# COMMENT AND ANALYSIS

## CONVERGENCE AND THE REGULATION OF TELEPHONE AND CABLE TELEVISION COMPANIES

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Advances in the technology used to deliver telecommunications and broadcasting services have given rise to a number of issues hotly debated by relevant government departments, regulators and industry participants. A number of studies and reports on related questions have been written. Yet another task force has been formed by the federal Department of Communications this fall to study the issues further and report on some of the implications of the introduction of new technology in telecommunications and cable television networks in Canada.

The effect of changing technology on telecommunications and cable networks is usually characterized as convergence. "Convergence" is a term widely used to refer to a coming together, a blurring driven by technology, of the boundaries between telecommunications and broadcasting. "Technical convergence" refers to the development of distribution methods common to both telecommunications companies, whose core or basic business has traditionally been the point-to-point switched transmission by copper wire of voice and data, and cable television companies, whose core business has traditionally been the point-to-multipoint distribution of video programming by coaxial cable, with the result that most communications can be carried on a common technology, principally a single strand of optical fibre. "Service convergence" refers to the delivery of similar services, either new or traditionally delivered by one industry or the other, by both the telecommunications and broadcasting industries.

Convergence, or the potential provision of common services by telephone companies and cable companies, appears to have pitted the two industries against one another in a race against time, during which each player tries to protect his own monopoly core market while being suspected of poising himself to invade the traditional core market of the other player.

Although the underlying technical distribution backbone used for signal transmission will fast become common to both telephone companies and cable companies in the 1990s, making it increasingly technically possible for each industry to deliver the same services, it is widely expected that service convergence will remain limited until well into the twenty-first century. In other words, the effect of changing technology on the physical networks of telephone companies and cable companies in the 1990s will likely far exceed the impact such changes will have in the same timeframe upon the common delivery of services by them.

A number of factors are likely to impede service convergence and the full deployment of new technologies as they become available. These include:

- the fundamental differences in the network architecture or topology currently used by telephone companies and cable companies respectively, and the limitations that flow from them;
- the fact that existing cable subscriber receiving equipment and the terminal equipment used for the transmission and reception of telephone and telephone-related services are optimized for existing means of signal delivery;

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- the need for further advances in broadband switching technology before telephone companies can provide switched video services;
- the need for further developments in other areas of technology, including microcellular technology, and in the telecommunications market structure, specifically long-distance telephone service competition, before cable networks can be used effectively to transport residential switched signals;
- the market and cost barriers to the full deployment of new technologies as they are developed; and
- the public policy, legislative and regulatory environment in which telephone companies and cable companies still operate.

This article will focus on the extent to which the legislative and regulatory structures now in place in Canada may exacerbate the barriers to the timely and cost-effective deployment of new telecommunications technology, and the likelihood that such structures will be affected by the increased deployment of new technologies.

**The Federal Regulation of Telephone and Cable Companies**

Historically, the regulatory context in which telephone companies and cable companies have developed has been one of legislated divergence. The two industries have been regulated separately, under different enabling legislation, and in accordance with different policy objectives. The two industries have been assigned different mandates and each has been allowed to fulfil that mandate on a monopoly basis in the territory served. Any synergy, and even cooperation, between telephone companies and cable companies has been discouraged by legislation and by regulation.

One obvious difference between most telephone companies and cable companies operating in any given market is their relative size and financial importance. While there is one major telephone company in each province, there are close to two thousand cable companies in Canada, ranging from single-proprietor operations with a few hundred subscribers to comparatively large and complex vertically integrated corporations with multiple cable operations licensed to serve many parts of the country. However, it should be noted that the ten largest cable companies in Canada currently account for approximately two-thirds of the cable market.

Canadian telephone companies under federal jurisdiction have been regulated substantively under the *Railway Act* on the basis of a framework developed at the turn of the twentieth century for transportation. In fact, telephone companies under federal jurisdiction were regulated until 1976 by the Canadian Transport Commission (now the National Transportation Agency). The pillars of this framework have been, and remain, the setting of just and reasonable rates for the carriage of personal information, non-discriminatory universal access to the transmission network of telephone companies and control of monopoly power.

Federal jurisdiction for the regulation of telephone companies was transferred in 1976 from the Canadian Transport Commission to the Canadian Radio-television and Telecommunications Commission (CRTC), the federal agency responsible for the regulation of broadcasting undertakings, including cable companies. The CRTC currently regulates the telephone companies representing approximately 79 per cent of the revenues generated by telephone and related services in Canada.

Rigorous regulation of rates on the basis of an allowed rate of return and a determined rate base has been the central feature of the federal regulatory régime applied to telephone companies. Rates for long-distance services have been established historically at a level which allows them to contribute to the cost of providing local telephone access and to further thereby the principle of universal accessibility to basic telephone service at affordable prices.

More recently, cost separation and accounting safeguards have also been developed as regulatory adjuncts to rate-setting procedures, especially as telephone companies have increasingly offered some services on a competitive basis. A separate construction program review process has been instituted by the CRTC to review the reasonableness of the capital programs and the capital requirement forecasts

of telephone companies. Extensive reporting requirements and the ongoing monitoring of intercorporate transactions between the telephone companies and their subsidiaries, affiliates or associated companies have also permitted the CRTC to oversee and rule on the reasonableness of all significant intercorporate transfers to protect monopoly subscribers from cross-subsidies.

Although only one telephone company, Bell Canada, is subject to an express statutory provision requiring it to act solely as a common carrier, and prohibiting it from controlling or influencing the messages it transmits, the telephone industry has generally been regulated on the basis of its carriage function, and indeed on the basis of a separation between content and carriage.

The cable industry, on the other hand, was made an integral part of broadcasting under the *Broadcasting Act* of 1968 which established federal jurisdiction over all broadcasting undertakings. "Broadcasting" was defined in that *Act* as radiocommunication intended for the general public, and "radiocommunication" was defined in turn as transmission by Hertzian waves. Cable companies have been licensed, pursuant to the *Broadcasting Act* of 1968, as broadcasting receiving undertakings. As such, they have been expected to participate in the achievement of statutory objectives concerned with the transmission of mass media communications whose overall content was deemed capable of furthering broadly stated, largely cultural goals.

Although developed initially as a means of retransmitting broadcast programming produced and/or transmitted by over-the-air broadcasters, cable companies were required, early in their development, to originate some local programming for the communities they served. Even with the addition to their offerings of so-called non-programming services, including alphanumeric or videotext services and surveillance and security services, cable companies continued to be characterized as part of the overall broadcasting industry, rather than by reference to their basic carriage function.

Cable companies are price-regulated but they have not been subject to anything near the formal rate-setting regulatory regime governing the telephone companies. Nor have they been subject to well defined or closely applied cost separation and accounting requirements between monopoly and non-programming services, despite their offering of some of the latter services in competition with other providers, mainly the telephone companies.

Entry into and continued participation in the broadcasting industry, including the cable industry, have been controlled through a licensing process. Under the provisions of the *Broadcasting Act*, no person can carry on a broadcasting undertaking, including a cable undertaking, without a valid and subsisting licence issued by the Commission, unless the class of undertaking concerned is exempted from licensing requirements. The CRTC is empowered to issue broadcasting licences for a maximum number of years, at the end of which time the licensee may be subject to a performance review which may result in the licence being renewed on the same terms and conditions as initially issued, or on different terms and conditions.

The *Broadcasting Act* conferred on the CRTC the power to attach to any broadcasting licence conditions which are specific to the licence holder. The CRTC was also authorized by the *Act* to make generally applicable regulations, currently the *Cable Television Regulations, 1986* in the case of cable television licensees. These two regulatory mechanisms have been used, either singly or jointly, *inter alia*, to require prior Commission approval of the rates charged by cable companies for service, to impose certain plant ownership requirements on cable companies, to establish the priority to be given to the services available for carriage by cable companies, to require signal substitution, and to require Commission approval for transfers of ownership and control of cable undertakings, a further mechanism used to control entry into the cable industry.

The transfer of federal jurisdiction over telephone companies to the CRTC in 1976 had little, if any, impact on the established divergent approaches to the regulation of the telephone and cable industries. Although the two industries were henceforth to share one single regulator, the provisions of the *Railway Act* and the regulatory mechanisms developed under it continued, unchanged, to govern telephone companies, while the provisions of the *Broadcasting Act* and the regulations made under it governed

cable companies. Jurisdiction over telephone companies and cable companies has continued to be exercised, not only pursuant to different legislative instruments, but in accordance with different rules of procedure, and with the assistance of two very separate staffs within the same regulatory agency.

**The New Broadcasting Act**

In June 1991, a completely reformulated *Broadcasting Act* was proclaimed in force, leaving in place the fundamental licensing and regulatory approaches applicable to cable companies.

A notable change in the government's approach to broadcasting in the new *Broadcasting Act* is its redefinition of "broadcasting", on which rests Parliament's assertion of federal jurisdiction over programming services. Such jurisdiction had been upheld in the past, with regard to cable undertakings whose physical plants do not extend beyond one province, by reference to the fact that cable headends receive and retransmit radio signals, a matter under federal jurisdiction. In the new *Act*, "broadcasting" is defined, not by reference to the means of transmission, but by reference to what is transmitted. It is defined as the transmission of programs by any means of telecommunication for reception by the public, unless the transmission is solely for display in a public place. "Program" is defined in turn as sounds or visual images, or a combination thereof, intended to inform, enlighten or entertain, excluding visual images, whether or not combined with sounds, that consist predominantly of alphanumeric text. "Alphanumeric text" is not defined.

The new *Broadcasting Act* characterizes cable companies as "distribution undertakings" whose mandate is the reception of broadcasting (i.e., "programs" as defined), and the retransmission thereof, by radio waves or other means of telecommunication, to more than one dwelling or to another distribution undertaking. The new *Broadcasting Act* nevertheless expressly recognizes that distribution undertakings may originate programming under certain circumstances.

Under the new *Broadcasting Act*, the programming and non-programming functions of distribution undertakings are clearly distinguished one from the other. The non-programming function is excluded from the definition of broadcasting. Jurisdiction is thus asserted only with regard to the distribution of programming services, allowing the cable distribution of non-broadcasting (i.e., non-programming) services without a licence and without regulatory control. However, the *Act* expressly authorizes the Commission to require a distribution undertaking to give priority to the carriage of broadcasting, i.e., programming services.

