ANTITRUST REVIEW OF MERGERS, ACQUISITIONS, AND JOINT VENTURES IN BRAZIL*

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I. INTRODUCTION

In 1994 Brazil adopted a new antitrust law that establishes a mandatory review process for mergers, acquisitions, and joint ventures by an independent enforcement agency.[1] While antitrust law in Brazil dates back to 1962, the new law expands the scope of antitrust enforcement to allow for independent agency review of mergers, acquisitions, and joint ventures. Moreover, Brazil's new Competition Act compels firms to notify transactions to the government. This mandatory reporting requirement aligns Brazil with the United States, European Union, and a growing number of other jurisdictions that have established independent competition agencies to enforce merger control laws. Because Brazil has the largest economy in the South America

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[1] Law 8,884 of June 11, 1994, *available at* http://www.mj.gov.br/cade [hereinafter the Competition Act]. For further discussion of the Competition Act, *see* Gesner Oliverira, *Competition Policy in Brazil and Mercosur: Aspects of the Recent Experience,* 24 BROOKLYN J. OF INT'L L. 466 (1998) (general overview of Brazil's privatization and competition policies, including description of the Competition Act); William H. Page, *Antitrust Review of Mergers in Transition Economies: A Comment, With Some Lessons from Brazil*, 66 CINC. L. REV. 1113 (1998) (discussion of Competition Act with criticism of some enforcement actions); Dallal Stevens, *Framing Competition Law within an Emerging Economy: The Case of Brazil*, 40 ANTITRUST BULL. 929 (1995) (discussion of Competition Act with overview of antitrust laws preceding it).

and great influence across the continent, the potential impact of the merger control law is very significant for multinational firms. This article will provide an overview and comparative analysis of Brazil's merger control law and the government enforcement actions taken under its provisions.

The new antitrust law grants principal enforcement authority to CADE, the Administrative Council for Economic Defense (in Portuguese, the Conselho Adminstrativo de Defesa Economica). Already, CADE and its antitrust enforcement actions have received considerable attention from the international business community, not all of it positive. As The Wall Street Journal reported last year, "As far as multinational corporations here are concerned, CADE is fast becoming a four-letter word."[2]

Since enactment of the Competition Act in 1994, CADE has taken enforcement actions in consumer-goods industries involving well-known multinational firms. CADE required Colgate-Palmolive to suspend a toothpaste brand on the grounds that the company's acquisition of a toothpaste producer in Brazil gave it a 78 percent share of a product market in Brazil.[3] The beverage industry has faced several enforcement actions by CADE. CADE has made initial rulings to enjoin joint ventures between Miller Brewing and Brahma, Brazil's largest beer producer,[4] and between Anheuser-Busch and Antarctica, Brahma's closest rival.[5]

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[2]*Brazilian Panel Is Foreign Firms' Nemesis*, WALL ST. J., July 9, 1997, at A10; *see also Is Brazil Antitrust – or Anti-Foreigner?*, BUS. WEEK (Int'l ed.), July 21, 1997, at 330.

[3]CADE, RECENT JURISPRUDENCE: KEY RULINGS BY CADE IN 1996, *available at* http://www.mj.gov.br/cade (showing that Colgate-Polmolive Company and Kolynos do Brasil S.A. would possess 78.1% of toothpaste market in Brazil). In addition to ordering suspension of a toothpaste brand (the Kolynos brand), CADE required Colgate-Palmolvie Company to sell about 20% of that Kolynos' toothpaste production to third parties for resale under their own brand names. *See Second Offer for Kolynos Production Capacity Ends Today*, GAZETA MERCANTIL INVEST NEWS, July 16, 1997; Page, *supra* note 1, at 1125.

[4] CADE initially enjoined a joint venture between Miller Brewing Company and Cervejaria Brahma to produce Miller Genuine Draft beer in Brazil. *See* Miller Brewing Co./Cervejeria Brahma, CADE Concentration Act 58/95 (June 11, 1997). CADE enjoined the joint venture because it eliminating potential competition from Miller Brewing. *Id*. In May 1998, however, CADE approved the joint venture on the condition that Cervejaria Brahma provide bottling facilities to a smaller brewer and technical assistance to three microbreweries. *See Miller's Brazil Venture Approved*, FIN. TIMES, May 15, 1998.

[5]CADE initially enjoined a joint venture in which Anheuser-Busch would purchase 5% of Antarctica with an option to purchase up to 30%. *See* Anheuser-Busch Inc./Antarctica Group, Concentration 83/96 (July 23, 1997) (initial CADE decision opposing Anheuser-Busch joint venture), *available at* http://www.mj.gov.br/cade. CADE also relied on the potential

CADE has taken other enforcement actions directed at mergers, acquisitions, or joint ventures. CADE restricted a transaction involving a Brazilian unit of Rhone-Poulenc, a multinational chemical company based in France. Rhone-Poulenc's Brazilian unit sought to purchase a polyester producer in Brazil, but CADE required divestiture of manufacturing assets in Brazil after finding high levels of concentration in a product market consisting of acrylic and polyester fibers.[6] CADE also has required divestiture of a steel plant after finding that an acquisition would create high concentration in a product market consisting of nonflat steel.[7]

These CADE enforcement actions broke new ground, especially when considering that Brazil instituted merger control by an independent agency only in June 1994. Brazil's original antitrust law, effective in 1962, contained general prohibitions similar to the Sherman Act.[8] It forbade price fixing and abuse of market power. The 1962 law created CADE to enforce these antitrust prohibitions, but CADE rarely undertook any enforcement actions.[9]

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competition doctrine in reaching this decision. *Id*. at 26 ("the entry of Anheuser-Busch by means of association with Antarctica eliminated a significant part of the potential competition represented by the American company"). Later, in December 1997, CADE agreed to allow the joint venture to proceed on the condition that Anheuser-Busch increase its ownership interest in Antarctica to about 30% by 2002, and contribute additional capital. *See* Anheuser-Busch/Antarctica, CADE Reconsideration Decision at 43-44 (Dec. 10, 1997); *Reprieve for Brazil Brewing Deal*, FIN. TIMES, Dec. 12, 1997, at 27; *Brazil Reverses Decision to Shut Down Local Anheuser Busch Venture*, WALL ST. J. INTERACTIVE ED. (Dec. 11, 1997), *available at* http://interactive.wsj.com. CADE and the parties reached a definitive agreement in April 1998. *See Regional Update: Anheuser-Busch/Antarctica Venture Gets OK*, SOUTH AMERICA REPORT, May 1, 1998.

