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JFTC Proposes Important Changes to Japan's Merger Guidelines

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On January 31, 2007, the Japan Fair Trade Commission ("JFTC") published for public comment a draft of the revised "Guidelines on the Application of the Anti-Monopoly Act to Reviewing Business Combination" (*Kigyo Ketsugo Shinsa ni Kansuru Dokusenkinshiho no Unyou Shishin*) (the "Revised Guidelines").[1] The draft of the Revised Guidelines contains several key provisions that propose significant changes to the current Merger Guidelines. If adopted, these changes are likely to have important implications for transactions that are subject to review by the JFTC.

Key Provisions

The key provisions in the Revised Guidelines include:

- **Market Concentration 'Safe Harbors' –** The Revised Guidelines expand the current "safe harbor" standards for mergers involving competitors, and the JFTC's proposed safe harbors are generally more permissive than similar thresholds used by U.S. and European enforcement agencies. This potentially widens the number of transactions that can avoid an in-depth review by the JFTC and be presumed lawful.

  Specifically, when the market concentration levels fall within certain thresholds and the transaction results in sufficiently low changes in the concentration level, the JFTC will presume that the transaction does not pose any antitrust concerns. To qualify for "safe harbor" treatment, a transaction must meet one of the following thresholds:

  - The HHI[2] for the relevant market is 1,500 or less
  - The HHI for the relevant market is between 1,500 and 2,500, and the transaction does not result in an HHI increase greater than 250[3]
  - The HHI for the relevant market is more than 2,500, but the HHI increase due to the transaction is 150 or less[4]

  By way of comparison, the U.S. antitrust agencies presume that a merger that increases the HHI by more than 50 to a level in excess of 1,800 will result in significant anticompetitive effects. Similarly, the European Commission's market concentration safe harbors use slightly lower thresholds than the levels proposed by the JFTC.

  Finally, the current "safe harbors" used by the JFTC had been criticized for their complicated structure. For instance, some of the current thresholds only created a presumption that the transaction would not give the combined firm the ability to exercise *unilateral* market power. The new safe harbors described above, however, also create a presumption that the transaction is unlikely to result in increased *coordination* among the remaining firms in the marketplace.

- **Geographic Market --** The Revised Guidelines expressly recognize that the relevant geographic market may extend beyond Japan's borders when competition from overseas suppliers restrains pricing behavior within Japan. Because a cross-border or worldwide market is now more clearly accepted as a possible geographic market definition, there is a greater likelihood that mergers involving one or more firms with a strong Japanese presence will be approved when there is evidence that the parties face competition in areas outside Japan.

- **Relevant Market Definition and Entry --** The Revised Guidelines explicitly adopt the so-called "SSNIP Test" (or the "hypothetical monopolist test") for determining the relevant market definition. This is a standard followed by other enforcement agencies, including the U.S. Department of Justice and the Federal Trade Commission. The Revised Guidelines also specifically set out a two-year time period for examining whether competition from new entrants or foreign imports is likely to occur and thereby eliminate any concerns about a transaction's impact on competition.

- **Additional Explanation of Factors Relevant to JFTC Analysis --** The Revised Guidelines contain a more detailed explanation of the types of information that the JFTC is likely to evaluate when analyzing a transaction. While the current Merger Guidelines enumerate a handful of factors the agency usually considers, including the positions of the parties and their competitors in the market, imports, entry, pressure from adjacent markets, overall business capability, efficiency, and financial soundness of the parties' corporate group, the Revised Guidelines provide additional details that offer firms planning an M&A transaction (or seeking to block a transaction) greater guidance on the types of information and evidence that the JFTC is interested in receiving during its evaluation of the transaction.

Although the Revised Guidelines remain subject to public comment, it is unlikely that there will be significant changes in the final version because the JFTC has already obtained informal approval from other government agencies and the Liberal Democratic Party, the governing party in Japan. The public comment period will end on March 1, 2007, and the Revised Guidelines are expected to become effective in April 2007.

Footnotes

[1] The current Merger Guidelines were published on May 31, 2004 and have been applied to a number of M&A cases. *See* http://www.mofo.com/news/updates/files/update1312.html.

[2] HHI denotes "Herfindahl Hirschmann Index," which can be obtained by summing up the square of the market share of every firm in the relevant market.

[3] For example, the HHI increment will be 250 if a firm with a share of 25% acquires another firm with a share of 5%.

[4] For example, the HHI increment will be 150 if a firm with a share of 25% acquires another firm with a share of 3%, or if a firm with a share of 15% acquires another firm with a share of 5%.