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English - Or. English

DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

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Working Party No. 3 on Co-operation and Enforcement

ROUNDTABLE ON THE STANDARD FOR MERGER REVIEW, WITH A PARTICULAR EMPHASIS ON COUNTRY EXPERIENCE WITH THE CHANGE OF MERGER REVIEW STANDARD FROM THE DOMINANCE TEST TO THE SLC/SIEC TEST

-- Japan --

9 June 2009

The attached document is submitted to Working Party No. 3 of the Competition Committee FOR DISCUSSION under item III of the agenda at its forthcoming meeting on 9 June 2009.

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1. In Japan, any business combination such as mergers, shareholding or other transactions, are prohibited if "the effect may be substantially to restrain competition in a particular field of trade". This is regarded as the so-called "substantive test" for merger review [Article 10, 13, 14, 15, 15-2 and 16 of the Antimonopoly Act (AMA)].

2. The Japan Fair Trade Commission (JFTC) has formulated and published the "Guidelines to Application of the Antimonopoly Act concerning Review of Business Combination[1]" (hereinafter referred to as the "Guidelines"), which clarified the interpretation of "the effect may be substantially to restrain competition in a particular field of trade" as the requirement for prohibition under the AMA. The Guidelines set out the analytical framework for assessing what kind of business combination may be substantially to restrain competition in a particular field of trade.

3. The "substantial restraint of competition" that refers to the anticompetitive effect is defined as "bring about a state in which competition itself has significantly decreased and a situation has been created in which a specific business operator or a group of business operators can control the market by determining price, quality, volume, and various other terms with some latitude at its or their own volition" (Decision of Tokyo High Court on December 7, 1953, concerning Toho Company, Limited, et al). Given the sentences handed down in this case, the Guidelines provided the interpretation of "the effect may be" as the likelihood of the emergence of conditions that could easily lead to the substantial restraint of competition. Concretely speaking, "if the market structure is altered in a non-competitive way by the business combination, and if conditions are likely to emerge that would allow the company a certain latitude to manipulate price, quality, volume, and other conditions by acting unilaterally or coordinately with other companies," the effect of the business combination may be substantially to restrain competition.

4. In this manner, "the substantive test" in Japan covers two types of anticompetitive effects: the unilateral conduct by the company group[2] and the coordinated conduct between the company group and its competitors. Individual business combinations are reviewed in respect of these two viewpoints. So, there may be a case in which a business combination may be substantially to restrain competition from the viewpoint of the latter even though it may not be substantially to restrain competition from the viewpoint of the former.

5. Under the Guidelines, the analysis of the substantial restraint of competition by unilateral conduct is classified into two cases, such as when goods are characterized as homogenous and when goods are characterized as differentiated.

1. When Goods Are Characterized as Homogenous

6. When goods are characterized as homogeneous, typical cases in which the effect may be substantially to restrain competition are, for example, when the company group raises the prices of the goods unilaterally, competitors cannot increase the amount of production or sales due to their small production or sales capacity, and therefore, users may be unable to switch suppliers to the other competitors.

2. When Goods Are Characterized as Differentiated

7. When goods are characterized as differentiated by brand, etc., if the price of the goods of one brand is increased, the users of the brand do not necessarily intend to buy the goods of other brands

1 http://www.jftc.go.jp/e-page/legislation/ama/RevisedMergerGuidelines.pdf

2 "The company group" refers to all companies that would form, maintain, and strengthen the joint relationships by the business combination.

indiscriminately as a substitute, but may buy goods of another brand that has higher substitutability. When goods are differentiated, typical cases in which the effect may be substantially to restrain competition are, for example, when business combinations are formed between business operators that sell substitutable brand goods and competitors do not sell such goods that are substitutable with those of the company group.

