 5, with regard to the wholesale supply of basic pay TV channels:
- (a) in the UK, the Parties have a combined market share of [30-40]% by revenue (Sky: [20-30]%; Comcast: [5-10]%) and [30-40]% by audience share (Sky: [20-30]%; Comcast: [5-10]%)
 - (b) in Ireland, the Parties have a combined market share of [10-20]% by revenue (Sky: [10-20]%; Comcast: [0-5]%) and [20-30]% by audience share (Sky: [10-20]%; Comcast: [5-10]%).
- (153) As Comcast does not wholesale any premium pay-TV channels there is no overlap in this regard.
- (154) In respect of the merged entity's ability to engage in input foreclosure, respondents to the market investigation consider that Sky holds a leading market position and "must have" channels. As concerns the Notifying Party, although a number of respondents consider that Comcast does have bargaining power, there is no indication that there would remain insufficient substitutes to its channels in the market after the Transaction.
- (155) When considering a potential sub-segment for general entertainment pay-TV channels, the Parties market shares are higher, as indicated in Tables 4 and 5 above. However, close competitors with audience shares higher or similar to Comcast's channels would remain active in the market in both the UK and Ireland (UKTV, with [20-30]% in the UK and [10-20]% in Ireland, Fox with [10-20]% in the UK and [5-10]% in Ireland).
- (156) The availability of alternatives is further supported by the market investigation which showed that several TV channels, which will remain available post-transaction, are close competitors to Comcast's main channels, Universal Channel and SyFy. Close competitors to Universal Channel and SyFy include Fox (21CF), W and Alibi (both UKTV). This result confirms the Parties' own assessment of closeness of competition and singles out channels whose audience is either higher or on par with Comcast's.
- (157) Based on the above, the Commission considers that the merged entity is unlikely to have the ability to foreclose competing TV distributors in the UK and Ireland post-transaction.

(b) Incentive to engage in input foreclosure

- (158) Several respondents to the market investigation consider that post-transaction the merged entity would have the incentive to exclusively supply its channels to Sky and not to other providers of TV retail services, or to degrade the terms and conditions to which it provides access.⁵⁷
- (159) However, Sky is already vertically integrated with regard to the upstream supply of TV channels and the downstream supply of retail TV services; the increment brought about by the Transaction is therefore limited to Comcast's channels. As noted above, Comcast's market share in the wholesale supply of TV channels is limited and the merged entity's incentives will therefore not be significantly changed as a result of the Transaction.
- (160) Moreover, despite being vertically integrated, Sky currently licenses basic general entertainment channels to competing distributors. There is no evidence on file to suggest that the change brought about by the Transaction would modify its overall incentive in this respect.
- (161) In any event, given the lack of ability to foreclose, it is not necessary to conclude as to whether the merged entity will have the incentive to foreclose competing TV distributors in the UK and Ireland post-transaction.

(c) Impact on effective competition

- (162) Regardless of whether the merged entity has either the ability or the incentive to foreclose competing downstream rivals with regard to the wholesale supply of basic pay-TV channels, the Commission does not consider that such a strategy would have an impact on competition.
- (163) As detailed above in paragraph (156) there are several providers of basic pay-TV channels that closely compete with Comcast's channels and will remain active post-transaction. Therefore even if the merged entity were to adopt a foreclosure strategy, downstream rivals would continue to have access to sufficient alternative inputs.

(d) Conclusion

- (164) In light of the above, the Commission considers that the Proposed Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of input foreclosure effects of TV channels to the detriment of competing retail providers of TV retail services in the UK or Ireland.

6.1.3.4. Germany and Austria

(a) Ability to engage in input foreclosure

- (165) As noted above in paragraph (80), Sky does not supply channels on a wholesale basis to retail TV distributors in Germany and Austria as it has adopted a self-retail model. Therefore, Sky's channels do not generate wholesale carriage

⁵⁷ Replies to Questionnaire Q3 to TV distributors of 7 May 2018, questions C8 and C9.

revenues and revenue-based market share estimates are unavailable. The present assessment will thus rely on audience shares. However, due to Sky's lack of wholesale activity, the audience of Sky's channels has been excluded from wholesale market share calculations. Finally, the Notifying Party has been unable to provide market share estimates for Austria alone, but considers that its position in that country is not materially different than its position in Germany, such that market share data provided for Germany provide an adequate proxy for its market share in Austria. On this basis, Comcast holds a [10-20]% audience share in basic pay-TV channels, and [20-30]% of the general entertainment segment in Germany and Austria.

- (166) Several respondents to the market investigation indicate that Comcast's channels are important inputs to compete. This is particularly true with respect to 13th Street, the channel generating the most audience out of Comcast's portfolio, with an [10-20]% audience share among all basic pay-TV channels. Several respondents thus claim that Comcast's channels constitute important inputs and indicate that their thematic content (general entertainment) is among the most popular in basic pay TV.
- (167) According to respondents to the market investigation, 13th Street and SyFy, which make up the bulk of Comcast's market share, compete most closely with Fox (21CF), RTL Crime (RTL), TNT Serie and TNT Film (both Time Warner). This assessment is consistent with the Notifying Party's views. According to the Notifying Party's analysis in terms of content and on the basis of customer surveys, in both Germany and Austria [*channel names*] are 13th Street closest competing channels and [*channel names*] are SyFy's closest competitors.
- (168) On the wholesale basic pay TV market, Fox Serie's audience share amounts to [5-10]%, TNT Serie [0-5]% and RTL Crime [5-10]%. Taken individually, these channels have lower audience shares than 13th Street ([10-20]%) but have higher to equivalent audience shares as SyFy ([5-10]%). However, the combined audience share of Fox Serie, TNT Serie and RTL Crime ([10-20]%) is slightly higher than the combined audience share of 13th Street and SyFy ([10-20]%). Other TV channels providing access to general entertainment content and TV series include: TNT Film, Romance TV and RTL Crime.
- (169) In order to assess whether 13th Street and SyFy should be considered as particularly important for TV distributors, more than their audience share could suggest, the Commission requested the Parties to provide viewer shares based on different parameters.⁵⁸ Table 8 summarizes such information in relation to the total viewing, continuous viewing and prime time viewing of Comcast's channels and their closest competitors in Germany and Austria.

⁵⁸ In line with M.7194 - *Liberty Global/Corelio/W&W/De Vijver Media*, the Commission requested viewership data based on (i) total viewing time per month, (ii) continuous viewing time per month and (iii) prime time viewing time per month. For each (i), (ii) and (iii), the Parties submitted data for (a) 6 minutes, (b) 30 minutes, (c) 60 minutes, (d) 180 minutes. Table 8 presents a summary of the data provided.

Table 8 - Viewership data of basic pay-TV general entertainment channels in Germany

Channel	total time 30 min	N.	total time 180 min	N.	continuous time 30 min	N.	Viewers continuous time 180 min	N.	prime time 30 min	N.	prime time 180 min	N.
TLC	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
13 th Street	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Fox Serie	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
RTL Crime	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
SyFy	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
TNT Serie	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

Source: Notifying Party using third parties reports

- (170) Although Table 8 above only lists Comcast's channels and the closest competing channels, the ranking provided is out of all basic general entertainment channels, including Sky-branded channels that are solely self-distributed on Sky's platform. As indicated, within its competitor group, 13th Street systematically ranks [redacted], when considering several viewership data: (i) total time viewed within a month, (ii) continuous time viewed within a month, and (iii) prime time viewed within a month. For each of these three measures, the Notifying Party provided data that rank the channels in terms of viewers who watched the channel for 6 min or longer, 30 min or longer, 60 min or longer and 180 or longer within a month. SyFy has a significantly lower ranking.
- (171) Among general entertainment channels, the [redacted] TLC, a channel broadcasted by Discovery. TLC's content, which mainly consists of reality shows, differs from Comcast's channels. TLC is therefore not a close competitor to Comcast, as confirmed by both the Notifying Party and the results of the market investigation.
- (172) Among 13th Street's close competitors within general entertainment, Fox Serie is systematically the [redacted] viewed channel, all categories of viewership included. The performance and ranking of RTL Crime and TNT Serie varies depending of the viewership category. However, these channels' ranking in relation to both 13th Street and SyFy's confirms that there currently exists a close competing relationship between these channels.
- (173) In addition, the Notifying Party has provided data indicating that the [redacted] content on its channels (representing [redacted] of 13th Street and SyFy's total viewing) are not exclusive to Comcast and are also available to viewers on other TV channels. Therefore, Comcast's channels do not constitute crucial inputs to competing distributors.
- (174) The Notifying Party has provided data according to which the top [redacted] TV series broadcasted on 13th Street and SyFy, which represent [redacted] of these channels' viewing, is not exclusive against FTA channels. Furthermore, Comcast's channels [Confidential information redacted relating to content licensing rights].

(175) Based on the above, despite their strong position in basic pay TV, the audience and viewership of Comcast's channels is at least matched by the combined audience and viewership of the three closest competitors. Given that these competitors will remain available post-Transaction, the Commission considers that the merged entity would not have the ability to foreclose its downstream rivals.

