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On March 27, 2007, the Japan Fair Trade Commission (the “JFTC”) released its amended *Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination* (“amended M&A Guideline”)¹, which provides substantial revisions to the original *Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination* (“original M&A Guideline”)², and its amended *Policies dealing with prior consultation regarding business combination plans* (amended *Consultation Guideline*)³. This article provides background on the amended M&A and Consultation Guidelines and analyzes the revised points.

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¹ Japan Fair Trade Commission, *Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination* (Mar. 28, 2007), available at <http://www.jftc.go.jp/e-page/legislation/ama/RevisedMergerGuidelines.pdf>.

² Japan Fair Trade Commission, *Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination* (May 31, 2004).

³ Japan Fair Trade Commission, *Policies dealing with prior consultation regarding business combination plans* (Mar. 28, 2007), available at <http://www.jftc.go.jp/e-page/legislation/ama/MApriorconsultation.pdf>.

I. INTRODUCTION & BACKGROUND

Section 4 of the “Law Concerning Prohibition of Private Monopolization and Maintenance of Fair Trade” (the “JAA”)⁴ prohibits business combinations through mechanisms such as possession of stock (Article 10), interlocking directors (Article 13), and merger (Article 15) which may be substantially to restrain competition in any “Particular Field of Trade”. Some of these business combinations require mandatory filing with the JFTC for review before they are consummated. Where prior notification is required, the parties may not implement the merger for a period of 30 days following the filing. The 30-day period can be shortened where it is apparent that the proposed business combination is unlikely to restrict competition in a particular field of trade. If the JFTC requests additional information from the parties, the parties are not prohibited from closing the business combination after the 30-day period, but the JFTC may still take action in relation to the business combination prior to the later of 120 days from the date of receipt of the notification or 90 days from the date of receipt of the additional information (the “Waiting Period”). Also, parties of business combination may request that the JFTC review whether or not the proposed business combination will cause anticompetitive effects to the relevant market before mandatory filing (the “Prior Consultation”). It should be noted that parties of a business combination may apply for the Prior Consultation even in instances where mandatory filing with the JFTC is not required. Many Japanese businesses have opted for the Prior Consultation to ensure that the JFTC will not block business combination. The JFTC may issue cease and desist

⁴ Law Concerning Prohibition of Private Monopolization and Maintenance of Fair Trade, Law No. 54 of 1947.

orders to parties attempting to conclude a prohibited business combination, albeit the green light is not given by the JFTC (Article 17). In addition, the JFTC may file an application for courts to declare null and void of merger and corporate spirit where:

- (i) mandatory filing is not lodged at the JFTC; and
- (ii) parties of merger and corporate spirit attempt to consummate during the Waiting Period (Article 18) (hereinafter “Japanese Merger Control”).

In order to clarify how the JFTC reviews business combination, the original M&A Guideline was published on May 31, 2004, and was the result of major revisions to the former Guideline concerning business combination and *Policies Dealing with Prior Consultation Regarding Business Combination* (the “original Consultation Guideline”)⁵, which was published on December 11, 2002.

The original M&A Guideline provides the definitions of business combinations to be reviewed by the JFTC, how to delineate a particular field of trade for review purpose, and factors to be taken into consideration in a review process, while the Consultation Guideline details the procedural aspects of the Prior Consultation regarding business combination with the JFTC (e.g., how to file an application of the Prior Consultation with the JFTC, what documents need to be attached to an application, how long it will take to go through review process, and when the JFTC render its decisions of consulted business combination).

Since the issuance of the original M&A Guideline, Japanese businesses have requested two major improvements to the Guideline:

⁵ Japan Fair Trade Commission, *Policies dealing with prior consultation regarding business combination plans* (Dec. 11, 2002)

- (i) make the review process faster and more transparent; and
- (ii) ensure consistency with decisions by foreign competition agencies.

In order to meet these requests, both the M&A and Consultation Guidelines were amended on March 28, 2007. There are several points worth mentioning regarding both Guidelines.

