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The Extraterritorial Application of German Antitrust Law

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THE EXTRATERRITORIAL APPLICATION OF THE GERMAN ANTITRUST LAWS

*By David J. Gerber**

The extraterritorial reach of national economic regulation, particularly of antitrust laws, is one of the most controversial topics in the international legal community, largely because that community has failed to develop jurisdictional principles that both accommodate the regulatory needs of regulating states and are discriminating enough to avoid impinging on the legitimate interests of other states. As a result, international conflicts related to the assertion of jurisdiction have greatly increased in both frequency and intensity.[1]

Assertions of extraterritorial jurisdiction by the United States have been the focal point of the controversy. Until the 1970's, the United States was the only country with both well-developed and strictly enforced antitrust laws and a legal regime permitting broad application of those laws to foreign conduct. Consequently, it was the only country with significant experience in applying antitrust provisions to conduct occurring outside its territorial boundaries.

Outside the United States, the extraterritoriality issue has been seen largely in a defensive context—namely, how to respond to excessive jurisdictional claims by the United States. These problems have reached critical dimensions. While American courts and commentators flail about in search of principles to use in grappling with jurisdictional issues,[2] major allies have ceased trying to cooperate with the United States to avoid excessive conflicts of jurisdiction and have turned to so-called blocking legislation to attempt to protect their nationals and enterprises from the reach of United States antitrust laws.[3]

The extraordinary difficulties that American law has encountered in this area may be ascribed to two major causes: (1) an inability to define more clearly and concretize the "effects" principle, which is the basis for extending American jurisdiction over foreign conduct; and (2) a failure adequately to take into account the sovereign interests of other states.

Recent West German law developments illuminate the dimensions of these two problems and provide guideposts toward useful solutions. In recent years,

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[1] *See, e.g.*, Samie, *The Extraterritorial Enforcement of United States Antitrust Laws: The British Reaction*, 16 INT'L LAW. 313 (1982).

[2] *See, e.g.*, Timberlane v. Bank of America, 549 F.2d 597 (9th Cir. 1976); Mannington Mills, Inc. v. Congoleum Corp., 595 F.2d 1287 (3d Cir. 1979); and Dominicus Americana Bohio v. Gulf & Western Indus. Inc., 473 F.Supp. 680 (S.D.N.Y. 1979).

[3] *See, e.g.*, Lowe, *Blocking Extraterritorial Jurisdiction: The British Protection of Trading Interests Act*, 75 AJIL 257 (1981); Toms, *The French Response to the Extraterritorial Application of United States Antitrust Laws*, 15 INT'L LAW. 585 (1981); Herzog, *The 1980 French Law on Documents and Information*, 75 AJIL 382 (1981).

German antitrust provisions have become stricter in many respects than their United States counterparts, and, especially in regard to international mergers, they are enforced at least as vigorously as are U.S. laws. Moreover, the extraterritorial reach of German antitrust law is, at least arguably, longer than that of U.S. antitrust law. Germany's experience is thus highly relevant to the American dilemma, especially because German law has taken important steps to alleviate the two above-mentioned causes of the American difficulties. Specifically, Germany has placed conceptual limits on the "effects" principle and used public international law to devise means of taking into account the interests of countries affected by extraterritoriality.

This article therefore has two main purposes: to describe the extraterritoriality issue in the German context,[4] and to relate the German experience with extraterritoriality to the pressing need to find international law solutions to an issue laden with the potential for ever-increasing international conflict.[5]

I. The Context: German Antitrust Law

In order to understand the extraterritorial application of German antitrust law, it is important to be aware of several basic characteristics of the German antitrust law system.[6]

German antitrust law operates within the framework of the civil law tradition. The principles of law are generally to be found in the codelike structure of the Law against Restraints on Competition (the GWB) rather than in court decisions.[7] This statutory orientation of German antitrust law contrasts sharply with the lack of systematic structure in United States antitrust law. Moreover, it corresponds with a far greater role for the legislative branch in German antitrust law than is the case in the United States.

The basic principles on which the GWB is based, however, derive from American experience. As the first true antitrust statute in German history, the GWB became law in 1957 after years of careful study of U.S. antitrust law by German scholars. German antitrust law thus has a much shorter history

[4] Not to be forgotten here are the needs of practitioners who are, or should be, aware of the practical importance of understanding the reach of German antitrust law. Any company that participates in an acquisition or joint venture involving either a German company *or* a company that is doing business in the German market may find itself affected by German antitrust rules.

[5] The issue of the extraterritorial application of German antitrust law is both substantively and procedurally separate and distinct from the application of the antitrust law of the European Community. The provisions of the Treaty of Rome, however, have been interpreted to require that the actions of national cartel authorities may "not jeopardize the uniform application throughout the Common Market of the Community cartel rule." Wilhelm v. Bundeskartellamt, 1969 ECR 1, [1969–1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶8056, at 7867. *See also* B. HAWK, UNITED STATES, COMMON MARKET AND INTERNATIONAL ANTITRUST 476 (1979).

[6] For a detailed description of German antitrust law in English, see K. STOCKMANN & V. STRAUCH, FEDERAL REPUBLIC OF GERMANY, 5 WORLD LAW OF COMPETITION (J. Kalinowski ed. 1981). For a leading German textbook, see F. RITTNER, WIRTSCHAFTSRECHT (1979).

[7] Gesetz gegen Wettbewerbsbeschränkungen, 1957 Bundesgesetzblatt [BGBl] I 1081 (July 27) [hereinafter cited as GWB]. For a useful German-English presentation of the text of the statute as well as a short commentary, see A. RIESENKAMPFF & J. GRES, LAW AGAINST RESTRAINTS OF COMPETITION (1977, Supp. 1980).

than does American antitrust law, with the result that little, if any, of it is "cast in stone."

The administration of the antitrust laws in Germany—and thus the constellation of forces affecting the development of the law—is also significantly different from the American system. One major difference is the fact that there are relatively few private antitrust suits under the German system, although the statute permits such suits under certain circumstances.[8] This has particular importance for the extraterritoriality issue because it means that in most types of cases, including merger cases, the problems created by private suits, which have helped to confound American efforts in this area,[9] play little or no role.

German antitrust law is enforced primarily by a government agency, the Bundeskartellamt (Federal Cartel Office or FCO), which can issue orders prohibiting violations of the statute and setting fines for such violations. The decisions of the FCO have a distinctly judicial character. Its actions must be approved by organs within it that are charged with judicial impartiality. As a result, the decisions of the FCO are often accorded interpretive weight similar to that of judicial decisions.

The decisions of the FCO are appealable to the regular courts. Since the FCO is located in Berlin, appeals are made to the Federal Appeals Court for Berlin, the Kammergericht (KG). By virtue of this arrangement, the KG has taken on special importance in the antitrust area. In reviewing the decisions of the FCO, the KG and the Supreme Court for Civil Matters (Bundesgerichtshof or BGH) both view their roles as that of interpreters of the will of the legislature. They generally do not consider their roles as including the search for "lawmaking" solutions.[10]

II. THE STRUCTURE OF THE EXTRATERRITORIALITY ISSUE

The American attorney who attempts to understand the extraterritoriality issue in its German setting is immediately faced with a conceptual structure that can be misleading. Consequently, it is necessary to delve briefly into some of the differences in the structure of the extraterritoriality issue in the two legal systems.

In the United States the antitrust laws may be applied to conduct occurring outside the country whenever the court has *power* over the parties (jurisdiction in personam) as well as authority to adjudicate the subject matter. These two concepts of jurisdiction are seen as unrelated. The extent of personal jurisdiction is a domestic issue, measured primarily according to due process prin-

[8] Private suits are permitted in cases where there has been a violation of a provision that is intended to provide so-called individual protection (*Individualschutz*)—*i.e.*, protection of individual competitors rather than protection of the institution of competition itself. *See* GWB §35.

[9] Many of the recent American cases involving extraterritorial application of the antitrust laws have been private suits. *See Panel Discussion on Antitrust and International Trade,* 49 ANTITRUST L.J. 1217, 1221 (1980), and cases cited.

[10] *See generally* Rittner, *Das Ermessen der Kartellbehörde,* in FESTSCHRIFT FÜR HEINZ KAUFMANN 307 (1972).

ciples. It is not related to the question whether there may be international law limits on the right of American courts to apply American antitrust law extraterritorially, an issue usually treated within the context of subject matter jurisdiction.[11]

The role of public international law in the application of the American antitrust laws is vague and uncertain. In *United States v. Aluminum Co. of America (Alcoa),*[12] Judge Learned Hand stated:

> [W]e are not to read general words, such as those in this [Sherman] Act, without regard to the limitations customarily observed by nations upon the exercise of their powers. . . . We should not impute to Congress an intent to punish all whom its courts can catch, for conduct which has no consequences within the United States. . . . [W]e shall assume that the Act does not cover agreements, even though intended to affect imports or exports, unless its performance is shown actually to have had some effect upon them.[13]

Since Congress could not be presumed to have violated norms of international law, and since international law requires domestic effects as a basis for prescriptive jurisdiction over foreign conduct, the effects principle was incorporated in American law. The role of international law is thus indirect and framed in the context of congressional intent.