(b) Incentive to engage in input foreclosure

(176) The Notifying Party argues that it would lack the incentive to foreclose access to its channels in Germany and Austria as this would adversely impact the revenues generated from Comcast's carriage agreements. In this regard, the Notifying Party notes that Sky accounts for only [redacted]% of its carriage revenues in Germany and Austria and argues that input foreclosure would not result in material diversion from rivals to Sky at the downstream level. The Notifying Party concludes that additional retail revenues would not outweigh wholesale losses and that input foreclosure would therefore be unprofitable.

(177) The Notifying Party provides no relevant data to support its arguments. In the absence of diversion and margin evidence and given the disproportionate importance of Sky's downstream revenues in relation to Comcast's carriage revenues, it cannot be assumed that reserving Comcast's channels to Sky's platform would be unprofitable for the merged entity.

(178) In addition, although, as indicated above in paragraphs (165) to (175) the merged entity will lack the ability to foreclose downstream rivals given that significant competitors will remain active at the wholesale level, Comcast's market shares both in relation to all basic pay TV and in general entertainment are material. It therefore cannot be excluded that the Transaction will have an impact on the merged entity's incentives.

(179) The Notifying Party also emphasizes that, as the Commission observed in its decision in case M.8354 – *Fox/Sky*, Sky Deutschland was previously controlled by 21CF which did not refuse to supply its TV channels to third parties despite being vertically integrated. The Notifying Party thus considers that, under the Commission's Non-Horizontal Merger Guidelines, 21CF's prior strategy constitute evidence that the merged entity's incentives would be no different.

(180) However, as explained in recital 45 (footnote 7) of the Commission's Non-Horizontal Merger Guidelines, past strategies adopted by competitors in relation to input foreclosure may be taken into account for the purpose of the competitive assessment in situations where these competitors held "*a similar market position*". This is not the case in the present instance as the Notifying Party's market share is twice as important as 21CF's market share.

(181) In any event, given the lack of ability to foreclose, it is not necessary to conclude as to whether the merged entity will have the incentive to foreclose competing TV distributors in the Germany and Austria.

(c) Impact on effective competition

(182) Regardless of whether the merged entity has either the ability or the incentive to foreclose competing downstream rivals with regard to the supply of TV channels,

the Commission does not consider that such a strategy would have an impact on competition.

- (183) As detailed above in paragraphs (165) to (175), the number of competing channels that will continue to be available to downstream competitors post-Transaction is sufficient to enable them to compete. The combined audience and viewership of channels that compete most directly with Comcast's main channels, 13th Street and SyFy, equate or exceed Comcast's audience and viewership.
- (184) Given the continued availability of channels that compete closely with Comcast's and represent significant viewership within the narrow segment of basic general entertainment pay TV channels, even in the event of input foreclosure, it is unlikely that downstream rivals would be significantly impacted and unable to compete effectively post-merger.

(d) Conclusion

- (185) In light of the above, the Commission considers that the Proposed Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of input foreclosure effects of TV channels to the detriment of competing retail providers of TV retail services in Germany or Austria.

6.1.3.5. Italy

- (186) In respect of the merged entity's ability to engage in input foreclosure, as explained above in paragraph (80), Sky does not supply channels on a wholesale basis to retail TV distributors in Italy whereas Comcast supplies Studio Universal and CNBC. With respect to Studio Universal, the Notifying Party estimates that it has a negligible market share in Italy, both out of all basic pay TV channels and within the general entertainment segment.
- (187) As a result of Comcast's negligible market share, the Transaction will bring no material change to the merged entity's incentives. In any event, for the same reason, were the merged entity to distribute Studio Universal exclusively on Sky's platform, this would have no appreciable impact on competition.
- (188) In light of the above, the Commission considers that the Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of input foreclosure effects of TV channels to the detriment of competing retail providers of TV retail services in Italy.

6.2. Customer foreclosure – TV markets

6.2.1. Introduction

- (189) The Proposed Transaction combines Comcast's and Sky's content with their respective downstream activities as acquirers of content for their TV channels and Sky's downstream activities as a pay-TV retailer.
- (190) According to the Non-Horizontal Merger Guidelines a downstream firm being part of a vertical merger may refuse to buy inputs from its rivals input suppliers as a result of the Proposed Transaction. This incentive to foreclose access to

customers downstream may result from the vertical integration of an upstream supplier with an important customer downstream. Due to their downstream presence, the merged entity may foreclose its upstream rivals' access to an important customer base. In turn this can inhibit upstream rivals to effectively compete.⁵⁹

- (191) In television markets, different forms of customer foreclosure may occur. First: (i) intermediate TV channel wholesalers; or (ii) downstream TV distributors; cease purchasing TV content from upstream rivals. Second, downstream TV distributors cease buying TV channels from their rivals at the intermediate level for the wholesale supply of TV channels.

6.2.2. *Supply of TV content*

6.2.2.1. Introduction

- (192) The following section assesses whether post-transaction, the merged entity would have the ability and incentive to cease acquiring TV content from its upstream rivals either: (i) for incorporation into TV channels to be wholesaled to third parties; or (ii) to be sold by the merged entity directly to end users. It then assesses what the overall likely effect on competition would be.

6.2.2.2. Notifying Party's views

- (193) The Notifying Party argues that post-Transaction, it would not have the ability to foreclose its upstream rivals for the following reasons: (i) there are multiple other downstream outlets to which upstream rivals could licence their content, including TV channels and OTT platforms such as Netflix and Amazon; (ii) Sky's multi-year output and other licencing agreements with suppliers would prevent the merged entity from ceasing to acquire content from its upstream rivals. Specifically as regards the downstream markets for the acquisition of sports content, the Notifying Party argues that there can be no prospect of customer foreclosure: although Sky is a significant acquirer of sports content in each of the vertically affected markets, it would not be possible for Sky to pursue a strategy of exclusively sourcing its sports content from NBCU, given NBCU's activity as a licensor in the EEA is negligible and only includes [*Business secret redacted relating to scope of Comcast's sports content licensing activities*].
- (194) The Notifying Party further submits that the merged entity would not have the incentive to stop acquiring content from other suppliers of TV content as its commercial success is based on the richness of the bundle of content and channels broadcast through its platform. In addition, while Sky could be considered as an important acquirer of film content, Comcast acquires very limited amounts of content.
- (195) It submits that such a customer foreclosure strategy would have a limited impact on competition given: (i) the existence of multi-year output agreements; (ii) the existence of a sufficient number of credible alternative content acquirers which will remain post-merger; and (iii) the fact that the impact of the hypothetical loss

⁵⁹ Non-Horizontal Merger Guidelines, paragraph 58.

of revenues from Sky and NBCU's European operations would not be sufficiently severe so as to render rival suppliers of content ineffective as competitors.

6.2.2.3. The Commission's assessment - UK and Ireland

(196) As noted above in paragraph (43), the Commission has left open whether the relevant market for the supply and acquisition of TV content should be considered as national or on the basis of linguistic region.

(197) Regardless of this question, the Commission considers that the conclusion of the competitive analysis does not differ depending on whether the UK and Ireland are considered separately or together.

(a) Ability to engage in customer foreclosure

(198) When considering whether the merged entity would have the ability to foreclose access to downstream markets, the Commission examines whether there are sufficient economic alternatives in the downstream market for upstream rivals to sell their output.

(199) In the first instance, the market shares indicate that Sky is an important purchaser of TV content, in particular for sports and films, as shown in Table 9 below.

Table 9 - Market shares for acquisition of TV content in share - by total spend - UK and Ireland - 2017

	All TV content (%)	All sports (%) ⁶⁰	All film (%)	Other TV content (%) ⁶¹
NBCU	[0-5]	[0-5]	[0-5]	[0-5]
Sky	[40-50]	[50-60]	[50-60]	[10-20]
Combined	[40-50]	[50-60]	[50-60]	[10-20]

Source: Annex 7.4, Form CO.

(200) Sky's market share for the acquisition of films further increases when segmented according to release window: (i) first pay-TV window: [70-80]%; and (ii) TVOD/PPV rights: [70-80]%. In addition, Sky has a [70-80]% market share for US films and [90-100]% for US films in the first pay-TV window. The other purchasers of film rights in the UK and Ireland overall are BBC: [5-10]%; ITV: [10-20]%; Channel 4: [10-20]%. With regard to the first pay-TV window, the OTT players are the other purchasers (Netflix: [5-10]%; Amazon: [10-20]%).

(201) Despite the importance of Sky as a purchaser of TV content, the Commission considers that it would have a limited ability to foreclose rivals by ceasing to

⁶⁰ In the sub-segment of acquisition of all other sports content in the UK and Ireland, Sky has a market share of [30-40]%.

⁶¹ This concerns all licenced other TV content. The Parties' market shares for the segment of licenced pre-produced other TV content are not materially different.

purchase from them and exclusively relying on the content of NBCU post-transaction, for the following reasons.

