MERGER CONTROL

POLICY GUIDANCE TO STRENGTHEN THE INDONESIAN COMPETITION FRAMEWORK[1]

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SUMMARY

- Merger control aims at preventing those mergers that have a high probability of generating significant harmful impact on the level of market competition.
- Merger control policy should allow for beneficial dynamic changes in market structure without unjustifiably increasing the cost for the government and businesses.
- Indonesia's merger control regime requires mandatory post-merger notification unlike most jurisdictions, although informal pre-merger consultations are allowed. This reduces the ability of the KPPU to stop mergers that are likely to harm competition and to design remedies that can mitigate potential competition concerns.
- In practice, the time needed to review the notified mergers, even those without competition concerns, is high compared to other jurisdictions partly due to procedural issues that limit KPPU efficiency and due to the definition of mergers that are subject to notification and review.
- In line with common international practice, the competition law (Law No. 5 of 1999 concerning the ban on monopolistic practices and unfair business competition) could be amended to
    1. **introduce a system of mandatory ex-ante merger notification**;
    2. **clarify the standard of theory of harm** to assess a merger by replacing references to carrying out potential anticompetitive (monopolistic) practices with a standard such as preventing significant lessening of competition (a similar concept as unfair business competition in the current law);
    3. **clarify the definition of merger** by introducing the concept of control and combination of previously independent economic units, so that merger review is concerned with transactions that combine at least two previously independent economic units through a lasting change in control.
- Complementary, and even if the competition law is not amended, **regulations and guidelines can be updated to increase the efficiency of merger review**:
    1. The threshold for merger notification could be raised and include a threshold of size for individual parties to the transaction and the combined resulting firm in terms of assets and/or annual turnover.
    2. A fast-track procedure or a two-phase procedure with different information requirements and substantive analysis could be adopted to focus KPPU resources on riskier mergers. incorporating different information requirements depending of the type merger.
    3. Regulations and guidelines can further define the mergers subject to review so as to: (a) exclude corporate restructuring within economic groups in Indonesia or international mergers that do not imply an amalgamation of independent economic entities operating in Indonesia; (b) provide rules on joint-ventures and other transactions that qualify as mergers; (c) explain factors for substantive economic analysis including the assessment of efficiencies; and (d) indicate policies regarding remedies to prevent harm.

[1] This note was prepared by the World Bank Group's Market and Competition Policy Team under the ongoing World Bank Group's engagement with the Government of Indonesia to contribute to the current discussion on the amendments of the law No. 5 of 1999 concerning the ban on monopolistic practices and unfair business competition.

A. BACKGROUND

Merger control aims at preventing those mergers that have a high probability of generating significant harmful impact on the level of market competition. This policy tool seeks to complement the enforcement of rules to address anticompetitive behavior and identify situations in which a change in market structure will likely affect market outcomes and harm consumers. This instrument is not intended to be implemented intrusively so as to define market structures (for example, the number of firms in the market), but in a complementary manner to address clear and grounded competition concerns if a merger is carried out.

Merger control policy should allow for beneficial changes in market structure without unjustifiably increasing the cost for the government and businesses. Merger review should be designed in such a way that the costs for government and businesses are proportionate. At the government level, if not appropriately designed, merger reviews can displace investigations on actual anticompetitive behavior reducing the effectiveness of the whole competition framework. For businesses, overly burdensome information requirements, long review process, and an unclear and broad scope of merger review would increase administrative costs, economic costs of delaying the completion of the transaction, and business risks. Entry, growth and exit of business are natural in a competitive business environment; therefore, merger regulations should not obstruct these efficient processes.

Merger review is concerned with transactions that combine at least two previously independent economic units through a lasting change in control. A merger is a method by which firms can increase their size and expand into existing or new economic activities and markets. Mergers are classified as: *horizontal* (a merger between firms that produce and sell the same products, i.e. between competing firms); *vertical* (a merger between firms operating at different stages of production); or, *conglomerate* (a merger between firms in unrelated business).

It is widely recognized that mergers, amalgamations, acquisitions and other similar transactions are in most cases good for competition and consumers. Mergers allow firms to reduce costs and realize efficiencies that can drive investment and innovation and ultimately reduce prices for consumers. However, because mergers inherently lead to consolidation of assets, elimination of competitors and changes to market structure, some mergers may significantly harm competition, harm consumers or trigger other competition policy issues. These undesirable mergers are the exception, not the rule. The purpose of merger control is to prevent them occurring, or to mitigate or prevent the harm that may result if they are allowed.

Merger control processes can be time-consuming, expensive and resource-intensive. Competition authorities therefore typically limit their review to those mergers most at risk of causing significant harm to competition. Merger control frameworks often apply jurisdictional or monetary thresholds to identify such mergers, allowing other mergers to proceed without any notification or review process at all. Upon review, a competition authority may decide to approve a merger, prohibit a merger or approve a merger subject to conditions intended to neutralize or reduce the anticompetitive effects of the merger (e.g., a requirement to divest part of the business).

The four main components of an effective merger control framework are summarized in *Table 1* – this note will address the first two.