II. ANALYSIS OF THE AMENDED M&A GUIDELINE

A. Delineation of the Term “Particular Field of Trade”

Under the JAA, the term "Particular Field of Trade" is used to describe "relevant market". There are three major revisions concerning how to define a particular field of trade:

- (i) although a particular field of trade will primarily be delineated in light of substitutability of demand, if necessary, substitutability of supply will be taken into consideration;
- (ii) the SSNIP test will be used in order to analyze the substitutability of demand and supply; and
- (iii)a “Geographical Field of Trade” may be determined by looking beyond the Japanese jurisdiction.

It should be noted that the SSNIP test is the methodology to define a particular field of trade through analyzing whether or not a hypothetical profit-maximizing firm, not subject to price regulation, that was the only present and future producer or seller of relevant products in relevant areas, would likely impose a "small but significant and nontransitory increase in price", assuming that terms of sales of all other products are

held constant.

1. Substitutability of supply

Under the JAA, a particular field of trade is an area that is analyzed by determining whether or not competition may substantially be restrained and delineated within relevant product lines and geographical regions. The JFTC has primarily focused on demand substitution factors (i.e., possible consumer response, in particular field of trade definition).

In the original M&A Guideline there was a description which indicated that supply substitution may be taken into consideration. Moreover, there was a merger review case in which a particular field of trade appeared to actually be delineated through the analysis of supply substitution.⁶ However, under the original M&A Guideline, there was no clear concept as to the relationship between substitutability of supply and demand, and whether or not the JFTC may take into consideration supply substitution factors to delineate a particular field of trade.

Through the amendment, it is now made clear that a particular field of trade will first be delineated in light of substitutability of demand and, if necessary, substitutability of supply.

2. Application of the SSNIP test

Through the amendment, it is now made clear that the JFTC uses the SSNIP test to analyze the substitutability of demand and supply. It should be noted that the JFTC comments that regardless of whether the JFTC uses the SSNIP test or analysis of

⁶ See Japan Fair Trade Commission, Japan Air Line/Japan Air System (JFTC decision of Mar. 15, 2002).

similarity in terms of feature and function of products,⁷ the JFTC will likely reach the same conclusion (i.e., the same area will be delineated for a particular field of trade).⁸

According to the amended M&A Guideline, in order to analyze substitutability of demand, the JFTC must examine whether or not consumers of the products will switch to other similar products based on the assumption that a hypothetical monopolist of products imposes at least a "small but significant and nontransitory increase in price" but the terms of sale of all other products remains constant. Also, in order to analyze substitutability of supply, the JFTC needs to examine whether firms not currently producing the relevant products in the relevant area will likely commence producing the relevant products and/or enter the particular field of trade within one year and without bearing significant cost of entry to and exit from a particular field of trade in response to a "small but significant and nontransitory price increase".

In addition, the amended M&A Guideline elucidates that "small but significant increase in price" will mean a 5 to 10 percent increase of price and "nontransitory" will mean one year, which is the same standard in the United States and European Community.

3. Geographic field of trade beyond the Japanese jurisdiction

Under the amended M&A Guideline, it is made clear that, in the event that consumers are dealing with suppliers regardless of whether or not they are situated in

⁷ This is another approach the JFTC has applied to business combination cases before the amended M&A Guideline.

⁸ See Japan Fair Trade Commission, The Gist of Main Opinion made to Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination and the JFTC's Response to Them (attachment 1-2) (Mar. 28, 2007), available at <http://www.jftc.go.jp/pressrelease/07.march/07032801-01-tenpu01.pdf> and <http://www.jftc.go.jp/pressrelease/07.march/07032801-01-tenpu02.pdf>.