It could be said that the revised *Broadcasting Act* contemplates a certain degree of technical convergence. A paragraph in the section enunciating a broadcasting policy for Canada expressly recognizes the need for distribution undertakings to provide efficient delivery of programming at affordable rates, using the most effective technologies available. A provision in the section setting out the objects and powers of the CRTC in relation to broadcasting exhorts the Commission to regulate the broadcasting system in a flexible manner which is readily adaptable to scientific and technological change and does not inhibit the development of information technologies and their application, or the delivery of resultant services to Canadians. Another provision expressly empowers the CRTC, in furtherance of its objects, to require any licensee to obtain Commission approval before entering into any contract with a telecommunications common carrier for the distribution of programming directly to the public, using the facilities of that common carrier. Moreover, a consequential amendment of the provisions of the *Railway Act* makes it possible for telephone companies to discriminate, or to accord a preference or advantage within the meaning of the *Railway Act*, with respect to the transmission of programs to the public through their facilities, whether alone or in conjunction with facilities owned by a cable company, if the CRTC is satisfied that the discrimination, preference or advantage will further the implementation of the broadcasting policy set out in the *Broadcasting Act*.

It may be argued that the new *Broadcasting Act* also opens the door for some service convergence. The *Act* makes a consequential amendment to the *Railway Act* in a manner that suggests the possibility

of a telephone company holding a broadcasting licence, by providing that a telephone company is not subject to tariff regulation under the *Railway Act* in respect of the tolls it charges subscribers for the delivery of broadcasting pursuant to a broadcasting licence. It has been argued that the *Act* may thereby recognize implicitly that a telephone company (except Bell Canada) may also be a broadcasting licensee.

Despite these possible openings, the new *Broadcasting Act* perpetuates the inclusion of the cable industry as part of the broadcasting system and generally reaffirms the historical divergence, from a legislative and regulatory perspective, between telephone companies and cable licensees.

**Legislative and Regulatory Impediments to Convergence**

The major legislative and regulatory impediments to convergence have been identified by the telephone companies. They involve cable plant ownership rules, restrictions on use by telephone companies of unused portions of facilities leased by them to cable companies, the principle of separation of control over carriage and content applied to telephone companies and limitations on the licensing of telephone companies as broadcasters.

Telephone companies have also expressed concern that the continued inclusion of the cable industry as part of the broadcasting system results in an unfair discrepancy in the level and type of regulation applied to two industries moving increasingly toward the delivery of similar services.

Out of concern that cable licensees be in a position to respond directly to subscribers and to exercise the control over their cable undertakings necessary to meet their regulatory obligations under the *Broadcasting Act*, and in order to guarantee the cable industry reasonable security of tenure through the ownership of its principal means of carrying on business, the Commission has required cable licensees to own and operate their basic network plant, with some exceptions, especially where the telephone company in the market concerned is not under its jurisdiction. Specifically, cable licensees have been required to own their local headend, amplifiers and subscriber drops. Cable companies have also been prohibited by regulation from using or permitting the use of their local headend, distribution system or subscriber drop for the distribution of programming services, except as required or authorized by their licence or the Cable Regulations.

Such a plant ownership requirement is seen by some telephone companies as a serious impediment to convergence as it discourages any joint strategic planning or cooperative and cost-effective approaches in the deployment of emerging technologies.

Cable companies have traditionally shared support structures with telephone companies, and have leased some facilities from telephone companies for signal transmission pursuant to approved tariffs. A restriction referred to as the "scope clause" has prevented telephone companies, for example Bell Canada, from imposing restrictions on the use of the transmission facilities they provide to cable companies. Bandwidth, rather than the full-frequency spectrum available in a facility furnished by the telephone company, cannot be leased to a cable company with the telephone company reserving the right to use any unused portion. Joint approaches by the two industries have thereby been discouraged further in a major part of the Canadian market.

The principle of the separation of content and carriage is enshrined, as noted earlier, in a provision of the *Bell Canada Act* with regard to Bell. The Commission has already relied in part on this provision to impose restrictions on Bell's ability to initiate or offer certain enhanced services, for example the provision of Yellow Pages directories in machine-readable form.

Although there is no statutory provision restricting other telephone companies to carriage, the general principle of the separation of content and carriage has been applied by the Commission to other telephone companies, for example, in a 1984 CRTC decision establishing the rules governing the provision of enhanced services. The CRTC considered in that decision that the principle should apply

to other telephone companies since their participation in the electronic publishing and database markets would, in the Commission's view, prejudice diversified development.

The principle of the separation of content and carriage is not known to the cable industry, whose role as an originator of programming has been encouraged and is expressly recognized. Cable operators are also free, as noted, to initiate and/or distribute non-programming services.

A prohibition in the *Bell Canada Act* stipulates that neither Bell, nor any person controlled directly or indirectly by Bell, may hold a licence issued under the *Broadcasting Act* or carry on a broadcasting undertaking within the meaning of that *Act*. A direction issued by Cabinet which establishes agents of Her Majesty in right of any province, except in certain limited circumstances, as a class of persons ineligible to hold broadcasting licences, has the effect of prohibiting the issuance of a broadcasting licence to Manitoba Telephone or Saskatchewan Telecommunications.

There is no express statutory prohibition against telephone companies other than Bell Canada holding broadcasting licences. However, the CRTC has more than once expressed its belief that it would not be in the public interest to encourage common carriers to hold cable licences. In May 1988, a draft Cabinet Directive to be issued pursuant to the *Broadcasting Act* was made public. It proposed to prohibit the CRTC from granting a licence to any company providing local telephone service, including cellular telephone service. Although no Order-in-Council confirmed the Directive, the draft may be considered indicative of a continued reluctance on the part of the government to allow telecommunications carriers to participate in the provision of broadcasting services. Interestingly, one year later, the Department of Communications invited comments on issues surrounding the development of local distribution telecommunications networks with the deployment of new technologies, stating that the Department was in favour of a competitive environment for locally distributed services with regard to both carriage and services, and concluding that the Department was also supportive of local duopolies for this competitive service provisioning.

**Some New Developments in the Telephone and Cable Industries**

Technical convergence is already a reality. Service convergence is just around the corner and, to a certain extent, is here already in specific niches of the telecommunications business market.

Due to the broadband nature of their network, cable companies are well positioned to offer point-to-point transmission of high-speed data communications and interactive consumer information services. Large cable operators, especially in urban areas, can maximize the utilization of their network by using for profit excess capacity for the provision of some telephone-type services as a logical extension of the delivery of television programming services. They can thereby rationalize the increased use of fibre in their plant to optimize its general performance and efficiency. The incremental revenue source generated can serve to underwrite in part the cost of network modernization.

Increasingly, leading edge cable operators in Toronto, Vancouver, Montréal and Québec City offer telecommunications services to business customers. At present, these services consist mainly of making circuits available for local interconnection between businesses and large computing facilities, as well as for intercity private-line service. These offerings now account for a modest proportion of the cable business, but the participation of large cable operators as alternative suppliers of some private-line telecommunications service to high-volume users, in competition with telephone companies, is expected to grow in importance as more fibre is deployed in the cable network and as cable companies make alliances with computer technology providers.

There is little doubt that the changing fibre-based architecture of cable networks will increasingly allow some cable companies to share with telephone companies the growing enhanced consumer information and business telecommunications market. Moreover, the deployment of microcellular technology and the introduction of personal communications network (PCN) technology may provide opportunities for bypassing the local telephone network for the provision of residential voice service in

selected markets, under a scenario where long-distance competition is permitted or mandatory local interconnection of new providers with established telecommunications carriers is introduced. PCN technology can eventually provide an alternative to conventional switched telephone service and create for the cable industry an opportunity to carry voice traffic on their local networks in association with a long-distance provider competing with a telephone company.

Competition between telephone companies and cable companies in the delivery of local voice service in some markets may actually become a technically and economically feasible scenario by the end of this decade. The relationship between Rogers Cable TV and Unitel, for example, suggests that by the end of the decade, should Unitel be authorized to offer long-distance service, there may exist an incentive to bypass the local telephone network in order to minimize the required contribution to local service and to reduce Unitel reliance on local telephone facilities. Interconnection arrangements between cable companies and a telecommunications carrier competing with a telephone company in the provision of long-distance service may make good business sense, as the transportation of local voice signals could prove to be an additional income source for cable companies.

Interactive services such as video-on-demand and personalized services nevertheless continue to present a challenge to coaxial cable technology, since they require two-way capability and switching technology and since, unlike the architecture of telephone companies, the tree-and-branch architecture of cable companies is ill-suited to this application. This limitation is a source of concern for cable companies, especially in light of the impending U.S.-based high-power Direct Broadcast Satellite (DBS) programming services delivered directly to the home. DBS is widely perceived by the Canadian cable industry as a major threat since it has the potential of eroding cable subscriber penetration unless cable companies are in a position to improve the quantity and quality of the channels available on their systems. However, with improvements in coaxial cable technology, the deployment of fibre in cable networks and advances in digital transmission and compression technology in the next decade, cable operators may be in a position to offer near video-on-demand, as well as other interactive television services, without reliance on switched video capability.

Telephone companies, for their part, continue to upgrade the technology used in their networks. They now see an emerging need for higher bandwidth networks capable of transporting large quantities of information, including image, video, data and voice, within the same network. Under this vision, both narrowband and broadband services would be provided on an integrated basis.

Developments in digital video switching technology and the replacement of copper plant with fibre will eventually lead to the elimination of the existing bandwidth limitation in telecommunications networks, making it possible for telephone companies to provide switched broadband video services involving more direct and personalized transactions between viewers and service providers. True service convergence will then be possible, with the telephone companies entering the home video entertainment market in competition with cable companies, barring regulatory impediments.

It is commonly believed, however, that the full deployment of fibre in the local telephone networks as the platform for integrated broadband services delivery will not be possible without significant new revenue sources. It is also felt that only the delivery of interactive entertainment broadband video services, some of which are only conceptually defined and others which are yet to be invented or identified, is likely to generate a sufficiently broad-based consumer demand to produce the incremental revenues required to deploy fibre to the home.