- (202) First, NBCU has an extremely limited market position in the UK and Ireland with regard to the supply of sports rights (less than [0-5]% share by revenue in 2017 and the Parties together do not have more than [0-5]% under any other sub-segment considered). It is therefore not possible for Sky to exclusively rely on the sports rights licenced by NBCU in the UK and Ireland.
- (203) Second, the results of the market investigation indicate that a majority of rights holders consider that there are other players to which they could licence their content as an alternative to the merged entity in the event that the merged entity ceased acquiring their TV content or otherwise degraded the terms on which it acquires their TV content.⁶² Therefore, the merged entity would have no ability to restrict the access of rival upstream licensors to downstream purchasers of those rights given the multiple other outlets available to TV content licensors. A broad range of other TV broadcasters and content platform operators compete to acquire TV content, each of which will continue to be credible purchasers of TV content post-Transaction, thus allowing rival upstream licensors to continue to operate efficiently.
- (204) Third, Sky has multi-year output agreements and other licensing agreements in place with a wide range of rights holders. Accordingly, Sky cannot unilaterally cease to licence such content from these third parties or otherwise degrade the terms of supply until their expiry without being in breach of these agreements.

(b) Incentive to engage in customer foreclosure

- (205) The Commission does not consider that the merged entity would have the incentive to foreclose access to downstream markets by reducing purchases from upstream competing rivals for the following reasons.
- (206) The attractiveness of a pay-TV operator's offer to consumers is based on the richness of the bundle of content and channels broadcast through its platform.⁶³ On this basis, the merged entity would not have the incentive to cease purchasing content from upstream competitors. Sky does not limit its offering to NBCU film content, including its entire output of new films but it purchases similar premium film content also from NBCU's competitors.
- (207) A majority of the respondents to the market investigation stated either that they considered that the merged entity would not have the incentive to stop sourcing TV content from other producers/licensors and exclusively rely on content provided by NBCU or stated that they considered it unlikely that the merged

⁶² Replies to Questionnaire Q1 to TV rights holders of 7 May 2018, question C.9. As to the comment made during the market investigation that there may not be actual demand from such alternatives in the first pay-TV window for movies, as claimed by a respondent to the market investigation, the Commission notes that when considering the ability to foreclose upstream rivals, the Commission may also take into account potential demand (see Non-Horizontal Merger Guidelines, paragraph 61).

⁶³ See for example: Commission decision of 21 December 2010 in case M.5932 – *NewsCorp/BskyB*, paragraph 154; Commission decision of 16 September 2014 in case M.7282 *Liberty Global/Discovery/All3Media*, paragraph 68.

entity would cease licensing content from third parties all together.⁶⁴ Among the latter category of respondents, a major content supplier noted that "*consumers generally prefer a broad selection of content, so [we consider] that a broadcaster is likely to maintain such a broad selection (including content of third parties)*".

- (208) In this regard, the Commission notes that over the past three years, Sky has had output agreements with [*business secret re. sources of supply redacted*] major US film studios for the UK and Ireland. Therefore, any strategy by the merged entity that reduced the number of licensor relationships would likely be detrimental to Sky's downstream TV channel and TV retail business.
- (209) A number of respondents to the market investigation noted that post-transaction, the merged entity may have an incentive to favour its own content above others but have not provided substantiated submissions explaining how the merged entity would implement such a potential partial foreclosure strategy.
- (210) As noted above, the Commission considers that the merged entity will continue to have a strong incentive to carry a broad range of the most attractive content on its platform therefore, as with the incentive to fully foreclose, the merged entity would not have the incentive to partially foreclose its upstream rivals.

(c) Impact on competition

- (211) Given that there are multiple alternatives to the merged entity to which rights holders can supply their content, a large number of rights holders are protected from a foreclosure strategy: a broad range of other TV broadcasters and content platform operators compete to acquire TV content, each of which will continue to be credible purchasers of TV content post-Transaction thus allowing rival upstream licensors to continue to operate efficiently. Moreover, due to the existing output agreements with Sky, Sky cannot unilaterally cease to licence content from these third parties or otherwise degrade the terms of supply. In light of this, the Commission does not consider that a potential customer foreclosure strategy for content would have a material effect on competition in the UK or Ireland.

(d) Conclusion

- (212) In light of the above, the Commission concludes that the Proposed Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of customer foreclosure for the supply of TV content in the United Kingdom or Ireland (or in relation to a linguistic region encompassing both the United Kingdom and Ireland).

6.2.2.4. The Commission's assessment - Germany and Austria

- (213) As noted above in paragraph (43), the Commission has left open whether the relevant market for the supply and acquisition of TV content should be considered as national or on the basis on linguistic region.

⁶⁴ Replies to Questionnaire Q1 to TV rights holders of 7 May 2018, question C.6.4.

(214) Regardless, the Commission considers that conclusion of the competitive analysis does not differ depending on whether Germany and Austria are considered separately or together.

(a) Ability to engage in customer foreclosure

(215) In the first instance, the market shares indicate that Sky is an important purchaser of sports and film TV content in Germany and Austria, as shown in Table 10 below where Sky has a pre-transaction market share of [30-40]% for sports rights and a share of [20-30]% for films.

Table 10 - Market shares for acquisition of TV content – by total spend – Germany and Austria - 2017

	All sports (%)	All film (%)
NBCU	[0-5]	[0-5]
Sky	[30-40]	[20-30]
Combined	[30-40]	[20-30]

Source: Annex 7.4, Form CO.

(216) Sky's market share for the acquisition of films materially increases when segmented according to release window, in particular the first pay-TV window where Sky has a market share of [60-70]% by revenue. Sky's market share is slightly lower than that in the sub-segment of US films in the first pay-TV window ([60-70]%).

(217) Despite the importance of Sky as a purchaser of TV content for sports and films, the Commission concludes that it would have a limited ability to foreclose rivals by ceasing to purchase from them and exclusively relying on the content of NBCU for the following reasons.

(218) The arguments articulated in relation to the UK and Ireland are also applicable in this market.

(219) First, with regard to sports rights, NBCU has an extremely limited market position in Germany and Austria ([0-5]%) and the Parties have a combined share for the licencing of sports of [0-5]%. It is therefore not possible for Sky to exclusively rely on the sports rights licenced by NBCU in Germany and Austria.

(220) Second, as noted above in with regard to the UK and Ireland, a broad range of other TV broadcasters and content platform operators compete to acquire TV content, each of which will continue to be credible purchasers of TV content post-Transaction, thus allowing rival upstream licensors to continue to operate efficiently.

(221) Third, Sky currently has multi-year output agreements with a wide range of rights holders which prevent Sky from ceasing to purchase their content and the multitude of agreements with the other US studios renders content foreclosure strategy risky.

(b) Incentive to engage in customer foreclosure

(222) As noted with regard to the UK and Ireland in paragraphs (205) to (210) above, the Commission does not consider that the merged entity would have the incentive to either fully or partially cease licencing content from third parties in relation to the markets in Germany and Austria as it would reduce the quality of the Sky offering thereby risking the loss of customers.⁶⁵

(c) Impact on competition

(223) Given that there are multiple alternatives to the merged entity to which rights holders can supply their content, a large number of rights holders are protected from a foreclosure strategy: a broad range of other TV broadcasters and content platform operators compete to acquire TV content, each of which will continue to be credible purchasers of TV content post-Transaction thus allowing rival upstream licensors to continue to operate efficiently. Moreover, due to its existing output agreements, Sky cannot unilaterally cease to licence content from these third parties or otherwise degrade the terms of supply. In light of this, the Commission does not consider that a potential customer foreclosure strategy for content would have a material effect on competition in the Germany or Austria.

(d) Conclusion

(224) In light of the above, the Commission concludes that the Proposed Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of customer foreclosure for the supply of TV content in Germany or Austria (or on in linguistic region encompassing both Germany and Austria).

6.2.2.5. The Commission's assessment - Italy

(a) Ability to engage in customer foreclosure

(225) In the first instance, the market shares indicate that Sky is an important purchaser of TV content in Italy as shown in Table 11 below.⁶⁶

⁶⁵ With respect to the agreements with major US films studios for Germany and Austria, the Commission notes that Sky has had output agreements with [*business secret re. sources of supply redacted*] major US film studios over the past three years.

⁶⁶ Vertically affected markets arise in Italy as regards the licensing/acquisition of all sports content and the licensing/acquisition of other sports content, due to NBCU's presence as a licensor of other sports content in Italy ([*Business secret redacted relating to scope of Comcast's sports content licensing activities in Italy*]). However, given the [*Business secret redacted relating to scope of Comcast's sports content licensing activities in Italy*], customer foreclosure is not likely in these segments. Therefore these market segments are not further discussed in the present Section.