[6]*Rhondia and Sinasa Plan to Divest Certain Polyester and Acrylic Fiber Production Assets in Brazil*, PR NEWSWIRE, June 28, 1995.

[7]CADE, RECENT JURISPRUDENCE: KEY RULINGS BY CADE IN 1996, *available at* http://www.mj.gov.br/cade (CADE discussion of divestiture relating to acquisition between Gerdau Group and Korf GmbH involving steel); *Gerdau Gets Brazil OK to Sell Portion of Pains*, AMERICAN METAL MARKETS, May 28, 1997, at 2 (discussing divestiture in steel industry acquisition); *Sale of Contagem to Cabomat is Official*, GAZETA MERCANTIL INVEST NEWS, Mar. 18, 1998 ("the Gerdau steel group had reached an agreement with CADE to complete the sale of the Contagem steel plant . . . to Metalurgica Cabomat S.A.").

[8]For an English language copy of Law 4137/62, *see* UNCTAD, Preparation for a Handbook on Restrictive Business Practices Legislation, U.N. Doc. TD/B/RBP/82 at 17-24 (1991).

[9]*See* E.Q. Farina, POLITICA ANTITRUSTE: A EXPERIENCIA BRASILEIRA (1990) (between 1963 and 1990, there were only 16 cases prohibiting or condemning conduct); Dallas Stevens, *Framing Competition Law Within an Emerging Economy: The Case of Brazil*, 40 ANTITRUST BULL. 929, 937 (1995) (discussing limited prior enforcement efforts).

The Competition Act adopted in 1994 replaced the prior antitrust laws and introduced merger control by an independent competition agency in Brazil.

The Competition Act is comprehensive, as it covers single-firm conduct, concerted action, distribution, and other matters in addition to merger control. This article focuses on one aspect -- merger control, including the relevant sections of the 1994 law, the implementing regulations, and the enforcement actions and policies. Section II of this article reviews the Competition Act's mandatory notification requirements. Section III examines the antitrust review process following notification. This includes the roles of the relevant government agencies, timing considerations, and litigation issues concerning reconsideration and appeal. Section IV discusses substantive antitrust standards for reviewing mergers, acquisitions, and joint ventures. This final section focuses on how the enforcement agencies have treated market definition, entry, efficiencies, performance commitments or consent orders, and other substantive matters critical to the antitrust review.

II. NOTIFICATION REQUIREMENTS

A. INTERPRETATION AND APPLICATION OF THE NOTIFICATION RULES

Article 54 of the Competition Act contains two separate reporting requirements, one specific and the other more general, that apply to mergers, acquisitions, and joint ventures. It requires firms to notify any transaction in which either (1) the resulting firm accounts for 20 percent or more of a relevant market, or (2) one of the firms involved has annual gross sales of at least R$ 400 million (approximately U.S. $ 345 million).[10] Firms also must report for review a transaction that may "restrain open competition" or "result in the control of relevant markets."[11] Consequently, a merger, acquisition, or joint venture that falls below the more specific thresholds may nonetheless be subject to reporting on the general grounds that it restrains open competition or advances control of a relevant market. This separate broad reporting requirement of Article 54 has been used rarely for notification by firms engaged in mergers, acquisitions, or joint ventures. It can be invoked by the competition agencies or competitors, however, to review transactions that fall below the more specific market share or size-of-the-person tests. The parties

[10] Competition Act, art. 54.

[11] *Id*.

to a transaction that meets either of the thresholds must submit a notification within fifteen business days of closing.[12]

1. THE MARKET SHARE TEST

The parties to any form of economic concentration must notify CADE if the resulting firm or group of firms accounts for twenty percent or more of a relevant market. To determine whether the 20 percent market share test is satisfied, the parties to a transaction must first define the relevant product and geographic markets. The parties must conduct this market definition analysis at the outset to determine whether to notify. The parties' decisions on product and geographic market definition may affect not only the transaction at hand, but subsequent transactions before the Brazilian competition agencies or agencies in other jurisdictions. In the United States, for example, the competition agencies or private litigants can obtain discovery of statements made to foreign competition agencies concerning market definition. Rash statements on market definition may put at risk and possibly damage the parties' credibility in subsequent investigations.

As discussed further below, CADE's regulations and decisions leave open some questions on how to define product and geographic markets. But even where antitrust regimes are well established, particularly in those of the United States and European Union, market definition remains a highly uncertain undertaking. The United States, European Union, and several other jurisdictions use objective, verifiable thresholds such as sales or asset values rather than market shares to determine whether a notification obligation exists. This provides much more certainty. The Competition Act's use of the 20 percent market share test will continue to create uncertainty over the basic question of whether firms need to notify.[13] CADE has imposed penalties in several cases for failure to notify, but it has not done so for failure to notify based solely on the market share threshold.

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[12] *Id*. ¶ 4.

[13]For additional criticism of market share thresholds, *see* William E. Kovacic, *Merger Enforcement in Transition: Antitrust Controls on Acquisitions in Emerging Economies*, 66 CINC. L. REV. 1075, 1098 (1998); Roger Alan Boner, *Competition Policy and Institutions in Reforming Countries, in* REGULATORY POLICIES AND REFORM: A COMPARATIVE PERSPECTIVE 46 (Claudio R. Frischtak ed., 1995).

The 20 percent market share test of Article 54 presents some uncertainty beyond that inherent in any market share test. What if a firm with 40 percent of a relevant market acquires a firm with 0 percent? CADE has informally indicated that transactions should be reported in such circumstances. Thus, firms that already have market shares exceeding 20% percent may need to notify an acquisition in an unrelated product line. This result finds some support in the language of the Competition Act. Article 54 does not state that the resulting firm must account for a 20 percent share as a result of or by reason of the transaction. It merely states that the notification obligation applies when "the resulting company or group of companies accounts for twenty percent (20%) of a relevant market."[14] The implication is that a firm with 20 percent or more of a market must always report its transactions for antitrust review. This interpretation, however, may lead to unnecessary reporting. For example, a firm with 30 percent share of a grain market might need to report its acquisition of a small automotive parts supplier.

While not adopted by CADE, an alternative reading is that Article 54 covers only transactions resulting in an increase in concentration. Arguably, use of the term "relevant" market limits Article 54's scope. In the above example, the grain market (where the buyer already maintains a 30 percent share) would not be relevant to an acquisition of an automotive parts supplier. In this respect, a relevant market would exist only when each of the firms participate at some level in the market. This approach would have the benefit of eliminating the reporting requirement for many transactions posing no competitive concerns. It might, however, reach too far and eliminate reporting of transactions presenting potential anticompetitive vertical effects, e.g., a firm with an 80 percent share acquires a supplier vital to its few competitors. This reading also fails to account for potential competition, e.g., a firm with an 80 percent share acquires a firm that currently has a 0 percent share but plans to enter the market on a large scale. Indeed, CADE in its enforcement decisions has placed considerable weight on potential competition.[15]

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[14]Competition Act, art. 54, ¶ 3.

