Antitrust & Competition practice In Israel

A practical guide by BDO Consulting Israel

BDO

M&A activity has significant economic benefits. However, it may also have a negative impact on competition and for the consumer. Therefore, most countries have enacted antitrust laws that enable regulators to block mergers that have a detrimental effect on competition.

There is a definite advantage in negotiating by having advance knowledge and understanding of anti-trust legislation in the target country.

In Israel, M&A transactions fall under the provisions of the Restrictive Trade Practices Law (RTPL) which requires foreign companies that operate directly or indirectly) in Israel to obtain prior approval from the director general of Israel's Antitrust Authority (IAA) if the merger exceeds certain scale or with certain characteristics.

The IAA examines over 160 mergers annually. In roughly 13% of the cases, one or both parties were foreign bodies. On average, the IAA blocks 3 proposed mergers and issues conditional approval to five more a year. The deliberation process runs on average around 26 days.

We have drawn up a user-friendly guide of the main provisions of the RTPL that could have an impact on M&A transactions in Israel. The guide includes a brief description of the IAA's activity and the deliberation process prepared by BDO's antitrust and competition team together with antitrust lawyers from leading law firms in Israel.

The competition and antitrust team is part of office of the chief economist at BDO Consulting Israel and advise foreign companies operating in Israel and abroad. Among clients we have advised are Germany's Axel Springer media group, investment banks HSBC and Goldman Sachs, pharmaceutical companies Teva and GlaxoSmithKline to name just a few.

We would be happy to assist both you and your clients with business activities in general and with competition and antitrust issues in particular. Please feel free to distribute this guide to your clients and do not hesitate to contact us for additional background.

Yigal Toledano, partner
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Mergers Review in Israel

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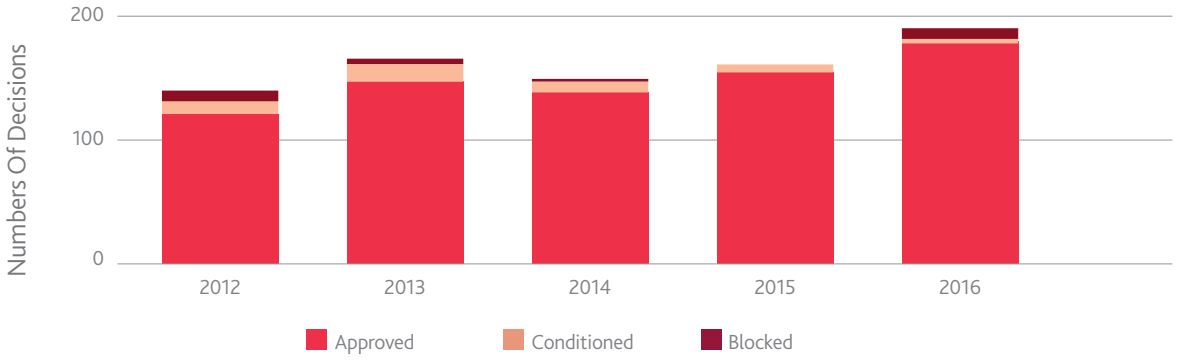
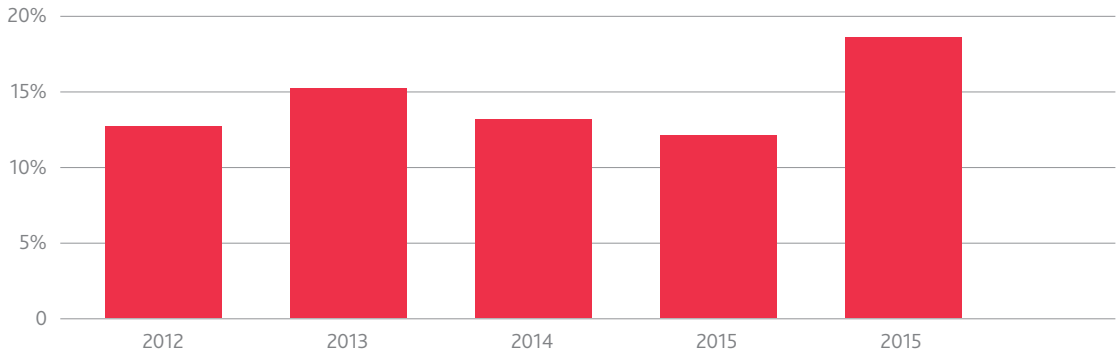
In 2016 the Israel Antitrust Authority (IAA) issued decisions on 192 proposed mergers. The vast majority, 183 were approved unconditionally. Four were blocked; two others were withdrawn after the IAA stated its objections and three were granted conditional approval.
The trend in recent years has been similar.