Japan, a geographical field of trade may be delineated beyond the Japanese jurisdiction, as a price increase by suppliers in Japan might be hindered if consumers will switch to imported products. This is the major shift of Japanese Merger Control as the original M&A Guideline explicitly denied that a particular field of trade will be defined beyond the jurisdictional border. Example of products for which a particular field of trade will be defined beyond the border are those products: (i) whose transportation costs and regulations are not so different from those for Japanese, (ii) where there is high substitutability, in terms of quality, between domestic and overseas' products, and (iii) where international price is formed through international transaction. It should be noted that although a geographical field of trade may be defined beyond the Japanese jurisdiction, the JFTC's analysis focuses on effects to competition in Japan due to the proposed business combination.⁹

B. Revision to the “Safe Harbour”

The “Safe Harbour” is an area where the JFTC usually regards that competition in a particular field of trade will not substantially be restrained through business combination, and therefore the green light will likely be given. It should be noted that the original and amended M&A Guidelines use the Herfindahl-Hirschman Index (“HHI”) to measure market concentration. HHI is calculated by summing the squares of the individual market shares of all participants to a particular field of trade and reflects both distribution of the market shares of the top firms and composition of a particular field of trade outside of the top firms.

⁹ See *supra* note 1.

Three major revisions are made through the amendment. First, the standard of the safe harbor was amended for horizontal business combinations. The standards are now:

- (i) the post-business combination HHI of less than 1,500
- (ii) the post-business combination HHI of more than 1,500 and less than 2,500 and an increase in the HHI of less than 250; and
- (iii) the post-business combination HHI of more than 2,500 and an increase in the HHI less than 150.

For vertical and conglomerate business combination, the standards are:

- (i) post-business combination market share of less than 10 percent;
- (ii) post-business combination HHI of less than 2,500 and market share of less than 25 percent.

Second, the amended M&A Guideline sets the uniform standard regarding the likelihood of being blocked by the JFTC, which will be applied to all forms of business combination (e.g., horizontal, vertical, or conglomerate), regardless of the type of anticompetitive conducts such as unilateral (e.g., price increase and discrimination) or coordinated conduct (e.g., cartel behaviors). More specifically, the amended M&A Guideline articulates that there is generally a small likelihood for a business combination to substantially restrain competition in a particular field of trade where the post-merger HHI is less than 2,500 and the post-merger market share is less than 35 percent. The standard is set based on the past precedent of business combination cases in which the JFTC did not raise competitive concerns. To that end, the JFTC decided to release the number of business combination cases in which the JFTC conducted detailed reviews, the

number of cases where the JFTC raised competition concerns as a result of detailed review, statistics showing market share, and statistics detailing the HHI and expected increase of HHI thereof after business combination.¹⁰

C. Principal Factors to Analyze the Substantial Restraint of Competition

There are four major revisions made in this area:

- (i) the most current market share data will be used to measure market share after a business combination (if there are factors which might affect post-business combination market share or competitors are no longer able to produce competitive constraint after business combination, such factors will also be taken into consideration);
- (ii) given that a geographical field of trade will be defined beyond the Japanese jurisdiction, market share and ranking of such a global level market will be taken into account;
- (iii) analytical processes of import and market entry is now made clear; and
- (iv) competitive pressure from consumers is now made easier to assess.

The sections that follow provide detail of (iii) and (iv).

1. Analytical process of import and market entry

The amended M&A Guideline touches on two factors considered necessary to analyze whether the substantial restraint of competition may occur. First, the JFTC comments that import is one method of market entry, such that the same analytical

¹⁰ Japan Fair Trade Commission, Past Precedents of Business Combination Case (Jun. 19, 2007), available at <http://www.jftc.go.jp/pressrelease/07.june/070619-tenpu.pdf>.

process will be applied to both.¹¹ Second, if the competitive constraint due to potential entry is sufficient, parties to the business combination will unlikely be able to raise the price. In order to analyze sufficiency of competitive constraint due to potential entry, the JFTC needs to examine factors such as the degree of legal as well as practical entry barrier, substitutability of products sold by potential competitors and those sold by market participants, and likelihood of entry by potential competitors in a timely manner. According to the amended M&A Guideline, “timeliness” of entry will generally mean “within 2 years”, which is the same standard in the United States and European Community.

