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Working Party No. 3 on Co-operation and Enforcement

INVESTIGATIONS OF CONSUMMATED AND NON-NOTIFIABLE MERGERS

-- Israel --

25 February 2014

This note is submitted by Israel to the Working Party No. 3 of the Competition Committee FOR DISCUSSION under Item III at its forthcoming meeting to be held on 25 February 2014.

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– Israel –

1. Status of antitrust regulation

1. Israel, like most developed economies, regulates mergers in order to verify that proposed mergers do not harm competition and consumers. The Restrictive Trade Practices Law (5748-1988) (hereinafter: "**The Antitrust Act**") requires prior notification from the merging parties to the Israel Antitrust Authority (IAA) of mergers meeting the following conditions (hereinafter "**mergers**").

2. Mergers defined

2. A 'merger' is broadly defined in the Antitrust Act to include the acquisition of the principal assets of a company by another entity (a separate division in the company may be regarded as a 'principal asset', even if it does not produce most of the company's revenues), or the acquisition of shares in a company by another entity through which the acquiring company is accorded:

1. More than 25 percent of either the nominal value of the issued share capital or of the voting power of the acquired company;
2. The power to appoint more than 25 percent of the directors of the acquired company; or
3. Participation in more than 25 percent of the profits of the acquired company.

3. The acquisition may be direct or indirect or by way of rights accorded by a contract (article 1). Nevertheless, since the law does not provide a conclusive set of characteristics that constitute a merger, even the acquisition of less than 25 percent of any of the above-mentioned rights may constitute a merger if the nature and outcome of the transaction is the creation of a structural link between two companies. The term "structural link" refers first and foremost to the granting or strengthening of a foothold, to the acquiring company with respect to the other company's decision-making mechanisms, which prior to the acquisition had been separate and independent.[1]

3. Mergers requiring prior notification

4. A pre-merger notification must be submitted to the IAA Director General if one or more of the following alternatives, a, b, or c, applies:[2]

a) As a result of the merger, the merged entity's market share exceeds one half of the total market share; or

b) The revenues of the merging entities are such that:

   1. The cumulative revenues of the merging entities in the previous financial year exceeded 150 million new Israeli shekels ("NIS"); and
   2. The revenue of each merging entity exceeded 10 million NIS for the same period.

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1 For more information visit the IAA Guidelines for Reporting and Evaluating Mergers: http://eng-archive.antitrust.gov.il/ANTItem.aspx?ID=177&FromSubject=100232&FromYear=2014&FromPage=0.

2 Restrictive Trade Practices Law, 5748 – 1988; Chapter III (A)(17).

c) One of the merging entities is a monopoly as defined in The Antitrust Act (an entity which holds more than 50 percent market share in any relevant market).

5. Some transactions which do not meet the abovementioned thresholds may however be regarded as restrictive arrangements, which are also subject scrutiny.

4. Discovery of violations of the pre notification provision

6. Methods of discovering companies that merged without obtaining prior permission from the IAA include:

1. **Third-party complaints** that alert the IAA of companies that merged without obtaining pre-merger authorization.

2. **The IAA may become aware of a consummated merger** in the course of a nonrelated inspection or market analysis.

3. **One of the merging entities voluntarily reveals** that a merger took place without prior permission from the IAA. In these cases, the merging entity will usually argue that the merged companies failed to notify the IAA because they were not aware of their obligation to do so.

7. In such situations, the IAA will verify whether the consummated merger meets the notification thresholds, and, in appropriate cases, proceed to analyze the merger's competitive effects.

5. Challenges of non-notifiable transactions

8. Consummating a merger without prior authorization of the IAA may be subject to either criminal prosecution or administrative sanctions, depending on the matter at hand. In the case of criminal prosecution, according to the Antitrust Act, the court may impose fines or prison sentences (up to 5 years in aggravating circumstances), while the Director General has the power to impose fines of up to 8% of the company's turnover (but no more than 24 million NIS).

9. In July 2012, the Director General released "Guideline 1/12: IAA Guidelines on enforcement procedures for the use of administrative fines". These guidelines outline the IAA's policy regarding enforcement of the law, and are intended to draw the line between breaches of the Law that are subject to criminal prosecution and those that are subject to administrative fines. Under the guidelines, where appropriate, an illegally consummated horizontal merger is subject to criminal sanctions, while a non-horizontal merger will usually be subject to administrative fines.

10. Additionally, the Director General may petition the head of the Antitrust Tribunal for injunctive relief against an illegally consummated merger under Section 50A of the Act. This allows for a settlement or for interim relief under Section 36 – pending the resolution of the underlying Tribunal case.

11. When appropriate, the IAA may settle matters regarding illegally consummated mergers in lieu of seeking criminal or administrative sanctions through consent decrees authorized by the Antitrust Tribunal.

12. As a general note, the decision whether to initiate criminal proceedings, impose administrative fines, apply for injunctions, or to seek settlement with the companies, is always examined on a case by case basis.

5.1 Case #1- Sewage treatment market

13. In 2006, Mekorot Development and Enterprise Ltd ("Mekorot") and Mekorot Yizom Minrav Ltd ("Minrav") purchased equal shareholdings of a sewage treatment plant. In September 2012, Mekorot purchased Minrav's shares so that after the purchase, Mekorot was the sole shareholder of the sewage facility. As both parties failed to notify the IAA of the purchase, both allegedly breached the Antitrust Act.