Table 11 - Market shares for acquisition of TV content – by total spend – Italy - 2017

	All TV content (%)	All film (%)
NBCU	[0-5]	[0-5]
Sky	[20-30]	[30-40]
Combined	[20-30]	[30-40]

Source: Annex 7.4, Form CO

- (226) Sky's market share for the acquisition of films materially increases when segmented according to release window, in particular the first pay-TV window where Sky has a market share of [60-70]%. Mediaset is the other purchaser of first pay-TV rights in Italy with a share of [40-50]%.
 (227) With regard to TVOD/PPV rights, Sky is an important player ([40-50]%) with a number of other players purchasing a more limited amount of movies rights for this distribution platform (iTunes: [10-20]%; TimVision: [5-10]%).
 (228) Despite the importance of Sky as a purchaser of film content, the Commission concludes that it would have a limited the ability to foreclose rivals by ceasing to purchase from them and exclusively relying on the content of NBCU.
 (229) The arguments articulated in relation to the UK and Ireland are also applicable in this market. There are many other potential purchasers of content that compete with NBCU's content. Moreover, Sky currently has multi-year output agreements with a wide range of rights holders which prevent Sky from ceasing to purchase their content and the multitude of agreements with the other US studios renders content foreclosure strategy risky.

(b) Incentive to engage in customer foreclosure

- (230) As noted above with regard to the UK and Ireland in paragraphs (205) to (210), the Commission does not consider that the merged entity would have the incentive to either fully or partially cease licencing content from third parties as it would reduce the quality of the Sky offering thereby risking the loss of customers.⁶⁷
 (231) In particular, as noted above in with regard to the UK, Ireland, Germany and Austria, a broad range of other TV broadcasters and content platform operators compete to acquire TV content in Italy, each of which will continue to be credible purchasers of TV content post-Transaction, thus allowing rival upstream licensors to continue to operate efficiently.

⁶⁷ With respect to the agreements with major US films studios Italy, the Commission notes that Sky has had output agreements with [*business secret re. sources of supply redacted*] major US film studios over the past three years.

(c) Impact on competition

- (232) Given that there are multiple alternatives to the merged entity to which rights holders can supply their content, a large number of rights holders are protected from a foreclosure strategy: a broad range of other TV broadcasters and content platform operators compete to acquire TV content, each of which will continue to be credible purchasers of TV content post-Transaction thus allowing rival upstream licensors to continue to operate efficiently.
- (233) Moreover, due to the existing output agreements with Sky, Sky cannot unilaterally cease to licence content from these third parties or otherwise degrade the terms of supply. In light of this, the Commission does not consider that a potential customer foreclosure strategy for content would have a material effect on competition in Italy.

(d) Conclusion

- (234) In light of the above, the Commission concludes that the Proposed Transaction does not give rise to serious doubts with regard to its compatibility with the internal market as a result of customer foreclosure for the supply of TV content in Italy.

6.2.3. *Wholesale supply of TV channels*

6.2.3.1. Introduction

- (235) At the wholesale level, Sky is already vertically integrated in that it already owns a portfolio of channels in addition to being present downstream as a distribution platform. The merger specific aspect in this regard is the addition of Comcast's TV channels.
- (236) The Commission has therefore assessed the risk of the following types of customer foreclosure strategies in the United Kingdom, Ireland, Austria, Germany and Italy: (i) complete foreclosure of rival TV broadcasters through the denial of access to Sky's downstream distribution platform; and (ii) partial customer foreclosure of rival TV broadcasters through for instance a degradation of the quality of the viewer experience for competing channels on Sky's platform or through a reduction in carriage fees.
- (237) Pay TV providers have to offer a diverse portfolio of channels in order to maximise their attractiveness for a large number of viewers. The risk of broad foreclosure strategy not targeting closely competing channels with Comcast's channels, but foreclosing also channels that are not close competitors to Comcast's channels can therefore be excluded at the outset. In the following Section 6.2.3.2, the Commission identifies those closely competing channels which could potentially be the target of customer foreclosure.

6.2.3.2. Potential targets of customer foreclosure

- (238) Comcast broadcasts general entertainment channels and CNBC, a business news channel. CNBC is available free-to-air ("FTA") in the UK, Ireland and Italy. In Germany and Austria, its audience share is negligible such that customer

foreclosure can be excluded. The below analysis will thus focus on customer foreclosure in relation to general entertainment channels.

- (239) In the general entertainment genre, Comcast broadcasts Universal Channel, Syfy, E! in the UK, Ireland, Germany and Austria; as well as Movies 24 in the UK and Ireland; 13th Street in Germany and Austria; and Studio Universal in Italy.
- (240) For the purposes of its assessment, the Commission has considered, in particular, as the more likely potential targets of a customer foreclosure strategy, the channels that compete closely with Comcast's channels.
- (241) As noted in paragraphs (156) and (167) above in relation to the UK, Ireland, Germany and Austria, Comcast's channels can be considered to closely compete with the following:
- (a) In the UK and Ireland: close competitors to Universal Channel and Syfy include Fox (21CF), W and Alibi (both UKTV);
 - (b) In Germany and Austria: 13th Street and Syfy can be considered to closely compete with Fox (21CF), RTL Crime (RTL), TNT Serie and TNT Film (both Time Warner).
- (242) In addition, the Notifying Party submits that Universal Channel closely competes with TNT Serie (in Germany); E! closely competes with MTV (Viacom) and TLC (Discovery) (both in the UK and Ireland) and Sixx (ProSieben Sat)(Germany and Austria); and Movies24 closely competes with TCM (Time Warner) (UK and Ireland).
- (243) Finally, in Italy, the Notifying Party states that Studio Universal, the sole general entertainment channel wholesaled by Comcast, has a negligible audience: while there are no close competitors to Studio Universal, channels with similar content include: FOX, Viacom A+E Crime and Investigation, Gambero Rosso.

6.2.3.3. The Notifying Party's views

- (244) The Notifying Party submits that the merged entity would have no ability to totally or partially foreclose rivals as there are other TV retailers competing to purchase broadcasting rights in each of the relevant Member States. In addition, because Sky has entered in multi-year carriage agreements, wholesale suppliers would be protected against any attempt by the merged entity to impede access to its retail platform. Furthermore, the merged entity would lack the ability to partially foreclose competing channels due to regulatory and contractual protections in favour of wholesale suppliers.
- (245) Furthermore, the Notifying Party argues that Sky's product offering relies on content diversity, such that any degradation in its retail line-up, especially in general entertainment, would only benefit its competitors. The Notifying Party notes that any benefits from total or partial customer foreclosure in the form of increased viewership of NBCU and Sky channels on Sky's platform would be speculative and minimal in comparison to Sky's much greater downstream subscription revenues. Accordingly, the Notifying Party submits that it would be commercially irrational for the merged entity to fully or partially foreclose competing TV channels.

(246) The Commission's assessment of customer foreclosure risks in each of the relevant territories is set out below.

6.2.3.4. The Commission's assessment - UK and Ireland

(247) From the outset, the Commission recalls that Sky is already vertically integrated in that it already owns a portfolio of channels in addition to being present downstream as a distribution platform. The merger specific aspect in this regard is limited to the addition of Comcast's TV channels.

(a) Ability to engage in customer foreclosure

(i) Sky's importance as a distribution platform

(248) At the outset, for customer foreclosure to be a concern, the transaction must involve a company with a significant degree of market power as a customer in the downstream market.

(249) Downstream, Sky has a market share of [30-40]% in the UK and [40-50]% in Ireland for the acquisition of TV channels.⁶⁸ Sky is the leading pay-TV retailer in the UK and Ireland. Sky's share of all pay-TV services on the basis of revenues is [60-70]% in the UK and [60-70]% in Ireland.⁶⁹ Sky's platform allows broadcasters to access [30-40]% of pay-TV subscribers in the UK and [40-50]% in Ireland.⁷⁰

(250) Several TV channel suppliers consider that distribution on Sky is very important to them given Sky's position as a pay-TV platform with a large customer base resulting in higher audiences and accompanying revenues.⁷¹ Several TV broadcasters also indicated that the majority of their revenues are derived from distribution on Sky's platform.⁷²

(ii) Ability to engage in total foreclosure

(251) As to the extent of Sky's bargaining power, the results of the market investigation were mixed. While the majority of wholesale suppliers of TV channels in the UK and Ireland consider that Sky currently does not have significant bargaining power, a small but significant minority of them considered that Sky has such bargaining power.⁷³ Furthermore, market participants do not expect new entry at the retail level in the UK or Ireland offering a distribution scale comparable to Sky.⁷⁴

⁶⁸ Form CO, Table 25.

⁶⁹ Form CO, Annex 7.4, Tables 38.1 and 38.2.

⁷⁰ Form CO, Annex 7.4, Tables 38.6 and 38.7.

⁷¹ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.4.1.

⁷² Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.3.

⁷³ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.4.

⁷⁴ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.10 and D.11.