What, then, of situations where the effects principle provides a jurisdictional base, but the application of U.S. antitrust laws to foreign conduct could lead to conflicts with other nations? The answer in American law relies on the concept of comity.[14] American courts take the position that where the United States has a basis for the exercise of jurisdiction, it has a right to exercise that jurisdiction, and there is no further legal issue. Nevertheless, a court may decide, as a matter of comity, to refrain from exercising that right in cases of potential conflict.[15]

Under German law the conceptual structure of the extraterritoriality issue is fundamentally different.[16] The analysis centers on two main questions. First, does the relevant choice-of-law rule mandate the application of German law? And second, would the application of German law violate public international law?

In the antitrust context the relevant choice-of-law provision is section 98(2) of the GWB, which provides that the GWB is to be applied wherever a restraint of competition has domestic effects.[17] Thus, the effects principle is explicitly anchored in the GWB.

[11] *See generally* Ongman, *Be No Longer a Chaos: Constructing a Normative Theory of the Sherman Act's Extraterritorial Scope,* 71 NW. U.L. REV. 733, 735 (1977).

[12] 148 F.2d 416 (2d Cir. 1945).

[13] *Id.* at 444.

[14] *See generally* Yntema, *The Comity Doctrine,* 65 MICH. L. REV. 9 (1966).

[15] *See* Maier, *Extraterritorial Jurisdiction at a Crossroads: An Intersection between Public and Private International Law,* 76 AJIL 280 (1982).

[16] For a comparison, see I. SCHWARTZ, DEUTSCHES INTERNATIONALES KARTELLRECHT 154–57 (1962).

[17] For text, see text accompanying note 22 *infra.*

If the restraint of competition has the required effects, the next question is whether international law prohibits the application of the GWB to the particular circumstances of the case. This issue must be taken much more seriously by German courts than by their American counterparts, for the German Constitution mandates that general international law binds the legislature and the courts.[18] For years the requirements of international law were considered to have been met by virtue of the fact that the effects principle was an approved basis of jurisdiction under international law. This answer is no longer sufficient, however, and German law now requires that additional international law requirements be met that are designed to avoid conflicts with the sovereignty of foreign states.

Where the conflict-of-laws rule mandates the application of the GWB, and international law does not prohibit the exercise of jurisdiction, a German court will apply German antitrust law, provided that the court is "internationally competent" (*zuständig*).[19] The concept of international competence performs a function similar to that of the concept of personal jurisdiction in American law. It is not to be confused with the issue of the GWB's extraterritorial reach. It refers to the requirement that the court have a sufficient relationship to the facts of a given case to adjudicate the issues.[20] This is determined solely by reference to domestic law, which focuses on factors such as whether the defendant has sufficient contacts with the state to be subjected to its judicial power.[21]

III. THE "EFFECTS" CONCEPT CODIFIED AND PURIFIED

The focal point of the extraterritoriality issue in German antitrust law is easily located. The effects principle is codified in section 98(2) of the GWB: "This statute applies to all restraints of competition which have an effect within the territorial scope of the statute, even when they are caused outside of the territorial scope of the statute." The extraterritorial reach of the German antitrust laws centers on the construction and application of this provision.

The legislative history of section 98(2) is not extensive, but it leaves little doubt as to what the legislature intended.[22] According to the report of the committee of the federal legislature (Bundestag) that proposed the GWB, "The committee intends to achieve with the very general and broad version of the last half-sentence [of section 98(2)] that all restraints of competition that have domestic effects fall within the statute, regardless of where and by

[18] *See* GRUNDGESETZ art. 25 (W. Ger.).

[19] *See generally* G. KEGEL, INTERNATIONALES PRIVATRECHT, ch. 22 (4th ed. 1977); and J. SCHRÖDER, INTERNATIONALE ZUSTÄNDIGKEIT (1971).

[20] *See generally* A. HELDRICH, INTERNATIONALE ZUSTÄNDIGKEIT UND ANWENDBARES RECHT (1969).

[21] The court must also have "jurisdiction" (*Gerichtsbarkeit*). In the German view, however, jurisdiction is an accessory of sovereignty and exists generally, except as limited by public international law. Thus, it should not be confused with American concepts of jurisdiction. *See generally* I. SCHWARTZ, *supra* note 16, at 138.

[22] The legislative history is reviewed in *id.* at 17–21.

whom such restraints were agreed upon or caused."[23] All "restraints of competition that have domestic effects" were thus intended to fall within the statute.

The only limitations on the scope of extraterritoriality mentioned by the committee were (1) practical limitations relating to the international competence of German courts to adjudicate some foreign-related cases, and (2) the limitations of international law. The committee stated:

> The possibilities for the cartel officials to take action against such restraints will obviously depend on whether the participants in such agreements are represented within the area of application of this statute by statutory representatives, attorneys in fact, or agents and whether the participant enterprises are, according to the principles of international law, subject to the jurisdiction of the Federal Republic and whether German law is applicable to the agreements.[24]

The committee, however, does not appear to have expressed any specific ideas about what the limitations deriving from international law might involve.

The scope of section 98(2) is intended to be extremely broad. It fails, in fact, to limit the "effects" concept in any way, and it thus can be said to contain a "pure" effects principle, completely shorn of limiting concepts. Moreover, section 98(2) appears to be the only codification of a "pure" effects doctrine.[25]

The German effects principle is therefore broader than the American effects principle on which it was based.[26] Even in *Alcoa* the court required that the domestic effects had to be *intended* in order to establish a basis of jurisdiction.

The purity of the GWB's effects principle may, in part, be explained by the timing of its codification. Section 98(2) was part of the GWB when it was enacted in 1957. Since there had never before been a true antitrust statute in Germany, German legislators had had little experience with the problems of extraterritorial jurisdiction. Their main source of guidance in this context was the United States, but at that time American experience was also misleading. Following the precedent of the *Alcoa* case, the United States had been expanding the jurisdictional ambit of the antitrust laws for more than a decade, but the broad assertion of extraterritorial jurisdiction by the United States had not yet led to the widespread and intense resistance from affected countries that has developed in recent years.[27] This was most likely due to the

[23] BUNDESTAGSDRUCKSACHE NO. 3644, at 40 (June 28, 1957) [this quotation and all others of German sources were translated by the author].

[24] *Ibid.*

[25] Bunte, *Völkerrechtliche Fragen bei Auslandszusammenschlüssen,* 1981 WIRTSCHAFT UND WETTBEWERB [WUW] 605, 606.

[26] Huber, *Auswirkungstheorie und extraterritoriale Rechtsanwendung im internationalen Kartellrecht,* 10 ZEITSCHRIFT FÜR UNTERNEHMENS UND GESELLSCHAFTSRECHT 509, 511 (1981).

[27] To be sure, significant international conflicts related to the extraterritorial application of antitrust laws had begun to occur earlier in the postwar period. *See* J. ATWOOD & K. BREWSTER, ANTITRUST AND AMERICAN BUSINESS ABROAD §4.13 (1981).

dominant position of the United States in the post-World War II period, which made many foreign states reluctant to confront it openly on this issue. In these circumstances, the U.S. experience gave misleading signals to the German legislators.

In addition, in its initial form the GWB was a relatively mild statute that contained few provisions likely to cause conflicts in the international arena. Moreover, the newly formed and inexperienced FCO was expected to try to avoid controversy and to be restrictive in its attempts to enforce the GWB in international cases. Thus, the broad effects principle must have seemed innocuous to its framers, and it is only with the tightening of the GWB's substantive provisions and the change in the climate of international legal relations that the conflicts inherent in the exclusive use of this principle have become apparent.

IV. Peaceful Development: Nonmerger Cases

The development of the extraterritoriality issue in German antitrust law has gone through two distinct phases: a relatively peaceful stage of incremental development and relative confidence in the adequacy of the solutions being proffered, and the stormy, controversial period of intense uncertainty in which it finds itself at present. This dichotomy has corresponded largely to the types of cases in which extraterritorial application has been asserted. During the initial phase of development, the FCO was concerned with extraterritoriality in the nonmerger context, looking primarily at international licensing agreements, vertical restraints, and international cartels. The second phase has centered on the problems of applying the statute's merger control provisions to international mergers and acquisitions. Although our specific focus in this article is on the merger context, developments during the preceding period set the stage for that drama.

