



# Antitrust in the downturn

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The credit crunch and economic downturn have brought about new challenges for competition law, for those subject to it and for those who administer it. In response to the liquidity crisis and associated deterioration of market conditions, antitrust enforcement authorities have demonstrated some flexibility in both the timing and substantive standards applied to the review of mergers and other collaborative activities in the financial industry. This flexibility, however, carries the additional challenges of ensuring consistency in enforcement and the implications of what may be more permissive legal precedents in relation to potentially anti-competitive practices and transactions.

These challenges – and how they play out for companies and financial institutions – are explored in this briefing.

## Merger control

The financial crisis has had significant implications in the merger control field.

The UK government, for example, took radical steps to facilitate the Lloyds TSB/HBOS merger. With HBOS in difficulties, the government promised that it would introduce new rules to allow the transaction to avoid the merger being blocked by the competition authorities – a real possibility given that the transaction will create the UK's largest bank and mortgage provider.

The government, which largely removed the political role from the merger control with some fanfare in 2002, introduced a new 'public interest consideration' relating to financial stability. This allowed Lord Mandelson, the

Secretary of State for Business, to trump the competition concerns expressed by the Office of Fair Trading: he concluded that the merger should nonetheless be allowed to go ahead in the interests of financial stability.

At a European level, the European Commission (the Commission) has shown a willingness to be flexible on its usual requirement to wait for clearance before closing. Where a rescue package has to be put together very swiftly, the suspensory effect of the European Community merger rules could seriously hamper rescue acquisitions. This could have been a real problem in the Bradford & Bingley case, where Santander emerged as the leading bidder. The Commission, though, was willing very swiftly to grant a derogation from the suspensory effect of its rules to permit Santander to close the deal immediately.

Similarly, the US Department of Justice (DOJ), in collaboration and consultation with other financial industry regulators (including the Federal Reserve Board and the Treasury Department), has afforded expedited and largely unburdened review of several mergers and acquisitions between and among commercial banks and investment banks. Many of these transactions involved largely vertical or conglomerate issues that likely would not have resulted in enforcement actions even in more stable and positive industry conditions, at least under enforcement standards applied by the DOJ during the Bush Administration. Others, however, presented direct horizontal combinations (eg Wells Fargo/Wachovia and JPMorganChase/Washington Mutual) that could have resulted in extensive review and possible demands for remedies.

Whether the incoming Obama Administration will continue this relatively non-interventionist approach to consolidation in the financial industry is uncertain. Before the full onset of the credit crisis, the Obama campaign severely criticised the Bush Administration antitrust enforcement and, in particular, promised to ‘reinvigorate’ merger enforcement. To the extent that the credit crunch and macroeconomic weakness continue, however, the Obama DOJ may find it difficult to maintain this promise, especially in relation to financial industry consolidation. If financial institutions can demonstrate that their proposed consolidation transaction will create substantial efficiencies and otherwise enhance stability (especially if other financial industry regulators support the transaction), the Obama DOJ is likely to continue the current flexible, permissive merger control policies.

## State aid

Similarly, the European Union rules on State aid have been at the centre of the major developments in the past months.

Until the crisis events of October this year, the Commission was sticking to its traditional, relatively strict line on the notification and approval procedures. The European rules require that all State aids must generally be notified and approved by the Commission before they are implemented, a process that typically takes many months.

In some cases the Commission has latterly moved more quickly. For example, the guarantee put in place by the public owners of WestLB was cleared as rescue aid relatively quickly, although the Commission has demanded far-reaching measures in the ongoing restructuring procedure (which may explain why other public banks, eg in Germany, have searched for market-based risk shields to avoid heavy restructuring being imposed on them by the Commission).

At the end of September, the UK’s rescue of Bradford & Bingley was approved by the Commission in record time – within 24 hours (albeit after productive initial discussions with the Commission in the period before this). Moreover, the Commission recognised that the emergency situation demanded some flexibility in its rules: it accepted a structural element to the rescue package that would likely not have been approved in

normal circumstances. Other banks like Germany’s HRE were similarly bailed out with quick Commission approval.

The same approach marked subsequent approvals of aid schemes throughout Europe, with the Commission acknowledging that its previous refusal to approve aid on the basis of a ‘serious disturbance in the economy of a Member State’ had to be rethought.

The Commission helpfully issued guidance on the application of State aid rules to financial institutions in the current financial crisis, in an attempt to place a structure around the approach that had been emerging on an ad hoc basis. The guidance retained familiar concepts, such as keeping aid to the minimum necessary and minimising distortions to competition. However, it did indicate a greater degree of flexibility for certain institutions in timing for approvals, the restructuring plans that need to be submitted, the duration of permissible aid and the extent to which structural solutions might be approved.

Based on its guidance note, the Commission authorised a number of national rescue schemes by Member States including guarantee schemes and recapitalisation facilities. Most of these authorisations come with strict obligations concerning minimum capital quotas and minimum remuneration for stabilisation measures under the scheme. Moreover, in the same way as for the ad hoc authorisation of measures for individual banks, in depth Commission scrutiny is in fact merely postponed: the Commission will soon start looking at the restructuring plans that must be submitted; the results of its review will be critical for the banking sector going forward.

## What happens next?

Although its initial effects – in the competition law field and more widely – have been felt in the banking sector, the international financial crisis has far wider implications.

The next few months and years seem likely to see consolidation mergers in many sectors – witness, for example, the talk of consolidation in the US automotive industry. In many cases, regulators will be faced with a case that presents challenging competition issues, but a strong commercial imperative to get the deal done quickly. Historically, authorities have resisted suggestions

that they should soft-pedal merger control for companies in straitened circumstances – unless their exit from the market was certain and imminent – but there may be pressure to adopt a more flexible stance.

Moreover, where such consolidation has already taken place – such as in the UK banking sector – regulators can be expected to maintain a watchful approach. The UK Office of Fair Trading has already been tasked with keeping watch on the new Lloyds TSB/HBOS banking giant.

In the US, the Obama Administration will be faced with the challenge of reconciling its promise of increased antitrust enforcement with the exigencies of the financial crisis, including the claimed benefits of further consolidations in the financial industry. The Obama campaign also promised increased enforcement against unilateral anti-competitive conduct. Therefore, it may be reasonable to expect that the new Obama DOJ will conduct retrospective reviews of the claimed benefits of financial industry consolidations and to investigate allegations of anti-competitive conduct by recently consolidated firms.

In the State aid field, the Commission's guidelines for aid to financial institutions during the present crisis have put a framework around its current case load, but they say nothing about the longer term implications for companies or sectors that receive State aid. The Commission is already trying to send out signals that its flexible approach for the banks is a one-off, but it may find it difficult to hold the line against calls for increased flexibility in other sectors. Having accepted that the current crisis constitutes a 'serious disturbance of the economy' for the purpose of the rules, there must be a good chance that Member State governments will seek to push aid schemes in other sectors through this gateway. The Commission's response in the near term and the way in which it will deal with the restructuring of the European banking industry will be critical for the future of the State aid rules and for those affected by them.

At the highest level, the European competition authorities and their equivalents around the world have been insisting that their rules are 'part of the solution, not part of the problem'. The next few months will demonstrate whether their political masters, commentators and the markets agree.

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