Merger decision distribution 2012-2016



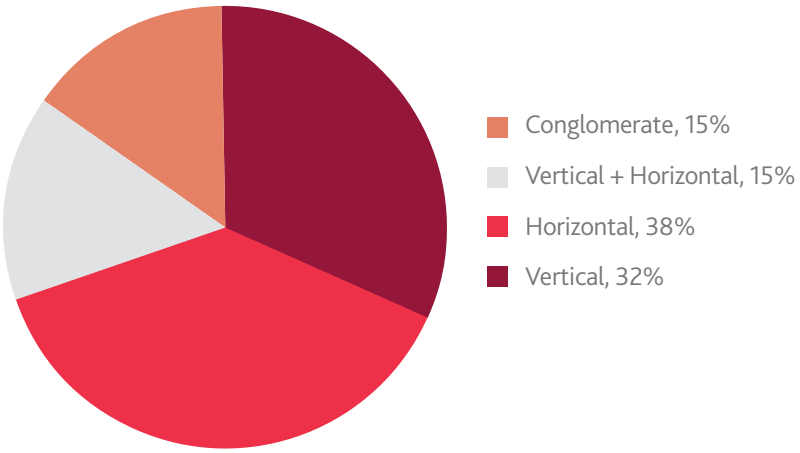
Mergers that include at least one non-Israeli company comprise an average of 13% of all mergers reviewed by the IAA.
Mergers involving an international company:

Mergers Involving non-Israeli company:



The IAA issued its decision on average within 26 days. However, the duration of the review varied in accordance with the type of merger and the concerns over competition in the particular sector.
More than half of the mergers reviewed by the IAA in 2016 were deemed horizontal in nature, namely between direct competitors.

Distribution of mergers by type



The IAA reviews horizontal mergers according to the following guidelines:

Market Definition:

The IAA defines the relevant market based solely on demand-side substitution using the Hypothetical Monopolist Test. In most cases, the IAA will apply the test based on the use of qualitative information (functional identity, prices etc.). When possible, critical loss analysis will also be used.

When defining relevant markets DG COMP also relates to supply-side substitution. Therefore, markets as defined by the IAA may be narrower in scope than those defined under DG Comp.

Market Participants:

Market participants will be companies that currently operate in the market and companies that have invested the majority of the sunk cost necessary to do so. Potential competitors will be deemed companies that are very likely to enter the market due to price increases.

Market shares:

The IAA usually calculates market share based on the financial results in the two years that precede the proposed merger. In special cases, the IAA will calculate market share according to projected annual results, reserves, tender filings, peak production capacity and other factors.

Concentration indices:

Generally, the IAA measures the level of concentration in a particular market using the Herfindahl-Hirschman Index (HHI) and the Concentration Ratio Index (CR). A post-merger HHI that does not exceed 2,500 points or pre-merger HHI of 2,000 points and a merger than will add less than 500 points will not usually raise competitive concerns. This is also the case when CR3 is less than 40% or when CR4 is less than 60%. However, the IAA can reject mergers with lower concentration levels.

FTC and DOJ set the bar for competitive concerns at a pre-merger HHI that exceeds 1,800 points and the merger adds another 50 points. By contrast DG COMP sets the level at a pre-merger HHI of over 2,000 points and a merger adding 150 points.

Unilateral Market Power:

When the market share of the merged firm is less than 50% the IAA will generally refrain from declaring that a unilateral market power exists, unless there is clear evidence that indicates the utilization of such market power. However, when the market share exceeds 50% unilateral market power is assumed to exist and the merging companies in this case should present evidence to contradict this assumption.

Notification of Mergers Involving a Foreign Company

Adv. Mazor Matzkevich and Adv. Niv Sever
M. Firon and Co.

Under the Restrictive Trade Practices Law, mergers of a certain scale or with certain characteristics require notification and approval from the Israel Antitrust Authority (IAA). Failure to obtain such approval prior to the merger taking place may result in both criminal and monetary penalties on directors and the corporations themselves.

A partial list of transactions that are likely be deemed a merger includes: acquisition of the principal assets of a company; acquisition of more than 25% of the issued share capital; 25% of the voting power; the power to appoint directors; or the participation in more than 25% of the company's profits. The acquisition may be direct, indirect or by means of a contract.
Acquisition of 25% or less of the above-mentioned rights may also constitute a merger if other forms of affinity exist between the parties in the form of loans or direct involvement in the management of the firm.