The Issue Framed

During the initial decade and a half of the life of the GWB, extraterritoriality was, at best, a secondary issue. The newly created FCO was careful to avoid asserting itself in areas that were likely to lead to international conflicts and/or excessive controversy about its enforcement activities.[28] In several international cases in which the exercise of jurisdiction might have been expected to lead to international conflict, the FCO sidestepped the potential problems by naming as defendants only the domestic participants in the allegedly anticompetitive arrangements. In 1971, for example, the FCO determined that the GWB should apply to an international shipping conference with members in many countries, but it named only the domestic participants as defendants.[29] The FCO's position during this period was that the GWB

[28] *See generally* Markert, *Die Anwendung des GWB auf internationale Wettbewerbsbeschränkungen*, in ZEHN JAHRE BUNDESKARTELLAMT 205 (1968).

[29] FCO, Sept. 10, 1971, WuW/E BKartA 1361 (Fernost-Schiffahrtskonferenzen).

could be applied to foreign conduct wherever such conduct had substantial anticompetitive domestic effects, but it generally avoided testing this position in court.

There were international cases, however, in which the FCO did attempt to apply the GWB against foreign defendants with limited contacts in Germany. It found on several occasions, for example, that section 98(2) empowered it to review the validity of international licenses where they involved either domestic licensors and foreign licensees or foreign licensors and domestic licensees.[30] Yet even where the FCO did extend the application of the GWB to foreign conduct, it seldom engaged in significant analysis of the transnational reach of the statute.

The FCO's success in avoiding confrontation with regard to the extraterritorial scope of the GWB is attested to by the fact that during this period the issue of extraterritoriality seldom played a role in cases appealed to the regular courts, and the first major Supreme Court case dealing directly with the construction of section 98(2) was not decided until 1973.

The lack of elaboration of this issue by the FCO and the courts did not mean, however, that there were no developments in the area. The developments were largely provided, as is often the case in German law, by legal scholarship. Two seminal studies—by Rehbinder and Schwartz[31]—in the 1960's arrived at similar conclusions with regard to several basic questions regarding the application of section 98(2).

The most important of these conclusions was that the effects principle enunciated in section 98(2) was unequivocally in accord with the requirements of public international law. Rehbinder and Schwartz concluded not only that the effects principle was clearly justified under international law, but that it was perhaps the only reasonable basis for a conflict-of-laws principle in international antitrust law. This proposition was quickly accepted by the legal community, and it has become a cornerstone of all subsequent discussions of the issue.

These conclusions, however, led to a trap. Having established that the effects principle satisfied the jurisdictional requirements of international law, German law assumed, as had American law, that this was the end of the issue. The special postwar circumstances, the relatively low level of international business interdependence, and the relative weakness of the GWB allowed extraterritoriality to appear to be a one-dimensional issue. These elements obscured the fact that by so limiting the role of international law, German law was prevented from considering the interests of other states. More than a decade would pass before the nature of the trap thus created would become apparent and this one-dimensional approach to extraterritoriality would lead to serious controversy.

[30] *See* U. IMMENGA & E. MESTMÄCKER, KOMMENTAR ZUM GWB 1904–09 (1982).

[31] E. REHBINDER, EXTRATERRITORIALE WIRKUNGEN DES DEUTSCHEN KARTELLRECHTS (1965); and I. SCHWARTZ, *supra* note 16.

Limiting the Effects Principle

In the interim, however, the sculpting of the effects principle was the central focus of the extraterritoriality issue. There was full agreement in the legal community that section 98(2) could not mean what it seemed to mean. It could not be construed to mean that any violation of any part of the GWB that had any kind of effect in Germany would be subject to the GWB. This interpretation would involve an extraordinarily broad application of the GWB that would be both unworkable and a constant embarrassment. The issue was how to go about limiting the effects principle.

The basic approach developed by German scholarship in the 1960's was to tie the effects principle directly to the protective purposes of the GWB, in general, and to the protective purposes of the specific provision of the GWB whose violation was at issue, in particular.[32] The "general protective purpose" of the statute is to protect free *domestic* competition. It requires, therefore, that the GWB be applied only where there is harm to the *domestic* competitive system.

More important is the requirement that domestic effects include only those which violate the specific protective purpose of the statutory provision being applied. Whenever a statutory provision is alleged to have been violated, the court must analyze the "sphere of protection" established by that provision. For an effect to be cognizable for purposes of section 98(2), it must interfere with that protected sphere. Only when the violation of a provision "injures" or "invades" the protected sphere of that provision are its effects relevant. The acceptance and development of this principle by the BGH was a key element in its first major decision dealing specifically with section 98(2).

The long awaited occasion for Supreme Court guidance concerning the application of section 98(2) finally came in 1973 in the *Oil Field Pipes* decision.[33] Ironically, it was not a case of extending extraterritorial jurisdiction at all. Rather than extending jurisdiction on the basis of effects, it limited the reach of the GWB. The central issue in the case was whether section 98(2) should apply to prevent application of the GWB to an agreement that was made in Germany, but that related solely to the export of goods from Germany and thus arguably had no "domestic effects."

The case involved an agreement among leading European—including German—and Japanese producers of oil field pipes to establish a cartel arrangement affecting markets outside of Germany. Section 6 of the GWB permits participation in such cartels by German companies, provided they are limited to regulating competition in markets outside of Germany. In order to qualify for this exemption from the antitrust laws, however, such agreements, including revisions thereof, must be reported to the FCO. Failure to report such an arrangement is punishable by fine.

The participants here failed to report a major revision of their cartel arrangement to the FCO, and the FCO fined the German participants for vi-

[32] *See, e.g.*, I. SCHWARTZ, *supra* note 16, at 32.

[33] BGH, July 12, 1973, WuW/E BGH 1276 (Ölfeldrohre) [hereinafter cited as Ölfeldrohre].

olation of the statute. The appeals court reversed the FCO's decision, and the BGH confirmed. The court held that the arrangement had no "domestic effects," and therefore that the GWB was not applicable to it.[34] According to the court, "Section 98(2) of the GWB, as the determinative conflict-of-laws rule, contains not only an extension but also a limitation on the area of application of the GWB to certain foreign-related facts."[35]

The decision's importance lies less in its specific holding, however, than in its enunciation of the general principles of construction to be used in applying section 98(2), in particular its treatment of the concept of "domestic effects." The court affirmed and established the "protected sphere" limitation that had been developed by Rehbinder and others during the previous decade. The key language in the decision dealt with this issue.

> In light of the variety of conceivable effects of foreign restraints on competition on the domestic market, a limitation and concretization of the concept of domestic effects is required in order to prevent the unlimited expansion of the international application of the substantive rules. . . . As §98(2) is not a substantive law rule, but rather a conflict-of-laws principle, . . . clarity concerning . . . which foreign-related effects fall within the GWB can only be achieved by construing §98(2) in relation to the general protective purpose of the statute as a whole and the protective purpose of the relevant substantive rules. Thus, the consequences of foreign-related restraints on competition can be viewed as "domestic effects" only when they constitute a domestic violation of the area of protection of the particular substantive rule.[36]

This decision helped set the stage for the second phase of development of the issue of extraterritoriality in German antitrust law.

V. The Breaking Point: Mergers and Acquisitions

The principles that were developed during the initial phase of development of the extraterritoriality issue had appeared to many to be adequate. The "effects" concept had been accepted as being in conformity with international law, and it had been sufficiently concretized to allow it to be applied in a reasonable and effective manner.

By the end of the decade, however, this picture had begun to change. As merger cases became the focus of international application of the GWB, confidence in the adequacy of the existing scheme was shaken. The principles developed for defining and concretizing the effects test of section 98(2) no longer seemed satisfactory, for it became clear that they did not provide a means of avoiding the potential for international conflict inherent in extraterritorial assertions of jurisdiction.

[34] The decision was overturned in the 1980 revisions of the GWB, by which the GWB was expressly made applicable to export cartels. *See* Viertes Gesetz zur Änderung des Gesetzes gegen Wettbewerbsbeschränkungen, 1980 BGBl.I 458 (April 26). *See also* Grauel, *Zur Novellierung des §98 Abs.2 GWB betr. Exportkartelle,* 1981 WuW 763.

[35] Ölfeldrohre, *supra* note 33, at 1277.

[36] *Id.* at 1278–79.

The German Merger Control Provisions

In 1973 the GWB was amended to include premerger notification requirements and to authorize the FCO to prohibit certain mergers,[37] and the potential problems of applying the GWB to foreign mergers quickly became the key issue in the area of extraterritoriality. They have remained so since, and with the 1980 amendments to the GWB,[38] which further tightened the merger control provisions, they have become one of the most controversial subjects in German law.[39]

Three separate sections of the GWB relate to mergers, and each has a distinct function. One section establishes reporting requirements; another provides premerger notification rules; and the third contains the rules that authorize the FCO to take action to prevent mergers.

