ALERT MEMORANDUM

German Parliament Passes Powerful New Toolkit for Competition Agency

17 July 2023

Introduction

On July 5, 2023, the German Parliament (*Bundestag*) passed the Competition Enforcement Act, amending the German Act Against Restraints of Competition ("**ARC**") for the 11th time ("**11th Amendment**"). This comes only two and a half years after the last significant amendment in 2021, which granted the Federal Cartel Office ("**FCO**") unprecedented investigative powers. The 11th Amendment once again equips the FCO with additional enforcement powers.[1]

There were only minor changes to the draft government bill prior to the final vote in the German Parliament. More fundamental changes had been made to the first draft prepared by the Ministry of Economic Affairs and Climate Action ("**first draft**") in response to concerns voiced in the public and academic debate.

The government bill must still be submitted to the *Bundesrat*, Germany's second legislative body, which convenes on September 19, 2023. We therefore expect that the new law will not enter into force before the end of September 2023.

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[1] 11th Amendment to the ARC, *Gesetzes zur Änderung des Gesetzes gegen Wettbewerbsbeschränkungen und anderer Gesetze*, as of July 5, 2023, only available in German here.

Background

The 11th Amendment includes the following three main changes:

— First, and most remarkably, the FCO receives the power to intervene in the aftermath of a sector inquiry to remedy identified disruptions of competition, for example parallel pricing behavior by market participants in an oligopolistic market with market transparency (so-called tacit coordination). This is essentially a kind of New Competition Tool similar to the one recently considered by the European Commission ("**EC**")[2] and the UK's market investigation tool.

  The introduction of the German New Competition Tool constitutes a paradigm shift: The FCO can currently only intervene if it establishes an infringement of competition law (cartel or abuse of dominance). The German New Competition Tool enables the FCO to impose both behavioral and structural measures without the actual occurrence of a competition law infringement or any individual wrongdoing of a company.

  It is noteworthy that the three-party government's proposal found the necessary support, given that earlier initiatives to introduce this type of power for the FCO had to be withdrawn due to lack of consensus.

— Second, the new law empowers the FCO to assist the EC in the enforcement of the Digital Markets Act ("**DMA**")[3] and, at the same time, extends the Damages Directive to cover private enforcement of the DMA in Germany.

— Third, it facilitates disgorgement of economic benefits derived from a violation of the competition law rules by the FCO, which could be useful in situations where follow-on private damages claims are unlikely.

Introduction of German New Competition Tool

The German New Competition Tool provides for a two-step process. Once the FCO has concluded an in-depth inquiry into a specific business area or sector by a final report, the FCO may first issue an order to one or several undertakings identifying "*significant and persistent distortion of competition*". In a second step, the FCO may order remedies.

(1) Order identifying distortion of competition

First, the FCO must identify "*significant and persistent distortion of competition*" in at least one market that is at least nationwide, several individual markets or across markets.

The terms "*distortion of competition*" and "*persistent*" have been clarified in the final version of the 11th Amendment after significant concerns were raised in the public debate by business, academia and private practice regarding the vast new powers of the FCO and the lack of well-defined use cases.

The definition of "*distortion of competition*" now includes examples of theories of harm such as (1) unilateral supply or demand power, (2) restrictions on entry, exit or capacity of firms or on switching to another supplier or buyer, (3) tacit coordination, or (4) input or customer foreclosure through vertical relationships. The FCO will have to consider multiple criteria in its assessment such as (1) the number, size, financial strength and turnover of the undertakings concerned, their market shares and the degree of concentration of undertakings, (2) interconnection between the undertakings on upstream, downstream, and neighboring markets, (3) prices, quantity, choice for end users and quality of the products or services, (4) transparency and homogeneity of goods, (5) agreements between undertakings, (6) market dynamics and (7) efficiencies on the concerned markets.

[2] *Cf.*, Single Market – new complementary tool to strengthen competition enforcement – public consultation, abandoned 23. June 2023, available in English here.