[15]Anheuser-Busch Inc./Antarctica Group, Concentration Act 83/96 at 31 (July 23, 1997) ("the association … is damaging to competition because, … it eliminates perceived and effective potential competition between the established firm and potential entrants"), *available at* http://www.mj.gov.br/cade; Miller Brewing Co./Cervejaria Brahma, Concentration 58/95 (June 11, 1997).

CADE has not issued any regulations addressing whether there must be a change in concentration or market share. Brazil's Economic Monitoring Office, known as SEAE, has tried to persuade CADE that there must be some change in concentration to trigger the notification requirement. CADE, however, has not accepted this argument and has indicated informally that there need not be a causal link between the transaction and the market share threshold.

2. THE SIZE-OF-THE-PERSON TEST

Even if the combined firm's market share falls below the 20 percent threshold, the parties may still need to notify based on the Competition Act's alternative size-of-the-person test. A transaction meets the size-of-the-person test if any of the firms involved "has posted in its latest balance sheets an annual gross revenue equivalent to R$ 400,000,000 (four hundred million of Reais)."[16] This represents about U.S. $345 million. Revenues from controlled affiliates must be counted when applying the size-of-the-person test.[17]

The size-of-the-person test ensures that Article 54 reaches transactions involving at least one large firm, even if the combined firm's current market share is less than 20 percent. Compared to the market share test, the size-of-the-person test has the advantage of greater clarity and certainty. It may not, however, serve as a useful measure of the types of transactions likely to raise competition concerns because sales or revenue data do not necessarily reveal a firm's market power.

Some interpretive questions have arisen in other jurisdictions that use similar size-of-the-person tests. The European Union, which like Brazil uses a revenue threshold, has issued a regulation clarifying how revenue should be computed. It establishes that firms should exclude rebates and value-added taxes directly related to the sales and exclude any revenue generated from internal sales among controlled divisions or subsidiaries.[18] The European Union also has adopted rules to guide the computation of sales revenues in

[16]Competition Act, art. 54, ¶ 3.

[17]CADE Resolution 15/98 of Aug. 19, 1998, Exhibit V, *available at* http://www.mj.gov.br/cade (with definitions of "Group of Companies" and "Control").

[18]Commission Notice on Calculation of Turnover 1994 O.J. (C 382) 15.

service industries, particularly the financial and insurance industries, which present some unique technical problems in assessing revenues.[19] Thus far, CADE has not issued any similar rules or decisions guiding the R$ 400 million sales computation, but can be expected to follow European Union principle, as it has in other settings.

The-size-of-the-person test raises the question of which balance sheet is appropriate to use. The choice between balance sheets can alter the antitrust analysis substantially, particularly if either firm involved recently engaged in substantial acquisitions or sales. A firm's balance sheet for calendar year 1997, for instance, will not reflect an acquisition made in the first quarter of 1998. Whether the firm meets the revenue threshold often may depend on which balance sheet it uses -- a prorated recent quarterly balance sheet reflecting the acquisition or the prior annual balance sheet that does not. CADE's practice has been to use only the most recent annual balance sheet. Moreover, the notification form asks for revenue data or other data based on the previous fiscal year, and does not require updating to account for more recent activity.[20]

The Competition Act does not expressly address how a firm should compute its revenue vis-à-vis its affiliates, subsidiaries, or parent entities. CADE has followed the ultimate parent entity concept, which is used in the United States and European Union. By this approach, a firm's revenues should include the revenues of any subsidiary or affiliate over which the firm involved in the transaction has control.[21] Similarly, a firm's revenues should include its parent company's revenues if the parent controls it. Accordingly, when Miller Brewing Do Brasil Ltda. executed an agreement with Cervejeria Brahma in September 1995, CADE, in its assessment of the notification thresholds, considered not only the revenue of the two signatories to the agreement, but also that of a parent company, Miller Brewing, USA.[22] Control for purposes of revenue computation will ordinarily depend on

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[19] *Id*.

[20] CADE Resolution 15/98 of Aug. 19, 1998, Exhibit I, *available at* http://www.mj.gov.br/cade.

[21] *See* CADE Resolution 15/98 of Aug. 19, 1998, Exhibit V, *available at* http://www.mj.gov.br/cade (with definitions of "Group of Companies" and "Control").

[22] Miller Brewing Co./Cervejeria Brahma, CADE Concentration Act 58/95 (June 11, 1997).

whether there exists a greater than 50 percent interest in shares or board representation. CADE also may consider other evidence of control.[23]

The size-of-the-person test of Article 54 means that large firms engaging in mergers, acquisitions, and joint ventures that affect the Brazilian marketplace may need to report all their transactions to CADE. Because of their sheer size, large firms that have been active in Brazil since 1994, such as Colgate-Palmolive, have had little choice but to report to CADE their transactions impacting the Brazilian marketplace. Large multinationals attempting to enter the Brazilian market through merger, acquisition, or joint venture will likely report gross revenues exceeding R$ 400 million, and thus need to report their transactions.

There is a growing view within CADE that the R$ 400 million threshold should be raised. CADE has informally indicated that the low threshold may lead to reporting of too many transactions that do not raise any competitive concerns. But it remains to be seen whether the law will be changed to raise the threshold.

1. THE TYPE OF TRANSACTION OR CONCENTRATION

Another question raised by the notification requirement is whether the transaction constitutes a "form of economic concentration" or other form of corporate grouping under the Competition Act. The notification requirement of Article 54 applies to "any action intended for any form of economic concentration, whether through merger with or into other companies, organization of companies to control third companies or any other form of corporate grouping . . . ."[24] It is clear from the broad language of Article 54 that joint ventures, as well as mergers and acquisitions, may be covered. CADE has applied the language broadly to cover joint ventures and other forms of integration or collaborative conduct. For example, the Competition Act covered the 1995 Miller Brewing Co./Cervejeria Brahma production and distribution agreement which allowed Cervejaria Brahma to start producing and distributing Miller beer in Brazil.

While covering mergers, acquisitions, and various forms of joint ventures, the Competition Act itself leaves open many questions. What if a firm purchases

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[23] CADE Resolution 15/98 of Aug. 19, 1998, Exhibit V, *available at* http://www.mj.gov.br/cade (with definitions of "Group of Companies" and "Control").

