Sony BMG joint venture saga – ECJ *hits* CFI *one more time*

In a ruling dated 10 July 2008, the European Court of Justice (**"ECJ"**) set aside the judgment of the European Court of First Instance (**"CFI"**) relating to the Sony BMG joint venture.[1] The ECJ ruling goes against the non-binding Opinion of its Advocate General, Juliane Kokott, who said in December that the ECJ should uphold the CFI's judgment.[2] It is not very often that the ECJ disagrees with both its Advocate General and the CFI.

This Client Alert summarises the background of the ECJ ruling, its potential impact on the Sony BMG joint venture, and its wider implications for the application of the European Merger Control Regulation (**"ECMR"**)[3] to future transactions.

In summary, the ECJ ruling clarified the following two points of procedure and one point of substance:

- First, there is no general presumption that a notified transaction must be cleared unless the Commission can prove to the requisite standard that the transaction significantly impedes competition. Accordingly, a clearance decision by the European Commission (**"Commission"**) is subject to the the same burden and standard of proof as a decision by it to prohibit a transaction.
- Second, the Commission is not obliged to explain any differences between its preliminary findings in the Statement of Objections (**"SO"**) and its final decision, when, in their reply to the SO, the parties provide sufficient evidence to discharge the Commission's provisional concerns. Moreover, the Commission is not required to market test the new evidence adduced by the parties, due to the tight timetable for the ECMR procedure.
- Third, the Commission had met the relevant standard of proof in finding that, at the time of the contested decision, recorded music markets, and in particular campaign discounts for recorded music, were *not* transparent enough to allow major music companies to monitor any deviations from the terms of the tacit collusion which the Commission had originally alleged in its SO.

1 Case C-413/06 P, *available at* http://www.curia.europa.eu.
2 Opinion of Advocate General Kokott in Case C-413/06 P, *available at* http://www.curia.europa.eu.
3 **Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings,** OJ 2004 L 24, p.1.

On the one hand, the ECJ ruling on the substance of the case should assist Sony BMG and other major music companies to devise their legal strategy, as the recorded music industry moves towards further consolidation. On the other, the procedural implications of the ruling will likely go beyond this particular sector.

Background

On 20 July 2004, the Commission authorised the creation of the joint venture Sony BMG, combining the recorded music divisions of Sony Corporation and Bertelsmann AG. After examining the proposed transaction, the Commission found that it would not create or reinforce a collective dominant position with the other music majors (Universal, Warner and EMI).[4] Impala, an international association of independent music production companies, challenged the Commission clearance decision before the CFI.

On 13 July 2006, the CFI concluded that the Commission clearance decision was vitiated by manifest errors of assessment and was inadequately reasoned.[5] In doing so, it referred the case back to the Commission for a new examination. This was the first time the CFI had quashed a Commission clearance decision.

On 3 October 2007, after a new investigation, the Commission cleared the Sony BMG joint venture once again.[6] In doing so, the Commission said it has performed "one of its largest and most complex econometric analysis so far in the context of a merger investigation". The new clearance decision also assessed the market for the licensing of recorded music in digital format, which was nascent at the time of the Commission 2004 investigation.

On 14 June 2008, Impala challenged the Commission's second clearance decision before the CFI and this case is currently pending.

In the meantime, Sony and Bertelsmann have created their joint venture, following the two approvals from the Commission.[7]

The ECJ ruling

In its recent ruling, the ECJ found that the CFI committed an error of law in concluding that the Commission had failed to comply with the duty to provide an adequate statement of reasons for its first clearance decision.

In that regard, the ECJ noted that the contested decision showed the reasoning followed by the Commission in a way which subsequently allowed a party such as Impala to challenge its validity before the CFI. Furthermore, the CFI was aware of the reasons for which the Commission decided to approve the concentration and devoted numerous paragraphs in its judgment to the analysis of whether those reasons were well founded. It could not therefore be claimed that it was impossible for the CFI to exercise its power of judicial review (para. 180-181 of the ECJ ruling).

Accordingly, the ECJ referred the case back to the CFI. In so doing, the ECJ established the following principles of law that are binding on the CFI.

4 **Commission Decision 2005/188/EC of 19 July 2004 (Case COMP/M.3333 – Sony/BMG) OJ 2005 L 62, p. 30.**
5 **Case T-464/04** *Impala v Commission* [2006] ECR II-2289.
6 See Commission official press release IP/07/1437, *available at* http://europa.eu/rapid/.
7 See http://www.sonybmgmusic.co.uk.