### Pressure for New Regulatory Approaches

Immediate regulatory implications are expected to flow from limited forms of convergence throughout the decade, including service convergence in the private-line business market and possible convergence in the delivery of switched voice traffic later in the decade. The possibility of full-service convergence through telephone company video delivery capability in the post-2000 timeframe may also

require regulatory attention in the immediate future, considering the potential impact of regulatory policy on current telephone company and cable company planning and deployment strategies.

As noted, there are no statutory or regulatory restrictions to cable company entry into the local telecommunications services market. Cable licensees are free to develop the infrastructure required for the purpose, since they are regulated pursuant to the new *Broadcasting Act* with regard only to the use of their equipment and facilities for the distribution of programming services. At the same time, until they offer basic voice telephone service, cable companies do not readily fall within the definition of a "company" within CRTC jurisdiction pursuant to the *Railway Act*.

The result, the telephone companies have argued, is that the cable companies can provide telecommunications services in competition with them without the regulatory oversight applied to telephone companies with regard to tariff filings, cost separation, cross-subsidy tests, capital program revenues, network access rules and contribution requirements—in fact with little or no regulatory oversight. Bell Canada has asked the CRTC, in a proceeding it has yet to rule on, to regulate pursuant to the *Railway Act* certain activities conducted by Rogers Network Services, a division of Rogers Cable TV. Bell Canada has also argued before the Commission, unsuccessfully, that certain capital expenditures to be recovered in the rates charged to cable subscribers for cable services were actually expenditures related to the upgrading of the cable network, not for the purpose of the provision of programming but for the purpose of providing telecommunications services.

Another source of concern centres on the fact that, while telephone companies are subject to non-discriminatory statutory requirements with regard to access to their facilities for the delivery of services, "must-carry" rules do not affect the non-programming offerings of cable companies. Cable companies are thus in a position, it can be argued, to inhibit the development of non-programming services by unrelated service providers by limiting access to their distribution systems.

By contrast, the provision of broadcast programming by telephone companies would require a licence pursuant to the *Broadcasting Act*. Not only are there statutory and policy barriers to telephone company entry into programming delivery, such as a prohibition against telephone companies holding a broadcasting licence and the application of the principle of separation of content and carriage that preclude telephone company participation in the delivery of broadcast services; it is also arguable that, given the broad definition of broadcasting under the new *Broadcasting Act*, services which would normally be provided by telephone companies may be captured as broadcasting or programming services, thereby impeding the development and introduction by the telephone companies of new and innovative offerings using emerging technologies.

Not only telephone companies, but also service providers and consumers of monopoly cable services may press for equal and consistent regulation where the provision of telecommunications services is concerned, without regard to the technological means used to deliver similar services or to the statutory classification of the carrier. There may be increasing demand, for example, for more rigorous cost separation and accounting mechanisms, as well as for the close monitoring of intercorporate transactions where cable companies are involved in the provision of both monopoly and competitive services. Certain parts of the regulatory framework, and some of the regulatory instruments developed under it, will require reexamination as service convergence develops further, and as technological barriers between cable companies and telephone companies are gradually eroded.

It is generally expected that for some time to come the networks of the telephone and cable companies will continue to develop largely in accordance with the business imperatives of the core activities of each industry, with each industry deploying new technology in its respective network at the same time as the other. This network duplication may not be the best option in areas where cooperation or joint ventures between telephone companies and cable companies make economic sense, and where the inability to cooperate may delay or preclude the introduction of emerging technologies.

It has been argued that the cable plant ownership regulatory requirements and other constraints now in place will encourage the continued development of two completely separate local networks. Joint efforts, common planning, cooperative ventures, business arrangements or strategic alliances between telephone companies and cable companies for the building, expansion and upgrading of local network infrastructures may be discouraged or precluded, even where these alternatives may make economic sense. Such constraints may be an important factor in inhibiting the penetration of new technologies and the development and promotion of innovative new services in some areas of Canada where economies of scale may be required for cost-effective deployment.

There may be compelling reasons to allow network convergence in smaller communities, where cable operators may not be in a position to justify the costs of deploying new technologies unless a certain degree of integration of local telephone company and cable company facilities is encouraged. As noted, the deployment of such technologies may be a crucial defensive strategy in countering the DBS threat. There are fewer opportunities available in more sparsely populated and rural areas to tap an incremental non-programming services business market and to benefit from economies of scale. In those markets, the sharing of one unified upgraded infrastructure by multiple distribution systems may be the only cost-effective way to modernize the network, expand cable service to unserved areas and deliver a full range of video and other services to subscribers.

Even where large cable companies are concerned, a more appropriate policy framework may be to recognize the wisdom of facilitating some degree of network convergence for broadband distribution. This may avoid untimely and duplicative investment. As the telecommunications environment is increasingly shaped by market forces, commercial accommodation between telephone companies and cable companies, and even the development of one major advanced local distribution network (possibly jointly owned), may have to be considered as a desirable cost-effective alternative in many parts of the country.

A single local infrastructure for the integrated delivery of telephone company and cable company services would obviously require a regulatory régime aimed at providing non-discriminatory access to service providers and ensuring that the monopoly network supplier does not abuse its privileged position. The costs of such regulation may nevertheless be lower than those associated with wasteful duplication in technology deployment and delays in the introduction of new services where joint efforts are necessary to achieve cost effectiveness.

It is a given that networks will continue to be modernized on the basis of expected cost effectiveness. Since broadband video services may be, in the long term, the only services capable of generating the incremental revenues required to justify the deployment of fibre to the home by telephone companies, regulatory barriers to telephone company entry into any part of this market may have the effect of inhibiting the upgrading of telephone network facilities in a timely fashion, and prohibiting it altogether in some areas. If interactive entertainment services such as video-on-demand continue to be included in the definition of broadcasting, their delivery to subscribers will require a broadcasting licence. Existing regulatory barriers to telephone company entry into this market may have a deleterious impact on telephone company planning and strategies for the upgrading of their local networks, due to the importance of this type of broadband video service in justifying the cost of fibre deployment.

Prudent investment in new technologies will require a prejudgment by the telephone companies of the future opportunities available to recoup the costs of their introduction. Rigid regulatory barriers to service convergence may therefore have an important impact on the economics of their deployment. For example, it is estimated that fibre to the home may not be warranted for telephone companies far into the next century if they are effectively precluded from any participation in developing and introducing new entertainment video technologies.

**Conclusion**

Technical convergence in telecommunications and broadcasting is here to stay. The deployment of optical fibre technology and other developing technologies is making it increasingly possible for either the telephone companies or the cable companies to provide to the public, through their respective networks, services traditionally provided by the other.

Some service convergence exists already. More is around the corner, although full service convergence will only materialize, it can be argued, when telephone company delivery of video programming is made possible. It is inevitable that service convergence, and the introduction of new applications and services made possible by technological innovations, will occur only to a limited degree, and in any event in nowhere near the same timeframe as technical convergence, unless certain elements in the established legislative and regulatory framework are carefully reviewed with a view to ensuring the flexibility necessary to take timely advantage of the opportunities made possible by technical convergence.

It is more than likely that service convergence and the full development of some new services such as switched video services will be impeded by the federal legislative and regulatory structures now in place, even absent technical, cost or market constraints. Such legislative and regulatory structures could retard technical convergence itself by exacerbating the cost and market barriers to the timely and cost-effective deployment of new technologies as they become available.

## NATIONAL INTERESTS AND THE NEW EEC MERGER REGULATION: THE CASE OF THE (POSSIBLE) TAKEOVER OF ICI BY HANSON INDUSTRIES

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The prospect of a hostile takeover bid for the U.K.'s largest manufacturing company by a controversial British conglomerate has brought home to many in the United Kingdom the realization that the European Community's new merger rules now govern the biggest and most significant takeovers in their economy.

This paper first reviews the terms of the European Community Merger Control Regulation[1] (the Regulation) which came into effect on September 21, 1990. The Regulation gives wide-ranging powers to the EEC Commission to review and, in appropriate cases, attach conditions to or veto large-scale mergers found to impact adversely on competition in the EEC market. After considering the early experience under the new merger rules and the circumstances of the initial investment by Hanson Industries (Hanson) in Imperial Chemical Industries (ICI), the Regulation's application to Hanson's possible bid for ICI will be studied. Then an assessment will be made of the legal grounds available to the United Kingdom government to investigate the takeover on public interest grounds that are not listed or otherwise authorized in the Regulation. Whether ICI could separately challenge a hostile bid by Hanson under the *Treaty of Rome* or the U.K. *Fair Trading Act* is the final question to be addressed.

Whatever the eventual outcome of the Hanson-ICI case, the incident has driven home dramatically the Regulation's emphasis on competition grounds for evaluating significant internal market mergers. The absence of broader national "public interest" tests concerns a number of Hanson's critics who argue that non-competition questions such as employment, regional development and R&D commitments are legitimate evaluation considerations for the host jurisdiction most directly affected by a "Community dimension" merger.

**The Advent of the EEC Merger Regulation**

Prior to the Regulation, the separate and complementary authority of the EEC Commission to regulate mergers was found in the general language of Articles 85 and 86 of the *Treaty of Rome* dealing with restraint of trade and abuse of dominant position situations, respectively.[2] In fact, Article 86 was relied upon only once in a manner accepted by the European Court of Justice (although the Commission decision itself was overturned by the Court on the facts), and many doubted that the Article 85 jurisdiction was adequate to deal with most takeover situations.[3] Neither provision provides a clear authority to the Commission for a system of prenotification or approval with or without conditions.