8. In particular, when goods are differentiated, if there is a case in which business combinations are formed between business operators that sell substitutable goods while competitors do not sell such substitutable goods, the company group can offset the loss of sales of one of the goods by its price increase with the gain of sales of the other substitutable good after the business combination would be offset by the gain of sales of the other substitutable good after the business combination. As a result, the company group will be able to raise the price of goods without an overall reduction in group sales, and so this business combination will have a large impact on competition even if the market share or ranking of the company group is not so high. Therefore, it is essential for the analysis of the anticompetitive effect of a business combination to consider whether goods are differentiated or not.

9. In deciding whether the effects of business combinations may be substantially to restrain competition through unilateral conduct, the following determining factors are given comprehensive consideration:

(1) The Position of the Company Group and the Competitive Situation

- i). Market Share and Ranking
- ii). Competition among the Parties in the Past
- iii). Market Share Differences from Competitors
- iv). Competitors' Excess Capacity and Degree of Differentiation

(2) Import

(3) Entry

(4) Competitive Pressure from Related Markets

(5) Competitive Pressure from Users

(6) Overall Business Capabilities

(7) Efficiency

(8) Financial Conditions of the Company Group

10. In deciding whether the effect of business combinations may be substantially to restrain competition through the coordinated conduct, the following determining factors are given comprehensive consideration:

(1) The Position of the Company Group and the Competitive Situation

- i). Number of Competitors
- ii). Competition among the Parties in the Past

iii). Excess Capacity of Competitors

(1) Trade Realities

i). Conditions of Trade

ii). Trends in Demand, Technological Innovation

iii). Past Competitive Situation

(1) Import

(2) Entry

(3) Competitive Pressure from Related Markets, etc.

(4) Efficiency

(5) Financial Conditions of the Company Group

3. A hypothetical case – A bank merger

11. As explained in paragraphs 1 and 4 above, in Japan, any business combinations are prohibited if "the effect may be substantially to restrain competition in a particular field of trade" (the so-called "substantive test"). Whether business combinations might raise competition problems should be considered in respect of two viewpoints: through unilateral conduct by the company group and through coordinated conduct between the company group and one or more of its competitors.

12. As described below, the JFTC would review the hypothetical merger along with the Guidelines and analyze whether or not it may be substantially to restrain competition in any particular field of trade in light of the substantive test under the AMA.

13. With respect to the business activities of the company group, the JFTC defines the product range or geographic range that are the subjects of a particular field of trade, in principle, from the perspective of substitutability for users[3], and then determines whether the effect of a business combination may be substantially to restrain competition in a defined particular field of trade.

14. Market share is mainly used for the following purposes: (a) for calculating the HHI (Herfindahl-Herschmann Index) to decide whether it is normally considered that the effect of a horizontal business combination may not be substantially to restrain competition (safe harbor) and (b) for using it as one of the determining factors for considering the effect of the merger from perspectives of unilateral conduct and coordinated conduct (when failing to fulfill the safe harbor).

15. The safe harbor of a horizontal business combination is determined by a combination of the HHI after the business combination and the increment of the HHI. When the business combination falls under either of the following standards (a) to (c) below, it is normally considered that the effect of a horizontal business combination may not be substantially to restrain competition in a particular field of trade:

(a). The HHI after the business combination is not more than 1,500.

[3] The JFTC adopts the so-called Hypothetical Monopolist Test in considering substitutability for users. Further, when necessary, substitutability for suppliers is also considered.

(b). The HHI after the business combination is more than 1,500 but not more than 2,500, while the increment of the HHI is not more than 250.

(c). The HHI after the business combination is more than 2,500, while the increment of the HHI is not more than 150.

16. Based on the relevant markets and market shares indicated on the table, as the HHI after the business combination in any retail bank market would be at least over 1500[4] and the increment of the HHI would be more than 250[5], the hypothetical case would not fall under the safe harbor. Therefore, the JFTC would determine the effect from the perspectives of unilateral conduct by the company group and through coordinated conduct between the company group and one or more of its competitors by comprehensively taking into consideration all relevant determining factors described in 4 and 5 above. The market share is a critical factor in considering the position of the company group and the competitors' situation. However, as described in 3 above, the impact on competition depends on whether goods are homogenous or differentiated in the particular field of trade.