Table 1: Key components of an effective merger control framework

Components	Key areas
1. Defining transactions that will be evaluated	• Voluntary or mandatory, ex-ante or ex-post notification. • Definition of economic concentration: definition of control and change in control, types of transactions. • Thresholds for merger notification: variables, values, and calculation method.
2. Establishing formal procedures for merger review	• Timeframe: time limits, staggered process (phases for less and more complex cases). • Required documentation and confidential treatment of information. • Required payments: calculation of merger filing fees. • Due process: transparency, consistency, accountability.
3. Setting the economic framework for analysis	• Criteria for evaluating potential anticompetitive effects: unilateral and coordinated effects. • Treatment of efficiencies, pass through to consumers and compensation of anticompetitive effects. • Criteria to set remedies or conditions that can remove anticompetitive concerns.
4. Addressing institutional constraints	• Availability of resources to conduct merger review. • Optimization of organization structure for effective enforcement.

Source: Adapted from WBG Markets and Competition Policy Assessment Tool

B. EFFECTIVE MERGER CONTROL – KEY ELEMENTS

1. Approaches to merger notification

Countries with merger control regulations can choose different approaches to identify potentially anticompetitive transactions. An effective merger control regime should focus on mergers that are likely to significantly lessen competition within its jurisdiction, and therefore should restrict the number of mergers subject to premerger notification. This reduces the resources expended (i.e. time, money) by competition agencies and firms and is usually achieved either through *voluntary* or *mandatory* notification for mergers that exceed certain thresholds. The most common framework is *mandatory pre-merger notification*. This is usually defined in the primary competition law which is then followed by regulations or guidelines that delve deeper into definitions and procedures of merger control.

Pre- or ex-ante notification refers to the notification of an impending merger to a competition agency prior to consummation. Ex- ante notification is beneficial as it provides the competition agency enough time to review the transaction and respond to anti-competitive challenges that may arise beforehand, thus avoiding an 'unscramble-the-egg' situation once merger has already been effected. However, it may result in delaying transactions that may be beneficial to society and increases opportunity cost of the merging parties.

On the other hand, ex-post notification is the notification of a merger after consummation. It is considered less costly for businesses and avoids the rejection of mergers that are not harmful to competition, but it can allow for harmful mergers. Under an ex-post notification system, it is difficult to apply structural remedies (i.e. undo or restructure a merger), which are more suited to ex-ante merger control and thus may result in the failure to remedy those mergers that are anticompetitive.

Mandatory notification is the compulsory requirement to notify a merger, either pre- or post-consummation, especially those that meet certain set thresholds. Mandatory notification is aligned with most merger regimes and provides merging parties with legal certainty once the merger has been cleared by the competition agency. However, it imposes a regulatory burden on the parties and affects efficiency for mergers that would not cause any harm to competition. Smaller mergers that may fall below notification thresholds would not be reviewed yet they may, in some circumstances, cause significant lessening of competition.

Voluntary notification does not require merging parties to notify the competition authority prior to completing the transaction, but parties that believe their merger may substantially affect competition are encouraged to notify ex-ante. The approach is said to reduce the cost burden on companies and competition agencies thus increasing efficiency, because merging parties will only notify mergers that might likely limit competition to avoid risks of having the merger overturned by the competition authority. Therefore, even those mergers that have economic significance but are less likely to harm competition are relieved of the regulatory burden. Disadvantages of the voluntary approach include: (i) the risk that certain problematic mergers may be overlooked by the authority which could harm competition; (ii) lack of legal certainty; and, (iii) increased business risk should the merger be reviewed, and remedies applied. Moreover, remedying the effects of harmful mergers using structural remedies - such as demergers- is challenging for the competition agency. Voluntary notification usually involves ex-post monitoring, and for it to be an efficient approach, there must be incentives in place or fines to encourage voluntary notification of potentially harmful mergers. The voluntary approach, in most cases, should allow for pre-merger consultation to reduce the risk of completing mergers that would raise competition concerns and avoid costly intervention.

Table 2: Comparison of merger notification systems

	Mandatory/Voluntary	Ex ante/ex post notification	Fast Track and/or 2-phase procedures
Australia	Voluntary	NA	x **
Brazil	Mandatory	Ex ante	√
China	Mandatory	Ex ante	√
EU	Mandatory	Ex ante	√
Germany	Mandatory	Ex ante	√
India	Mandatory	Ex ante	√
Indonesia	Mandatory	Ex post	×
Korea	Mandatory	Ex ante	√
Laos	Mandatory	Ex ante	×
Mexico	Mandatory	Ex ante	√
New Zealand	Voluntary	NA	×
Philippines	Mandatory	Ex ante	√
Russia	Mandatory	Ex ante	√
Singapore	Voluntary	NA	√
South Africa	Mandatory	Ex ante	√
Thailand	Mandatory	Ex ante: merger which may create dominance; Ex post: merger which may materially reduce competition	×
Turkey	Mandatory	Ex ante	√

	Mandatory/Voluntary	Ex ante/ex post notification	Fast Track and/or 2-phase procedures
UK	Voluntary	NA	√
USA	Mandatory	Ex ante	√ *
Vietnam	Mandatory	Ex ante	×

** Waiting period before full investigation (similar to phase I)*
*** Informal and formal merger review*
Source: WBG Markets and Competition Policy Database

Some jurisdictions, for example South Africa, apply either mandatory pre-merger and voluntary post-merger notification depending on the size of the parties. South Africa's merger system defines three types of transactions - small, intermediate or large as per the combined annual turnover in the preceding year or asset value of the acquiring firm (*See Box 1*). Only intermediate or large mergers are subject to pre-merger mandatory notification. Notification of small mergers is post-merger voluntary, unless the Competition Commission requests the merging parties to file a small merger notification.