[24] *Id.*

less than a 50 percent interest (e.g., a 25 percent interest) in another firm? At what point does collaboration among firms or competitors amount to a reportable joint venture or corporate grouping under the Competition Act? Is it necessary that firms make some substantial commitment (e.g., over U.S. $5,000,000 invested by each firm) to a long-term, joint production effort? What if two firms or competitors merely agree to a limited joint purchasing arrangement, such as joint purchases of insurance?

In the United States, these types of questions are addressed by the detailed Hart-Scott-Rodino Act regulations.[25] Similarly, the European Union notices and implementing regulations address many of these questions.[26] CADE, however, has not issued detailed regulations clarifying the notion of a "form of economic concentration" under Article 54. The language of Article 54 suggests coverage over a broad range of transactions, but further clarification may be helpful to assist firms in accurately assessing their compliance obligations.

A CADE decision has, however, explained the notification requirement in the area of share acquisitions.[27] Parties may need to notify an acquisition of shares even though the acquisition is of less than 50 percent of the acquired firm's shares.[28] The dispositive issue for notification purposes is whether the transaction transfers control.[29] A firm may obtain control over another firm, even though it possesses less than 50 percent of the shares, by virtue of corporate governance rules, shareholder agreements, or other contracts that give it authority over the board or other decisionmaking group. For example, corporate governance rules may give a firm with less than a 50 percent share veto rights over fundamental corporate management decisions. In Worthington/Metalplus, CADE found that a firm with a 48 percent interest maintained control by virtue of corporate governance rules requiring a two-

[25] *See* 16 C.F.R. §§ 801-803.

[26] *See* Commission Notice on Notion of Undertakings Concerned 1994 O.J. (C 385) 31; Commission Notice on Calculation of Turnover O.J. [1994] C382/15; Commission Notice on the Notion of a Concentration Under Council Regulation (EEC) 4064/89; Commission Implementing Regulation 1994 O.J. (L377) 1.

[27] Worthington/Metalplus, Concentration 139/97 (Oct. 21, 1997) (firm with 48% interest maintains control because of supermajority voting requirement).

[28] *Id*.

[29] *Id*.

thirds vote for various management decisions.[30] In these circumstances, the acquisition of a minority interest may confer control. CADE's focus on de facto control corresponds with the European Union rules, which consider a wide range of evidence of control.[31]

Because of CADE's focus on control, a firm that already has a controlling interest need not notify transactions that merely add incrementally to the controlling interest. For example, a firm that already maintains a 60 percent controlling interest need not notify when it purchases an additional 20 percent of the shares of the firm it already controls. The notification requirement arises only when the transaction causes a change in control.

2. SPECIAL INTER-AGENCY REPORTING

In addition, the Competition Act provides that any change in the stock control of publicly held companies or registration of amalgamations shall be reported by the Brazilian Securities Commission to Brazil's Economic Law Secretariat, known as SDE.[32] Under the Competition Act, SDE is the agency that receive the notification forms for antitrust review, and has investigative functions in the antitrust review process. The Brazilian Securities Commission must notify SDE for review within five business days of the change in stock control or registration.[33] The Competition Act states that this special inter-agency reporting rule is without prejudice to the parties' other obligations. Thus, the parties must notify SDE even though they reasonably expect the Brazilian Securities Commission to do so as well.[34]

B. JURISDICTION OVER FOREIGN FIRMS

The Competition Act expressly establishes jurisdiction over foreign firms that engage in acts that have or may have a detrimental effect upon competition within Brazil. Specifically, the Competition Act applies "to acts wholly or

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[30] *Id*.

[31] Council Regulation (EEC) No. 4064/89, art. 3(3), 1989 O.J. (L 395).

[32] Competition Act, art. 54, ¶ 10.

[33] *Id*.

[34] *Id*.

partially performed within the Brazilian territory, or the effects of which are, or may be suffered therein."[35] There is no question as to the jurisdiction of Brazilian antitrust authorities over foreign firms that conduct business in Brazil. If a firm operates or has a branch, agency, subsidiary, office, establishment, agent, or representative in Brazil, it shall be deemed situated in the Brazilian territory, and accordingly, will be subject to the laws of the nation.[36]

Through its jurisdictional language, the Competition Act incorporates the so-called effects doctrine of antitrust enforcement. Under the effects doctrine, antitrust enforcement reaches conduct based outside the country that has an effect within the country. The Competition Act appears to incorporate a broad version of the effects doctrine, as it covers conduct "the effects of which are or may be suffered" in Brazil.[37] A transaction between firms whose business activities do not presently have an effect in Brazil may be covered, based on a potential or likely future effect.

While the Competition Act reveals the government's intent to establish jurisdiction broadly over foreign firms, many important practical issues remain unresolved. Application of the effects doctrine may be difficult in varied factual settings. For example, how does the Competition Act apply to a foreign firm that has trivial sales in Brazil (e.g., less than U.S. $200,000), but has total worldwide revenue exceeding R$ 400 million? This could involve a large German firm with no sales in Brazil, acquiring an Italian firm with trivial exports there. Under a broad view of jurisdiction, the exports alone may constitute evidence of effects or potential effects in Brazil sufficient to confer jurisdiction.

The U.S. antitrust laws expressly exempt from notification transactions involving foreign firms with trivial sales or assets in the United States.[38] Likewise, the European Union's notification thresholds require a certain, significant amount of sales within the European Union.[39] CADE has not specified the amount of exports or sales in Brazil that constitutes a cognizable

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[35] *Id*. art. 2.

[36] *Id*.

[37] *Id*. (emphasis added).

[38] 16 C.F.R. §§ 802.50-51.

[39] Council Regulation (EEC) No. 1310/97 amending Council Regulation 4064/89, 1997 O.J. (L 180).

effect for purposes of jurisdiction. In fairness, many other national competition agencies have yet to promulgate specific rules on their jurisdiction over foreign firms, like those implemented by the United States and European Union. Thus, CADE is one of many other competition agencies that has not provided clear standards for determining jurisdiction over foreign firms' transactions. In any event, CADE should provide more guidance by identifying a threshold sales level for jurisdiction over transactions involving foreign firms.