The reporting provisions are contained in section 23, which has been part of the GWB since its inception. They are designed to provide information on the basis of which the FCO can monitor merger activity. When a merger meets certain market share or size criteria,[40] the acquisition and certain basic details about it must be reported to the FCO "without delay" after consummation of the transaction. The scope of coverage is very broad, applying to virtually all significant acquisitions.

A much more limited category of acquisitions is subject to the premerger notification requirements of section 24a of the GWB. Acquisitions meeting these requirements must be reported to the FCO *before* they are consummated, and they may not be consummated until a fixed period of time has elapsed without a negative response from the FCO.[41] In essence, the criteria here are that the merger be anticompetitive and likely to violate the substantive merger control provisions. The premerger notification provisions were added to the GWB in 1973.

A third type of merger control provision was also added to the GWB in 1973—namely, the substantive merger control provisions. Section 24 gives the FCO authority to prohibit mergers "[w]here it is to be expected as a result of the merger that a market-dominating position will be created or strengthened. . . . unless the participants can demonstrate that as a result of the merger improvements in competitive conditions will occur that outweigh the disadvantages of the market domination." Although the FCO is thus directed to prohibit a merger that will result in creating "a market-dominating posi-

[37] Zweites Gesetz zur Änderung des Gesetzes gegen Wettbewerbsbeschränkungen, 1973 BGBl. I 917 (Aug. 3).

[38] *See supra* note 34.

[39] *See, e.g., Extraterritoriale Rechtsanwendung unter Berücksichtigung der Entwicklung im U.S. Antitrustrecht,* 1982 WuW 22.

[40] For text, see *infra* note 54.

[41] In order to alleviate unnecessary hardship in premerger notification cases where it is obvious that the requirements of §24 will not be met, the Minister of Economics on May 30, 1980, ordered the FCO to respond to notification in such cases "without delay." Bundesanzeiger No. 103 (June 7, 1980), *reprinted in* 1980 WuW 591.

tion,"[42] it is given the discretion to refrain from prohibiting such a merger if it is shown that these negative results will be outweighed by improvements in competitive conditions.[43]

The Effects Principle in the Merger Context

Development of the Legal Concepts. In 1975 the FCO took an important step regarding the application of the effects principle to international mergers.[44] Recognizing the potential for confusion and controversy in applying the new merger provisions in an international context, the FCO in that year issued guidelines intended to clarify the extraterritorial scope of the merger provisions.[45] These guidelines established several aspects of what has come to be the accepted analysis of extraterritoriality in merger cases, and they continue to reflect the FCO's policy in the area.

The starting point of the guidelines is the basic principle enunciated in *Oil Field Pipes* that the protective purpose of each of the individual substantive provisions must determine the scope of its international application. The critical analytical development provided by the guidelines pertained, however, to what this meant in the merger context, in particular to the question of what constituted the "restraint of competition" required by section 98(2). According to the guidelines:

> The purpose of §23 *et seq.* of the GWB is to deal with concentration, for it can harm competition. The concept "restraint of competition" in §98(2) is the summary designation for all restraints of competition subject to the substantive provisions of the GWB. In regard to §23 *et seq.* of the GWB, the restraint of competition within the meaning of §98(2) is the merger as such. Whether the intensity of domestic competition is actually diminished is not relevant.

By defining the "restraint of competition" for purposes of section 98(2) as the merger itself, the FCO was forging an important link in the present chain of analysis,[46] for this obviates the need to ask about actual effects in merger cases and thus greatly reduces the scope of inquiry.[47]

[42] The concept of market domination is defined in detail in §22 of the GWB.

[43] A losing party may also request "special permission" from the Minister of Economics, who may allow a merger where "the restraint of competition is outweighed by macroeconomic advantages of the merger or the merger is justified by a transcending public interest." GWB §24(3).

[44] Since the statute specifically refers to the effects principle as the relevant conflict-of-laws concept, the nationality principle is not considered a sufficient basis of jurisdiction. U. IMMENGA & E. MESTMÄCKER, *supra* note 30, at 1878.

[45] FCO, TÄTIGKEITSBERICHT (Annual Report) 45 (1975). For text, see also W. KLEINMANN & R. BECHTOLD, KOMMENTAR ZUR FUSIONSKONTROLLE 467 (1977). For a discussion of merger control in Germany and an English translation of the guidelines, see Markert, *Merger Control in Western Europe*, in COMPETITION IN INTERNATIONAL BUSINESS 293 and 332 (O. Schachter & R. Hellawell eds. 1981).

[46] Critics of the guidelines have attacked this assumption, arguing that the merger should not itself be considered a restraint of competition. *See generally* Huber, *supra* note 26.

[47] If, for purposes of applying §98(2) to the reporting requirement of §23, a "restraint of

Having declared that the merger was itself the restraint of competition for purposes of section 98(2), the FCO then took the position that the place where the merger was realized would determine whether it had the required domestic effects. According to the FCO's scheme, mergers "realized" within the country automatically created domestic effects, whereas mergers realized outside the country created domestic effects only under certain circumstances. "Realized within the country" includes, for example, the acquisition of the assets or shares of a domestic corporation as well as the creation of a domestic joint venture corporation. The acquisition outside of Germany of a foreign corporation with a domestic subsidiary is deemed—with respect to the subsidiary—to be realized within the country.

Other mergers realized outside the country are deemed to have domestic effects if "through the merger the structural requirements for domestic competition are effected and at least one domestic enterprise (including subsidiaries and other related enterprises) is involved." This category includes, for example, acquisitions of foreign enterprises by German companies.

According to the FCO, some mergers realized outside the country have domestic effects by virtue of the activity of the involved foreign corporations on the domestic market; in other such cases domestic effects will be found only where additional factors are present. For example, domestic effects exist where, prior to the merger, both the acquiring and acquired enterprises were active within the country, either directly or through subsidiaries or agents. Domestic effects *may* exist where only one of the participating companies was active, but in such cases other direct domestic economic effects must be found. The examples given include situations where, in the event the merger is consummated, the foreign participant (generally, the target company) is "likely" to supply the domestic market or to transfer significant technology to the domestic enterprise.

The guidelines have been an important aid in clarifying the position of the FCO, at least in regard to section 23, and the FCO continues to attach weight to them.[48] Moreover, they have established several basic propositions regarding the application of section 98(2) to merger cases. They have, however, been sharply criticized for vagueness and oversimplification.[49]

Some of the issues raised by the guidelines were dealt with in the BGH's *Organic Pigments* decision,[50] which was the first major Supreme Court case involving the application of section 98(2) in the merger area. The central issue was whether the GWB's reporting provisions were applicable to the acquisition in the United States of a division of a U.S. corporation that had been doing

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competition" required proof of actual anticompetitive effects, far fewer mergers would be required to be reported, and the task of the FCO would be far more difficult.

[48] For a statement of the present position of the FCO, see Niederleithinger, *Zur Problematik einer Praeventivkontrolle von Auslandszusammenschlüssen,* 1981 WuW 469.

[49] *See, e.g.,* Harms, *Zusammenschlusskontrolle,* in GEMEINSCHAFTSKOMMENTAR 60 (4th ed. 1981).

[50] BGH, May 29, 1979, WuW/E BGH 1613 (Organische Pigmente) [hereinafter cited as Organische Pigmente].

business in Germany by another U.S. corporation that was the subsidiary of a German corporation.

The defendant company took the position that the reporting provisions could not extend to the transaction. It argued that the reporting requirements were merely procedural rules designed to improve the ability of the FCO to enforce substantive provisions. Since they were not substantive provisions (*Sachnormen*), they could have no "protected sphere." Therefore, since a provision of the GWB could be applied only where its protected sphere had been violated, section 23 could not be applied to such a transaction.

The BGH refused to accept this logic and held that the reporting requirements were substantive provisions within the meaning of the *Oil Field Pipes* decision. In the opinion of the court, the merger control provisions of the GWB represented a differentiated approach to merger control, with each of the three sets of provisions serving a specific purpose in that scheme. In the court's view, "This differentiated regulatory scheme resulted from the fact that the legislature did not view mergers as necessarily inimical to competition and therefore created a graduated statutory scheme designed to limit the interference of the state to necessary levels."[51] The reporting provisions were thus considered an independent and substantive component of this structure. As substantive provisions, their extraterritorial application was to be measured directly, in terms of whether or not the "effects" of the transaction invaded the "protected sphere" of the provisions.

Since the size criteria of section 23 had been met by the participants in the merger, albeit with the inclusion of foreign sales data, the question was whether this was sufficient to require the merger to be reported. Apparently concerned, however, about the possibility of "unlimited expansion" of the extraterritorial application of the provision, the BGH answered in the negative. It imposed a further modification on the statutory scheme by asking whether the merger, in addition, had a "direct effect" on the German market. Presupposing—without discussing the issue—that the acquisition was itself the restraint of competition whose effects were to be measured, the court stated that "the issue of whether the acquisition of the organic pigments division of ACC created relevant domestic effects depends entirely on whether the acquisition had a direct effect on the competitive conditions in the domestic market."[52] In the following paragraph it also required that the effect be "substantial."