Box 1: Merger control in South Africa

South Africa's merger thresholds and methods of calculation provide that:

- A *small merger* is one where the combined annual turnover or asset value of the acquiring firm and the target firm (combined figure) in, into or from South Africa is below ZAR560 million (around USD 48 mln), and the asset value in South Africa or turnover value in, into or from South Africa of the target firm (depending on which is the highest) is below ZAR80 million (around USD 7 mln).
- An *intermediate merger* is one where the combined figure is ZAR560 million or more, and the asset value in South Africa or the turnover value in, into or from South Africa of the target firm (depending on which is the highest) in the preceding financial year is ZAR80 million or more.
- A *large merger* is one where the asset value in South Africa or the turnover value in, into or from South Africa of the target firm (depending on which is the highest) in the preceding financial year is ZAR190 million (around USD 16 mln) or more and the combined figure is ZAR6.6 billion (around USD 560 mln) or more.

The combined figure is the combined asset values in South Africa, or turnover values in, into or from South Africa of the acquiring firm and the target firm in their respective preceding financial years, or the assets of the one and the turnover of the other, whichever combination reaches the highest figure.

A transaction must meet both aspects of the threshold enquiry before it can be classified as either intermediate or large. For example, if the target's asset/turnover is greater than ZAR80 million, but the combined asset/turnover is less than ZAR560 million, the transaction fails to meet the thresholds of an intermediate merger and will therefore be classified as a small merger which is not automatically notifiable.

Only intermediate or large mergers are subject to mandatory pre-merger notification. Notification of small mergers is voluntary, unless the Competition Commission requests the merging parties to file a small merger notification within six months after implementation if it believes the merger may substantially prevent or lessen competition or cannot be justified on public interest grounds.

Source: South Africa Government Gazette No.31957, 6 March 2009: Determination of Merger Thresholds and Method of Calculation

Recommendations for Indonesia

1) *Change the current post- notification regime with a mandatory pre-merger notification*.

The mandatory pre-notification framework will provide KPPU with sufficient time to review transactions beforehand, and respond appropriately to any anti-competitive concerns. In absence of a change in the law to introduce ex-ante mandatory notification, KPPU should implement a

stronger voluntary pre-notification regime as a complement to the existing mandatory post-merger notification regime. Both these approaches would increase the effectiveness of Indonesia's framework only if implemented in an efficient way considering a risk-based approach.

2. Definition of notifiable mergers

Definition of transactions subject to merger control determines the effectiveness of the regime in isolating mergers that are likely to harm competition in the market. It is important to properly define what constitutes a merger to identify transactions suitable for merger review and avoid capturing too many ownership changes that will not have any effect on the structure of the market or competition; or defining it too narrowly thus missing some problematic transactions.

Jurisdictional criteria for defining mergers differ but economic criteria are commonly used which focus on whether a transaction will enable a firm to acquire the ability to exercise some form of control over a previously independent firm[2]. Defining control, controlling interest and how that control can be exercised are important factors to consider in defining merger transactions. These essentially answer the question: 'what is a merger?' with the main aspect being acquiring 'controlling interest.' The UNCTAD model law on competition provides general definitions of concentration, control and different forms of transactions that would constitute a merger – see *Box 2*.

Box 2: UNCTAD Definition of Transactions

Concentration describes the acquisition of control over another undertaking through merger and acquisitions activity or otherwise. It may therefore be used interchangeably with the term "merger". Concentration may also be used to describe the number of players in a given market. Two requirements inherent in the notion of concentration are: (a) change of control (control of the faculty, conferred by contracts, rights or any other means, to exercise, in fact or in law, decisive influence in a company); and (b) **stability of control** (concentration necessarily requires an element of permanence).

The following transactions could qualify as concentrations:

Merger: It is generally defined as a fusion between two or more enterprises previously independent of each other, whereby the identity of one or more is lost and the result is a single enterprise. They take various forms:

a) ***Acquisition/takeover:*** the acquisition or takeover of one enterprise by another usually involves the purchase of all or a majority of shares of another company, or even of a minority shareholding, so long as it is sufficient to exercise control and substantial influence. The acquisition of substantial assets of another company, production site or another functional unit of another company also qualifies as notifiable transactions. Acquisitions may take place without the consent of the target company. This is known as a "hostile" acquisition or takeover.

b) ***Joint Ventures*****:** joint ventures are agreements between firms to engage in a specific joint activity, often through the creation of a jointly owned and controlled subsidiary, to perform a task useful to both or to realize synergies from the parents' contributions. Depending on the degree of integration between the two businesses, a joint venture can be reviewed as a merger or just as an agreement among competitors.

c) ***Interlocking Directorship*****:** an interlocking directorship describes a situation where a person is a member of the board of directors of two or more enterprises, or the representatives of two or more enterprises meet on the board of directors of one firm. The competition concerns here lie in the possibility that an interlocking directorship may lead to administrative control whereby decisions regarding investment and production can, in effect, lead to the formation of common strategies among otherwise competing enterprises, on prices, market allocations, and other concerted activities.