The Timing of the Notification

One difficulty with merger control in Brazil is that the parties cannot easily receive approval or clearance of their transaction prior to consummation. A firm may notify either before closing or within fifteen business days after closing. CADE ordinarily approves or denies transactions only after the transaction has occurred and money has changed hands. Since the enactment of the Competition Act in 1994, most notifications have been made after consummation because prior notification has not increased the chances of receiving a prompt, favorable decision.[40]

CADE has dealt serious setbacks to some companies, such as Miller Brewing and Colgate-Palmolive, after the companies made costly expansions in Brazil. CADE initially ordered Miller Brewing to dissolve its joint production and marketing venture with Cervejeria Brahma after Miller already had made substantial investments in Brazil. Similarly, CADE ordered Colgate-Palmolive to suspend the Kolynos toothpaste brand from use in the Brazilian market for four years, after it had already spent substantial sums to acquire the popular brand. To avoid such situations, firms may include in their transaction agreement a suspension clause, by which they agree that the transaction will become effective only after CADE issues a favorable decision.[41] In other words, the closing of the transaction will be suspended until CADE's decision, whenever that occurs. But because CADE may take more than a year to reach a decision in any given case, firms typically will forgo suspension clauses in order to take advantage of business opportunities in Brazil without such significant delay.

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[40]Oliveira, *supra* note 1, at 479 ("In more than 95% of the cases, CADE examines the merger only after the fact").

[41] Urbiratan Mattos & Cristianne Saccab Zarzur, *The Emergence of Competition Law in Brazil*, Antitrust Rep. Mar. 1998.

The fifteen-day notification requirement is triggered by either formal consummation or de facto combination of the firms. CADE adopted a regulation in August 1998 defining the closing or the triggering event as the first formal act effectuating the transaction.[42] Alternatively, the CADE regulation provides that the triggering event may occur at the time in which the competitive relation between the relevant firms changes to the degree that they no longer behave like independent firms. In this latter scenario, the change in relationship between the firms must be of such a nature that it has effects on the marketplace.[43] As such, the regulation attempts to cover not only formal acts at closing but also instances in which the parties stop competing and behave as a single, united firm.

CADE's recent regulation clarifying the timing requirement followed its decision in August 1998 penalizing a firm for failure to notify in a timely manner. In Mahle/Metal Leve, CADE held that the fifteen-day time period begins the moment the acquiring firm has the ability to influence the competitive behavior of the other.[44] CADE rejected the parties' argument that the time period should begin from the date of share transfer and payment. The agreement gave the buyer, Mahle, rights over management decisions, including new expenditures, before the date of share transfer and payment.

The Notification Form

CADE has issued regulations concerning the notification form, which Article 54 of the Competition Act refers to as the application for authorization. In August 1998 CADE adopted Resolution 15, which established a new notification form.[45] As required by Resolution 15, the parties must provide in the notification form information on shareholders, affiliates, the structure and nature of the transaction, annual revenues, product lines, supplies and suppliers, customers, competitors, imports, the relevant markets, market shares, and entry.[46] Consequently, Resolution 15 requires the parties to

[42] CADE Resolution 15/98 of Aug. 19, 1998, art. 2, *available at* http:/www.mj.gov.br/cade.

[43] *Id*.

[44] Mahle/Metal Leve, Concentration 84/96 (Aug. 12, 1998).

[45] CADE Resolution 15/98 of Aug. 19, 1998, art. 1, Exhibit 1, *available at* http://www.mj.gov.br/cade/laws. Resolution 15 replaced Resolution 5, which contained the prior notification form.

[46] *Id*. Exhibit I.

engage in a substantive antitrust analysis involving difficult judgments concerning market definition and other sensitive antitrust matters.[47]

Resolution 15 requires submission, along with the notification form, of the transactional agreements, certain corporate governance records, and annual reports.[48] It does not require submission of any business records analyzing competition issues. In this respect, the notification form does not contain requirements similar to the Item 4(c) requirement in the United States or the Item 5.3 requirement in the European Union.[49]

Under Resolution 15, a single notification form, known as the application, applies to all transactions that must be notified. This marks an important change, one aimed at advancing consistency and certainty in the notification process. An earlier CADE regulation, known as Resolution 5, created different reporting requirements for transactions considered complex and those considered less complex.[50] It did not, however, provide clear guidance for determining whether a particular transaction should be treated as a complex one for reporting purposes.[51] Resolution 15 eliminates this confusion by establishing a single form applicable to all transactions.

Firms must submit the notification form and two duplicates including attachments to SDE.[52] SDE will then forward the forms to SEAE and to CADE, which will ultimately approve, condition, or deny the transaction.[53] Neither the Competition Act nor Resolution 15 requires a filing fee. Resolution 15 provides that, whenever possible, firms should submit a single, joint notification form.[54] If a firm must notify separately, it should provide all available information concerning the other party or parties to the transaction. A written justification must be provided in the event that the firms cannot

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[47] *Id*.

[48] *Id*.

[49] *See* 16 C.F.R. Pt. 803, Appendix (U.S. Hart-Scott-Rodino Act notification form); Implementing Regulation and Form CO available at http://europa.euoint (EU Form Co).

[50] CADE Resolution 5 of Aug. 28, 1996, art. 1, *available at* http://www.mj.gov.br/cade.

[51] *Id*.

[52] Competition Act, art. 54, ¶ 4.

[53] *Id*.

[54] CADE Resolution 15 of Aug. 19, 1998, art. 3, *available at* http://www.mj.gov.br/cade/laws.

supply any of the information requested by the form.[55] The parties are required to notify CADE of any alterations or changes in the data after submission.[56]

Second Requests

For transactions requiring further investigation, CADE may issue a second request for information, beyond that covered in the notification form. CADE will issue a second request for information after deciding that the notified transaction requires an additional investigation, referred to in Resolution 15 as a "complementary investigation."[57] Resolution 15 provides that CADE must decide whether to conduct a complementary investigation within sixty days after receipt of the notification form from SDE.[58]

The second request requires the parties to submit additional documents and provide narrative responses to interrogatories or questions covering various antitrust issues. With respect to documents, the second request asks the parties to supply their documents analyzing the transaction.[59] Business records treated as Item 4(c) documents under the Hart-Scott-Rodino Act in the United States fall within the scope of this request.[60] The second request also requires the parties to submit certain financial records prepared over the preceding three years.[61] The interrogatories or questions sets forth in the second request relate to market definition, supply side substitution, demand substitution, entry conditions, and efficiencies.[62] These questions require a more in-depth and detailed analysis compared to those in the notification form.

Compared to a second request in the United States, Resolution 15 second requests call for far fewer documents. In this respect, Resolution 15 does not impose significant document production costs. But Resolution 15 requires far more information than the initial notification form, especially in its

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[55] *Id.* art. 1, ¶ 1.

[56] *Id*. art. 3.