2. Competitive pressure by consumers

The amended M&A Guideline states that if consumers have enough bargaining power against suppliers, it will hinder the exercise of market power by parties of business combination. Examination is then necessary to determine to what extent consumers may be able to exert bargaining power. According to the amended M&A Guideline, factors to be taken into consideration are (i) whether or not consumers are active enough to demand discounted price to suppliers, and (ii) how easily consumers are able to switch to other suppliers. There was a case in which the JFTC analyzed whether users had enough bargaining power to assess if competition in a particular field of trade would substantially be restrained.

¹¹ *See supra* note 1.

The amended M&A Guideline is the first instance of the JFTC creating an independent section in the Guideline to mention that bargaining power of consumers must be examined.

D. Analysis of Efficiencies

The amended M&A Guideline articulates that if efficiencies will be enhanced through a business combination, whereby it is reasonably expected that parties of business combination may compete more actively, such efficiencies are also to be taken into consideration. In the original M&A Guideline, there was a description suggesting that efficiencies accomplished through a business combination could be evaluated. This analytical process is made clearer through the amendment.¹² The sophistication of efficiencies analysis can be said to be step forward to achieve a more consistent outcome with foreign competition agencies, as for decades merger analysis was primarily accomplished through studying statistics of market share based on a presumption of illegality.

Also, the amended M&A Guideline elucidates that efficiencies will rarely justify a business combination creating a monopoly or a near-monopoly, where there is no competition or, if any, competition is almost entirely eliminated.¹³

In addition, conditions which allow for the JFTC to call into account efficiencies are articulated in the amended M&A Guideline are:

¹² Japan Fair Trade Commission, The Main Revision to the Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination “(attachment) Recruitment of Opinion about the amendment to the Guideline to Application of the Antimonopoly Act Concerning Review of Business Combination” (Jan. 31, 2007), *available at* <http://www.jftc.go.jp/pressrelease/07.january/070131.html>.

¹³ *See supra* note 1.

- (i) efficiencies are likely to be accomplished with the proposed business combination and unlikely to be accomplished in the absence of either the proposed business combination or another means having comparable anticompetitive effects (“Specificity Condition”);
- (ii) enhancement of efficiencies are feasible (“Feasibility Condition”); and
- (iii) consumers’ welfare will be achieved through enhancement of efficiencies (“Welfare Condition”).

Regarding the Specificity Condition, the amended M&A Guideline requires that efficiencies are business combination specific and cannot be accomplished by less restrictive alternative methods. However, it is not clear whether the amended M&A Guideline still implies that the JFTC will insist upon a less restrictive theoretical alternative to reject taking into consideration efficiencies realized through the proposed business combination. Regarding the Feasibility Condition, the amended M&A Guideline makes clear that it needs to be feasible and efficiency claims that are vague or speculative will not be considered. Regarding the Welfare Condition, the amended M&A Guideline articulates that efficiencies need to produce benefits to the society such as reduction of price of goods and services, improvement of quality, and development of new technologies. According to the amended M&A Guideline, in order to analyze the Feasibility and Welfare Conditions, parties to a business combination need to submit documents such as: internal documents detailing internal decision-making processes concerning business combinations; explanatory documents to shareholders and financial

markets regarding expected efficiencies and; explanatory documents to external experts regarding enhancement of efficiencies.

E. Failing Firms and Divisions

Before the amendment, the capability of firms was a factor to be considered by the JFTC when a business combination was occurring with failing firms or divisions. Although the original M&A Guideline regarded the market share of less than 50 percent after the business combination as where competition would not substantially be restrained, this standard is abolished through the amendment. Now, regardless of market share after a business combination, where:

- (i) failing firms or division will likely exit from market but for the business combination;
- (ii) such failing firms or divisions would be able to reorganize successfully through the business combination; and
- (iii) there is no less anticompetitive alternative choice than the proposed combination, it will be generally regarded as unlikely producing anticompetitive effects.