Source: UNCTAD 'Model Law on Competition'

[2] See "Definition of Transaction for the Purpose of Merger Control Review", OECD 2014 http://www.oecd.org/daf/competition/Merger-control-review-2013.pdf

Joint Ventures are in most cases considered mergers if they are full-function joint ventures. This means that 'it must perform, for a long duration, all the functions of an autonomous economic entity.' [3] The definition of 'long duration' differs per jurisdiction but ranges between 5 to 10 years.[4]

Minority interests may also include certain rights that would exert significant influence in the management of an entity and thus may be considered controlling interest. This includes the ability to veto decisions concerning the strategic plan of the entity, appointment of senior management and the budget. Therefore, where the minority interest acquired brings about powers tantamount to controlling interest, the transaction would be considered a merger. Other means of control that might constitute a merger include when control is acquired upon exit of a shareholder or on a contractual basis for long duration contracts.[5] The regulations should also have provisions for treatment of foreign companies that enter the market through acquisition of a local market and provide clear criteria for transactions that are exempted from merger review.

Recommendations for Indonesia

2) *Clarify what transactions are caught under the law and thus are notifiable by including or expanding the definitions of core concepts of merger control in the law or in government regulations.*

In particular, the definitions of concentration or merger (for example, to state it covers transactions that combine at least two previously independent economic units), control and change of control should be included. The inclusion of examples of various forms of transactions that constitute a merger are also important, especially joint ventures which are not captured by the current law. The law or regulation should also include descriptions of control over an undertaking such as ability to veto or appoint directors, owning majority of shares, etc.

3. Thresholds for merger notification

Thresholds are used to determine the scope of merger control as they identify mergers with economic significance that could potentially harm competition. Setting appropriate thresholds ensures that resources expended by companies as well as competition agency in notifying and review are limited to only those mergers that would have a material anti-competitive effect on the market. The thresholds should be clear, accessible and based on objectively quantifiable criteria to permit parties to readily determine whether a transaction is notifiable. In determining objective thresholds, the first step would be to identify the *applicable measurement tool* (assets, sales, market shares etc.), followed by identifying the *geographical scope* (national or worldwide) and lastly the *time frame*.

Objective thresholds (based on sales (turnover) of merging parties, assets of merging parties, amount of transaction) are the most commonly used and are recommended internationally. Thresholds can also be based on market shares of merging companies. However, in the recent years, jurisdictions started to

[3] See Competition Authority of Kenya Merger Guidelines'
[4] For example, EU and Kenya define a long duration as being 10 years while the COMESA guidelines define it as being 5 years.
[5] COMESA Competition Commission (CCC) *'Merger Assessment Guidelines'*

move away from the practice of using market shares. For instance, Brazil and Turkey eliminated the use of market shares in 2011.

Objective thresholds have important advantages over those based on market shares or other market variables. They are (a) understandable, (b) based on the information readily available to merging parties, and (c) calculated through a process that is easier and more transparent than calculation of market variables. Although market shares can be a better predictor than objective thresholds of whether a merger could have anticompetitive effects, predictive power of this instrument depends heavily on how well it is measured. In many cases, it is not easy to define relevant product and geographic markets - a task required to estimate market shares – before a substantive analysis. The costs for merging parties to calculate market shares and for an authority to examine the validity of provided information are substantial, especially in countries where market information is scarce.

With regards to geographical scope, the thresholds should be based on local revenues, assets and activities within the jurisdiction of the competition agency. Moreover, jurisdiction should be asserted only over those mergers that have an appropriate nexus with their jurisdiction, therefore only transactions that are likely to have a significant direct and immediate economic effect within the jurisdiction i.e. if each of the parties has significant activities (, significant sales or assets) within the jurisdiction. The thresholds should also cover the whole economic group and this should be explicitly stated.

It is further recommended that size thresholds be defined *individually* for at least two parties to the transaction as well as *combined* for all the merging parties. The use of only one of the two i.e. individual or combined, could lead to notification of transactions that do not imply an important change of structure in the market. Individual thresholds ensure that both parties are of economic significance and therefore avoids capturing '*de minimis'* transactions which would otherwise be reviewed if only combined thresholds were used. Combined thresholds could therefore be defined together with an individual threshold for at least two parties to the transaction. Additionally, the value of the thresholds should be determined by an analysis of the most common operations and transactions executed within the concerned economy and their respective market size; and on a balance of costs of unnecessary merger review and harm from anti-competitive mergers that are completed. Regulations should also provide for the regular review of the size or value of thresholds.

The whole economic group of the individual merging parties should be considered in calculating the annual turnover and value of assets. Therefore, the annual turnover and value of assets of a party to the merger should be calculated by adding together the turnover or assets of (i) the party to the merger (ii) its subsidiaries; (iii) its parent companies; and (iv) other subsidiaries in of its parent company. However, if the parent will no longer be the parent of the target undertaking or the merged undertaking post-merger, the annual turnover and/or asset value of the parent and that of its subsidiaries should be excluded.