- (252) The market investigation did not provide reasons to consider that switching to FTA distribution and self-retailing on Sky's platform would constitute viable alternative supply options for broadcasters.⁷⁵
- (253) In any event, the Commission considers that the following factors militate against a finding of ability on the part of Sky to engage in full foreclosure of Comcast's closely competing channels Fox, W, Alibi, MTV, TLC or TCM.
- (254) First, Sky's carriage agreement with [*company name*] will not expire until [*term time*] and termination by Sky is only possible in very specific and limited circumstances; [*company name*] carriage agreements will not expire until [*term time*] and termination by Sky is only possible in very specific and limited circumstances. Therefore, an ability on the part of Sky to foreclose [*company names*] cannot be held to arise in light of the applicable contractual provisions.
- (255) Second, despite limited retail market shares, alternative purchasers in the UK and Ireland represent a material share of acquisition of licensing rights: namely Liberty Global, BT and Talk Talk in the UK (respectively [50-60]%, [5-10]% and [5-10]% of shares in the acquisition of TV channels) and Liberty Global, Eir and Setanta in Ireland (respectively [40-50]%, [10-20]% and [5-10]%). Therefore, a strategy of ceasing to purchase from competing wholesale TV channel suppliers would still leave broadcasters with the possibility to access a material portion of the market.
- (256) In light of the above, the Commission considers that overall the merged entity would lack the ability to engage in the total customer foreclosure strategies considered above.

(iii) Ability to engage in partial foreclosure

- (257) The market investigation indicated that a small majority of respondents in the UK and Ireland consider that the merged entity will be able to degrade distribution terms in particular by diminishing carriage fees.⁷⁶ UK-based broadcasters are also concerned with EPG slot degradation and Sky pushing for its own content over the Sky Q interface although respondents also emphasize that Sky's UK EPG listing is subject to regulation and adheres to its published methodology.⁷⁷
- (258) As indicated above, however, the only merger specific element pertinent to the present assessment of partial foreclosure is the addition of Comcast's channels. Comcast's general entertainment channels comprised just [*redacted*]% of all

⁷⁵ FTA distribution involves a different business model which essentially relies on advertising revenues where pay-TV channels generate revenues from carriage fees and advertising. Switching from a pay-TV to an FTA model would entail considerable uncertainty and may induce losses in revenues. Furthermore, in *Fox / Sky* (paragraph 308), the Commission noted that in the course of the market investigation, several market participants explained that self-retailing does not constitute a commercially viable alternative absent premium content capable of attracting clients to channels marketed outside of a Sky package.

⁷⁶ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.6.

⁷⁷ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.7.

viewing on Sky's platform in 2015 to 2017, which is lower than the channels of UKTV, Viacom and Discovery.⁷⁸

- (259) The Commission considers that a number of elements exist which militate against a finding of the ability of the merged entity to engage in partial customer foreclosure in the present case.
- (260) As regards potential partial foreclosure via a reduction of carriage fees, the Commission notes that [*details of Sky carriage agreements including term*]. This therefore affords protection in relation to [*supplier names*] carriage fees revenue until at least the expiry of those contracts.
- (261) As regards a degradation of EPG ranking, the Commission notes that EPG regulations are applicable to Sky in the UK.
- (262) The UK regulator, Ofcom, has a code of practice on EPGs (the EPG Code) which ensures that any agreement with broadcasters for the provision of an EPG service is made on FRAND terms. Moreover, Sky is required to refrain from giving undue prominence in any listing or display to a channel connected to Sky. Sky also needs to carry out periodic reviews of its listing policy and of channel listings made in accordance with that policy, in consultation with channel providers.⁷⁹
- (263) In addition, Sky is subject to Sky-specific regulation (EPG Conditions) that requires Sky (i) to provide EPG services upon request and on a fair, reasonable and non-discriminatory basis, (ii) not to discriminate or show undue preference to any particular persons or class of persons, (iii) a requirement to publish a notice specifying, or specifying the method that is to be adopted for determining, the charges and other terms and conditions.⁸⁰ Consequently, Sky set out its EPG listing methodology in a public document ("Method of Allocating Listings in Sky's EPG"). A violation of those regulatory obligations would be easily detected by the interested party, which would likely complain with the competent regulatory authorities.
- (264) The Commission considers that in light of these regulations in the UK, the merged entity would not be able to foreclose Comcast's closely competing channels via EPG degradation in the UK without infringing regulation which would expose it to significant penalties, as described below in paragraph (280).
- (265) The Commission notes that whereas no comparable regulation exists in Ireland, the information submitted by the Notifying Party indicates that Sky broadcasts the same EPG in the UK and Ireland and therefore the Irish EPG also reflects the UK regulatory constraints.
- (266) The Commission has also considered partial foreclosure via the Sky Q set top boxes, which Sky has introduced in the UK and Ireland. The Sky Q set-top box provides users with new services available on its interface, including "Home" (previously "My Q") an application listing content available to subscribers based on the type of content that they have been watching, using algorithms determined

⁷⁸ Reply to RFI 4, page 57.

⁷⁹ See Form CO, paragraph 364.

⁸⁰ See Form CO, paragraph 365.

by Sky to suggest viewing recommendations. The criteria used to select content and channels through these algorithms are not subject to regulation.

- (267) However, in this regard the Commission notes that Sky Q is currently only available to new subscribers or to customers who seek to upgrade to that set-top box. Accordingly, only [number of Sky Q box subscribers] subscribers in the UK, and [number of Sky Q box subscribers] in Ireland have Sky Q box. This amounts to c. [redacted]% and [redacted]% of Sky subscribers in respectively the UK and Ireland.⁸¹ Moreover, the Sky Q box does not present channels only via the Home application. On the contrary, the Sky EPG is positioned at the top of the list of options in the Sky Q box menu, above the My Q application. Data submitted by the Parties regarding the Sky Q box also indicates that [Sky's confidential internal analysis]. These elements do not indicate neither an ability on the part of Sky to engage in a partial foreclosure strategy via the Home (previously My Q) function of Sky Q, nor a material likely impact on effective competition if the ability of Sky to partially foreclose via the Home (previously My Q) function of Sky Q were to be assumed.
- (268) Furthermore, the Commission notes that, based on the Notifying Party's submission, [confidential information about the functioning of the "Home" section]. On this basis, the Commission considers that a partial foreclosure via the Sky Q set top boxes can be excluded.
- (269) Finally, contractual commitments also restrict the way in which Sky makes available non-Sky VOD content on its on-demand platform in the UK and Ireland.⁸²
- (270) In light of all the above, the Commission considers that overall the merged entity would lack the ability to engage in the partial customer foreclosure strategies considered above.

(b) Incentive to engage in customer foreclosure

(i) Incentive to engage in full foreclosure

- (271) The Commission has assessed the likelihood of full foreclosure in the UK and in Ireland.
- (272) First, the majority of the UK and Irish broadcasters are not concerned that the transaction would result in full customer foreclosure: they consider that the merged company would probably carry on licensing third party TV channels as the separate companies do today and would not stop sourcing TV channels from third parties, and exclusively rely on its own TV channels.⁸³ In this regard, a broadcaster noted that the merged entity was more likely to maintain a broad selection of channels (including of third parties) given that consumers generally prefer a wide selection of channels.

⁸¹ Form CO, Table 28.

⁸² According to the Notifying Party, Sky has provided guarantees in its carriage agreements with each of [company names] with regard to [details of guarantees included in Sky's carriage agreements].

⁸³ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.5.

- (273) Second, a number of Sky's internal documents indicate that [*description of Sky's internal documents*].⁸⁴ The Notifying Party states that offering a wide variety of channels is particularly important for a premium pay-TV operator such as Sky, which needs to justify its tariff structure to subscribers in order to ensure they do not switch away to more cost-effective alternatives. Notably, in this respect, while UKTV (W and Alibi) is concerned about the merged entity's potential to engage in partial customer foreclosure, it believes that is unlikely that it would be fully foreclosed.
- (274) Third, given NBCU's limited presence as a wholesale supplier of TV channels, representing less than [*redacted*] % of viewing share on Sky's retail platform⁸⁵, the Proposed Transaction is unlikely to bring about changes in the merged entity's incentives in its purchasing of TV channels from other wholesaler suppliers.
- (275) Fourth, the closest competitors of NBCU in the general entertainment genre are major TV broadcasters that typically supply a popular suite of channels to Sky's retail platform, including in respect of channels outside of the general entertainment segment and in respect of content used by Sky on its own TV channels. The importance of Sky's commercial relationships with broadcasters renders a hypothetical wholesale foreclosure strategy in the basic pay-TV general entertainment segment risky as the affected broadcasters could retaliate on the basis of commercial relationships in other markets.
- (a) For example, UKTV, which is a close competitor to Universal Channel and Syfy in the UK and Ireland, has an audience share in general entertainment of [20-30] % in the UK and [10-20] % in Ireland. Therefore, the Commission considers it unlikely that Sky would be incentivised to foreclose UKTV's channels to benefit the Universal and Syfy channels, which represent a less significant proportion of the genre in the UK and Ireland. Moreover, the Notifying Party submitted an internal document of Sky, indicating that “[*quote from Sky's internal document*]”.⁸⁶
- (b) Another example is Viacom, the owner of MTV, which is a close competitor to E! in the UK and Ireland. At group level, Viacom supplies a broad range of channels to Sky's retail platform, including other key general entertainment channels like Comedy Central. Its share of audience is greater than that of all NBCU channels in aggregate in the UK and in Ireland, thereby demonstrating its importance to Sky.
- (c) Discovery, the owner of TLC which is a close competitor of E!, is an important wholesale supplier of Sky in the UK and Ireland, particularly in the factual genre. In the UK, Discovery accounts for an audience share of [5-10] % in the segment for all basic pay-TV and of [10-20] % by audience in Ireland. Its importance to Sky in the factual genre has been acknowledged in the *Fox/Sky* decision.
- (d) Time Warner, the owner of TCM, which competes closely with NBCU's Movies 24 in the UK and Ireland, is an important input across the

⁸⁴ Response to RFI 4, page 56.