Although the Commission had first proposed a draft merger control regulation as far back as 1973, the momentum to adopt a separate regulation did not pick up in the Council until 1987 following the troubling precedent of the *Philip Morris* decision,[4] resulting in the December 1989 adoption of Merger Control Regulation 4064/89.[5]

**The Merger Wave in Anticipation of 1992**

The Regulation's adoption came amidst a rising number of cross-border mergers and corporate reorganizations in the Community, no doubt encouraged by the prospect of the dismantling of internal borders[6] in 1992. According to the most recent figures,[7] the number of mergers and acquisitions made by Europe's one thousand leading firms—either within a member state, across EC frontiers or internationally—jumped from 227 in 1986-87 to 492 in 1988-89. The size of these transactions has grown apace. In 1986-87, about seventy percent of the mergers involved firms with combined sales of over one billion ECUs (about $1.2 billion). By 1988-89, that figure had climbed over the ninety percent mark. By 1990, for the first time, there were more EC mergers than national mergers and twice as many acquisitions of EC companies by third-country firms as the previous year. Chemicals, food and drink, paper and printing were the most active merger sectors.[8]

**The EEC Commission's Authority over "Community Dimension" Mergers**

Under the *European Communities Act 1972*, the Regulation is now part of U.K. competition law. The Regulation specifically transferred the exclusive jurisdiction over subject mergers to the Commission.[9] This means that the Secretary of State for Trade and Industry, notwithstanding the earlier language of the *Fair Trading Act 1973*, generally is no longer able to refer a "Community dimension" merger to the U.K. Monopolies and Mergers Commission (MMC) for review.[10] The transaction instead must be vetted by the Mergers Task Force of the EEC Commission in Brussels. A separate question remains, however, as to whether the Secretary may still refer the same merger to the MMC for assessment on wider public interest grounds (i.e., of a non-competition character) than those found in the Regulation.

Under the Regulation, the Commission has the sole authority, subject to a few exceptions, to review and if necessary veto or attach conditions to any merger (called a "concentration") having a "Community dimension."[11] This refers to deals, expected to number between forty and fifty yearly, which involve firms with a combined turnover of more than five billion ECUs (about $7.2 billion) providing that at least 250 million ECUs (about $360 million) of at least two of the undertakings concerned are in the EEC. Article 5 sets out detailed rules for the calculation of turnover. The only exceptions to this rule are mergers involving companies that derive two-thirds of their business from the same EC state. These mergers are to be policed by the country's national merger authorities.[12]

The thresholds were initially set so high to give the Commission time to recruit appropriate staff and develop competence in the area before taking on a broader range of mergers.[13] In the first nine

(September 1990 to May 1991), the Mergers Task Force of the Commission reviewed some thirty proposed takeovers.[14] Given the first thresholds, this was about the expected caseload. The thresholds are to be reviewed in 1993 when the combined turnover figure threshold likely will be reduced to the level of two billion ECUs (as recommended by the Commission),[15] with a proportionate drop in the EEC market sales figure. Then about 150 "Community dimension" mergers are expected to be vetted annually in Brussels.[16]

### Market Compatibility Criteria

Article 2(1) directs the Commission to determine the compatibility of "Community dimension" mergers with the Common Market. The criterion is whether:

> a concentration ... creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it.

If the finding is in the affirmative, then the concentration may not proceed without the Commission's consent, which may be denied or given with conditions *per* Article 8. So long as the thresholds remain at their current levels, the Regulation is "likely to catch mainly conglomerate mergers—which are the kind least likely to restrict competition" except in the case of "a few overlapping products, in which the loss of competition between the parties might give cause for concern."[17] As we shall see, this appears to be the most likely prospect for the Hanson-ICI merger if a bid for control goes ahead.

Under Article 2(1), the assessment of whether a dominant position is created or strengthened requires the Commission to consider, among other things,

> (a) the need to preserve and develop effective competition within the common market in view, among other things, of the structure of all the markets concerned and the actual or potential competition from undertakings located either within or without the Community;
>
> (b) the market position of the undertakings concerned and their economic and financial power, the opportunities available to suppliers and users, their access to suppliers or markets, any legal or other barriers to entry, supply and demand trends for the relevant goods and services, the interests of the intermediate and ultimate consumers, and the development of technical and economic progress provided that it is to consumers advantage and does not form an obstacle to competition.

Except for the closing reference to "the development of technical and economic progress" (discussed below), the grounds for review in Article 2 are limited to competition reasons. Article 21 provides for several very limited situations where member states may take action to protect carefully defined non-competition interests and thereby override the market compatibility tests set out in Article 2. The scope of this "national interests" provision is also reviewed below. The general restriction to competition criteria in Article 2 was resisted by a number of member states but strongly urged by the U.K. government.[18]

In addition to provisions for prenotification and powers of search and investigation,[19] the Regulation requires the Commission to initiate formal review proceedings where compatibility concerns are identified. In these cases, the Commission must rule on the matter within four months, failing which the merger will be deemed to have been approved.[20] The Commission's Mergers Task Force may negotiate for spinoffs of overlapping lines of business or other steps to render the merged operations "compatible with the Common Market." Article 8(2) allows the Commission to attach conditions and obligations and "this less drastic remedy may encourage it to prohibit fewer mergers."

### The Initial Experience

The Commission's track record in its first nine months of working with the Regulation has confirmed this prognosis. By late May 1991, over thirty actual notifications had come before the Mergers Task Force (with a total staff of fifty) and a preliminary profile of case handling was starting to emerge. In the view of the *Financial Times*, "recent decisions have illustrated a desire to thrash out compromise solutions where it looks as though a deal can be done, to try out new ideas, and not to clog

up commercial transactions unnecessarily." Fiat's takeover of Ford's tractor subsidiary, for instance, was cleared when it relinquished some of its distributorship controls over its Italian dealers. In another case involving Fiat, the company reduced its stake in a large French battery producer and limited the number of its directors on its board to obtain approval for the Magneti-Marelli takeover. However, at this relatively early stage of operation, the Task Force has "yet to encounter a knotty merger problem"[21] and a definitive assessment of the Commission's administration of the Regulation would be premature at this time.

The question to address now is the effect of the Regulation on any possible bid for control of ICI by Hanson Industries which, all sides admit, would be a "Community dimension" merger or "concentration" as defined by Article 2 of the Regulation.

### The May 1991 Hanson Stake in ICI

Imperial Chemical Industries (ICI), the "pillar of Britain's industrial establishment,"[22] is the world's fourth largest chemical company and the country's biggest manufacturing firm, employing nearly half of its 130,000 employees at over thirty sites in the United Kingdom. Historically strong in bulk and petrochemicals, ICI expanded energetically in the 1980s into pharmaceuticals, paints and agrochemicals. Analysts estimate that it would cost some $22 billion to buy control of ICI and that its breakup value would be in excess of $28 billion. The company spends nearly $1.4 billion on research and development every year, with seventy percent of that in its U.K. operations. To many members of the public, ICI is the premier British company decisively influencing value-added exports, regional employment levels, R&D investments and home-grown technology advances.[23]

However, in 1990 ICI's pretax profits dropped by 36 per cent, reflecting a continuing downturn in bulk chemicals and several other product lines badly affected by the recession. By the end of last year, ICI directors had begun to consider several restructuring options, and in February 1991 they announced plans to focus on fewer activity areas, look for joint venture partners in some lines and shed the unpromising ones. The fertilizer business was closed. Up to ten thousand jobs were to be made redundant and more than $600 million was to be spent on the exercise. But actual details of the ICI reorganization were few and far between and the City waited. Share performance continued to be sluggish.[24]

The City was awaiting further news when, on May 14, 1991, Hanson Industries made a surprise bid in the open market for ICI shares, buying up just under three percent or twenty thousand shares for $400 million.[25] This made Hanson, a U.K.-based conglomerate, the second largest holder of ICI shares (behind Prudential Assurance, who is also the largest shareholder in Hanson), and immediately raised questions as to whether Hanson was taking a first step towards seeking a controlling interest in ICI.

Nearly 75 percent of ICI's shares are held by British pension and insurance funds. Hanson would only confirm that the purchase was "for investment purposes" and that it was "keeping its options open." That did not deter it, however, from suggesting that it knew how to cut over one billion dollars from ICI's costs and as a "friendly" bidder would consider buying good-value ICI selloffs or going into joint venture arrangements with ICI. Particular reference was made to a minority interest in the pharmaceuticals line, where analysts look for an ICI link-up with a well-financed co-venturer to retain competitiveness with stronger megafirms like Glaxo or Smithkline Beecham.[26]

### Looking at Hanson and ICI More Closely

One of the most visible and successful British firms over the past decade, Hanson has consistently outperformed the London market[27] by aggressively buying up underpriced companies on both sides of the Atlantic at less than their breakup value, then selling off marketable parts and running the

remaining units tightly. The managers of ICI's pension fund were sufficiently attracted by Hanson's growth record to become a sizeable shareholder in it. Another ICI connection occurred in 1986 when Hanson sold to ICI the Glidden Paints subsidiary of its newly purchased SCM Chemicals in the United States. The deal made ICI the biggest paint maker in the world and the Glidden unit has emerged as one of its best profit centres.[28]

Hanson's profit strategy is "driven by buying other firms" and according to City analysts, it has about $14 billion in cash available to buy out new targets.[29] Past experience suggests that Hanson tends to sell off over fifty percent of the assets of companies it buys,[30] a prospect seized upon in one academic study which predicted massive selloffs, the severe contraction of R&D investment and over fifteen thousand jobs at risk in a Hanson-controlled ICI (above and beyond the ten thousand jobs to be cut in the restructuring already announced by ICI).

The critics specifically warned of "the dangers of such a bid being considered by the EEC on purely competition grounds". Hanson's "financial engineering" style of management, in which "ever larger slabs of assets are unbundled and rebundled" is "likely to reduce employment and exports" as "productive operations are always subordinate to the requirements of dealing." ICI, its friends have noted, has performed as well as any of its European competitors in the face of a cyclical slump that has hurt its bulk chemical business.[31] In the context of the serious recession (accompanied by mounting job losses) presently afflicting Britain, these predictions have caused an unprecedented interest in how the merger control authorities in Brussels and Whitehall would review any Hanson takeover bid for ICI.[32]

For its part, ICI's management is not waiting to find out. Significant selloffs are already underway, and several joint ventures have been launched as part of a restructuring plan to concentrate on seven distinct product lines—drugs, paints, explosives, farm chemicals, materials, industrial chemicals and specialties.[33] In mid-June, ICI consolidated the backing of its five U.K. unions by extending the legal right to redundacy payments of up to $40,000 each to its 53,000 local workers.[34] Then ICI hived off control of its $12 billion pension fund to independent managers after pensioner representatives expressed fears that Hanson would go after the fund's $1 billion surplus as it had attempted to do in its earlier Imperial Tobacco and Courage Brewing takeovers.[35] Hanson's advisers have questioned the legal strength of the severance pay commitment and complained that ICI was "more interested in fighting a mythical bid than in improving shareholders' value."[36]

ICI then confirmed that it was preparing a $60 million claim against Hanson to cover pollution cleanup claims arising from its 1986 purchase of Glidden Paints from Hanson's U.S. subsidiary.[37] The timing of the news, according to ICI, was dictated by the limitation period in the purchase agreement, but the story served to remind potential investors that "environmental liabilities could pose a (costly) hurdle to Lord Hanson's designs on the chemical giant, ICI," citing the potential liabilities accruing to the new owners under present and forecast U.S., U.K. and EEC legislation.[38] It will be more difficult to break up a chemicals operation, they were reminded, where potential buyers always insist on lengthy investigations of potential environmental liabilities.