The basis and method of calculation of asset value and turnover should be clearly defined in the regulations or guidelines. Determining the value of assets or annual turnover should be based on the merging parties' financial statements[6] for the preceding year. For example, the asset value could be

[6] The financial statements relied upon should be prepared and audited as per the Generally Accepted Accounting Principles (GAAP) or the standards generally used in the jurisdiction.

defined as the '*gross value of the firm's assets as recorded on the balance sheet for the end of the preceding financial year*' while the turnover could be '*based on the amounts derived by the merging parties from the sale of products or provision of services falling within the firm's ordinary activities in the particular jurisdiction, after deduction of sales rebates, value added tax and other taxes related to turnover.'*[7]The turnover should therefore be allocated based on where the customer is located or where the product or service is sold. This should not include the sale of products or provision of services to any of the merging parties' subsidiaries or parent companies. The values should be adjusted for any material changes that occur between the date of the financial statements being used to calculate the asset/turnover value and the date on which the calculation is being made.

Recommendations for Indonesia

3) *Amend merger threshold regulations by including both combined and individual thresholds for notifiable mergers and specify the definition of assets, turnover and basis/ method of calculating group assets/turnover in the regulations or guidelines.*

4. Establishing efficient formal procedures for merger control

To achieve efficient, sound decisions that safeguard competition and minimize undue burden on the private sector, most competition authorities now conduct two-phase investigations into mergers or have a formal simplified notification procedure for certain transactions that allow for fast-track decisions. In two-phase procedures, the first phase allows filtering out of mergers unlikely to prevent or lessen competition in a relevant market. The second phase is reserved for mergers that are judged to be potentially harmful to competition and therefore merit deeper analysis. Filtering merger investigations in this way significantly reduces unnecessary administrative costs for the merging enterprises and for competition authorities. In addition to two-phased review process, some jurisdictions such as the EU have formal simplified notification rules. These mechanisms that allow for a 'fast-track' process enhance the efficiency of a competition authority, allowing it to focus on harmful anticompetitive practices (such as cartels) and make considerable savings in terms of resources and costs devoted to merger investigations overall. In addition, voluntary pre-notification enquiries to the competition agency with basic information on the transaction is recommended to assist in determining whether the transactions amounts to a merger, whether it falls under notifiable mergers and what is the information required for the actual notification.

Most countries with merger control statutes have adopted a two- phase merger review process which is considered best practice. Phase I of the review involves an initial market assessment to determine whether the merger is likely to prevent or lessen competition. Determining the effect that the merger would have on the market is based on a combination of factors such as: existence of overlapping markets, level and trend of concentration, market power, characteristics of the product market, ease of market entry, etc.[8] If it is found that the transaction is not likely to harm competition, the merger is cleared. The decision to clear a merger at Phase I should be based on a combination of factors indicated above and not

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[7] CCC '*Rules on the Determination of Merger Notification Thresholds and Method of Calculation*.' Available at: http://www.comesacompetition.org/wp-content/uploads/2015/04/Amendments-to-the-Rules-to-the-Determination-of-Merger-Thresholds-and-Method-of-Calculation-adopted-by-COM-26-March-2015.pdf . These Rules capture best practices in the European Union and other jurisdictions.

[8] Gooch, Anthony; Nyman, Sara; Begazo, Tania (2014) *'Two-Phase Merger Review: Background and Rationale' : A Policy Note under the support of IFC's Zambia Investment Climate Program II for the Competition and Consumer Protection Commission od Zambia*

entirely on a single element such as market concentration (using concentration indices such as the Herfindahl-Hirschmann Index or HHI). Should there be evidence indicating that the merger is likely to raise some competition concerns, it then moves on to Phase II analysis. Phase II is a much deeper analysis of the transaction and its potential effects on competition which requires more time as it involves collection of data from various parties and extensive economic analysis. In Phase II the analysis focuses on establishing whether it is more likely than not that the merger will harm competition. Within Europe, the European Union sets a model for a two-phase approach to the conduct of merger investigations, the features of which are summarized in Box 3.

Box 3: European Community Two-phased Merger Review Process and Simplified Process

After the compulsory notification of a merger, the European Commission has 25 working days to analyze the deal during the phase I investigation.

A *phase I* review may involve the following:

- Requests for information from the merging companies or third parties;
- Questionnaires to competitors or customers seeking their views on the merger, as well as other contacts with market participants, aimed at clarifying the conditions for competition in a given market or the role of the merging companies in that market.
- The Commission keeps the merging companies informed about the progress of its analysis. Towards the end of phase I, a "state-of-play meeting" is typically held, where the Commission informs them about the results of the phase I investigation. If there are competition concerns, companies can offer remedies, which extends the phase I deadline by 10 working days.

There are two main conclusions of a phase 1 investigation:

- The merger is cleared, either unconditionally or subject to accepted remedies; or
- The merger still raises competition concerns and the Commission opens a phase 2 investigation.

Over 90% of all cases before the European Commission are resolved at phase I, generally without remedies.

Phase 2 is an in-depth analysis of the merger's prospective effects on competition and requires more time. It is opened when the case cannot be resolved at phase I, i.e. when the Commission has concerns that the transaction could restrict competition in the internal market. A phase 2 investigation typically involves more extensive information gathering, including companies' internal documents, extensive economic data, more detailed questionnaires to market participants, and/or site visits. In the phase 2 investigation the Commission also analyses claimed efficiencies which the companies could achieve when merged together.