The court found such direct and substantial effects on the basis of two factors. First, the merger eliminated actual competition because the acquired enterprise ceased to be a domestic competitor. Second, the acquiring corporation's German subsidiary increased its sales as a result of the merger and gained access to the know-how of the acquired company. The court, however, did not provide further guidance for the use of the "direct" and "substantial" tests in other cases.

[51] *Id.* at 1614.

[52] *Id.* at 1615.

The court's failure to follow its own prescribed line of analysis confused the extraterritoriality issue. It introduced independent limiting principles of "directness" and "substantiality," but it failed to indicate how these limiting principles were to be applied and how they related, if at all, to the issue of the provision's protected sphere.[53]

Application of the Effects Principle to Specific Merger Provisions. In analyzing whether a merger must be reported or notified to the FCO, the substantive merger prevention provisions of section 24—*i.e.,* the issue of whether the merger involves the "creation or strengthening of a market-dominating position"—are irrelevant. As required by the *Organic Pigments* decision, each of the three merger control provisions is treated separately.

The criteria for the reporting and premerger notification provisions are of two kinds: a market share test in section 23 and absolute size tests in sections 23 and 24a.[54] The market share test of section 23 presents little difficulty in the international context, for it refers solely to shares of the domestic market. In general, reporting is required on the basis of market share only where the participants have a combined domestic market share of at least 20 percent, regardless of whether the merger takes place within the Federal Republic. Here the effects principle is satisfied by the fact that a merger involving this level of domestic involvement necessarily affects the protected sphere of section 23.

The absolute size criteria of sections 23 and 24a present more complex issues. Where the parties to a merger meet these standards with respect to the domestic market, the respective reporting and notification obligations obviously arise. Unresolved, however, is whether foreign sales and foreign employees may be counted in determining if the size criteria have been met. The case law suggests that these criteria need not in all cases be fulfilled domestically, but may be met, at least in part, by the inclusion of foreign data. The theory is that the "absolute size criteria are an indication of the competitive parameters of the enterprise,"[55] and therefore sales that occur outside

[53] *See generally* U. IMMENGA & E. MESTMÄCKER, *supra* note 30, at 1887–94 and 1911–15.

[54] The text reads, in relevant part, as follows:

> [§23] (1) The merger of enterprises shall immediately be reported to the Federal Cartel Office, if
>
> 1. the merger results in or increases a market share of at least 20% within the entire territory in which this Law applies or within a major portion thereof, or if one of the participating enterprises has a market share of at least 20% in another market, or
>
> 2. the participating enterprises combined had at any point during the fiscal year preceding the merger at least 10,000 employees during such period or combined sales of at least 500 million DM.
>
> [§24] Notification of a proposed merger shall be given to the Federal Cartel Office if at least two of the participating enterprises had sales of DM 1 billion or more during the preceding fiscal year. . . .

[55] U. IMMENGA & E. MESTMÄCKER, *supra* note 30, at 1912.

the domestic market, for example, must be considered in measuring the domestic effects of the merger.[56]

Because the inclusion of foreign data in applying the absolute size criteria could greatly broaden the extraterritorial application of the provision, the BGH's "direct and substantial" requirement must also be met in such cases. Only if such a merger has a "direct and substantial" effect on domestic competition are the requirements of section 98(2) considered to be fulfilled.

The interaction of these rules can best be understood by reviewing the basic categories of relevant situations. When a domestic enterprise is acquired, reporting, or, as the case may be, premerger notification, is required whenever either the market share criteria are met domestically or the absolute size criteria are met on a worldwide basis. The theory is that the acquisition of a domestic enterprise necessarily entails the required effect on domestic competition, and the market share and size criteria simply measure the intensity of that effect.

In the case of foreign mergers, the situation is unchanged with respect to the market share criterion of section 23. Since, however, the absolute size criteria may be met either domestically or outside the country, the "direct and substantial" test must be applied—*i.e.*, the merger must not only meet the stated criteria, but it must also have a direct and substantial effect on competitive conditions on the domestic market.

There have been too few cases to clarify the issue of when effects are "direct and substantial," but a distinction is generally drawn between situations involving at least one domestic participant and those which are totally foreign. When one of the participants is a domestic enterprise, domestic effects result if, for example, both parties to the merger are actual or potential competitors on the domestic market or if the acquisition results in growth in the "competitive resources" of the domestic enterprise.[57]

In the case of a foreign merger in which there are no domestic participants, the required effect on domestic competition will normally be found only when one of the participants has substantial sales in the domestic market prior to the merger.[58] It is not clear, however, whether this condition must necessarily be fulfilled in order to find such effect.

As for the substantive merger control provisions, section 24 authorizes the FCO to prohibit a merger that is expected to result in the creation or strengthening of a domestic market-dominating position, provided the resulting improvements in competitive conditions do not outweigh the anticompetitive consequences. Since the creation or strengthening of a dominant position on the domestic market is defined by the statute as a serious domestic effect, the only issue that remains is when, in fact, a *foreign* merger may create or strengthen such a position.

[56] Allowing only domestic size data to be used in applying these tests would significantly restrict the scope of those provisions, but critics of the FCO argue that this would more fully reflect the GWB's "protective purpose" guidelines. *See, e.g.,* Harms, *supra* note 49, at 59–61.

[57] U. IMMENGA & E. MESTMÄCKER, *supra* note 30, at 1912.

[58] *Id.* at 1914.

The determination of this issue generally centers on a series of presumptions relating primarily to market share and size. A discussion of the elaborate system of statutory presumptions would go beyond the scope of this article, but the applicable principles are generally the same as those outlined above for the reporting and premerger notification provisions—*i.e.*, market share presumptions relate solely to the domestic market, while presumptions based on size relate to the enterprise as a whole, regardless of where, for example, sales occur.

By tying the jurisdictional concept of domestic effects to the protective purposes of the statutory provisions being applied, German law has substantially sharpened its "effects" analysis. It has developed a definable and manageable framework for continuing refinement of the protective purposes of particular provisions and the types of foreign conduct that can interfere with them. Additional refinement is necessary, however, especially in regard to the role and content of the "direct and substantial" requirement.

The Limits of Sovereignty

While merger cases have provided the context for further development of the effects principle, they also have confronted German antitrust law with a new aspect of the extraterritoriality issue—namely, the problem of external jurisdictional restraints. The reason is that extraterritorial application of the GWB threatens to collide with the sovereign interests of other states. Refining and developing the limits of the effects theory serves to reduce the likelihood of such conflicts, but the effects concept can itself neither take them into account nor respond to them.

Owing in large part to the restrained enforcement policies of the FCO during the first decade and a half of the GWB's existence, the potential for external conflict was seldom directly encountered in the nonmerger cases. Recent cases, however, have shifted the focus from reliance on the effects principle to filter out inappropriate exercises of jurisdictional positions to recognition and clarification of principles of jurisdictional restraint.

Prior to the *Organic Pigments* decision in 1979, there had been little consideration of the issue of external restraints in German law.[59] The extraterritoriality problem was viewed essentially as a matter of properly defining the effects principle. Even in *Organic Pigments* the BGH refused to take the issue seriously.[60] Attempting to convince the court that section 23 should not apply to a foreign merger, the defendant corporation had there argued that the principles of international law prohibited the application of a nation's *public law—e.g.*, regulatory laws—to foreign transactions. The judges were unimpressed. The court stated:

[59] *But see* K. MEESSEN, VÖLKERRECHTLICHE GRUNDSÄTZE DES INTERNATIONALEN KARTELLRECHTS (1975), discussed *infra* note 65.

[60] *See* Kersten, *Zur Anwendbarkeit des GWB auf ausländische Unternehmenszusammenschlüsse mit Inlandswirkungen*, 1979 WuW 721.

> The appellant cannot . . . claim that according to international law all states are obligated to mutual accommodation and therefore in principle may not apply their public law [*öffentliches Recht*] to fact situations which have arisen in foreign countries. The appellant thus fails to appreciate the importance of the conflict-of-laws principle of §98(2) GWB, which does not focus on the foreign conduct but on the effects that occur within the country.[61]

In effect, the court's position was that the relevance of international law to the extraterritoriality issue was limited to the question whether the effects principle was or was not sanctioned by it.[62]

The *Organic Pigments* case did not, however, as it could not, put an end to the external restraints issue. Awareness of the potential for international conflict inherent in the application of section 98(2) to foreign mergers quickly led to increasing concern in the legal community.[63] This development was primarily due to three factors. The first involved the internal legal situation in Germany. The merger control provisions that had been introduced in 1974 had given the FCO the authority to attack international mergers, an authority the FCO had now shown it was quite willing to use. Moreover, the FCO's authority in this area was further strengthened in 1980. Second, several of Germany's neighbors (including France and Britain) had introduced, or were considering, blocking legislation to thwart the extraterritorial application of foreign (particularly United States) antitrust laws within their respective borders.[64] Finally, the extraordinary international expansion of German investment, especially in the United States, vastly increased the potential for international application of merger control provisions and concomitantly increased the sensitivity of Germany's international corporations to their exposure in this area.