[3] Regulation (EU) 2022/1925 of the European Parliament and of the Council of 14 September 2022 on contestable and fair markets in the digital sector and amending Directives (EU) 2019/1937 and (EU) 2020/1828 (Digital Markets Act).

A distortion of competition is considered "*persistent*" if it "*existed permanently over a period of three years*" or "*occurred repeatedly*" and there is no indication that the distortion is likely to cease within two years. This generally excludes the situation of start-ups that may initially enjoy first-mover advantages as a consequence of their innovative offering—until imitators and new market entrants exercise increased competitive pressure.

The new rules require the FCO to show that its other powers of intervention appear not to be "*sufficient to effectively and permanently eliminate*" the distortion of competition. The explanatory note in the government bill clarifies that the FCO can rely on a "*cursory review*" and does not need to conduct a further investigation to substantiate its prognosis. It remains to be seen how and at what level of detail the FCO will show the insufficiency of other proceedings in practice.

(2) Remedies

The FCO may impose any behavioral and structural remedies necessary, including that companies: (1) grant access to data, interconnections, networks, and other facilities, (2) provide specifications on the business relationship between undertakings on the concerned markets (*e.g.*, ordering the termination of a supplier relationship or to pass on administrative licenses), (3) create transparent, non-discriminatory and open norms and standards through undertakings, (4) use certain contracts or contractual terms, including rights to disclosure of information (*e.g.*, to establish customer service management or to limit the contract period), (5) do not unilaterally disclosure information, which may favor coordinated behavior, (6) organizationally separate company or business divisions.

As a last resort (*ultima ratio*), the FCO may even order the divestment of shares or assets with a view to changing an unfavorable market structure. Addressing concerns raised in the public and academic debate on the first draft, the final version of the new law includes additional safeguards restricting the FCO's power in this regard:

— Only companies that either hold a dominant market position or have already been designated—by separate decision—as undertakings with paramount cross-market significance pursuant to Section 19a ARC may be ordered to divest assets and shares.

— Assets must only be sold if the sales price amounts to at least 50% of the value, determined by an independent auditor. If the actual sales price remains below the value determined by the auditor, the company is entitled to additional compensation from the German Government amounting to half of the difference. The introduction of this rule—*i.e.*, requiring the German Government to participate in any loss in value resulting from any forced divestment—is intended to prevent an excessive use of the divestment option.

— A company cannot be required to divest assets if their acquisition was cleared in merger control proceedings by the FCO or the EC less than 10 years ago (in comparison to five years in the first draft).

As a procedural safeguard, the new law obliges the FCO to hold a public oral hearing, which is exceptional in German competition law, before imposing any remedies. The Federal Network Agency must approve any remedy imposed on an undertaking in a regulated sector (railways, postal services, telecommunications, electricity, and gas). An appeal against the remedies imposed by the FCO will have suspensory effect.

(3) Power to call-in mergers

The new law further empowers the FCO to demand that undertakings active in the relevant markets of the Sector Inquiry notify any mergers provided that the acquirer's turnover exceeded EUR 50 million and the target's turnover exceeded EUR 1 million in Germany in the last financial year. The FCO order is valid for three years and may be extended up to three times by three more years each. The thresholds of this new call-in function for mergers are lower than those of a similar provision introduced with the 10th Amendment to the ARC in 2021.

(4) Timeline

The FCO should issue any orders under the German New Competition Tool within 18 months of the publication of the final sector inquiry report.