⁸⁵ Form CO, Table 26.

⁸⁶ Response to RFI 4 of 4 June 2018, question 17, Annex 17.2.

spectrum of Sky's retail offering and particularly in film content licensing. The Notifying Party submits that [*details about Sky's negotiating power*].

- (276) Fifth, given Sky's subscription revenues largely outweigh Comcast's wholesale revenues, the adoption of a customer foreclosure strategy which would risk deteriorating Sky's offering in the hope of improving Comcast's upstream revenues does not appear to be profitable. Although the Notifying Party did not provide an assessment of the amount of customer diversion that would result from foreclosing competing channels nor quantifies the resulting gains for Comcast, the difference between NBCU's 2017 revenue from its wholesale operations (UK: EUR [redacted]; Ireland: EUR [redacted]) and total subscription revenues for Sky (UK: EUR [redacted]; Ireland: EUR [redacted]) appears significant.
- (277) Furthermore, if a foreclosure strategy were to focus on certain but not all of Comcast's competitors, any resulting diversion of audience would also benefit Comcast's competitors that would remain on Sky's platform, reducing the prospective benefit of such a strategy.
- (278) In light of the above, the Commission considers that overall the merged entity would lack the incentive to engage in the total customer foreclosure strategies considered above.

(ii) Incentive to engage in partial foreclosure

- (279) The majority of broadcasters responding to the market investigation were concerned about possible incentives of the merged entity to degrade the terms and conditions of acquisition of rival TV channels.⁸⁷ One respondent mentioned that as Sky already has an incentive to favour its own channels and content over those of third parties and, as the Proposed Transaction will increase the merged entity's own channel portfolio, it will also increase this incentive.⁸⁸
- (280) In the UK, as explained above, there are strict restrictions on Sky's (and therefore the merged entity's) ability to degrade the way in which wholesalers' TV channels appear on its platforms. The regulatory regime preventing Sky from degrading other wholesalers' TV channels acts as a deterrent to its incentives, not least given the potential remedies that the relevant communications authorities can impose are stringent, including, the revocation of Sky's licence. Such sanctions are significant potential costs that reduce the merged entity's incentive to degrade the way in which it partners with third party wholesalers. The information submitted by the Notifying Party indicates that Sky has never been found in breach of this regulation.⁸⁹
- (281) As regards degradation via My Q on Sky's "Sky Q," as indicated above in paragraph (267), viewing data for Sky Q subscribers from March 2018 show that [*Sky confidential internal analysis*]. Therefore, the role that alternative program recommendation tools play remains [redacted] to date, thus providing little incentive for Sky to use this tool to divert viewing to Comcast's channels.

⁸⁷ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.6.

⁸⁸ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.6.2.

⁸⁹ See Form CO, paragraph 363.

- (282) As regards EPG degradation in Ireland, whilst the British EPG regulations are not mandatory, the information submitted by the Notifying Party indicates that Sky broadcasts the same EPG in the UK and Ireland and therefore the Irish EPG also reflects the UK regulatory constraints. This may be considered to constrain Sky's incentives to engage in partial foreclosure by way of EPG degradation.
- (283) In light of the above, the Commission considers that overall the merged entity would lack the incentive to engage in the partial customer foreclosure strategies considered above.

(c) Impact on effective competition of full/partial foreclosure

- (284) In *Fox/Sky*, the Commission noted that given Sky's importance as a distributor of pay-TV services, Sky appears to be an important source of advertising and carriage revenues.⁹⁰ The market investigation did not provide indications that this would no longer be the case. UK broadcasters have stated that being foreclosed from Sky's platform would have a significant adverse impact on their revenues.⁹¹
- (285) However, as indicated above, the agreements in place between Sky and wholesale TV channel suppliers afford protection in relation to carriage fees. The regulation in place in the United Kingdom in relation to EPG also affords protection against impact on wholesale TV channel suppliers which may result from partial foreclosure via EPG degradation for wholesale TV channel suppliers' channels. Similarly, the information on file from the Notifying Party indicates that Sky broadcasts the same EPG in the UK and Ireland and therefore the Irish EPG also reflects the UK regulatory constraints. As regards degradation via My Q on Sky Q, the Commission considers that the effect on wholesale TV channel suppliers, which may result from such a foreclosure strategy, is, in light of information on file and referred to above in paragraph (267), unlikely to be significant.
- (286) In addition, Sky's retail platform is not the only purchaser of general entertainment TV channels in the UK and Ireland, where Sky's downstream share of TV channel acquisitions is in the range of [30-40]% ([30-40]% in the UK and [40-50]% in Ireland). In the event that Sky sought to cease carrying third party channels on its platform, a large proportion of the retail market would remain for third party wholesalers to access.
- (287) As a consequence, it is unlikely that the customer foreclosure strategies considered above would have a significant negative impact on consumers. Consequently, the adoption of a foreclosure strategy would not appear to have a material effect on competition in the UK and Ireland.

(d) Conclusion

- (288) On the basis of the foregoing, the Commission therefore concludes that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market resulting from partial or total customer foreclosure in the United Kingdom and Ireland.

⁹⁰ *Fox/Sky*, paragraph 338.

⁹¹ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.9.

6.2.3.5. The Commission's assessment - Germany and Austria

(289) From the outset, the Commission recalls that Sky is already vertically integrated in that it already owns a portfolio of channels in addition to being present downstream as a distribution platform. The merger specific aspect in this regard is only the addition of Comcast's TV channels.

(a) Ability to engage in customer foreclosure

(i) Sky's importance as a distribution platform

(290) Downstream, Sky has a market share of [30-40]% in Germany and [40-50]% in Austria for the acquisition of TV channels.⁹² The Notifying Party estimates that Sky's share of all retail pay-TV services amounts to [20-30]% by revenue in each of Germany and Austria⁹³ (which makes Sky the leading pay-TV retailer in Germany by revenue and the second largest in Austria) and [10-20]% by subscribers in Germany and [10-20]% in Austria.

(291) However, as the Commission noted in its decision in case M.8354, *Fox/Sky*, other sources credit Sky with higher market shares by revenue, in the range of 50 to 60%.⁹⁴ While the Notifying Party disputes these estimates, it admits that Sky's position in the retail market in Germany and Austria has not changed significantly in the last two years.

(292) The results of the market investigation confirm that Sky's retail platform is significant to channel broadcasters, respondents to the market investigation having indicated that Sky is the biggest pay-TV platform in the German speaking territories.⁹⁵

(ii) Ability to engage in total foreclosure

(293) The market investigation revealed that the majority of wholesale suppliers of TV channels consider that Sky currently has significant bargaining power and is able to impose unfavourable contract terms.⁹⁶ Furthermore, a respondent noted that the revenues it derives from Sky exceeds the revenues of all other pay-TV platforms combined.

(294) As indicated above, the only merger specific element pertinent to the present assessment of full customer foreclosure is the addition of 13th Street and Syfy, Universal Channel and E!.

(295) 13th Street and Syfy can be considered to closely compete with Fox (21CF), RTL Crime (RTL), TNT Serie and TNT Film (both Time Warner); Universal Channel also with TNT Serie; and, E! with Sixx (ProSieben Sat). Comcast's general entertainment channels comprised just [redacted]% of all viewing on Sky's

⁹² Form CO, Table 25.

⁹³ Form CO, Annex 7.4, Tables 38.3 and 38.4.

⁹⁴ Commission decision of 7 April 2017 in case M.8354 – *Fox/Sky*, recital 342.

⁹⁵ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.4.1.

⁹⁶ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.4.

platform in 2015 to 2017, which is lower than the channels TLC, TNT Serie and RTL Crime.⁹⁷

- (296) Sky's offering relies on a wide range of high quality content in order to satisfy customers' expectations. Accordingly, no respondent to the market investigation expressed a concern that Sky would cease licensing all third party channels. Therefore, customer foreclosure, if any, could not concern more than a few of Sky's current suppliers.
- (297) In this context, Sky's carriage agreements with third party channel providers are typically [*duration of Sky's carriage agreements*]. In this respect, Sky currently has carriage agreements with providers [*names of suppliers and term of carriage agreements*], such that the merged entity's ability to foreclose these suppliers can be excluded.
- (298) However, Sky' carriage agreement with [*supplier names*], which broadcast channels that closely compete with Comcast's channels, will terminate [*term of Sky's carriage agreements*].
- (299) On this basis, while several elements will constrain the merged entity's ability to engage in total foreclosure, the Commission cannot rule out that the merged entity will have the ability to cease carrying a number of channels that compete closely with Comcast's in Germany and Austria.