17. It is difficult to determine for sure whether this hypothetical merger will have anticompetitive effects or not with the limited information provided. However, given the highly concentrated market structure with the Big Five banks, the hypothetical merger can be analyzed in terms of the following viewpoints, for example, as explained below: (a) Regarding the market share, Bank One has consistently remained the market leader of the relevant market. Though the new bank (BOC+BOI) could be the leader in the field of short-term credit for SMEs, Bank One would remain as a strong competitor anyway, (b) BOI which has the reputation of a "maverick" would be acquired.

(a). Market Share

i). Analysis from the perspective of unilateral conduct

When the difference of the combined market share of the company group from the market shares of competitors is large, it is more difficult for the competitors to maintain a sufficient supply of goods at the same price in place of the company group, in response to the company group's attempt to raise the price. The ability of the competitors to constrain the company group's price rise is therefore weaker. On the other hand, if there are competitors with market shares equal to or greater than those of the company group even after the business combination, these competitors could be factors that prevent the company group from controlling the price and other factors to a certain extent. (It should be mentioned that, in considering the market share differences from the competitors, the excess capacity of competitors and the degree of substitutability between goods sold by the company group and those by the competitors are considered.)

4 Based on the provided market share information, the HHI in retail banking services to personal consumers after the business combination would be at least 1989 ($=30^2+33^2$) and the HHI in retail banking services to SMEs would be at least 2125 ($=35^2+30^2$).

5 The increment of the HHI derived from a business combination can be calculated by doubling the multiplied value of each market share of the company group.

In the retail banking market to personal consumers: the BOC share (before combination)×the BOI share (before combination)$\times 2 = 20\times 10\times 2 = 400$.

In the retail market to SMEs: the BOC share (before combination)×the BOI share (before combination)$\times 2 = 25\times 10\times 2 = 500$.

ii). Analysis from the perspective of coordinated conduct

On the other hand, regarding the analysis of coordinated conduct, when there are few competitors or the market share is concentrated on a few leading business operators, the behavior of the competitors can be forecast with high probability. In this hypothetical case review, if Bank One, as the competitor, does not have any particular limitation of its ability from the perspectives of excess capacity and the substitutability for the products of the new bank, the perspective of coordinated effect[6] would be more emphasized than that of unilateral conduct in the review of the hypothetical case, as the market structure will become more oligopolistic.

(b). "Maverick"

The existence of a maverick is generally regarded as a deterrence factor to coordinated conduct among competitors in the market. In analyzing coordinated conduct, the JFTC considers competition among the parties in the past relating to cases where the parties have been competing for market share or one of these parties has been aggressive in cutting prices[7]. In this hypothetical case review, the impact on competition of the acquisition of the BOI by the BOC is considered by taking into consideration information like how the BOC has behaved in the market competition in the past.

In addition, as explained in paragraphs 9 and 10 above, factors such as the possibility of potential new entries are also considered in the review from the perspectives of unilateral conduct and coordinated conduct.

6 See paragraph 10 above. Generally speaking, competitors can more easily forecast each other's behavior and more easily take coordinated conduct in cases where there are few competitors, the market share is concentrated on a few leading business operators, the companies sell homogeneous goods, competitors have similar cost conditions or conditions of trade in the market are highly transparent.

7 In cases where the parties have been competing for market share or one of these parties has been aggressive in cutting prices, the fact that the parties have competed vigorously or the fact that their conduct in the market has stimulated competition may be deemed to contribute to a reduction in prices, an improvement in quality or an extension of the range of goods throughout the market. If the business combination eliminates these conditions, it will have a serious impact on competition, even if the combined market share or the rank of the parties is not high. (Part Ⅳ-3 (1) B. Competition among the Parties in the Past, etc. of the Guidelines.)