F. Remedial Measures

Even in the original M&A Guidelines, remedial measures were mentioned as a factor considered by the JFTC when analyzing whether the substantial restraint of competition may occur. However, the original M&A Guidelines were criticized for not clarifying under what conditions and factors the JFTC would likely find that competition of a particular field of trade would be maintained due to remedial measure.

In the amended M&A Guideline, several factors have been clarified. First, it is now clearly stipulated that structural measures such as transferring a part of divisions are the principal remedial means to preserve competition in a relevant particular field of trade. Furthermore, measures regarding certain actions could be appropriate means in the event that the market structure changes so frequently due to technological innovation. Second, the amended M&A Guideline makes it clear that the JFTC may request parties to a business combination to alter or finish the remedial measures based on a competitive situation after the business combination. Third, examples of remedial measures are added to the amended M&A Guideline (e.g., termination of business cooperation with third parties and prohibition on jointly purchasing raw materials).

III. AMENDMENT TO THE REVIEW PROCESS

The amended Consultation Guideline has made the Prior Consultation process more clear. Specifically, parties to a business combination may apply for the Prior Consultation by submitting materials showing concrete contents of business combination plan. Within 20 days from the day when such materials are submitted, the JFTC will either notify the parties that additional materials need not be submitted, or produce a list of additional materials to be lodged at the JFTC in writing. Examples of materials to be submitted are:

- (i) items demonstrating an outline of parties;
- (ii) concrete contents of business combination plan;
- (iii) outlines of products and services subject to combination;
- (iv) outline of companies providing products subject to combination;

(v) materials showing the basis for factors thought to bear a significant influence on the judgment regarding competition; and

(vi) additional materials which the parties consider are to be tendered.

It should be noted, however, that even after the amendment, it takes a lot of time before the JFTC finally finds that all the materials have been submitted.

From the day on which notice is provided to parties that additional materials need not be submitted or from the day on which additional materials are submitted in accordance with a list of materials, the JFTC will commence its review and, as a general rule, within 30 days, will render a notice that there are no issues relating to the JAA or state that a further detailed review is required. It should be noted that the JFTC commented that parties of prior consultation may submit any documents that they deem necessary anytime during the procedure.

In the event that notice is given to the effect that detailed review is required, the JFTC will explain the specific concerns of the JAA and request the submission of concrete materials which the JFTC decides to be necessary to undertake detailed review. Parties to a business combination need to submit the requested materials within approximately 3 to 4 weeks. If a business combination for which parties apply for prior consultation has not been made public, before commencement of detailed review, the parties are required to make a public announcement enabling the JFTC to conduct interviews with third parties such as competitors and suppliers of relevant products. Then the JFTC will make a public announcement to the effect that a detailed review is

conducted, whereby any parties are allowed to lodge their opinion regarding the business combination within 30 days from the date of notice.

From the day on which the parties submitted the concrete materials, the JFTC will, as a general rule, within 90 days, render its response to the proposed business combination as well as the rationale behind the result and make a public announcement within one week from the date of its response.

IV. CONCLUSION

Although it is the JFTC's basic approach to review business combinations on a case-by-case basis according to various factors which might differ in each case, the amendment now clarifies how the JFTC will define a particular field of trade and analyze competitive effects and what review process the JFTC will pursue. The amended M&A Guideline introduces several concepts already adopted in the United States and European Community and clarifies the factors to be analyzed in the JFTC's review process.

Under the amended M&A Guideline, it can be expected that the analytical process of the JFTC will be closer to those of the United States and European Community and hopefully the transparency of the review process will improve given the framework for analysis provided by the amendment.

As the JFTC has been concerned with securing consistency with competition policy adopted by foreign competition authorities, the amendment is in line with the current policy trend held by the JFTC. The amendment can also be said, to a degree, to respond to the two major requests of Japanese business. However, how strictly the JFTC will follow the amended M&A Guideline especially in finding a particular field of trade

is still unclear. Despite the adoption of the SSNIP test, the finding of a particular field of trade has not changed, which indicates a particular field of trade could be still defined narrowly as before. In that case, the amendment may not provide as much harmonization with U.S. and EC competition policy rules as expected.