(iii) Ability to engage in partial foreclosure

- (300) A small majority of respondents fear that the merged entity will be able to degrade distribution terms, in particular by diminishing carriage fees or the granting of unfavourable EPG slots.⁹⁸
- (301) As indicated above, the only merger specific element pertinent to the present assessment of partial customer foreclosure is the addition of Comcast's channels to Sky's portfolio.
- (302) The Commission considers that a number of other elements exist which militate against a finding of the ability of the merged entity to engage in partial customer foreclosure in the present case.
- (303) As regards partial foreclosure via lowering carriage fees, the Commission notes that Sky's ability to foreclose channels competing with Comcast's channels is strictly constrained by applicable contractual provisions. In this regard, the merged entity's ability to reduce carriage fees can be excluded in relation to broadcasters currently protected by multi-year agreements, as noted above in relation to total foreclosure.
- (304) As regards EPG ranking, in Germany, Sky is subject to regulation requiring it to (i) allocate listings based on an objective metric (audience viewing figures) and (ii) refrain from unduly discriminating between channels. Any changes to Sky's

⁹⁷ Reply to RFI 4, page 57.

⁹⁸ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, questions D.6 and D.6.1.

EPG methodology in Germany are subject to mandatory prior notification to the State Media Authority.⁹⁹

- (305) In Austria, Sky employs an EPG listing methodology similar to the one implemented in Germany in order to comply with the Austrian EPG Regulation. The Austrian EPG Regulation removes any ability for the merged entity to deteriorate the EPG listings of third party wholesale channels. The regime is founded on the principle of non-discrimination. The Austrian Communications Authority (KommAustria) has significant powers to sanction Sky were any discriminatory behaviour substantiated (including the revocation of its licence to operate its Sky Sport Austria channel in the country).¹⁰⁰
- (306) A violation of those regulatory obligations would be easily detected by the interested party, which would likely complain with the competent regulatory authorities.
- (307) In light of all the above, the Commission considers that overall the merged entity would not be able to engage in the partial customer foreclosure strategies in the form of EPG degradation without infringing regulation which would expose it to significant consequences, as described below in paragraph (318).

(b) Incentive to engage in customer foreclosure

(i) Incentive to engage in full foreclosure

- (308) The Commission has assessed the likelihood of full foreclosure in Germany and in Austria.
- (309) While a number of German broadcasters are concerned that the merged entity might reduce its reliance on third party channels, albeit not for the totality of its line-up,¹⁰¹ other broadcasters consider that the merged entity's incentives in relation to third party channels will not change as a result of the Proposed Transaction.¹⁰² Therefore, no clear view on the merged ability's incentives to foreclose competing channels can be deducted from the market investigation.
- (310) Given Comcast's limited presence as a wholesale supplier of TV channels, representing [redacted]% of viewing share on Sky's retail platform,¹⁰³ the Proposed Transaction is unlikely to bring about changes in the merged entity's incentives in its purchasing of TV channels from other wholesaler suppliers. Moreover, channels which compete closely with Comcast's channels (including TNT Serie and RTL Crime) have significant individual audience shares (of [5-10]% and [5-10]% respectively), demonstrating their importance as inputs to Sky's retail platform.

⁹⁹ Form CO, paragraph 366.

¹⁰⁰ See Form CO, paragraph 367.

¹⁰¹ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.5.

¹⁰² Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.5.1.

¹⁰³ Form CO, Table 26.

- (311) Sky's internal customer surveys further demonstrate the importance of channels that closely compete with Comcast's for subscriber retention. Sky's 2017 survey results show that [*results of Sky's customer survey*].
- (312) In Germany and Austria, FTA television remains more developed than pay-TV. Pay-TV retailers like Sky therefore have an overall incentive to improve pay-TV's penetration by making its basic pay-TV offering attractive to consumers. Therefore, full foreclosure of competing channels TLC, TNT Serie and RTL Crime would be at odds with this.
- (313) In addition, as noted by the Notifying Party, the closest competitors of NBCU in the general entertainment genre are major TV broadcasters that typically supply a popular suite of channels to Sky's retail platform, including in respect of channels outside of the general entertainment segment and in respect of content used by Sky on its own TV channels. The importance of Sky's commercial relationships with broadcasters renders a hypothetical wholesale foreclosure strategy in the basic pay-TV general entertainment segment risky as the affected broadcasters could retaliate on the basis of commercial relationships in other markets. In particular:
- (a) [*Details of Sky's carriage agreement and on-going negotiation*].
 - (b) [*Details of Sky's carriage agreement*]. The Notifying Party submitted an internal document¹⁰⁴ showing [*details of a Sky internal document concerning viewership data*].
- (314) Given that Sky's subscription revenues largely outweigh Comcast's wholesale revenues, the adoption of a customer foreclosure strategy which would risk deteriorating Sky's offering in the hope of improving Comcast's upstream revenues does not appear to be profitable. Although the Notifying Party did not provide an assessment of the amount of customer diversion that would result from foreclosing competing channels nor quantifies the resulting gains for Comcast, the difference between NBCU's 2017 revenue from its wholesale operations (Germany: EUR [*redacted*]; Austria: EUR [*redacted*]) and total subscription revenues for Sky (Germany: EUR [*redacted*]; Austria: EUR [*redacted*]) appears significant.
- (315) If a foreclosure strategy was to focus on certain but not all of Comcast's competitors, any resulting diversion of audience would also benefit Comcast's competitors that would remain on Sky's platform, reducing the prospective benefit of such a strategy.
- (316) In light of all the above, the Commission considers that overall the merged entity would not have the incentive to engage in total foreclosure of Comcast's competing channels in Germany and Austria as a result of the Proposed Transaction.

¹⁰⁴ Response to RFI 4 of 4 June 2018, question 17, Annex 17.3.

(ii) Incentive to engage in partial foreclosure

- (317) The results of the market investigation show that a number of German broadcasters are concerned about potential degradation of the terms and conditions for the acquisition of their channels and the granting of unfavourable EPG slots.¹⁰⁵
- (318) However, as noted above, EPG regulations in Germany and Austria require that broadcasters be treated fairly and in a non-discriminatory fashion. Under the applicable German regulation, in the event of an infringement of those obligations, the State Media Authority would be able to impose an administrative fine of up to EUR 500 000. The State Media Authority also has the power to revoke an infringing operator's EPG licence. Similarly, in case of an infringement of Austrian EPG regulations, the Austrian Communications Authority can order remedies and, should Sky fail to comply, revoke Sky's licence. Sky's incentives in relation to degradation of EPG rankings could therefore also be considered to be constrained in light of these significant consequences.
- (319) Furthermore, as noted in relation to total customer foreclosure, in Germany and Austria, FTA television remains more developed than pay-TV.¹⁰⁶ Pay-TV retailers like Sky therefore have an overall incentive to improve pay-TV's penetration by making its basic pay-TV offering attractive to consumers. As a consequence, it is unlikely that Sky would have an incentive to make its basic offering less attractive to consumers by degrading access to Comcast's competing channels.
- (320) In light of all the above, the Commission considers that overall the merged entity would not have the incentive to engage in partial foreclosure of Comcast's competing channels in Germany and Austria as a result of the Proposed Transaction.

(c) Impact on effective competition of full/partial foreclosure

- (321) As indicated above, certain broadcasters' current distribution agreements with Sky in relation to Germany and Austria will protect them against total foreclosure until their term, thus safeguarding their position for the foreseeable future.
- (322) As regards [*supplier names and term of carriage agreements*], these broadcasters generate significant licensing revenues from alternative sources. The evidence on file shows that these broadcasters do not generate the majority of their licensing revenues from Sky in Germany and Austria. Therefore, even in the event of total or partial foreclosure from Sky's retail platform, these broadcasters would continue to operate efficiently.
- (323) Consequently, in light of these elements, the Commission considers that full or partial foreclosure strategies are not likely to have an overall likely significant impact on effective competition in the market in question in Germany and Austria.

¹⁰⁵ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, questions D.6 and D.6.1.

¹⁰⁶ The FTA audience in Germany in 2017 was [10-20] million, compared with [0-5] million for pay-TV (see Reply to RFI 4, para. 18.9))

(d) Conclusion

(324) On the basis of the foregoing, the Commission therefore concludes that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market in relation to full or partial customer foreclosure in Germany and Austria.

6.2.3.6. The Commission's assessment - Italy

(a) Ability to engage in customer foreclosure

(i) Sky's importance as a distribution platform

(325) Downstream, Sky represents [90-100]% of the total spend on the acquisition of TV channels.¹⁰⁷ In Italy, Sky's share of all retail pay-TV services amounts to [70-80]% by revenue and [50-60]% by subscribers.¹⁰⁸

(326) A majority of respondents to the market investigation indicate that Sky currently has normal bargaining power, with negotiations being on an ordinary and equal footing.¹⁰⁹ However, a broadcaster expressed concern about Sky's large market position.