[57] *Id*. art. 7 & Exhibit II.

[58] *Id*. art. 7.

[59] *Id*. Exhibit II.

[60] *Id*.

[61] *Id*.

[62] *Id*.

interrogatories or questions relating to market definition, entry conditions, and other substantive antitrust issues.

Penalties

Failure to notify SDE may subject a firm to fines ranging from R$ 6,000 to R$ 6,000,000 (about US$ 5,300 to US$ 5,300,000).[63] The exact monetary figure for such penalties may vary widely and will be larger for firms committing purposeful or egregious notification violations. The relevant factors for assessing fines include: the severity of the violation; the violator's good faith (or lack thereof); any advantages obtained by the violator; the extent of damages or threatened damages to open competition; the adverse economic effects on the market; the violator's economic status; and recurrence.[64] A firm that fails to provide SDE or CADE with requested information may be fined R$ 5000 per day, a sum that may be increased twenty-fold based on the firm's size.[65] This fine may be imposed on third parties subject to information requests as well as the parties involved in the transaction. CADE has issued penalties in several cases for failure to notify a transaction.[66]

III.ANTITRUST REVIEW PROCESS AFTER NOTIFICATION

The Government Agencies

There are three government agencies in Brazil involved in antitrust investigation and enforcement: (1) SDE, the Economic Law Office of the Ministry of Justice; (2) SEAE, the Economic Monitoring Office of the Ministry of Finance; and (3) CADE, the Administrative Council for Economic

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[63] *Id.* art. 54.

[64] *Id.* art. 27.

[65] *Id.* art. 27.

[66] Lazzuril/Sherman-Williams, Concentration 80120022740/98-02 (Aug. 19, 1998); Elgin/Sherman-Williams, Concentration 8012002730/98-81 (Aug. 19, 1998); Mahle/Metal Leve, Concentration 84/96 (Aug, 12, 1998); CADE Questions the Pao de Acucar Group, GAZETA MERTANTIL ONLINE, Oct. 26, 1998 (discussing CADE enforcement actions against Brazilian supermarket chain, Pao de Acucar, for failure to notify); Usiminas/VUPSA/CBRD, Concentration 53/95 (July 9, 1997).

Protection. All three agencies have investigatory functions (sometimes overlapping), while CADE alone has the adjudicative function. Since 1994, CADE has enlarged its role, originally intended to focus on adjudicative functions, into the investigation phases.

1. SDE

SDE, headed by an Economic Law Secretary, serves as a clearinghouse for Brazilian antitrust investigations and plays both an investigative and an advisory role. As part of the Ministry of Justice, SDE's expertise and experience tends toward legal rather than economic analysis. Firms must submit their notification forms to SDE. SDE can request firms to provide additional information beyond the information submitted in the notification form.[67] In the review of notified transactions, SDE's primary function is to conduct fact investigations and advise CADE of its findings. Its responsibilities include issuing data and other information requests.[68] Following fact investigation, SDE submits a case report and evidentiary documents to CADE.[69]

A new CADE regulation – Resolution 15 – gives CADE more influence over the fact investigation.[70] Within sixty days from receipt of the notification form, CADE can decide that the transaction need not be investigated further.[71] Before making its decision to cease investigation, CADE must consult with SDE, as well as SEAE.[72] This change will likely reduce the investigating role of SDE and SEAE, as CADE may now decide on the basis of the notification form alone that the transaction should not be investigated further.[73] While Resolution 15 may substantially reduce the roles of SDE and SDE, CADE

[67] *Id.* art. 54, ¶ 8.

[68] *Id*. art. 14.

[69] *Id*. at ¶ 6.

[70] CADE Resolution 15/98 of Aug. 19, 1998, *available at* http://www.mj.gov.br/cade.

[71] *Id*

[72] *Id*

[73] *See CADE Resolution Diminishes Powers of SDE and SEAE*, GAZETA MERCANTIL INVEST NEWS, Aug. 19, 1998.

may not completely bypass these agencies without violating the Competition Act.[74]

During the first several years of the Competition Act, the SDE's review contributed to delay in the merger review process. But during 1998, SDE has worked much more quickly. SDE's improvements in 1998 may reduce the need for CADE intervention designed to reduce SDE's investigatory role. Indeed, the existence of Resolution 15, providing for the prospect of CADE intervention, may well cause SDE to continue to expedite the timing of its investigations.

Separately, SDE may conduct preliminary investigations to determine whether firms have improperly failed to notify a transaction. It may carry out such investigations on its own or at the written request of interested parties.[75] Within sixty days of the conclusion of its preliminary investigation, SDE must either order commencement of an administrative proceeding or termination of the case.[76] The Competition Act sets forth procedures for administrative proceedings applicable to investigations involving failure to notify a transaction. These are the same administrative procedures that govern alleged anticompetitive conduct outside the area of merger control. [77]

2. SEAE

SEAE's role in merger enforcement is to assist SDE in its fact investigation. As part of the Ministry of Finance, SEAE's strength lies in economics and finance. At the conclusion of its fact investigation, SEAE must prepare a technical report with its findings.[78] SEAE submits the report to SDE to assist SDE in its preliminary investigation. SDE may include information from SEAE's technical report in its preliminary findings submitted to CADE. The division of labor between SDE and SEAE in merger investigations has been a source of some problems. CADE officials have indicated that SEAE should focus on the economic aspects of the investigation and SDE the legal aspects. But this division of labor between SEAE and SDE has not worked well, and

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[74] *Id*. ("According to specialists in monopolies and mergers, a company could appeal against a CADE decision on the basis that CADE had not sought counsel from SDE and the SEAE.").

[75] Competition Act, art. 30.

[76] *Id*.

[77] *Id*. arts. 32-41.

[78] *Id*. at ¶ 6.

has been a cause of delay in the review process. As indicated earlier, CADE Resolution 15 enables CADE to intervene to limit both SEAE's and SDE's fact investigations.[79] This may well curtail SEAE's fact investigation role.

3. CADE

The Competition Act gives CADE exclusive authority to approve, condition, or deny notified transactions.[80] Although created earlier, CADE did not become an independent agency until 1994, when the Competition Act became effective.[81] The Competition Act has made CADE more independent by eliminating oversight by the Ministry of Justice, which no longer can review, approve, or overturn CADE decisions, as had been the situation prior to the Competition Act.

But CADE may not be as independent as competition agencies in other nations. CADE does not have its own budgetary resources, and often has to wait for the executive branch to allocate resources to it. Also, CADE board members have two-year terms with the possibility of reappointment once. This may give them more ties to the executive branch, compared to competition officials with longer terms in other countries. The Competition Act limited CADE member terms to two years because of executive branch fear of transferring power to an independent agency.