In addition to the two-phased review process, the simplified merger review procedure allows companies to use a shorter notification form for mergers that are unlikely to raise competition problems. The companies need to provide much less detailed information, and the Commission can clear the merger without investigating its effects amongst customers, competitors and other parties. The following transactions qualify for this procedure:

(i) for markets in which two merging companies compete ("horizontal overlap markets"), combined market share below 20%;

(ii) for markets where one of the merging companies sells an input to a market where the other company is active ("vertically related markets", for instance where a manufacturer of cars acquires a manufacturer of car parts), individual or combined market share below 30%;

(ii) when the companies' combined market shares in overlap markets are between 20% and 50% and the increase in market share after the combination of their activities is limited (change of HHI of 150 points);

(iv) a party is to acquire sole control of an undertaking over which it already has joint control;

(v) when parties are not engaged in business activities in the same product and geographic market, or in a product market which is upstream or downstream from a product market in which any other party to the merger is engaged;

(vi) two or more undertakings acquire joint control of a joint venture, provided that the joint venture is negligible (turnover or total value of assets transferred to the joint venture less than EUR 100 million in the European Economic Area).

Source: European Commission, World Bank Group elaboration

A formalized fast track process (simplified procedure) applies to transactions that are not likely to raise any competition concerns. These transactions include for example those that include merging parties that do not operate in the same market or are not in a vertical relationship, or *de minimis* thresholds for

combined market shares or changes in market structure. These notifications have fewer information requirements during notification to the competition agency. The European Union and Mexico apply a simplified procedure (*See Box 3 and Box 4*). This is mostly on a voluntary basis and takes a shorter period to review as compared to the normal procedure. Several jurisdictions combine phased and simplified procedures, for example Mexico and EU. In many cases, however, the fast track process is used to refer to Phase I of the merger review process. Conversely, in the UK where notification is voluntary, the fast track process is applied to cases in which there is significant evidence that the investigation should go directly to phase II. Therefore, the transaction could be fast tracked to full review on phase II investigations.

A fast track process can be formalized in a simplified procedure or be the result of the implementation of a 2-phase review (mergers analyzed in phase I are considered under fast track). While both two – phased and formal simplified procedures mechanisms increase efficiency, they have important differing characteristics. First, the review period for the simplified procedure is significantly shorter than phase I review under the normal procedure - since it applies to certain transactions that are generally not likely to raise competition concerns. For example, if the merger does not include any market overlaps or vertical relationship between the parties, the potential economic effects are not even analyzed. Second, merging parties are required to specifically request the use of the simplified procedure if they fall under its scope, unlike the two – phase merger procedure which is applied to any merger notification. Third, the onus is on the merging parties to show that, despite their transaction being notifiable, the transaction falls under the cases covered by the simplified procedure, unlike the phased process where the competition authority conducts the assessment and has to prove whether it is more likely than not that the merger will significantly harm competition. Finally, information requirements are minimal for the formal simplified procedure, compared to the phased process.

Box 4: Simplified Merger Review Process in Mexico

Mexico's framework provides for both fast-track ("notoriedad") and normal process (two-phase merger review) for mergers exceeding thresholds prescribed by law. Mergers that exceed the stated thresholds require mandatory pre-merger notification.

For notifiable mergers, Mexico offers a fast-track review where parties can provide evidence to demonstrate that the merger will be unlikely to raise competition concerns. This includes the following situations, among others:

- Merging parties are not actual or potential competitors or merging parties do not operate in markets related to the relevant market for the operation; and
- The merger implies that a new player enters into the market for the first time, so market structure does not change; or it involves change in shareholding that does not imply change in control.

The fast-track process is voluntary, rather than automatic. In the event the Commission is not satisfied with evidence presented for fast-track review, the merger is subjected to a two-phase review. In the absence of a fast-track application, all notifiable mergers are automatically subject to a two-phase review.

Source: COFECE, elaborated by World Bank Group

In addition to two-phase and fast-track procedures, there are several additional factors to consider in establishing formal procedures for merger review. These include setting timeframes for notification and scrutiny of the merger, clarifying the information required for filing, ensuring due process and confidential treatment of information received, and including appropriate mechanisms for third parties to participate

in the review process. These are typically articulated in regulations or guidelines: Annex 1 provides a summary of some of the more effective international practices.

Recommendations for Indonesia

4) *Speed up and reduce the costs of the merger review process and improve its quality by adopting a two-phase review process (combined with a formal simplified process)*

   This would minimize undue burden on the private sector and on KPPU. Regulations and guidelines could be developed to provide details to operationalize and provide guidance on the two-phase and/or formal simplified processes including information requirements, timetables, mechanisms for due process, and elements for substantive analysis.

5. Setting the framework for economic analysis

The standard of proof for merger review should be based on sound and robust economic principles, and not on rigid legal standards that account only for certain indicators. Merger review laws and policies should establish a framework for analysis that permits the authority to identify the likely anticompetitive effects of a merger, but also to retain sufficient flexibility to adapt to economic developments. Secondary legislation and guidelines should set out clear, comprehensive, and transparent legal and analytical standards and the authority should apply its merger analysis reasonably and flexibly on a case-by-case basis.

A key part of analyzing the anticompetitive effects of mergers is to demonstrate a theory of harm of the potential transaction. This involves identifying ways in which the merger might lead to a harmful outcome. So, the competition authority needs to identify what evidence would be needed to demonstrate (in the case of each theory) that harm would indeed be the most likely result. This helps to focus the merger analysis because the competition authority can look for particular evidence depending on each hypothesis of theory of harm, instead of conducting a general and broad market inquiry. Then, if the evidence is found, remedial action can be taken - or, if the evidence is not found, the merger can be cleared. See Annex 2 for a summary of factors to be considered in substantive analysis of mergers.