Consequently, when in late 1980 the KG handed down its *Bayer/Firestone* opinions, the situation looked much different from its appearance a year and a half earlier in *Organic Pigments.*[65] The *Bayer/Firestone* case represented the first major test of the FCO's authority to prohibit a foreign merger, and with it the external restraints issue reached center stage.

[61] Organische Pigmente, *supra* note 50, at 1615.

[62] The fact that there was a domestic enterprise involved in the merger put the court in the position of having little incentive to look toward international ramifications. Its basic position was that "there is no legal basis to remove the reporting obligation of the domestic enterprise merely because the interests of the [acquiring foreign enterprise], which it indirectly controls, are affected." *Ibid.*

[63] *See, e.g.,* Autenrieth, *Die Anzeigepflicht beim Zusammenschluss ausländischer Unternehmen,* 1980 RECHT DER INTERNATIONALEN WIRTSCHAFT 820.

[64] *See supra* note 3.

[65] The intellectual background for this change in position was the excellent study by Professor Karl Matthias Meessen published in 1975. Meessen confirmed that the effects principle remained a valid basis for jurisdiction under international law, and he made several important suggestions with regard to its application. He also discussed the external restraints issue and laid the foundation for subsequent case law developments with regard to it. *See* K. MEESSEN, *supra* note 59, and text accompanying note 72 *infra.*

In May 1980, Bayer France, a wholly owned French subsidiary of a Canadian holding company owned by Bayer AG, a German corporation, reported to the FCO in accordance with applicable reporting requirements that it intended to purchase a division of Firestone France S.A., located in France. Firestone France was a French subsidiary of Firestone, Inc., a U.S. corporation. The contract required as a condition of the acquisition that necessary governmental approvals be obtained, and the French Government had approved the plan. The FCO held, however, that the acquisition violated the GWB and ordered that it not proceed.

Curiously, the FCO's decision failed to discuss the external restraints issue, in spite of the fact that it had been a focus of discussion about the case, and the KG held that this omission was in itself a sufficient basis for dismissing the case and allowing the merger.[66] According to the court:

> [I]n the case of an acquisition which is to take place directly between two or even three foreign enterprises and which, as the FCO admits, has its center of gravity [*Schwergewicht*] outside the country, the [FCO] must deal with the issue whether §98(2) is applicable and whether as a result of the recognizable effects outside the country there are international law barriers to the proposed prohibition that are based on factors other than internal factors.[67]

Less than 2 years earlier, the BGH in *Organic Pigments* had held that the existence of "effects" was all that international law required. In *Bayer/Firestone* the KG explicitly required that the FCO take into account external restraints imposed by international law.

The court was given the opportunity to carry its thinking further, for the defendant corporation also sought an order allowing the transaction to be carried out immediately.[68] The court granted the order not only on the basis of procedural mistakes made by the FCO during the case and the lack of consideration of the external restraints issue, but also on the basis of "serious doubt" about whether the FCO's prohibition was susceptible of legal justification:

> These [doubts] result from the fact that . . . the center of gravity of the acquisition plan—which was prohibited *in its entirety*—is outside the country, while within the country, in contrast, a relatively unimportant additional restraint of competition would result from the strengthening of a market-dominating position of Bayer. The competent French legal office approves of the acquisition and the competent French authorities welcome it on the basis of economic and sociopolitical considerations. In this situation, prohibition of the acquisition with respect to the involved foreign enterprises [presents] a conflict between the conflicts-of-law rule of §98(2) of the GWB . . . and generally recognized principles of international law, namely, the principles of (1) reasonable forum contacts

[66] KG, Nov. 26, 1980, WuW/E OLG 2411 (Synthetischer Kautschuk I, 1980).
[67] *Id.* at 2417.
[68] KG, Nov. 26, 1980, WuW/E OLG 2419 (Synthetischer Kautschuk II, 1980).

> in international administrative law and (2) the principle of nonintervention.[69]

The court thus framed the entire issue much differently than it had been framed in *Organic Pigments.* The effects principle, the application of which had previously been seen as satisfying the requirements of international law, was no longer sufficient to satisfy those requirements.

The KG admitted that under section 98(2) the merger created a domestic effect, for there was a strengthening of a domestic market-dominating position. It held nevertheless that the prohibition violated international law principles of external restraint—namely, the principles of nonintervention and reasonable forum contacts:

> Since the prohibition . . . relates to the entire acquisition and thus, due to the contractual conditions requiring the approval of all responsible government bodies, prevents consummation of the transaction even by the foreign enterprises, which are primarily involved here, it constitutes a violation of the above-named and generally recognized rules of international law. . . . In a special case such as this one, in which the acquisition takes place only between foreign enterprises, the assets sold are located outside the country and [their foreign] production is only to a very limited extent available to the participants domestically, the prohibition cannot be allowed to have legal force.[70]

The court thus held that the application of international law prevented the FCO from taking the proposed action.[71]

The court did not elaborate the basis for its claim that these international law principles restrained its jurisdictional reach. It referred instead to the leading work by Professor K. M. Meessen, *Völkerrechtliche Grundsätze des internationalen Kartellrechts* (1975), in which these points were developed.[72] Meessen concluded that restraint principles were applicable in jurisdictional cases. He argued, in particular, that the principle of nonintervention had become an accepted principle of international law, and that it should therefore be applicable to jurisdictional issues, provided only that it could be concretized and given substance. He then suggested as a basis for this concretization process the tests that were implicitly adopted by the court in *Bayer/Firestone* and more fully developed by the FCO in the case that was to follow.

The FCO wasted no time in finding another case in which to press its position. Having been chastised for failure to take into account the issue of external restraints in the *Bayer/Firestone* case, it was careful to present a carefully reasoned argument to support its prohibition of a proposed acquisition in *Rothmans/Philip Morris.*[73]

[69] *Id.* at 2420.

[70] *Id.* at 2420–21.

[71] The case has been widely discussed in the legal literature. *See, e.g.,* Ebenroth & Autenrieth, *Die Fusionkontrolle beim Zusammenshcluss ausländischer Unternehmen unter indirekter Beteiligung eines inländischen Unternehmens,* DER BETRIEBS-BERATER, Jan. 10, 1981, at 16.

[72] *See* K. MEESSEN, *supra* note 59, ch. 5.

[73] FCO, Feb. 24, 1982, WuW/E BKartA 1943 (Morris/Rothmans) [hereinafter cited as Morris/Rothmans].

In a highly publicized opinion,[74] the FCO prohibited a merger outside of Germany between two non-German corporations. The case involved the purchase by Philip Morris, Inc., an American corporation (Philip Morris), of 50 percent of the shares of the Rothmans Tobacco Company, a British corporation (Rothmans), from a South African holding company called the Rembrandt Group, Ltd. (Rembrandt). Rothmans, in turn, controlled the Martin Brinkmann AG, a German corporation that was a major competitor of Philip Morris in Germany (Brinkmann). The remaining 50 percent of the Rothmans shares continued to be held by Rembrandt, and the sale constituted part of an arrangement by which Rembrandt and Philip Morris would exercise joint and equal influence over Brinkmann through Rothmans. Rothmans became, in effect, a joint venture corporation of Rembrandt and Philip Morris, the purpose of which was to provide joint distribution, research, and production efforts between the former competitors. In contrast to the *Bayer/Firestone* case, the acquisition here had already been carried out. Moreover, although the plan of acquisition entailed transactions other than the purchase of Brinkmann, the FCO sought to act against it only insofar as it affected the German economy—namely, by prohibiting the acquisition of Brinkmann.[75]

The FCO ordered that the acquisition be prohibited with respect to Brinkmann on the grounds that it would lead to the strengthening of a market-dominating position on the part of the leading German cigarette makers, *i.e.*, a tightening of the oligopoly that controlled the cigarette market. The acquisition would have resulted in the merger of Philip Morris's German subsidiary with Brinkmann, and thus a merger of the third largest seller (Brinkmann, 16.9 percent) with the holder of the fourth largest market share (Philip Morris, 14.3 percent).

The most controversial issue, however, was the jurisdictional basis of the decision. Building on the principles enunciated by the KG in *Bayer/Firestone*, the FCO specifically addressed itself to the external restraints imposed by international law, carefully responding to the objections expressed by the court in that case. It articulated a clear standard on which to base its extraterritorial reach:

> The authority for [this decision] is based on the effects principle, which is recognized by international law and which establishes the jurisdiction of a state to regulate matters that have a *direct* effect within its borders. Limitations on this authority can only result from the principle of non-

[74] *See, e.g.*, N.Y. Times, March 5, 1982, at D4.