If a transaction is deemed to constitute a merger IAA approval will be required if one of the following conditions is applicable:

- The cumulative turnover of the merging entities in Israel in the preceding fiscal year exceeded NIS 150 million; and the turnover in Israel of each of at least two of the merging parties exceeded NIS 10 million.
- As a result of the merger, the market share of the merging entities would exceed 50% of any relevant market; or
- The market share of any of the merging entities (including an affiliated company) exceeds 50% of any relevant market.

A merger involving a foreign company will also require the IAA's approval if each of the merging parties meets any of the following conditions:

- If the foreign entity is also registered in Israel; or,
- If the foreign entity has a 'merger affiliation' with an Israeli company, which includes, inter alia, holding or having rights to more than a quarter of: the issued share capital, voting power, power to appoint directors, the profits - in respect of an Israeli company;
- If the foreign entity maintains a place of business in Israel, or if it holds a significant influence over the conduct of a local representative.

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Fast Track for Review and Approval of 'Ultra Green Mergers'

FBC&Co
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פישר בכר חן וול אוריון ושות'

Adv. Ziv Schwartz
Fischer Behar Chen Well Orion & Co.

In 2016, the Israel Antitrust Authority (IAA) initiated a 'fast-track' review and approval procedure of mergers that do not raise competitive concerns. According to the procedure, a merger that clearly does not present a threat to competition will be granted an internal classification by the IAA of an 'Ultra Green Merger'. The proposed merger will be examined in an abbreviated proceeding and the IAA will make the decision regarding the merger within a significantly shorter period than the 30-day limit that Israeli law specifies.

According to the IAA, this procedure is meant to achieve three main goals: first, to focus the IAA's resources and second to reduce the burden on the notifying parties submitting the merger notices and finally to cut the waiting period for receiving the IAA's decision. IAA data for 2016 showed that on average decisions approving mergers that met the 'Ultra Green Merger' requirements were issued in five days or less.

To qualify for the 'fast-track' procedure, the merging parties must meet the following requirements:

1. Submission of full merger notification instead of the abbreviated form that contains only limited details.

2. If possible, the merger notices should specify and expand on relevant information for analyzing the impact of the transaction on competition. To the extent this is possible the information should be objective and supported by objective data.

3. The CEO of the submitting party is required to sign off on the merger notification and if it has an internal legal counsel, he or she is also required to sign the merger notification.

4. Along with the submission of the merger notification, the parties to the merger must provide their holding structure, that includes complete details on the direct shareholders of each party and on the controlling entities of every direct shareholder from each party involved in the merger.

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Remedies Affixed by the IAA in Conditional Approvals of Mergers

Adv. Zohar David
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When drafting an acquisition, parties often tend to overlook the important issue of conditional approval of the transaction. An early assessment of the possible remedies can prove valuable in preventing limiting conditions, and in turn maximizing the deal's profitability.

The preferred remedies of the Israel Antitrust Authority (IAA) are structural conditions such as the disposition of assets. These conditions may force the acquiring party to sell considerable assets, including secondary assets (client lists, propriety rights, knowhow etc.), within a limited timeframe, often less than a year. The IAA prefers the acquirer sell off an independent economic entity rather than specific assets, with the buyer usually requiring the approval of the IAA.

The IAA views behavioral conditions as inferior since they are aimed at structural changes that enable the abuse of market power (price increases, productivity reduction or limiting product variety or quality) and not the formation of a control regime. Therefor their use is limited to specific situations, such as competitive concerns tied to specific behavior or that is expected to become irrelevant in the short-term as the result of regulatory changes or similar events. The IAA usually refrains from complex, long term conditions, preferring clear behavioral conditions that allow for the easy detection of violations by third parties.

That said the IAA recently forced a company to offer sale prices and special terms as a precondition for approving a merger. This policy was imposed following a statement in the media by an official of the acquired company in which he expressed his opinion on market prices.

Additional conditions include the transfer of knowhow to third parties (including competitors) or making it publicly available, conditions related to legal rights including the waiving of rights or allowing the use of rights. When doing so, it is important to remember the purpose of conditional approval, which is primarily the retaining of the level of competition that existed prior to the transaction.

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Disclosure of information during due diligence conducted prior to a transaction between competitors

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Disclosure of information during due diligence between competitors carries a risk of reduced competition and the creation of a restrictive arrangement.