Internationally, focus on market structure and strengthening of a dominant position has been shifted towards assessing likely effects on market outcomes. In EU, previous merger regulations prohibited mergers that created or strengthened a dominant position, thus impairing the possibility of challenging mergers that decrease welfare without creating a dominant position and including the effects of efficiency gains in merger review. Current EC regulations introduce the concept of substantial impediment to effective competition and are more explicit about the incorporation of efficiencies in the analysis. This principle has been adopted in at least nine countries. The concept of substantial lessening or lowering of competition for merger review is used in at least thirteen countries, including the US. The number of countries that use dominance as the main criteria for merger review has declined over time showing the importance of defining the theory of harm for each transaction. The standard of resulting in anticompetitive practices (as is the case in Indonesia) is seldom used in other jurisdictions since this standard is not feasible to assess with available information.

The authority has the burden to prove any competitive harm that arises from the analysis of the transaction while merging parties demonstrate the existence of efficiencies. As mentioned above, the competition authority should base its decisions on sound economic principles following assessment of the theories of harm which prove that the transaction will lead to the significant lessening or prevention of

competition**.** Further, due to the information asymmetry between the competition authority and merging parties, the merging parties must provide information to prove the efficiencies they claim will stem from the merger.

Remedies should be imposed in consultation with the merging parties and should address the identified competitive harm. Secondary legislation and guidelines should be developed defining the remedies available and procedure for imposing those remedies. These could be behavioral remedies such as periodic price reporting or structural remedies such as asset divestment. The remedies should be binding, clear and precise.

Recommendations for Indonesia

5) *Clarify the standard for merger assessment in the Law and focus on mergers that can significantly lessen competition in the market.*

6) *Develop guidelines for merger assessment to define the various types of mergers (horizontal, vertical, conglomerate, etc.), provide details on the economic analysis of their potential effect on competition and clarify provisions on burden of proof, theory of harm and standards for remedies.*

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ANNEX 1: PROCEDURAL ASPECTS FOR EFFECTIVE MERGER CONTROL FRAMEWORKS

Time frame for notification and scrutiny of the merger	• Parties should be permitted to notify proposed mergers upon certification of a good faith intent to consummate the proposed transaction. The regulations should clarify whether qualifying transactions for notification shall require authorization before execution. • It further recommends that merger reviews should be completed within a reasonable time frame. This should consider the complexity of the transaction and possible competition issues, the availability and difficulty of obtaining information and timeliness of responses by the merging parties to information requests. • Review of transactions that do not raise material competitive concerns should allow for an expeditious process. This may be in the form of a two-phase process whereby Phase I review usually takes a maximum of one or two months while Phase II takes between two to five additional months. • A voluntary advisory or pre-notification consultation mechanism is advisable to identify whether the transaction is notifiable and the information requirements. This should require submission of basic information and review and feedback should be within 10 or 15 days
Required information for filing	• Information requests for the first phase should be minimal and commensurate to the analysis to be done, and increase with mergers that require further in-depth analysis (Phase II). • Information provided does not necessarily need to be in the country's official language thus, allowing internationally accepted languages such as English, will reduce the burden on the firms especially for those transactions involving foreign firms. • The regulations should, however, include a disclaimer that the agency has the power to request any information necessary to complete its review. • These requirements should be included in the secondary legislation and guidelines in detail and not in the primary competition law.
Confidentiality treatment	• Clear and transparent confidentiality policies and practices are necessary for an effective regime.
Due process	• It is essential to guarantee merging parties the due process by allowing them to respond to any concerns especially prior to delivering an adverse decision. • The parties should be provided with sufficient and timely information and given reasonable time to respond. • Due process also involves providing for the consultation of the competition agency with other sector regulators in regulated industries as well as internal mechanisms that ensure consistency, accountability and transparency of merger review. • In addition, merging parties should have the opportunity for a review of the agency's adverse decision by a separate adjudicative body
Transparency	• Transparency of the competition agency's assessments and decisions can be enhanced by making public substantive laws, regulations and guidelines on how it conducts its assessments as well as its decisions
Rights of third parties	• Procedural fairness should be afforded to third parties with an interest in the merger, but safeguarding confidentiality

Source: World Bank Group elaboration

ANNEX 2: CONSIDERATIONS FOR THE SUBSTANTIVE ANALYSIS OF MERGERS [9]

Generally, merger review consists of the following elements: market definition, market structure analysis, assessment of unilateral effects, balancing efficiency and market power considerations, and assessment of coordinated effects – these and other substantive areas are summarized below. The extent of analysis and information required varies depending on whether it is a phase I or phase II assessment, with the latter requiring a more detailed analysis of all issues. Criteria for in-depth analysis should consider whether the mergers are horizontal, vertical or conglomerate as they each raise unique competition effects that should be analysed differently. The competition law or regulations should also have provisions for treatment of failing firm defense arguments.

a) ***Market Definition***: relevant market definition for each merger should be done on a case by case basis, as per the market definition guidelines of the competition agency, and depending on whether the merger is a horizontal or non-horizontal merger. Market definition in horizontal mergers should focus on product and geographic markets and on the theories of harm for non-horizontal mergers.