14. Immediately after the date of the transaction (which was not fully implemented at that time), the corporations approached the Director General and notified him of the merger. The Director General and the corporations later reached a consent decree: the IAA would not file for criminal or financial sanctions upon payment by the corporations of 30,000 NIS to the Israeli treasury. Additionally, the corporations were required to file the notice of merger for the transaction as required by law. A merger notification was filed.

15. The Director General found that the merger between the two contractors did not raise any competitive concerns and therefore approved the merger on 18/06/13.

16. Since the acquisition was not a horizontal merger, the IAA decided not to prosecute criminally and instead settle the case as mentioned above. Among the reasons were the Director General's finding that the merger did not raise significant competitive concerns, the fact that the IAA was notified of the merger shortly after the parties commenced (but did not finalize) the execution of the transaction and that the failure to notify was unintentional. The IAA believed that reaching a settlement would save costs, cut litigation time, expedite the case, and allow the IAA to direct resources to other matters.

5.2 Case # 2 –Life sciences market

17. Clal Biotechnology Industries LTD ("CBI") is a public holding company that invests in life sciences. Gili Medical LTD ("G. medical") is a private company that was established in 2010 and engages in the research and development of medical equipment such as non-invasive devices for nocturnal hypoglycemic events.

18. In 2010, an agreement was signed between CBI and G. Medical according to which CBI would purchase more than 25% of G. Medical's shares with the power to appoint more than 25% of the directors, allegedly in violation of the requirement to file of a merger notification.

19. The obligation to notify the IAA in this case was only due to the fact that CBI met the monopoly threshold. The monopoly threshold was met, however, in markets unrelated to the merger.[3]

20. Among the reasons that led the IAA to settle this case by consent decree was the fact that, under the procedural Guidelines for Reporting and Evaluating Mergers, parties to a merger transaction can apply for an exemption from their duty to submit a notification where the <u>only</u> reason for notifying of the merger is due to a party's monopoly in a market that is unrelated to the transaction. The IAA found that CBI and G. Medical could have been exempted from notification had they submitted a proper application in due time. In addition, the transaction did not raise any significant competitive concerns and the IAA was convinced the infringement was unintentional.

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[3] Restrictive Trade Practices Law (5748-1988); 17(A)(3).

6. Divestitures

21. In addition to criminal and financial sanctions, Section 25 of the Antitrust Act states that the Antitrust Tribunal may order a break up of an illegally consummated merger where it finds, upon application by The Director General, that the merger raises reasonable concerns for significant competitive harm or reasonable concern for harm to consumers.

22. The breaking up of merged companies aims to restore the situation to its former state by any means the Antitrust Tribunal deems fit. This could be done by transferring shares to a third party or by means of establishing another company to which some of the merged entity's assets shall be transferred.

6.1 Case #3 - The Tomato Paste Market

23. Prinir produces tomato-based products, while Milos processes, produces, and also markets tomato-based products. In September 2006, 24.8% of Milos' shares were purchased by Bogofen – a company allegedly controlled by Prinir. This transaction was not brought to the attention of the IAA before the parties started executing it in November 2006.

24. Following a criminal investigation of the case, the Director General submitted an application to the Antitrust Tribunal to order the separation of the merged entity. The Director General contended that this constituted a horizontal merger to a monopoly (i.e., holding more than 50%) in the relevant market (which, as mentioned above, requires prior approval from the Director General).

25. The Director General argued, *inter alia*, that the excess capacity the merged entity controls could hinder new competitors from entering the market and existing competitors from expanding within the market. This merged entity would also possess enough market power to allow it to raise prices at will. The market would be controlled by a duopoly – the merged entity and another relatively large competitor.

26. The merging parties argued that the transaction did not constitute a merger at all; furthermore, the parties argued that even if it was a merger, it was not anti-competitive.

27. The Antitrust Tribunal addressed these arguments separately. First, it addressed the question of whether or not the transaction was anti-competitive. If the transaction was not anti-competitive, it would be unnecessary to determine whether the transaction was a merger, since there would be no grounds for divestiture. Regarding the competitive analysis of the transaction, the Tribunal found that the market was concentrated. The Tribunal further found that high barriers to entry, limited by not only imports, did in fact exist (including the excess capacity controlled by the merged entity, high costs of entry, significance of marketing and brand recognition, shelf space availability, etc.). The Tribunal expressed doubt as to whether a new entity or and existing entity could or would enter or expand within the market. There was indeed a reasonable risk that, as a result of the merger, competition in the tomato paste sector would be significantly harmed.

28. Although deliberations concerning the Director General's application for the breaking up of the merger were expected to go through to the second stage, on March 2011, the Director General withdrew his application as Milos was eventually sold to a third party and Prinir and Milos were voluntarily separated.

7. Concluding Remarks

29. The Restrictive Trade Practices Law (5748-1988) and various guidelines published by the IAA provide the roadmap for the IAA's response to illegally consummated mergers. The IAA's policy is to criminally prosecute those involved in illegally consummated horizontal mergers. Administrative fines are usually appropriate in cases of illegally consummated non-horizontal mergers.

30. The recent introduction of administrative fines enables the IAA to make enforcement more efficient and appropriate in infringements involving non-horizontal mergers. At the same time, and for the most part, the IAA continues to criminally prosecute infringements involving horizontal mergers. This improved enforcement toolkit enables the IAA to optimize its resources while still achieving appropriate incentives to comply with the Antitrust Act.