The Israel Antitrust Authority (IAA) addresses the issue in an option dated May 19, 2014 (opinion).The opinion provides guidelines for conducting due diligence, for identifying sensitive information relating to competition and for managing the disclosure by minimizing the risk of injury to competition.

The more sensitive the disclosed information in terms of competition, or the more the transaction itself raises concerns of reduced competition, the level of caution required by the parties is heightened. The parties should make sure that disclosure is essential to the due diligence process, the volume of information transmitted is minimized and they take all necessary measures to minimize concerns over reduced competition.

In general, the IAA's guidelines consist of inter alia, rules of conduct regarding the process of disclosing information, documentation and the content of the disclosed information.

For example, disclosing information shall be subject to a non-disclosure undertaking. As much as possible, aggregate information should be transferred that does not allow the extraction of specific details through 'reverse engineering' providing that the disclosed material is minimum required to comply with the due diligence process.

Inspection of competitively sensitive information shall be carried out by an external entity that is not connected to or employed by the receiving party, and transferred to the receiving party at the 'bottom line' level.

Where there is a practical need to inspect competitively sensitive information, the receiving party may be assisted by its employees who do not engage in pricing, marketing or sales of competing products and at a 'bottom line' level.

Where there is a practical need to disclose competitively sensitive information to employees of the receiving party, who are involved in pricing, marketing or sales, a 'clean team' composed of a small number of employees who will upon exposure to the information be excluded from making decisions in these key areas for a sufficient period of time. The 'clean team' shall transfer information to the team handling the merger at the 'bottom line' level.

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Competition Law Aspects of Joint Financing in Israel

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Joint lending or joint financing is a common phenomenon in the world of finance. Joint lending is often organized by one entity (the arranger) who brings together and conducts the negotiations with the other lenders. This allows for the smooth procession of projects or acquisitions, which are in many cases too large for a single entity to finance. Joint financing also saves transaction costs, reduces credit risks and thereby allows the lenders to offer better credit terms.

Nonetheless, joint financing, by way of a consortium or in any other form, brings together entities that typically compete with each other in the financial markets. The Israel Antitrust Authority (IAA) holds the position that such joint lending may amount to a 'restrictive arrangement' as defined in the Restrictive Trade Practices Law (RTPL).

The IAA accepts that joint lending has significant benefits for both the lenders and the borrowers. Consequently, the IAA allows most joint lending agreements to proceed unchallenged.

The issue up to now has been dealt with by the IAA through a series of no-action letters (known as 'consortium letters') which limited joint lending by Israel's two largest banks-Hapoalim and Leumi-or required a specific exemption for such joint lending. The 'consortium letters' also required annual reporting from entities relying on the 'consortium letters'.

For the first time in 2015, the IAA expressly applied its 'consortium letters' policy to financial entities incorporated outside Israel.
More recently, in May 2017, the IAA issued a draft block exemption for joint lending (now termed 'syndication loans'). The draft forgoes the burdensome reporting requirements of the 'consortium letters'. The draft's numerous provisions will limit the ability of potential arrangers and the ability of large lenders (with greater than 20% of the Israeli market) to be parties to the same lending agreement.

Current Situation	Contemplated Block Exemption
Annual reporting of any joint lending transaction	No reporting requirement
Specific exemption for any transaction involving both largest Israeli banks.	Two largest Israeli banks will be able to participate without specific exemption if their part is lower than 20%.
Borrower must agree in advance for the arranger to involve additional lenders.	No Change
Borrower must be allowed to negotiate separately with each lender.	No Change

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BDO Consulting Israel provides clients guidance and consultancy on antitrust issues, including competition, restrictions imposed on business activity, and regulation, vis-à-vis antitrust and regulatory authorities as well as the business sector.

Our professional experience includes representing companies and organizations vis-a-vis government authorities and the business sector. This includes representation in the framework of legislation and regulation, mergers and acquisitions, hearings, arbitrations and legal proceedings, trade agreements, joint ventures and more. We have extensive knowledge and are closely acquainted with a wide range of industrial and service sectors such as communication, food, chemicals, energy, health, aviation, infrastructure, consumer products, environment and additional fields. Our work includes developing economic solutions for various issues in the specific field or activity required with a focus on precise and target-directed research and analysis based on up to date economic theory, empiric data and the latest professional studies.

The firm's consulting and support services, coupled with the solutions we place at the client's disposal can greatly assist them in assessing various business operations and opportunities.

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