b) ***Unilateral and coordinated effects***: a detailed analysis of unilateral and coordinated effects is required comparing the expected scenario if the merger is executed with a counterfactual. The analysis needs to foresee changes in the competitive conditions that are likely to occur without the merger. Unilateral effects are generated by the ability of profitably exercising market power to a materially greater degree than would have been possible for either of the merged parties prior to the merger. Ease of entry, capacity constraints, availability and responsiveness of alternative suppliers, buyer power, and efficiencies are key elements to identify the extent of unilateral effects. Coordinated effects refer to the likelihood that firms remaining in the market after the merger will be able to coordinate or strengthen existing coordination to exercise market power. For this purpose, competition agencies should assess (a) the ability to identify terms of coordination, (b) the ability to detect deviations from the terms of coordination, (c) the ability to punish deviations that would undermine the coordinated interaction, and (d) the extent to which existing competitive constraints and other factors would likely deter or disrupt effective coordination.

c) ***Measures of concentration***: mergers that lead to a substantial increase in market share and market concentration in the relevant market are more likely to lessen or prevent competition. Measurement of market shares should be on a case by case basis and may be based on sales revenue, production volume, capacity or reserves depending on availability of information. The guidelines should define the thresholds above which market share would be of concern and differentiate between horizontal and non-horizontal mergers. For example, post-merger market share would be of concern if above 15% for horizontal mergers and 30% for non-horizontal mergers. However, concentration has to be assessed together with other factors to decide on proceeding to a Phase II (in-depth) review.

[9] Adopted from COMESA Merger Assessment Guidelines that incorporate advisory by the World Bank Group.

d) ***Theories of harm***: in identifying and assessing the effects of a merger, the 'theory of harm' framework is an important tool which considers the likely effects of the merger against a counterfactual scenario (describing the competitive situation in the relevant market without the merger which in most cases will be the prevailing market conditions). This helps focus the merger review on specific effects and therefore determine the appropriate remedies to counter any negative effects of the merger.

   Assessment of the merger will require identification of the theory of harm which, in most cases, depends on the type of merge, industry supply and demand structure, product characteristics and existing and expected evolution of competitive dynamics. For horizontal mergers, assessment of non-coordinated effects (such as elimination of a competitor) and coordinated effects should be assessed. Although most non-horizontal mergers (vertical and conglomerate) are benign, and in some cases even result in efficiencies, potential non-coordinated effects such as input and customer foreclosure should be reviewed. In determining the theories of harm, the analysis should focus on the *ability* and *incentive* of the merged parties to carry out activities that would lead to the negative effects on competition and the *likely impact* of those effects on competition.

e) ***Entry and expansion***: the analysis should include an assessment of whether post-merger entry and expansion of competitors will be timely, likely and sufficient. Some mergers might increase concentration but because of the ease of entry and expansion, may not raise any competition concerns. Recent entries or expansions in the relevant market provide a good starting point for the assessment.

f) ***Assessment of efficiencies***: the merger may generate some efficiencies which would improve the merging parties' ability and incentive to compete. These are not guaranteed; however, the competition agency should consider the benefits of these efficiencies and potential to counteract any prevention or lessening of competition that may be caused by the merger. They should be cognizable[10], timely and must benefit consumers. The onus rests on the merging parties to provide relevant information substantiating the efficiency claims and demonstrating that less restrictive alternatives to the merger do not exist. Demand and supply side efficiencies should be considered, as well as the ability of the merged parties to conduct research and development which could potentially encourage innovation resulting in a positive knock-on effects in the market and therefore the consumers.

g) ***Countervailing buyer power***: countervailing power refers to the negotiating power of a buyer or group of buyers to limit the ability of the merged entity to raise prices. Buyer power is enhanced when customers have alternatives with limited switching costs, can sponsor new entry or can constrain the behaviour of the supplier. The extent of countervailing buyer power pre-merger and

[10] According to the COMESA Merger Guidelines, efficiencies are merger-specific efficiencies that have been verifies and do not arise from anticompetitive reductions in output or level of service.

its 'umbrella effect'[11] should be assessed, as well as the post-merger impact on countervailing buyer power.

h) ***Removal of a 'maverick undertaking'***: the removal of a vigorous and effective competitor through a merger would potentially lead to significant reduction and lessening of competition. This is especially true for mergers that involve maverick undertakings[12] that exert significant influence and might lead to unilateral market power of the merged entity or coordinated conduct by smaller market players. The extent to which each party to the merger is an effective competitor should be assessed with the aim of limiting mergers that seek to remove such competitors so as to maintain and enhance the benefits of competition in the market.

i) ***Effects from mergers of competing buyers***: the extent to which the merger of competing buyers could lead to increased buyer power in the upstream market, especially when parties have downstream market power, should be assessed as it could give rise to prevention or lessening of competition in the market. The assessment should therefore consider if the merged entity has an incentive to lower the amount it purchases so as to drive down its purchase price; and whether it has sufficient downstream market power such that it increases the price to consumers by reducing quantity sold in the market.

[11] COMESA guidelines describe the umbrella effect as 'Extent to which the buyer power of one customer, or group of customers can constrain the merged undertaking's prices to all its customers.'

[12] COMESA guidelines describe a maverick undertaking as one 'with a significant competitive advantage.'