[75] The FCO officially informed the Governments of the United States, the United Kingdom, and South Africa that it was considering taking action against the merger and gave them an opportunity to be heard. The United States did not respond to this opportunity. The Government of the United Kingdom held consultations with the FCO, and, on the basis of certain assurances from the FCO, it declared that it had no objection to the issuance of a prohibition order. The South African Government objected to the proceedings. It argued that the actions of the FCO would violate the international law principle of nonintervention because they would violate the rights of South African nationals to dispose of their foreign assets.

> intervention in the internal affairs of other states as well as the international law prohibition on abuse [of jurisdiction].[76]

Thus, the FCO explicitly based its authority on the "effects principle, which is recognized by international law," and then stated that the only limits on this authority were also provided by international law, the principles of nonintervention and abuse of jurisdiction.

These two principles are designed to incorporate and, perhaps, encapsulate the kinds of limitations referred to in the KG's *Bayer/Firestone* decision.[77] In formulating its version of these international law principles, the FCO had to deal with the stated concerns of the KG about external restraint without becoming too vague and without unduly limiting the reach of the GWB.

By applying the nonintervention principle of international law to the extraterritoriality issue, the FCO entered essentially new territory. This use of the nonintervention principle represented a new development in international law, but it also meant that there existed little guidance as to how the nonintervention principle should be adapted to its new role.

According to the FCO, the nonintervention principle prevented the exercise of prescriptive jurisdiction over a foreign merger where the interests of the regulating state in the exercise of such jurisdiction were significantly outweighed by governmental interests of a foreign state in the completion of the merger.

The nonintervention principle thus referred only to "governmental interest[s]," which the FCO described as fundamental state interests such as "politico-economic interest[s]." It did not apply to the interests of foreign individuals or corporations "because they are not subjects of international law."[78]

This important limitation on the scope of the nonintervention principle was a major issue, for the Republic of South Africa had argued against the FCO's proposed actions on the ground that the property interests of its citizens would be affected, which thus violated its own interests. It argued that its interests were governmental interests because it was obligated "to protect the property interests of South African nationals and enterprises." According to the FCO, however, such interests were not governmental interests for these purposes because they did not constitute an "original, state interest" of South Africa.[79] It thus distinguished between primary interests of states, such as regulatory interests, and derivative interests, which arise from the protection of private interests.

[76] Morris/Rothmans, *supra* note 73, at 1953.

[77] The external restraints concepts in the FCO's test were similar to those used by the KG in *Bayer/Firestone*. Both the FCO and the KG utilized the nonintervention principle, but the FCO utilized the international law abuse of jurisdiction principle in place of the reasonable forum contacts principle mentioned in *Bayer/Firestone*. This change represented a clear improvement because the abuse of jurisdiction principle is directly related to the external restraints issue, whereas the reasonable forum contacts concept is not.

In addition, the FCO significantly developed the content of the respective principles. The KG had only mentioned them in *Bayer/Firestone*.

[78] Morris/Rothmans, *supra* note 73, at 1953. [79] *Id.* at 1954.

The FCO's nonintervention principle required that the respective governmental interests be weighed according to a defined standard. According to the FCO, "Only when the interests of the foreign state in the execution of the merger significantly outweigh the German interest in preventing it can there be a violation of the nonintervention principle."[80] A significant preponderance of governmental interests on the part of the foreign state was thus required to establish a violation of the principle.

The second principle of international law that the FCO applied was the prohibition against abuse of jurisdiction, and here again the FCO found its proposed actions to be unobjectionable. It described the principle as follows: "The international law prohibition against abuse presupposes a crass disproportionateness between the domestic regulatory interests and the disadvantages that the affected foreign enterprises or the corresponding states suffer through the issuance of the sovereign act."[81] This principle had appeared previously in international law doctrine,[82] but it had apparently not been used in this context.

For purposes of this test, the FCO took into account both private and governmental interests and defined the types of interests to be included. It required that the *regulatory interests* of the state exercising jurisdiction be weighed against the harm that would be suffered either by the foreign enterprises involved *or* by foreign governments.

Which types of private harm are to be considered is not specified, but the FCO's treatment of several arguments advanced during the proceedings sheds light on its views in this regard. Injury to the property rights of South African shareholders of Rembrandt was not relevant to this balancing of interests, the FCO ruled, because the South Africans had, in effect, accepted the risk that the activities of a major multinational enterprise would "bring it into conflict with the national legal system of a state in whose markets it was active."[83] Similarly, the fact that the FCO's intervention would require the merger to be partially dissolved did not inflict relevant harm on the South African shareholders, who had argued that a partial dissolution would substantially reduce the value to them of the acquisition.

The standard to be applied in determining whether there was such abuse was one of "crass disproportionateness." A jurisdictional abuse would be found only where the specified disadvantages were crassly disproportionate to the interests of the regulating state. The FCO concluded that such disproportionateness could not be established in the instant case. According to the FCO, "The merger leads . . . to a substantial narrowing of the oligopoly dominating an economically very significant domestic market and therefore to a serious deterioration of the competitive structures."[84] Therefore, reasoned the FCO, there could be no disproportionateness.

The external restraints principles employed by the FCO are directly related

[80] *Id.* at 1953–54.

[81] *Id.* at 1954.

[82] *See* K. MEESSEN, *supra* note 59, at 203.

[83] Morris/Rothmans, *supra* note 73, at 1955.

[84] *Id.* at 1954.

to the avoidance of international conflict, for they provide a defined and structured balancing mechanism by which foreign interests can be taken into account. The tests represent novel usages of international law principles, and, although they require further refinement,[85] they expand the potential role of international law in this context.[86]

VI. Concluding Perspectives

Taking their cue from American experience, the drafters of the GWB started in 1957 with what appeared to be a simple and reasonable proposition—*i.e.*, that foreign anticompetitive conduct that had domestic "effects" should be subject to German antitrust law. After all, jurisdiction based on such effects had been held to be justified under international law. The German GWB did not even limit the effects principle; *any* effects within Germany appeared to justify extraterritorial application of the statute. As in the United States, the effects principle appeared to have almost magical powers: its mere existence seemed to solve the problem of extraterritoriality.

It soon became clear, however, that the effects principle would have to be modified, for construing it as broadly as it was written exceeded the limits of what was generally acceptable within the international community. Domestic effects resulting from foreign anticompetitive conduct could reasonably provide a basis for extraterritorial application of the law only under certain conditions.

At this point, German law took a portentous step. It sought to reduce the extraterritorial scope of the GWB by simply modifying the effects principle. It provided that only effects of a certain *level and intensity* would constitute a basis of jurisdiction. It asked, "What kinds of limitations must be put on the effects concept so that it will not reach too broadly?" But in order to answer that question it looked primarily to its *own* interests and applied modifying principles such as "direct" and "substantial" that referred to those interests.

The weakness of this approach is fundamental. Modifying the effects principle represents a one-dimensional solution to a two-dimensional problem. Conflicts between states are the core of the extraterritoriality issue. Modifying the effects principle reduces the *likelihood* of conflicts by reducing the number of situations in which effects can justify the exercise of jurisdiction, but it does not relate directly to the goal of conflict reduction, because it contains no means of accommodating the interests of other states. Its sole reference point is the regulating state.

This basic deficiency of an exclusively effects-based approach to extraterritoriality has become apparent in both Germany and the United States during

[85] *See, e.g.*, Meessen, *Zusammenschlusskontrolle in auslandsbezogenen Sachverhalten*, 143 Zeitschrift für das gesamte Handelsrecht 273, 282 (1979).

[86] Defendants have appealed, but officials of the European Community are reported to be considering taking action in the case, in which event the German courts would presumably not have the opportunity to review the FCO's decision. *See supra* note 5.

the last decade, and both countries have taken steps to remedy it. In some respects, these steps have been similar; in others, there have been significant differences.

German law has adopted a two-dimensional test that is designed to take into account foreign as well as domestic interests and also to minimize external conflict. The test has two components. The first is a carefully defined "effects" principle that allows effects to provide a basis for extraterritorial jurisdiction only when they are substantial and directly injurious to the purposes sought to be achieved by the specific provisions being applied. The second component relates directly to the issue of whether the state has overstepped its bounds and encroached on the sphere of sovereignty of another state, either by interfering with the governmental interests of that state or by abusing the jurisdictional authority that international law has conferred upon it.

United States law has also responded to this challenge, principally through the introduction of a so-called jurisdictional rule of reason.[87] This "rule" requires that in deciding whether to exercise jurisdiction in accordance with the notion of comity, a court is to "balance" the interests of the states involved and refrain from exercising jurisdiction where the interests of the foreign state "outweigh" the interests of the United States.