ICI's supporters fear that a corporate raider like Hanson is only interested in short-term profits and will decimate its R&D capacity and well-trained workforce, driving "another nail in the coffin of industrial Britain."[39] According to a former ICI chairman, a Hanson takeover would introduce such a "clash of philosophy and beliefs" that it is "difficult to see how either of the putative protagonists can gain by a misalliance."[40] ICI's basic strategy is to challenge Hanson's long-run ability to manage a large and complex technology-based group within a corporate culture that has allegedly stressed asset and tax manipulation over the sober, longer-run management of industrial assets. It is also inserting a "poison pill" clause in a new licensing agreement between the ICI pharmaceutical arm and a U.S. antibiotic producer to prevent new owners from inheriting the arrangement.[41] The practice is to be repeated in other licences and joint ventures currently under consideration.

Hanson has not been sitting on its hands during the phony war stage. Pro-Hanson observers have raised serious questions about the effectiveness of ICI's R&D claims,[42] the wisdom of ICI's defences on behalf of pensioners and employees and the timid, "nibbling" pace of ICI's restructuring program.[43] Vigorous defences have been mounted to counter accusations that Hanson is both an asset stripper and the consummate tax minimizer with neither the skills nor the experience to manage an enterprise like ICI. To the first charge, Hanson points to the fact that acquisitions have outpaced disposals since 1985.[44] On the question of tax games, the "more germane" issue, according to Hanson, is why ICI's tax rates are so much higher than Hanson's.[45] At the end of the day, Hanson's advisers predict, "pension fund managers (who hold 75 percent of ICI's shares) will show no sentimentality over ICI's fate." In the words of *The Economist*, "it is difficult to see what arguments could be marshalled to stop a Hanson bid if shareholders wished to sell."[46] But then came the news that "several prominent industrialists opposed in principle to the breakup of ICI" had instructed their pension fund managers to consult first with fund trustees for voting instructions in the event of a Hanson bid.

There is little doubt that the threat of a hostile bid by Hanson has accelerated the pace and size of ICI's reorganizational efforts. The management wants its institutional shareholders to hold on to their ICI shares. The slightly improved profit figures for the first half of 1991 may have made the company "less vulnerable to a hostile takeover bid from Hanson," but most City analysts seem to feel that a continuing Hanson presence is the necessary catalyst to force ICI to improve its shareholders' returns.[47]

Whether or not Hanson makes a move on ICI, the prospect of a bid prompts serious questions about how the new EEC Merger Regulation would apply to a Hanson bid in the face of opposition from current ICI management, the unions, many MPs and voters (a national election must be called by the spring of 1992). Will the bid be judged solely on competition/market compatibility grounds? Are there broader non-competition factors that could overturn Hanson's bid? If so, are these "national interests" limited to those enumerated in Article 21 of the Regulation or might they include those found in the U.K. *Fair Trading Act 1973*?

**The Control of "Community Dimension" Mergers: Applying the Regulation to a Hanson Bid for ICI**

*Prima facie*, any Hanson bid to buy ICI would create a "concentration with a Community dimension" within the scope of Article 1 of the Regulation, thereby making the takeover a notifiable merger subject to approval by the Commission. This result has been accepted by all interested parties including both managements, ICI's unions and the U.K. government. Hanson's initial stake in ICI was just under three percent of ICI's voting shares. By Article 2, a "concentration" will arise, *inter alia*, where the share purchases result in the transfer of "direct or indirect control" to the acquiring party. Article 3, in turn, defines "control" in terms of the "possibility of exercising decisive influence" on the "composition, voting or decisions" of the target firm. This means that the "decisive influence" threshold could fall below the control level of 51 percent, but how far below?

The Commission's recent interpretations only confirm that the threshold may be found at 39 percent in a friendly takeover where the next largest shareholder held under four percent.[48] Hanson's 2.8 percent holdings make it the second biggest shareholder of ICI, just below Prudential Assurance. Where, as here, shareholdings are widely held and any measureable increase in Hanson's ICI holdings would depend upon a premium price and a decision by a number of current institutional shareholders to favour a Hanson-directed management, the purchase of another 17 to 22 percent of ICI's shares by Hanson may be sufficient to constitute "decisive influence" under Article 3(3).[49] While the precise threshold figure may not be certain, the key point here is that the acquisition of a minority interest may be found to be a "concentration" under the Regulation.

ICI is no stranger to the EEC competition forum, having been a party to one of the biggest corporate fines in EEC history in 1990 for its part in the ICI-Solvay soda ash cartel case.[50] ICI is also familiar

with the Merger Regulation as a result of its acquisition of Cookson's fifty percent interest in Tioxide Group PLC, previously a fifty/fifty joint venture between ICI and Cookson.[51] In its ruling, the Commission held that the shift from shared to sole control amounted to a qualitative shift in ICI's "decisive influence" over Tioxide. As a result, the change from joint to individual control created a "concentration" under Articles 2 and 3(3).

If Hanson decides to make a bid for control of ICI, then the Commission must be notified within seven days of its announcement or the acquisition of a controlling interest, whichever occurs first. Following prenotification, the merger would automatically be suspended for three weeks[52] and the Commission would have a further four weeks to decide whether the merger was covered by the Regulation and whether there were serious doubts as to its compatibility with the Common Market.[53] Under Article 2, as has been seen, the merger must not create or strengthen a dominant position "as a result of which effective competition would be significantly impeded in the Common Market or in a substantial part of it". Only if the Commission determines, within the four-week period, that there are serious doubts as to its market compatibility, will proceedings be initiated. Failing that step, compatibility will be deemed and all parties, including the U.K. Office of Fair Trading, will be notified.[54]

The compatibility test in the Regulation is broader than the criterion found in Article 86 because "the mere creation of a dominant position which significantly impedes effective competition, as opposed to its abuse by a strengthening of that position, will be sufficent for a merger to be prohibited."[55]

The greatest antitrust danger for any takeover by a conglomerate (recall also that ICI itself is doing business in over five lines throughout the Community) is the strong possibility of "overlapping activities" between the buyer and the target company. According to comments by City analysts, this will certainly be a problem for ICI and Hanson in one product area, namely titanium dioxide, the white pigment in most plastics and paints.[56] If Hanson were to undertake to sell ICI's titanium dioxide business (or its own), then the most obvious condition for Brussels' approval would be satisfied. Whether there are available buyers is another question. Hanson's track record in breaking up and selling major parts of its prey infers that the subject has already been raised in its preliminary discussions with the Commission's mergers task force in Brussels.[57]

### The Consideration of Non-Competition Interests under Article 2

In measuring a proposed merger's compatibility with the Common Market, the Commission is required under Article 2 to take into account the need to "preserve and develop effective competition", the "market position" of the firms involved and "the development of technical and economic progress provided that it is to consumers' advantage and does not form an obstacle to competition." The meaning of the latter criterion is not entirely clear. It may open the door for the Commission to "balance alleged benefits against competition detriments"[58] and "consider matters such as the effect of a concentration on employment in assessing compatibility."[59] Recital 13 to the Regulation supports this wider interpretation in its direction to the Commission to measure compatibility within "the general framework of the achievement of the fundamental objectives referred to in Article 2, including that of strengthening the Community's economic and social cohesion, referred to in Article 130a."

The commission has suggested that Recital 13 could support a more liberal review of mergers in less developed parts of the Community where EEC industrial and social policies might outweigh competitive considerations in assessing the merger's compatibility. Thus, according to the Commission's statement to the Council explaining Recital 13, "account should be taken in particular of the competitiveness of undertakings located in regions which are greatly in need of restructuring owing, *inter alia*, to slow development."[60]

There is little evidence, however, that social and regional factors raised by Recital 13 would figure in any Commission review of a Hanson-ICI merger. The current Commissioner responsible for competition attaches little weight to such factors in assessing compatibility.[61] Informed sources within

the U.K. Department of Trade and Industry argue that the provision is "merely a reference to the need...to have regard to the state of technical development in the market as a whole."[62] Perhaps more importantly, the Recital 13 factors are intended for mergers which otherwise would be declared incompatible on the basis of their adverse effects on competition. On the basis of available evidence, this is not the case with any Hanson bid for ICI.

**The German Clause: Does Article 9 Fit?**

We should consider separately the application of the so-called "German clause," Article 9, to the Hanson-ICI case. The provision allows for member state review of a "Community dimension" merger where there is the possibility of dominant abuse in a discrete geographic market within the complaining member state. It does not matter whether the particular market comprises a substantial part of the Common Market. The discreteness of the market will be evident from its "sufficiently homogeneous" conditions of competition "which can be distinguished from neighbouring areas."[63]

In the event of the issue being raised and the Commission's acceptance that such a distinct market and threat exist, the Commission is free to deal with it on its own or to refer the case to the concerned member state for the application of its national competition law. Any steps taken by the member state, however, must be strictly limited to those necessary to safeguard or restore effective competition in the designated market. The provision has yet to be invoked in any "Community dimension" merger review. No suggestion has been made that Hanson-ICI raises the possibility of an Article 9 review request by any EEC member state, including the United Kingdom.

**The First Conclusion**

All of this suggests that while the size and complexity of any Hanson takeover of ICI would be a serious matter for investigation under the new Merger Regulation, the deal itself will not likely raise significant compatibility concerns for the Commission, provided Hanson gives an undertaking to resolve the very manageable question of any overlapping activities with its ICI acquisition.

**The Scope for a Separate U.K. Review of any Hanson Takeover Bid Under Article 21(3) of the Regulation**

But what of the U.K. merger authorities in this vetting exercise? Is there any role for national jurisdiction either under or separate from the EEC Merger Control Regulation? Why was ICI reportedly lobbying for the U.K. government to review immediately the anticipated bid by Hanson? Why have the unions representing ICI's employees urged the Secretary for Trade and Industry to ask the EEC Commission to let the U.K. Monopolies and Mergers Commission examine the Hanson offer? What did the Secretary mean when he promised, "consistent with my responsibilities under the Merger Regulation, to see whether there are grounds for an investigation by the U.K. authorities,"[64] while repeatedly conceding the EEC Commission's primary jurisdiction?