Enforcement of the DMA

While the EC remains the central public enforcement authority of the DMA—a law intended to regulate large digital gatekeepers—the new German rules authorize the FCO to assist the EC by reviewing compliance with Articles 5-7 of the DMA. Based on the new law, the FCO may initiate an investigation and even publish its reports on a company's compliance with the DMA before handing over the case to the EC. Although Article 38 (7) DMA expressly provides for this power of national competition authorities and only requires prior notification of the EC, the DMA only foresees the information of the EC by the national authority about the results of its investigation in order to support the EC; the issuance of a public report arguably goes beyond this supportive role. It remains to be seen if this will be viewed as an interference with the EC's investigative powers, especially if the FCO takes a divergent view to the EC on what constitutes non-compliant behavior, even if the report is marked as a "preliminary result". The German legislator emphasizes that it does not believe that the FCO's new investigative powers conflict with the EC's sole enforcement power of the DMA.[4] In light of Article 38 (7)(2) DMA, the FCO will be relieved of its jurisdiction if the EC opens its own investigation, even if the new law does not refer to this limitation.

On top of public enforcement by the EC, the DMA is directly applicable and enforceable by private parties in national courts, provided that they can derive rights and obligations from the DMA's rules. In order to facilitate the private enforcement of the DMA in Germany, the 11th Amendment extends the provisions transposing the Damages Directive[5] to the DMA where appropriate. This includes declaring the EC's designation decision and subsequent non-compliance decisions binding for national courts, tolling the statute of limitations during non-compliance investigations and enabling the participation of the EC and the FCO as *amicus curiae* in national private enforcement actions.

In private enforcement, there also remain some open questions since, under the DMA, the EC has a margin of discretion to interpret the gatekeepers' obligations. Third-party standalone claims may conflict with this discretion unless private enforcement actions are put on hold until the EC reaches a decision.

Disgorgement of Profits from Competition Infringements

The FCO has been able to order the disgorgement of profits derived from the effects of a cartel since 1999. However, it has never made use of this power. This is most likely, in part, due to the difficulty of calculating the economic benefits derived from the infringement.

To make this tool more effective, the 11th Amendment provides a presumption that will shift the burden of proof from the FCO to the company: The new law presumes that a company obtains an economic benefit of at least 1% of its domestic turnover with the affected product over the entire duration of a competition law infringement. Companies can only rebut the presumption if the "*obtaining of an advantage is excluded due to the special nature of the infringement*" or if the profits of the corporate group worldwide are less than the 1% of the domestic turnover with the products at issue. Within a period of up to seven years as of the termination of the infringement, the FCO can order the disgorgement for a maximum duration of five years and up to a maximum amount of 10% of the company's annual turnover in the preceding year.

Key Takeaways

The 11th Amendment further strengthens the FCO's powers, in particular due to the German New Competition Tool, which enables the FCO to impose behavioral or structural remedies without finding a competition law infringement. While the threshold for such interventions has been raised over the course of the legislative process, the German New Competition Tool is still a sharp sword. It will be interesting to see whether and how aggressively the FCO will use it, and how the interaction with

[4] Explanatory note in the government bill, BT-Drs. 20/6824, p. 36, only available in German here.

[5] Directive 2014/104/EU of the European Parliament and of the Council of 26 November 2014 on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, OJ L 349/1.

traditional infringement proceedings and the FCO's powers with respect to companies with paramount cross-market significance will play out.

As things stand right now, one limitation to an extensive use of the German New Competition Tool may be the FCO's resources. Andreas Mundt, the president of the FCO, explained in a press conference on July 11, 2023, that the FCO will have to balance its resources and decide what they can and cannot do in light of the fact that the FCO does not receive additional budget to hire new staff to assist in implementing the German New Competition Tool.[6]

We consider it likely that companies subjected to the German New Competition Tool will challenge the tool in court due to the significant consequences the FCO's orders may have and because some doubts remain on whether the tool complies with Regulation 1/2003 and European merger control.

A number of open issues also remain with regard to how the FCO's support of the EC's DMA enforcement will work in practice. It is no secret that the FCO was dissatisfied with its limited role in public enforcement of the DMA. This suggests that it will make use of its new investigative powers and not shy away from qualifying relevant practices by gatekeepers in its public report before handing over the case to the EC.

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[6] *See* https://app.parr-global.com/intelligence/view/intelcms-kkg793.