A comparison of German and American law regarding three central aspects of the extraterritoriality issue suggests similarities in approach that may reflect an emerging consensus in the international community and that highlight the potential value of the German experience to the further development of the legal principles in this area. These aspects are: the functioning of the effects principle, the use of interest-balancing concepts, and the role of international law.

In both the United States and Germany, "effects" has been the central concept in defining the extraterritorial reach of the antitrust laws, but there are significant differences between the two countries with regard to its content and function. In the United States, the concept has been little developed, and there is even uncertainty about which "effects" the concept refers to.[88] It is generally considered to refer, however, to effects on U.S. commerce—*i.e.*, to general economic effects caused by the anticompetitive conduct.[89] Using general economic effects as its reference point, American law has been able to make the test more precise only by introducing modifying concepts such as "direct" and "substantial," which refer to the level and intensity of such effects. Such modifying principles can yield only the vaguest of guidelines for court action, and, partially as a result of that fact, American law has had little success in forging the effects principle into a useful and discriminating legal principle.

[87] *See* cases cited *supra* note 2.

[88] *But see* National Bank of Canada v. Interbank Card Ass'n, 666 F.2d 6 (2d Cir. 1981), which represents an effort to sharpen the analytical structure of American law by requiring that the relevant effects also be anticompetitive.

[89] *E.g.*, Timberlane v. Bank of America, 549 F.2d 597 (9th Cir. 1976).

In Germany, on the other hand, the effects concept has been gradually concretized and defined by relating it to the procompetitive purposes of the statutory provisions being applied. The effects of foreign anticompetitive conduct serve as a basis for jurisdiction only where they interfere with the protective purposes of the specific statutory provision that defines such conduct as anticompetitive. This allows the legal process to define incrementally the specific elements that will constitute a basis for international jurisdiction—namely, the protective purposes of the respective statutory provisions and the kinds of effects that interfere with them.

Recognizing the need for flexibility in dealing with potential conflict situations, both legal systems have introduced balancing-of-interests concepts. Both states have recognized that world order demands that the effects principle be complemented by the use of legal mechanisms reflecting the interests of all states involved in the exercise of international regulatory jurisdiction.

The respective balancing tests, however, have significantly different characteristics. In the United States the balancing of interests does not, strictly speaking, take place within the domain of law.[90] It is performed within the context of "comity" and is thus essentially a discretionary political issue.[91] It is generally seen as informing a judge's answer to the question, "Having the right to apply our law to this situation, do we wish to abstain?"[92]

Corresponding to its nonlegal context is the fact that the balancing-of-interests test has not acquired a conceptual structure. The kinds of interests to be weighed are given little definition, and there are no standards to guide the weighing process. The court is merely instructed to look at a long list of factors,[93] attach relative weights to each, and weigh them against each other. How this is to be done is left to the discretion of the court. As a result, there is no basis for consistency in decision making, and there appears to be no way to arrive at even a modicum of predictability in judicial behavior.

The balancing concepts developed by German law are significantly more structured. First, both the nonintervention principle and the abuse of jurisdiction principle are applied in a *legal* rather than a political context. They require that a judge interpret and apply a principle of law. Conclusions reached on the basis of such application are legal conclusions, and each case is related to every other case by that fact.

In addition, the interests to be weighed are defined. In applying the nonintervention principle, for example, the regulating state's "governmental in-

[90] Tentative Draft No. 2 of the *Restatement of Foreign Relations Law (Revised)*, *infra* note 97, seeks to place balancing issues in a legal rather than a political and discretionary context. The draft is summarized in 75 AJIL 987 (1981).

[91] *See* Maier, *supra* note 15, at 281.

[92] The opinions in *Timberlane* and in other cases following it have been obscure on the issue of how the balancing test relates to the issue of subject matter jurisdiction. The analysis appears to be, however, that the effects test controls the right to exercise jurisdiction and the balancing test relates to whether we *should* exercise that jurisdiction.

[93] A recent list of factors is contained in Mannington Mills v. Congoleum Corp., 595 F.2d 1287 (3d Cir. 1979).

terests" are weighed against the "governmental interests" of other states that may be affected. Such interests are the only interests to be weighed. The abuse principle involves weighing the governmental interests of the regulating state, on the one hand, against the governmental interests of foreign states and the private interests of the merger participants, on the other hand.

Furthermore, each test has a standard of measurement. When the nonintervention principle is applied, governmental interests of the regulating state will suffice to justify the exercise of jurisdiction, unless the governmental interests of the foreign state *significantly outweigh* them. The exercise of jurisdiction will violate the abuse principle only if injuries to foreign interests are "crassly disproportionate" to the interests of the regulating state.

Both German and United States law recognize that international law places certain limits on the right of a state to exercise prescriptive jurisdiction over conduct outside its borders. Moreover, until recently, both systems considered that the requirements of international law were satisfied by use of the effects principle. The exercise of international jurisdiction based on a modicum of domestic effects was not considered capable of violating international law.

This remains the basic U.S. position concerning international law; it has not fundamentally changed. Introduction of the concept of a jurisdictional rule of reason reflects awareness of the importance of developing principles of conflict avoidance. The critical factor, however, is that this approach does not look to international law for guidance. It is conceived as a domestic United States solution based on United States law models. It is perhaps in part for this reason that its introduction seems not to have convinced other states that their interests will be adequately taken into consideration by its application.

In Germany, on the other hand, the courts and the FCO have responded to these changing conditions by altering their position with respect to international law.[94] They have moved from a one-dimensional effects-centered approach to a two-dimensional approach that includes both an effects test and an external restraints test. They have adapted external restraints concepts of international law and applied them to an area in which they previously had not been used. In doing so, they have substantially expanded the role of international law in the extraterritoriality context. In the German scheme, that role is no longer limited to sanctioning the effects principle as a basis for jurisdiction; it now includes the development and application of conflict-avoidance principles.

These external restraints concepts will undoubtedly require further refinement and clarification, but they seem well suited to the purposes for which they are being utilized. The principle of nonintervention is an established component of the international law system, whose purpose is to establish restraints on state action in violation of foreign sovereignty.[95] It is for the same

[94] *See generally* Meng, *Neuere Entwicklungen im Streit um die Jurisdiktionshoheit der Staaten im Bereich der Wettbewerbsbeschränkungen*, 41 ZEITSCHRIFT FÜR AUSLÄNDISCHES ÖFFENTLICHES RECHT UND VÖLKERRECHT 469 (1981).

[95] K. MEESSEN, *supra* note 59, at 203.

purpose that German law has adapted this principle for use in the extraterritoriality context. The concept of abuse of jurisdiction is an extension of the international law principle of reasonableness.[96] In the extraterritoriality context, it performs the important function of complementing the nonintervention principle by taking into account private as well as governmental harm.

Most important, perhaps, is the fact that German law has placed international law at the center of its effort to resolve the extraterritoriality problem. The experience of both countries in this area has been plagued by the generally deficient state of international law, which is, in turn, attributable to the fact that states have been reluctant to look to international law rules and processes for the resolution and avoidance of international jurisdictional conflicts. Consequently, guidance in the form of experience shared by other countries has been minimal, and the clarification and development of principles of external restraint has been thwarted.

In each of these areas, both German and American law have responded to international conflicts and the increasing potential for such conflicts. They have incorporated into their respective legal approaches to the issue of extraterritoriality mechanisms limiting the scope of the effects principle and taking into account foreign interests. This process is critical to the avoidance of international conflict based on the exercise of international jurisdiction, and can only be characterized as a major international law development.

The particular importance of German law in this process derives from the fact that German law has proceeded further than United States law in sharpening its analytical tools. American law has taken refuge in relatively vague notions such as "comity" and "jurisdictional rule of reason," and, as a result, it has yet to develop the conceptual and analytical strength necessary to accomplish its conflict-avoidance purposes effectively.[97]

A related and perhaps even more important fact is that German law has sought, and found, conceptual guidance and structure in the processes of public international law.[98] This is of critical importance, because a comparison of United States and German developments suggests that achieving a workable international jurisdictional framework may require greater reliance on public international law as a source of conflict-avoidance principles.

[96] *Id.* at 205.

[97] The draft *Restatement of Foreign Relations Law* (1981) seeks to meet this need by concluding that "reasonableness" is a principle of international law and by specifying the various considerations and the relevant circumstances that need to be weighed in determining whether an exercise of jurisdiction is unreasonable as a matter of law. *See* RESTATEMENT OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES (REVISED) §403, Comment and Reporters' Notes (Tent. Draft No. 2, 1981).

[98] This is to suggest neither that the German approach here outlined has been fully accepted in Germany nor that it is without weaknesses. *See, e.g.*, Harms, *supra* note 49.

Indeed, in regard to the specific issue of premerger notification, American law has achieved a more effective solution to the problems raised. Not coincidentally, however, this is an area in which American law relies not on case law principles, but on recent statutory developments. *See* 15 U.S.C. §18A (1981).