The CADE board consists of a president and six board members to be chosen based on legal or economic background.[82] The CADE board members must be appointed by the President of the Republic and approved by the Senate.[83] The CADE president has two votes in the event a CADE board member is absent from a session or cannot vote because of a conflict. CADE has an Attorney General who participates in CADE board meetings but does not have a vote. Once an official decision has been issued, the CADE President may order the CADE Attorney General to take all judicial action necessary to ensure the execution or enforcement of the CADE decision.[84]

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[79] CADE Resolution 15/98 of Aug. 19, 1998, art. 7, *available at* http://www.mj.gov.br/cade.

[80] Competition Act, art. 54.

[81] *Id*. art. 3.

[82] *Id*. art. 4.

[83] *Id*. art. 4.

[84] *Id*. art. 8.

While SDE will forward CADE the notification form and its investigative findings, the Competition Act authorizes CADE to order firms to provide additional information before reaching its decision on a transaction.[85] Resolution 15 now gives CADE greater powers over the investigation process. CADE can make a determination that further investigation is unnecessary, which may be appropriate when the notification form itself reveals that the transaction poses no threat to competition. This must occur within sixty days of CADE's receipt of the notification form from SDE. While CADE lacks statutory authority to terminate SEAE or SDE investigations, these agencies will likely abide by CADE's initial determination that no further investigation should be conducted. Alternatively, CADE can order within this sixty-day period a "complementary investigation," as discussed above.[86]

CADE has taken steps to ensure that the merger control process is transparent to the public. CADE publishes the Competition Act, its implementing regulations, and information on decisions at an internet site.[87] It also publishes an annual report summarizing its actions over the past year. The public may attend CADE deliberations or hearings on mergers or other notified transactions. CADE holds public deliberations on Wednesday afternoons each week.[88]

CADE adopted another regulation in 1998, Resolution 18, that may expand CADE's role relative to SDE and SEAE. Resolution 18 allows firms to consult directly with CADE prior to consummation.[89] This allows the firms to get an interim evaluation from CADE on the lawfulness of the transaction under the Competition Act. This way the firms can get some assurances without communicating with SDE or SEAE and without awaiting completion of their investigations. But an interim evaluation by CADE under Resolution 18 is not conclusive or binding.[90] A transaction can still be investigated by SDE and SEAE, and later declared unlawful by CADE based on the investigations.

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[85] *Id*. art. 43, 54, ¶ 8.

[86] CADE Resolution 15/98, art. 7, *available at* http://www.mj.gov.br/cade.

[87] *See* http://www.mj.gov.br/cade.

[88] *See* CADE ANNUAL REPORT at 7 (1997) (available in Portuguese only).

[89] CADE Resolution 18, effective Nov. 25, 1998.

[90] *Id*.

B. TIMING CONSIDERATIONS

The Competition Act sets forth a schedule for review, but this schedule typically does not hold. After a firm has submitted a complete notification form, SEAE should conduct its investigation and issue an initial technical report within thirty days.[91] Within thirty to sixty days thereafter, SDE should conduct and complete its preliminary investigation.[92] Once the SDE has forwarded its investigative findings to CADE, CADE should review the case and make all inquiries it deems necessary to render a decision within 60 to 120 days after its receipt of the case from SDE. If any of the agencies determines that it lacks adequate evidence or information necessary to complete its tasks, however, the deadlines will be stayed until such information is obtained.[93] Consequently, most CADE decisions do not meet the prescribed deadlines and, in fact, rarely are handed down in less than six months.[94]

The Competition Act provides that if CADE fails to render a decision in the time allotted, absent a stay, the transaction will be deemed automatically approved and not in violation of the Competition Act. While the Competition Act suggests the possibility of automatic approval in this manner, that has not occurred. The overwhelming majority of cases are stayed, thereby permitting the agencies to proceed under a slower schedule. Most of the delay can be attributed to SDE's and SEAE's fact investigations. SDE and SEAE have commonly requested delays to give them more time to investigate.

While the Competition Act envisions a total review period of 120 days, the typical review period has lasted much longer. Resolution 15 should expedite the process by curtailing the SDE and SEAE investigations, which have been a source of delay. Under Resolution 15, CADE can end the investigation sixty days after notification. It is widely expected that CADE will not

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[91] *Id*.

[92] *Id.* at art. 54 ¶ 6.

[93] *Id*. at ¶ 8.

[94] CADE, for example, was notified by the Brazilian steel producer Gerdau in March 1994 of its acquisition of a controlling share in Germany's Korf Gmbh., but partial approval of the acquisition was not given until a year later, in March 1995. CADE, RECENT JURISPRUDENCE, *supra* note 3.

completely bypass SDE and SEAE. But it is likely that in the wake of Resolution 15 cases will be resolved much more quickly.

In addition to Resolution 15, CADE has taken some other steps to reduce the time period from notification to decision. It adopted a regulation in October 1996 to allow firms to gain priority in the review process by giving notification before the closings or by negotiating transactions under suspension clauses.[95] Priority treatment would cease, however, at any time during the review process if the parties decide to put the agreement into effect or consummate the transaction.[96] While the regulation clearly intends to grant priority for early notification and for the use of suspension clauses, it fails to explain exactly what firms obtain through priority consideration. It gives no specific time commitments to the firms that notify before closing.

CADE has also adopted a regulation to give priority treatment to privatization transactions or transactions arising from a privatization program known as the Brazilian Denationalization Program.[97] But this regulation also suffers from the absence of any firm commitment to expedite review.

C. RECONSIDERATION AND APPEAL

A negative ruling from CADE will ordinarily require a performance commitment ordering divestiture of assets or other conduct. The review of any merger, acquisition, or joint venture will be followed by the publication of a CADE opinion in a Portuguese-language government periodical, the Federal Official Gazette. In addition to explaining CADE's analysis of the transaction, the opinion provides the decision of the CADE board either approving or denying the proposed transaction. The Competition Act provides that the CADE opinion must contain (1) a detailed report on any violations and an indication of the regulatory action or performance commitments; (2) the terms for commencement and conclusion of any regulatory action; (3) all applicable fines; and (4) daily fines which will be issued in the event of non-compliance with the CADE decision.[98] If CADE

[95] *Id*.

[96] CADE Resolution 6 of Oct. 2, 1996, art. 1, *available at* http:/www.mj.gov.br/cade.