(ii) Ability to engage in total or partial foreclosure

(327) During the market investigation, Italian broadcasters raised concerns that the merged entity would engage in complete customer foreclosure of certain third party channels.¹¹⁰

(328) The only merger specific change which is to be considered in relation an assessment of customer foreclosure is the addition of Comcast's channel Studio Universal to Sky's channel portfolio.

(329) While some channels, i.e. FOX, Viacom, A+E's Crime and Investigation and Gambero Rosso do broadcast content that to some degree overlaps with that of Studio Universal, there are no third party channels closely competing with Studio Universal in Italy within the general entertainment segment.¹¹¹ Studio Universal typically broadcasts library film content and is therefore not a close substitute for subscribers seeking alternatives to other general entertainment channels such as FOX, Fox Crime, Comedy Central or Crime + Investigation (which focus on crime dramas and comedy series). The latter channels have higher audience shares than Studio Universal (which does not register as generating an audience share in the data available to the Parties¹¹²): Fox ([50-60]% audience share), Viacom ([5-10]% audience share) and Gambero Rosso ([0-5]% audience share), Discovery ([0-5]% audience share).¹¹³

¹⁰⁷ Form CO, Table 25.

¹⁰⁸ Form CO, Annex 7.4, Tables 38.5 and 38.10.

¹⁰⁹ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.4.

¹¹⁰ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.5.

¹¹¹ Reply to RFI 4, para. 17.18.

¹¹² See Reply to RFI 4, para. 17.17, referring to Table 14 in Annex 7.4 to the Form CO.

¹¹³ Reply to RFI 4, para. 19.5.

- (330) As in other countries, Sky's offering in Italy relies on a wide range of high quality content in order to satisfy customers' expectations. Accordingly, no respondent to the market investigation expressed a concern that Sky would cease licensing all third party channels. Therefore, customer foreclosure, if any, could not concern more than a few of Sky's current suppliers.
- (331) In this context, Sky's carriage agreements with third party channel providers are typically [*duration of Sky's carriage agreements*]. In this respect, Sky's carriage agreements with the majority of its channel providers [*names of suppliers and term of carriage agreements*], such that the merged entity's ability to foreclose these suppliers can be excluded.
- (332) However, Sky' carriage agreement with [*company name*], which broadcast channels that fall under the same thematic content as Comcast's channels, will terminate [*term of the carriage agreement and details of the commercial relation between the parties*]. Nevertheless, [*company name*] alone represents the majority of the audience of basic general entertainment channels in Italy, such that Sky would not be in a position to cease to distribute its channels without significantly deteriorating its offering.
- (333) Furthermore, the structure of the Italian television sector is similar to that in Germany and Austria, in the sense that FTA television remains more developed than pay-TV. In *Fox / Sky*, the Commission noted that in 2015 the pay-TV services represented only 36% of all retail television revenues in Italy, with FTA channels generating 64% of all revenues. Pay-TV retailers like Sky therefore have an overall incentive to improve pay-TV's penetration. The market investigation did not provide any indication that such an incentive would no longer exist. As a consequence, Sky's ability to engage in full foreclosure appears impacted by its incentive to make its basic pay-TV offering attractive to consumers. Full foreclosure of channels with similar content as Studio Universal would be at odds with this.
- (334) Therefore, in light of Studio Universal's marginal position and the importance of other channels within its thematic category, the merged entity does not appear to be in a position to cease carrying third party channels.
- (335) As to partial foreclosure, the responses to the market investigation were mixed. Some broadcasters however, consider that the merged entity would degrade the terms and conditions of the acquisition of TV channels from third parties, in particular through worse contract terms.
- (336) In relation to potential EPG degradation, the Commission notes that no formal EPG regulation exist in Italy. However, the Italian Communication Authority (AGCOM) may impose on operators the obligation to guarantee access to resources, including EPGs, on equitable, reasonable and non-discriminatory conditions, to the extent necessary to guarantee access to digital radio and TV services by end users. AGCOM has the power to intervene by imposing rules relating to access to EPGs in the event it identifies any distortions in the behaviour of TV operators that affect end users' ability to access TV services. A breach of these rules can result in a financial sanction of up to EUR 2.5 million, or up to 5% of the total turnover of a company with significant market power in the relevant market to which the breach refers.

- (337) However, given the lack of formal EPG regulation, the Commission does not consider that these elements constitute factors liable to eliminate the potential risk of partial foreclosure.¹¹⁴
- (338) In light of all the above, the Commission considers that overall the merged entity would not have the ability to engage in total foreclosure of Comcast's competing channels in Italy as a result of the Proposed Transaction. However, whilst there are elements which suggest a constraint on Sky's ability to engage in partial foreclosure, the Commission cannot rule out that the merged entity will have the ability to partially foreclose Comcast's closely competing channels in Italy as a result of the Proposed Transaction.
- (b) Incentive to engage in customer foreclosure
- (i) Incentive to engage in full foreclosure
- (339) The Commission has assessed the likelihood of full foreclosure in Italy.
- (340) During the market investigation, Italian broadcasters raised concerns that the merged entity would have an incentive to engage in customer foreclosure of certain third party channels.¹¹⁵ Broadcasters have pointed out that Sky has decreased the number of third party licensed channels in Italy in the past 3 years while increasing promotional efforts for Sky-owned channels, thus forcing a number of channels to switch to an FTA model. Adding Comcast's general entertainment channel to its portfolio would accelerate this trend.
- (341) The only merger specific change which is to be considered in relation an assessment of customer foreclosure is the addition of Comcast's channel Studio Universal to Sky's channel portfolio.
- (342) In Italy, Comcast's sole channel (Studio Universal) has a negligible market share by audience: indeed, the channel does not register as generating an audience share in the data available to the Parties.¹¹⁶ The combination of this channel with Sky's retail platform in Italy is therefore unlikely to give rise to potential customer foreclosure. Sky relies on 21CF ([50-60]% audience share), Viacom ([5-10]% audience share) and Gambero Rosso ([0-5]% audience share) and other broadcasters for the vast majority of its audience. Even modest players like Discovery ([0-5]% audience share) are of greater value to Sky's retail service than Studio Universal.
- (343) In addition, as noted in paragraph (333), pay-TV retailers like Sky have an overall incentive to improve pay-TV's penetration. As a consequence, it is unlikely that Sky would have an incentive to make its basic offering less attractive to consumers by degrading access to channels that carry content that overlaps with the content on Studio Universal.

¹¹⁴ See in this regard, the Commission's Non-Horizontal Merger Guidelines, para. 46.

¹¹⁵ Replies to Questionnaire Q2 to TV broadcasters of 7 May 2018, question D.5.

¹¹⁶ See Reply to RFI 4, para. 17.17, referring to Table 14 in Annex 7.4 to the Form CO.

(344) In light of the above, the Commission considers that overall the merged entity would lack the incentive to engage in the total customer foreclosure strategies considered above.

(ii) Incentive to engage in partial foreclosure

(345) As to partial foreclosure, the responses to the market investigation were mixed, with some respondents considering that the merged entity would degrade the terms and conditions of the acquisition of TV channels from third parties. Other respondents were less concerned.

(346) By contrast with other Member States, Sky's EPG ranking of pay-TV channels does not appear significantly constrained by regulations. As a consequence, Sky's incentives may not be materially reduced by sector specific rules.

(347) However, in light of the structure of the Italian television sector (see paragraph (333)), it is unlikely that Sky would have an incentive to make its basic offering less attractive to consumers by degrading access to channels that carry content that overlaps with the content on Studio Universal. As noted above in relation to total foreclosure, Sky's retail service relies on third party channels for the vast majority of the audience within Comcast's channels thematic group. Therefore, in light of Comcast's negligible contribution to the merged entity's upstream position, a change of Sky's incentives in relation to the distribution of third party channels appears implausible.

(348) On this basis, the Commission considers, on balance, that the merged entity would lack incentives to engage in partial foreclosure of Comcast's competing channels in Italy post-Transaction.

(c) Impact on effective competition of full/partial foreclosure

(349) As indicated above, the majority of broadcasters' current distribution agreements with Sky in relation to Italy will protect them against total foreclosure until their term, thus safeguarding their position for the foreseeable future.

(350) In respect of 21CF, in the implausible event that the merged entity ceased distributing its channels, the Commission notes that this broadcaster generates significant licensing revenues from alternative sources. Therefore, even in the event of total or partial foreclosure from Sky's retail platform, 21CF would continue to operate efficiently.

(351) In light of these elements, the Commission considers that full or partial foreclosure strategies in Italy, are unlikely to have an overall likely significant impact on effective competition in the market in question.

(d) Conclusion

(352) In light of the above, the Commission therefore concludes that the Proposed Transaction does not raise serious doubts as to its compatibility with the internal market in relation to full or partial customer foreclosure in Italy.

7. CONCLUSION

(353) For the above reasons, the European Commission has decided not to oppose the notified operation and to declare it compatible with the internal market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) of the Merger Regulation and Article 57 of the EEA Agreement.

For the Commission

Signed
Phil HOGAN
Member of the Commission