The scope for member state intervention under the Regulation is restricted to a few carefully defined situations. The general rule, subject to these limited exceptions, is that the Commission is in charge of the review process for all "Community dimension" mergers. The decision to grant the Commission a comprehensive mandate to vet large mergers arose from much bargaining and more than a few compromises by the EEC member states. The Thatcher government, in particular, was determined to restrict the national reference windows to an absolute minimum[65] to give meaning to the principle of a "one stop" competition rule system for "Community dimension" mergers. Indeed, the review thresholds are to be reviewed in 1993, when it is anticipated that they will be halved. This will mean that three times as many mergers are expected to come under the Commission's exclusive jurisdiction, with a corresponding drop in business for member state merger authorities.[66]

Where compatibility proceedings are initiated, the Commission is required by Article 19 to keep in "close and constant liaison" during its investigation with the antitrust authorities of all member states, who are entitled to offer their views on the procedures within the terms of the Regulation. There is also provision for consultation with an advisory group of member states experts before significant decisions are made. However, throughout this contact phase, the Commission remains in charge and member states by Article 21(2) are precluded from applying their national competition legislation to the merger under review.

The Regulation, in Article 21, does identify three situations in which member states may protect specific national interests when confronted by a concentration having a "Community dimension". Under Article 21(3), the so-called "British clause", member states such as the United Kingdom may protect three "legitimate interests": public security, the diversity of control in the media ("plurality of the media") and integrity rules ("prudential rules") in the regulation of financial services. None of these interests seems likely to apply in the Hanson-ICI case.[67]

By Article 21(3), member states may take "appropriate steps to protect [additional] legitimate interests" beyond the three specified, provided they are compatible with Community law and recognized as such by the Commission before any steps are taken by the requesting member state under this head of authority against the merger in question. The Commission must decide upon the request within one month of being asked. Unless this happens, the question is simply one of the "public interest" of the requesting member state and does not provide authority under the Regulation to the member state to intervene.

Only those specific criteria accepted by the EEC Commission as "legitimate interests" under Article 21(3) will give authority to the U.K. government to question separately any Hanson bid for ICI. The provision appears to be the source of the Labour Opposition's call on the Major government to examine any Hanson bid for ICI for its feared impact on R&D investment, regional employment stability, export commitments and other factors.[68] In this scenario, the Secretary for Trade and Industry would argue that any buyout of ICI would have a disproportionate impact upon the U.K. economy (compared to other EEC member states), and that the effect on one or more legitimate interests calls for a parallel review of the bid by a reference to the Monopolies and Mergers Commission. The Commission in this situation would vet the merger as usual under the Regulation.

Beyond the three clawback situations (public security, media plurality and prudential rules) and the window afforded by the third paragraph, however, there is nothing in the wording or history of Article 21 to allow public interest concerns of complaining member states to figure in the appraisal of Community dimension mergers where these concerns do not relate to competition grounds. For the reasons cited, it is not presently evident how the United Kingdom would be able to review any Hanson takeover bid on national interest grounds under the provisions of Article 21.

The only guidance in Article 21(3) is that any additional "legitimate interests" must be "compatible with the general principles and other provisions of Community Law." In accordance with the EEC *Treaty*, a member state under this requirement would not be able to restrict or prohibit mergers on grounds that arbitrarily discriminate or serve to disguise trade restrictions between member states.[69] In addition, once a "legitimate interest" is recognized, any measure or action taken by the concerned state "must be limited to the minimum of action necessary to ensure protection of the legitimate interest in question." The Commission closes this point by stating that where alternatives exist, the member state must choose the "measure which is objectively the least restrictive to achieve the end pursued."[70]

None of this would appear to provide persuasive grounds for the U.K. government to argue for an Article 21(3) reference from the commission either on the grounds of either a recognized or new "legitimate interest."

**National Security as a "Legitimate Interest"**

Article 223 of the *EEC Treaty* deals with the additional "legitimate interest" of national security. It provides that

> any Member State may take such measures as it considers necessary for the protection of the essential interests of its security which are connected with the production of or trade in arms, munitions and war material; such measures shall not adversely affect the conditions of competition in the common market regarding products which are not intended specifically for military purposes.

This provision allows member states a degree of parallel jurisdiction with the EEC Commission in addition to the "legitimate interests" recognized in the Regulation. But, much as in Article 21(3) of the Regulation, the protection of national security is tightly defined and may only be exercised in the least restrictive manner. ICI's significant role in the production of explosives, industrial chemicals and petrochemicals could raise concerns for U.K. authorities about the future assurance of supply of "munitions and war material" from a Hanson restructured ICI. The possibility of this argument, however, has not surfaced to date in comments by any member of the U.K. government. This suggests either that there is no measurable security concern for the U.K. (most likely), or that Hanson has given private assurances that a Hanson-controlled ICI would continue its U.K. production of materials "specifically intended for military purposes." It is difficult to see, in the circumstances, how the separate chance for a U.K. intervention under Article 223 would come into play.

**Applying Local Non-competition Legislation to End-Run the Regulation**

Article 21(1) of the Merger Regulation confers exclusive competence on the EEC Commission to take decisions concerning "Community dimension" mergers. By Article 21(2), member states cannot apply "national legislation on competition" to such mergers. The *Fair Trading Act 1973* (*FTA*) is the primary U.K. competition statute. The *FTA* allows the Secretary of State for Trade and Industry to make references to the Monopolies and Merger Commission (MMC) of any mergers that fall within either the assets or market share tests set out in the *FTA*. If the EEC Regulation is put aside for a moment, it is clear that any bid for control of ICI would bring the transaction within the purview of the *FTA*.

Section 84 of the *FTA* requires the MMC to take into account all matters which appear relevant, and goes on to include a non-exhaustive list of matters to which the MMC should have regard in deciding whether any particular merger may be expected to operate against the public interest. In addition to competition questions, the MMC is to take into account "the maintenance and promotion of the balanced distribution of industry and employment" in the United Kingdom.

Is it open to the U.K. Secretary to refer a Hanson bid to the MMC solely on this ground and ignore the competition issues? That possibility is left open by the breadth of the MMC's "public interest" mandate and the capacity of the U.K. government to change its reference policy for MMC reviews. In the past twelve years there have been ten different Secretaries of State responsible for mergers policy, "each of whom have had varying degrees of interest and involvement in its formulation and application."[71] If a Labour government were in power, it is safe to assume that its MMC reference policy would be "more interventionist" than the present government.[72] Whether that would or could translate into an end-run attack on the EEC Merger Regulation's reservation of jurisdictional authority to Brussels is a moot point.

This tack would only be pursued under the interpretation that non-competition concerns outside Article 21(2) are to be addressed in the MMC reference. The result, it is submitted, would seriously undermine the "one stop" intent of the EEC Commission's "sole jurisdiction" and, in effect, mischieviously add by the back door new "legitimate interests" in addition to those found in Article 21(3). Even worse, these additional non-competition grounds would be considered outside the Regulation and the requirement that any newly claimed "public interests" must first be recognized by the EEC Commission. If the argument were successful, then any member state would be able to thwart the

Regulation by providing separately for its own vetting of big mergers on non-competition grounds.[73] The United Kingdom's "preponderant share of European merger and acquisition activity" means that an interventionist reference policy under the "public interest" test contained in the *FTA* would soon conflict with the Merger Regulation and put the U.K. government in an untenable position. For these reasons, the case for a separate public interest review of "Community dimension" mergers by the MMC, focussing on non-competition concerns, must be seriously doubted.

The present U.K. government's reference policy, in any event, "is designed to regulate mergers that have anti-competitive effects." In 1984, the then Secretary of State announced that references would be made "primarily on competition grounds," a view repeated in the 1988 Blue Paper on Merger Policy and reiterated recently by Mr. Lilley, the current Secretary, in the course of his "restatement" of the government's reference policy and its particular application to acquisitions by state-owned companies.[74] Under the reference policy, the fact that the acquiring company is state-owned will not be by itself sufficient. Rather, there will need to be a "high degree of state ownership," "hands-on control" by the state owner, evidence of prior anti-competitive behaviour elsewhere, and an attempt to buy a large market share, before a reference will be made. The fact that any government owns a controlling interest in the bidding company will not, of itself, be sufficient reason to refer the merger to the MMC.

This statement, by coincidence, came two days after the European Commission called on the U.K. government to explain and justify its policy of discrimination against state-owned companies, contrary to the Community's neutrality on public or private ownership as a relevant factor in its application of EEC competition law.[75]

It is not obvious how a Hanson-ICI merger (hostile or otherwise) would raise the required competition grounds cited in the reaffirmed 1984 reference policy. With the exception of the titanium dioxide situation, there do not appear to be any other significant common activities, and therefore market share, barriers to entry and competitiveness appear to be unaffected by a buyout. These factors perhaps account for the reported view of the Office of Fair Trading (OFT) that any Hanson-ICI merger would not appear to raise serious competition concerns.[76] Under the *FTA*, the Secretary first receives advice from the Director-General of the OFT before making any reference to the MMC. The OFT will consider competition issues in the context of the *FTA*'s public interest tests, especially if undertakings to ameliorate anti-competitive effects have been given by the acquiring firm of both parties to the subject takeover.[77] The practice of the Secretary "in the vast majority of cases" is to follow the advice of the Director-General.[78] If this practice is followed here, then the Secretary will not refer any Hanson bid to the MMC even if it is argued that there is an opening for a separate U.K. review under the *FTA*.[79]

**The Possibility of ICI Fighting a Hanson Takeover**

Article 86 of the *Treaty of Rome* deals with the abusive exploitation of a dominant position. In the 1973 *Continental Can* decision, the European Court held that

> the merger of a dominant firm with a potential competitor might infringe Article 86, although the shareholders in the target company had not been harmed; nor was it alleged that they had been forced to sell their shares because Continental Can enjoyed a dominant position.[80]

The effect of the case is that Article 86 applies to "conduct that affects the structure of the market by absorbing a potential competitor, and not only conduct that exploits the lack of competition: buyers may be harmed indirectly by the reduction of competition."[81]

A breach of the duty imposed by Article 86 not to abuse a dominant position will give grounds for seeking an injunction under U.K. law against the dominant party.[82] Damages are also available on the basis of a breach of statutory duty.[83] This case law has been used by competing bidders in a takeover offer and is available to the victim in a hostile takeover attempt.[84] This prospect takes on some weight when it is remembered that the new EEC Merger Regulation has lower legal standing than Article 86. This means that the Regulation cannot deprive Article 86 and its underlying case law of their pre-existing effect.