The principles of law established by the ECJ

The ECJ ruling clarified the following principles of law which will have implications not only for this case but also for future cases under the ECMR:

Standard of proof and statement of reasons

In its ruling, the ECJ established that there is no general presumption that a notified transaction is compatible with the ECMR. Accordingly, the Commission is subject to the same burden and standard of proof whether it prohibits or approves a proposed transaction (para. 52-53 and 174-175 of the ECJ ruling).

It has always been in the interest of the merging parties to prepare their Form CO and subsequent submissions in such a way that would assist the Commission to draft a decision which sufficiently states the reasons for clearance, particularly in cases where there is a third party complainant. This case demonstrates the importance of doing so.

Provisional findings in the SO

The ECJ established that, in its final decision, the Commission may depart from the provisional findings made in its SO, when the parties supplement or clarify their case in their reply to the SO (para. 75-76 of the ECJ ruling).

It should now be easier for the Commission to issue an SO in merger cases, where it has doubts, without having to revert to the parties regarding issues in their reply to the SO.

The parties may submit additional evidence after the SO

The ECJ established that the Commission is not required to undertake additional market investigations to corroborate the parties' submissions in their reply to the SO, and may reasonably rely on such submissions in the light of the evidence currently on its file at that stage of the proceedings (para. 94-95 of the ECJ ruling).

Depending on the strategy adopted, each party may therefore want to be judicious regarding the timing of the provision of information by it if it suspects that the notification is heading towards an SO.

Collective dominance

It is established case law that a collective dominant position may arise where, in view of the actual characteristics of the relevant market, the concentration would make it possible and economically rational for each member of the oligopoly to adopt on a lasting basis a tacit coordination policy on the market with the aim of selling at above competitive prices (para. 122 of the ECJ ruling).

In *Airtours plc v Commission*,[8] the CFI had established the following cumulative conditions for a finding of a collective dominant position:

- transparency of the market that allows the oligopolist players to detect cheaters of tacit collusion;
- deterrent mechanism that allows the oligopolist players to retaliate against cheaters; and
- absence of fringe competition or customers' buying power.

The ECJ has now established that, in applying these conditions, the Commission ought not to apply them mechanically in an endeavour to verify each of them separately. The Commission ought to apply the *Airtours* doctrine within the context of the overall economic mechanism of a "hypothetical tacit coordination" (para. 125 of the ECJ ruling).

This is an important clarification of how the Airtours doctrine ought to be applied.

8 **Case T-342/99,** *Airtours plc v Commission*, [2002] ECR II-02585.

Transparency

The ECJ established that assessing the transparency of a particular market requires the Commission to take into account "the monitoring mechanisms that may be available to the participants in the alleged tacit coordination in order to ascertain whether, as a result of those mechanisms, they are in a position to be aware, sufficiently precisely and quickly, of the way in which the market conduct of each of the other participants in that coordination is evolving" (para. 126 of the ECJ ruling).

In this case, the Commission found that the numerous and imprecise rules governing campaign discounts for recorded music would render their application complex and therefore not particularly transparent. The ECJ ruled that the burden to prove the contrary lies with the third party complainant (i.e., Impala).

Reliance on non-disclosed evidence

In examining the transparency of campaign discounts, the CFI referred to a number of documents submitted by Impala, which were classified as confidential. The appellants claimed that the CFI erred in law by relying on evidence that was not before the Commission and which had not been disclosed to them.

The ECJ held that the information in question was not disclosed in good time and in a sufficiently precise and clear manner to allow the notifying parties to reply effectively on the inferences which Impala drew from it. The Commission would not have been able to rely on such documents as it can base its decisions only on objections which the parties have been able to respond to. The CFI therefore committed an error of law in relying as a basis for annulling the decision on documents submitted by Impala which the Commission could not have used as a basis for adopting its decision (para. 102-103 of the ECJ ruling).

Concluding remarks

The Sony BMG joint venture has been approved twice by the Commission and both clearance decisions have been challenged and are currently pending before the CFI. It would be logical for the second approval decision to be stayed pending the result of the first, original appeal.

The ECJ ruling arguably gives Sony BMG some legal certainty. The fight is not yet over: the next stage of this saga is set to continue in the CFI.

The Antitrust & Competition Group of the London Office of Mayer Brown International LLP has a wealth of experience representing clients in all types of competition law proceedings. If you have any questions about the above news item, or would like to discuss any aspect of your own business conduct in confidence, please contact Frances Murphy or Gillian Sproul:

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