If this is an appropriate case, then ICI could upset Hanson's bid by claiming in the High Court that the takeover will amount to the abuse of a dominant position and that Hanson's bid for control should be enjoined under Article 86.[85] On the basis of public knowledge about ICI and Hanson, however, there is no pressing evidence that Hanson presently holds a dominant position in the *Continental Can* sense in any ICI product line, or that ICI ranks as a potential competitor to Hanson in any significant sense, subject to the case of titanium dioxide. As noted above, Hanson may be expected to meet any concentration problem with titanium dioxide by undertaking a divestment of one of the production companies as a condition of Commission clearance of the takeover.

Competition will not be reduced or weakened by the Hanson takeover. This is not an unusual result for a takeover involving a conglomerate bidder. As a result, there do not appear to be grounds for an ICI challenge to an unfriendly bid for control by Hanson under the separate competition provisions of the *Treaty of Rome*.

**Some Conclusions**

Regardless of its outcome, the Hanson-ICI case has engendered a public awareness of the force of the merger law governing the internal market and its application to company takeovers involving thousands of jobs and the welfare of entire communities in a Community member state. That the new EEC Merger Regulation is the primary authority for regulating a takeover of the country's largest manufacturing company by another U.K. firm has come as an unsettling surprise to more than a few workers, parlimentarians and local leaders in the numerous areas of the United Kingdom where ICI plants, laboratories and offices are significant contributors to the regional and national economy.

The prospect of a hostile takeover has focused sharp attention on the investment practices and management monitoring standards of the dominant institutional shareholders (insurance and pension funds), the propriety of "poison pill" defences and "financial engineering" practices, and the depth of community distrust sowed by an acquisitive corporate raider. As one observer noted, "the only certainty is that the world's fourth largest chemicals company will never be the same again."

The threat of a Hanson bid has accelerated (and perhaps extended) the pace and scale of ICI management's rationalization of the company. Whether or not Hanson moves on ICI, the current ICI management appears to be trimming jobs and selling off less profitable lines on a scale closer to that expected of a Hanson-controlled ICI. If this perception becomes the reality and share earnings materially improve, institutional shareholders will sit tight. The value of Hanson's minority holdings will similarly appreciate and ICI will soldier on, very mindful of the price for faltering down the line in the face of a takeover law that will not protect them from a buyout.

The case underlines the advent of a single internal market and the force of the Merger Regulation which controls significant takeovers in a manner largely irrespective of member state national interests. The market compatibility tests applied to these mergers concentrate on competition grounds, leaving little leeway for intervention by affected EEC countries to prohibit or place conditions on contentious mergers for "public interest" reasons.

In this light, the result predicted for any consummated Hanson bid makes eminent legal sense. But if hard cases make good law, the dislocative fallout (job losses, plant shutdowns, redirected production and asset selloffs) expected in the short and medium run by many from a Hanson takeover of ICI will do little to gain public support for the new European order. On the other hand, ICI's latest reorganization efforts come closer to the Hanson model and over time must soften the public's linkage between "cold" efficiency tests and the Regulation.

The ICI case does provide a useful illustration of the difficulties inevitably faced in defining a competition policy where other public policy concerns (employment, regional development and others) may be painfully evident. The challenge becomes more visible in a common market setting where non-competition factors of social and industrial policy have heretofore been employed by many member

states as part of their regulation of large mergers. The new EEC Merger Regulation represents a Community decision to severely restrict the scope for member states to exercise leverage in such cases on non-competition grounds.

There is some delicacy, if not irony, in the U.K. government's undiminished commitment to Brussels' jurisdiction over the control of its flagship industrial company. It comes at the very time that the Major government is enduring a divisive debate over the sharing of sovereignty with the Community on currency, defence and foreign policy matters.[86] The quest for a "process leading gradually to a union with a federal goal" promises to test the United Kingdom's commitment to the post-1992 community. On the issue of competition policy, however, the Merger Regulation asserts the continuing dominance of the Community's juridiction in the area and parallels the Commission's determination to open up national monopolies (rail, post, gas and electricity) to private competitors, an agenda it holds in common with the U.K. government.

**Notes**

1 Council Regulation (EEC) No. 4064/89 (December 21, 1989) on the control of concentrations between undertakings (revised text), published in the *Official Journal of the European Communities*, No. L257, 21.9.90, p. 14 and at [1990] 4 C.M.L.R. 859.

2 See [1990] 4 C.M.L. Reports (Antitrust Supplement) 288 for background notes for the E.C. Commission's explanatory memorandum on the Regulation.

3 In *Continental Can*, [1973] 12 C.M.L. Reports 199. According to D. Perrott in (1988) 22 Int'l Lawyer 1231, the "ruling was somewhat unexpected...since the wording of Article 86 gives no hint....that it is concerned with concentrations." The Commission's recent experience with its Articles 85 and 86 cases is discussed in Soames, "EEC Merger Control," in Beggs, ed., *Corporate Acquisitions and Mergers*, at 1.2.

4 Thieffry, "The New E.C. Merger Control Regulation," (1990) 24 *Int'l Lawyer* 543 at 543-44.

5 [1984] 2 C.M.L. Reports 40, in which the European Court of Justice held that any acquisition by one party of shares in a competitor might, on the facts, amount to an agreement prohibited by Article 85 even if it is not an abuse of dominance prohibited by Article 86. See *Carnand and Schmalbach-Lubeca* (1988) 51 C.M.L.R. 262 for a recent application of the *Philip Morris* decision, reviewed by Perrott, *supra*, note 3 at 1233-34. The Commission threatened to apply Article 85 to full mergers and not merely to minority shareholdings if the Council did not adopt a comprehensive Merger Regulation: Soames, *supra*, note 3, at 1.2-3.

6 The Regulation came into effect on Sept. 21, 1990. Generally, see C. Jones, "The Scope of Application of the Merger Control Regulation (1990-91) 14 Fordham I.L.Jnl. 359 and Davidow, "Competition Policy, Merger Control and the European Community's 1992 Program" (1991), 29 Col. Jnl.Transnat.Law 11.

7 The preamble to the Regulation emphasizes that the competition rules are "essential for the achievement of the internal market by 1992 and its further development" and must "include provisions governing those concentrations which may significantly impede effective competition in the Common Market or in a substantial part of it": [1990] 4 C.M.L. Reports (Antitrust Supplement) 286 at 291.

8 *The Economist*, June 8, 1991, p. 17.

9 *Financial Times*, June 25, 1991, p. 3, reporting on the release of the Commission's 1990 Competition Policy Report the previous day.

10 Sections 2(1), 2(4), and 3(1) recognize that in cases of conflict between national and community law, the EEC law prevails. But for the wording of exclusivity in the Regulation, the U.K. and EEC competition legislation would co-exist and operate side by side (even on the same fact situation) unless there was a conflict in their application or member state action was specifically excluded.

11 Korah, *An Introductory Guide to EEC Competition Law and Practice* (4th ed., 1990) at 219.

12 Article 21(2) giving sole jurisdiction to the Commission is discussed below. For a review of the facilitating 1990 amendments to the U.K. *Fair Trading Act 1973*, see Soames, "Merger Regulation: Member States and the

Commission" (1990), 27 Law Society Gazette 24 at 27. Article. 21(1) provides that "the Commission shall have sole jurisdiction to take the decisions provided for in this Regulation" and Article 21(2) follows that "no member state shall apply its national legislation on competition to any concentration that has a community dimension." Concentrative joint ventures are included in the Regulation's ambit but are not discussed here: see Venit, "The Merger Control Regulation: Europe comes of age...or Caliban's dinner" (1990), 27 C.M.L. Reports 7 at 37-40.

[13] *Per* Articles 1 and 5. See Thieffrey, *supra*, note 4, at 545.

[14] Korah, *supra*, note 11, at 213.

[15] *Financial Times*, May 28, 1991, p. 2.

[16] *Per* Commission statement on the final level of the thresholds, [1990] 4 C.M.L.R. 314.

[17] Thieffrey, *supra*, note 4, at 546.

[18] Korah, *supra*, note 11, at 213-14.

[19] *Id.*, at 217. The Confederation of British Industry (CBI) argued strenuously (and unsuccesfully) for a public policy defence. Under the U.K. legislation, "competition is only one of the matters habitually considered by the Monopolies and Mergers Commission": *ibid.*

[20] Articles 4, 11, 12, and 13.

[21] Article 6 commits the Commission to speedy appraisals, spelled out in specific deadlines in an accompanying policy and interpretative statement entered in the minutes of the EC Council (but not subsequently published in the official Journal as promised): see [1990] 4 C.M.L. Reports (Antitrust Supplement) 314 at 315.

[22] Korah, *supra*, note 11, at 218. The criteria and scope of review by the Commission are helpfully discussed in Soames, "The Commission's Role in the Merger Regulation", (1990) 26 Law Society Gazette 18.

[23] May 28, 1991, p. 2. The caseload was probably closer to one hundred for the first nine months of operation when applications for confidential guidance and informal advice are included.

[24] *Ibid.*

[25] *The Economist*, May 18, 1991, p. 87.

[26] See "ICI-first" profiles in *Guardian*, May 29, 1991, p. 9 and May 30, 1991, p. 18; *Financial Times*, June 10, 1991. p. 9.

[27] *The Economist*, May 25, 1991, p. 104.

[28] *Financial Times*, May 28, 1991, p. 20.

[29] *The Economist*, June 22, 1991 p. 18.

[30] *Financial Times*, *supra*, note 28.

[31] *The Economist*, May 25, 1991, p. 103, claims Hanson has outperformed the London market over the past 25 years by some three thousand percent, while ICI has underperformed it by fifty percent.

[32] *Ibid.*

[33] *Ibid.*

[34] *Financial Times*, May 25, 1991, p. 1.

[35] *Guardian*, June 7, 1991, p. 13. The authors are from the University College of Wales and the Business Studies Department of Middlesex and East London Polytechnics. By late July 1991, however, ICI's own reorganization plans forecast a net loss of twenty thousand jobs: *Financial Times*, July 26, p. 15.

[36] *Observer*, June 9, 1991, p. 25. Subsequent press reports concentrated on a 1989 restructuring operation involving the nearly $20 billion purchase of a number of offshore companies, mainly incorporated in Panama: *Observer*, June 23, 1991, p. 21.

[37] Although many analysts agreed with the prediction of the *Observer* (May 26, 1991, p. 25), that "it's a takeover proposal whatever the guise," Hanson has steadfastly refused to declare its eventual intentions, even after ICI's release of its first half financial results in July 1991. Profits dropped 31percent below 1990's results but were $100 million above market expectations: *Financial Times*, July 26, 1991, p. 1; also *The Economist*, July 27, 1991, p. 66.

[38] *Financial Times*, June 7, 1991, p. 12; with more details, *id.*, July 20, 1991, p. 1 and July 26, 1991, p. 15.

[39] *Id.*, June 15, 1991, p. 1.

[40] *Independent*, June 16, 1991, p. 3. Hanson's efforts have recently been compared to its readiness in 1989 to pay pension benefits of some $1.2 million and a $1.6 million salary to an anonymous employee of its overseas subsidiary: *Observer*, June 23, 1991, p. 21.

[41] *Financial Times*, June 15, 1991, p. 1.

[42] *Id.*, June 19, 1991, p. 1.

[43] *Guardian*, June 8, 1991, p. 13.

[44] *Id.*, editorial, June 7, 1991, p. 13.

[45] *Observer*, June 9, 1991, p. 1.

[46] *Guardian*, June 12, 1991, p. 1.

[47] *The Economist*, June 15, 1991, p. 92.

[48] *Id.*, May 25, 1991 at p. 104.

[49] *The Economist*, July 6, 1991, p. 75.

[50] *Id.*, July 13, 1991, p. 78.

[51] *Id.*, May 18, 1991 at p. 104.

[52] *Observer*, June 23, 1991, p. 21.

[53] *Financial Times*, July 26, 1991, p. 1.

[54] *Id.*, p. 14; according to "Lex" (*Financial Times*, July 26, 1991, p. 15), ICI share values have fallen twenty percent in real terms since 1978 and the "real job of improvig shareholder value has yet to be addressed."

[55] *Arjomari-Prioux SA/Wiggins Teape Appleton*, Case IV/MO25, December 10, 1990.

[56] See Cook & Soames, "The EEC Merger Regulation: A Practical View", *Int'l Lawyer*, July/August 1991, comparing "decisive influence" under the Regulation with the meaning of "material influence" in section 65 of the FTA.

[57] [1991] 4 C.M.L.R. 169. The Commission, following surprise raids, found clear evidence of a market splitting arrangement between ICI (U.K. and Ireland) and Solvay (Continent), plus an illegal rebate scheme to exclude competitors and tie in customers. ICI was fined 17 million ECUs ($21 million) and Solvay 30 million ($40 million), and is appealing both the fine and the findings of breach of Articles 85(1) and 86: *Financial Times*, June 27, 1991, p. 27. ICI's U.K. soda ash operations were sold to Penrice of Australia in June 1991 as part of "its strategy of concentrating on businesses with potential for international growth": *Guardian*, June 27, 1991, p. 12.

[58] Case IV/MO23, November 28, 1990.

[59] Article 4(1).

[60] Article 7(1). Public bids may proceed so long as they have been notified to the Commission and the acquiror does not exercise the voting rights: see Articles 7(3),(4) and (5).

[61] Commission statement on taking decisions as to compatibility: [1990] 4 C.M.L. Reports (Antitrust Supplement) 314 at 315.

[62] *Ibid.*

[63] Soames, *supra*, note 22, at p. 20.

[64] *The Economist*, May 18, 1991, p. 88, and May 25, 1991, p. 17. Recital 15 (one of the Commission's aids to interpretation but not evident in the words of the Regulation itself) presumes compatibility where the companies have only a limited market share, in particular of less than 25 percent in the market or a substantial part of it. Market share above that figure does not presume incompatibility. A finding of competition impairment is still required. ICI ranks first in Europe and second in the world in the production of titanium dioxide: *The*

*Economist*, July 27, 1991, p. 66. Hanson's SCM Chemicals is the world's third-ranking producer: *The Economist*, July 13, 1991, p. 79. Precise market shares are not known.

[65] Suggested in *Financial Times*, May 29, 1991, p. 21. According to Cook & Soames, *supra*, note 56, "[t]he Mergers Task Force...is always willing to discuss...matters on a confidential basis and advise whether it believes that a concentration would be likely to arise in a particular set of circumstances."

[66] Soames, *supra*, note 22, at 20 quoting an official of the U.K. Department of Trade and Industry.

[67] Soames, *supra*, note 3, at 1.26-27.

[68] Commission statement on Article 2, [1990] 4 C.M.L. Reports (Antitrust Supplement) 314.

[69] Soames, *supra*, note 60, at 1.27.

[70] Soames, *supra*, note 22, at 20.

[71] Discussed in Soames, *supra*, note 3, at 1.32-3.

[72] *Observer*, June 16, 1991, p. 21. The Regulation's preamble (cl. 19) provides an "opportunity to be heard" before the Commission to the managements, union representatives and "third parties showing a legitimate interest" *where proceedings have been initiated*: [1990] 4 C.M.L. Reports (Antitrust Supplement) 862 (emphasis added).

[73] Korah, *supra*, note 11, at 217.

[74] Thieffrey, *supra*, note 4, at p. 546.

[75] The Commission has issued ([1990] 4 C.M.L.R. 314) detailed interpretative principles for the application of the Article 21(3) "legitimate interests" to Community dimension mergers. There is a possibility that "public security" could be raised due to the nature of some of ICI's products but this prospect has not been seriously argued in any public commentary. See below the analogous discussion of "National Security" as a "legitimate" interest.

[76] *Financial Times*, June 4, 1991, p. 20.

[77] The Trade Secretary recently clarified his policy of referring takeover bids by state-owned companies to the MMC after taking into account the findings in five recent merger reports of the MMC involving state-owned companies. The EEC Commission had complained separately that the U.K. policy discriminated against undertakings on the basis of nationality contrary to EEC competition law. See text below accompanying note 87.

[78] *Per* Commission interpretative statement at [1990] 4 C.M.L. Reports (Antitrust Supplement) 317.

[79] See Soames, "Merger Policy: As Clear as Mud?", [1991] 2 E.C.L.R. 53 at 53-54.

[80] *Id.* at 70.

[81] *Ibid.*

[82] As Hornsby notes, for example, "Irish merger control law employs very widely drawn 'common good' criteria which include non-competition issues. Spanish competition law contains a balancing test according to which economic progress may compensate for any restriction on competition likely to result from the merger": "Back-Door Nationalisation and the Fair Trading Act," [1990] 5 I.C.C.L.R. 141 at 143.

[83] *Ibid.*

[84] Soames, *supra*, note 79, at 70.

[85] *Id.*, at p. 55 on the so-called "Tebbit Rule".

[86] "Mergers Policy: A Department of Trade and Industry Paper on the Policy and Procedures of Merger Control" (HMSO, 1988), particularly at paras. 2.21 and 2.27.

[87] *Financial Times*, June 13, 1991, p. 7. For critical reviews of the original U.K. policy, see Hornsby, *supra*, note 82 at 143 and Soames, *supra*, note 79 at 64-68.

[88] *Guardian*, June 11, 1991 p. 11.

[89] *Guardian*, May 29, 1991, p. 13. The OFT, with limited exceptions, is responsible for all monitoring and initiation functions under the *Fair Trading Act 1973*. See Howe, "U.K. Merger Control: How does the System Reach Decisions? A Note on the role of the Office of Fair Trading," [1990] 1 E.C.L.R. 3. A possible competition concern

might be the high leveraging of a Hanson bid but this is purely speculative and would depend eventually on how a bid might be structured.

[90] Soames, *supra*, note 79, at 54-55.

[91] *Ibid.*

[92] The Secretary may refer an anticipated merger attempt to the MMC *per* section 75 of the *Fair Trading Act*, but this cannot be done unless (at a minimum) it appears to the Secretary of State that events are contemplated which will result in a merger if carried into effect. In other words, prospective mergers can be referred to the MMC provided there is some solid evidence that they are contemplated. Cf. Merkins & Williams, *Competition Law: Antitrust Policy in the U.K. and the EEC* (1984) at 245. There is no directly comparable authority in the EEC Merger Regulation. However, a concentration must be notified in the case of a public bid (which is one type of contemplated or proposed merger in the sense used in section 75 of the *FTA*) within one week of its announcement (Article 4(1)), i.e., usually before it is a completed merger.

[93] Korah, *supra*, note 11, at 3.

[94] *Ibid.*

[95] *Garden Cottage Foods* v. *Milk Marketing Board* [1984] 1 A.C. 130, [1983] 3 C.M.L.R. 43.

[96] *Ibid.*, discussed in Merkin & Williams, *supra*, note 92, at 446-447.

[97] Thieffry, *supra*, note 4, at 550.

[98] See *Carnard & Schmalbach-Lubeca*, (1988) 51 C.M.L.R. 262, reviewed by Perrott in (1988) 22 Int'l Lawyer 1233; also Pathak, "EEC Concentration Control: The Foreseeable Uncertainties", [1990] 3 European Community Law Review 119 at 120-1.

[99] *The Economist*, May 25, 1991, at 17.

[100] Over one hundred MPs have signed a bipartisan motion stressing ICI's expenditure on research and their "appreciation of the investment which ICI has made in the future of the nation": *Financial Times*, June 21, 1991, p. 1. Under pressure from MPs openly critical of a possible Hanson bid, the Secretary has promised that in the event of a bid, the OFT Director-General would "gather views on competition and other matters" which would form the basis of the government's advice to Brussels: *Financial Post*, June 27, 1991, p. 12.

[101] Excerpt from the draft Union Treaty presented to the EEC Foreign Ministers on June 17, 1991 (*Guardian*, June 18, 1991, p. 7).

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