[97]CADE Resolution 7 of Apr. 9, 1997, art. 1, *available at* http:/www.mj.gov.br/cade.

[98]Competition Act, art. 46.

holds that a transaction will be approved only upon acceptance of a performance commitment by the firms involved, then the conditions and objectives of the commitment will be set forth explicitly in CADE's opinion.

If corporations agree to performance commitments defined by CADE, they must enter into a formal commitment within fifteen days of their declared acceptance.[99] In doing this, they are bound to comply with the conditions stated in the CADE opinion. In addition, the Competition Act provides that SDE may also ensure compliance by monitoring the business activities of the firms involved.[100] CADE has asserted its authority under the Competition Act to monitor any firm's compliance with the performance commitments it has issued, and thus SDE has not played a significant role in monitoring performance commitments.[101] In the event of non-compliance with a performance commitment, CADE may revoke its approval of the transaction and commence an administrative proceeding.[102] If firms refuse to accept performance commitments in exchange for CADE approval of their transaction, they may indicate their wish on an express form submitted to CADE, or tacitly through silence for a period of thirty days following the publication of CADE's opinion in the Federal Official Gazette.[103] CADE's decision may provide for a different time period (other than thirty days) for firms to decide whether to accept performance commitments.

Firms may file a petition for reconsideration to CADE following a CADE decision. The applicant must support the petition for reconsideration by carefully describing new documents or facts that CADE did not have at the time of its initial decision.[104] For transactions that have yet to be consummated, the petition must be submitted within sixty days of CADE's unfavorable decision.[105] For transactions that have already closed, the petition must be submitted within the period stated in the CADE decision for

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[99] *Id*.

[100] Competition Act, art. 58, ¶ 2.

[101] *Id.* art. 47.

[102] *Id*.

[103] *Id.* art. 58, ¶ 3.

[104] CADE Resolution 15/98 of August 19, 1998, arts. 10-14, *available at* http:/www.mj.gov.br/cade.

[105] *Id.* art. 13.

rescission of the transaction or for responding to the requested consent order or performance commitment.[106]

Each firm subject to a decision by CADE has a constitutional right of appeal to the courts. Since enactment of the Competition Act, only one CADE decision has been appealed to the courts. That case, which involved imposition of fines by CADE for failure to notify, has not yet been decided by the courts.[107]

Firms that have had a merger, acquisition, or joint venture approved based upon their acceptance of a performance commitment or other concessions imposed by CADE. Also, they have a right to request a court to change the performance commitment if they can show that the conditions have become burdensome and that the changes will not cause damage to third parties or constrain competition in the Brazilian market. Such requests can also be made directly to CADE after entry of a performance commitment.

D. THIRD-PARTY COMPLAINTS

CADE has issued a regulation authorizing interested parties, including competitors, to make direct written inquiries to CADE.[108] Such inquiries should concern acts that are likely to result in a restraint of trade or monopolistic business practices. The regulation broadly covers all types of potentially anticompetitive conduct, and thus can be used to complain about mergers, acquisitions, or joint ventures that may restrain trade or create a monopoly.

CADE will review an inquiry only if it meets specific criteria set forth in its regulation. It must describe in detail the intention of the inquirer and the inquirer's arguments in favor of its own position and in opposition to the activities of the accused firm or firms.[109] The inquirer must substantiate all arguments and provide concrete evidence.[110] CADE must review the third-

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[106] *Id.*

[107] Usiminas/VUPSA/CBRD, Concentration 53/95 (July 9, 1997).

[108] CADE Resolution 10 of Oct. 29, 1997, art. 25, *available at* http://www.mj.gov.br/cade/laws.

[109] *Id*. art. 26 § 1.

[110] *Id.* § 2.

party complaint consistent with its standard administrative proceedings.[111] This may result in an evidentiary investigation, hearings, and deliberations by CADE.

IV.SUBSTANTIVE ANALYSIS

A. MARKET DEFINITION

Brazil's 1962 antitrust law did not refer to the term relevant market, or make any attempt to define what the concept means. This changed, however, with enactment of the new Competition Act in 1994. While the Competition Act does not define the term "relevant market," it refers to the term in several contexts.

Article 54 of the Competition Act states that "[a]ny acts that may limit or otherwise restrain open competition, or that result in the control of the relevant markets for certain products or services shall be submitted to CADE for review."[112] Article 54 also requires notification of transactions when the combined firm accounts for at least 20 percent of "a relevant market."[113] The civil non-merger sections of the Competition Act also refer to the relevant market. Article 20 describes conduct that violates the economic order as including actions "to control a relevant market of a certain product or service." It further states that market control or dominance occurs when a firm or group of firms controls a substantial share of "a relevant market," and that such dominance should be presumed when a firm maintains a 20 percent share of "a relevant market."[114]

Similar to the Sherman Act or Clayton Act in the United States, the Competition Act does not distinguish between geographic and product markets. Prior to the Competition Act, CADE used the concept of relevant market in its analysis of non-merger cases. In a 1993 case involving FIAT, the Italian-based automobile manufacturer, CADE applied the principle of substitution as a basis to explain what constitutes a relevant market: "The

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[111] *Id.* art. 29.

[112] Competition Act, art. 54 (emphasis added).

[113] *Id*.

[114] *Id*.

relevant market is the competition space. It is related to the several goods or services that compete among them, in a given area, as a response to their substitutability in that area."[115] Thus, by June 1994, when the Competition Act became effective, CADE had correlated market definition with substitution, but it had yet to develop further the concept of a relevant market in a coherent and clear manner.

CADE Resolution 15, which became effective on September 19, 1998, contains definitions of the terms product market and geographic market.[116] This marks the first legislative or regulatory definition of these important antitrust concepts. In addition, CADE's earlier published decisions serve as a source for understanding the product and geographic market concepts and their application. CADE's published decisions frequently identify the relevant product and geographic markets and explain the reasons CADE defined the market in that manner.

Product Markets

CADE Resolution 15 expressly defines the relevant product market. The product market definition is based on the concept of demand substitution. Indeed, it expressly calls for consideration of substitution by consumers based on the product or service "characteristics, prices and utilization."[117] It is now apparent from Resolution 15 that CADE's product market definition will

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[115] Processo Administrativo 31/92, Transavto Transportes Especializades de Automóveis S.A./FIAT do Brazil (Oct. 6, 1993), Revista do IBRAC Cadernos de Jurisprudência, Vol. 2, No. 1 (1993-1).

[116] CADE Resolution 15/98 of Aug. 19, 1998, Exhibit IV, *available at* http://www.mj.gov.br/cade.

[117] CADE Resolution 15 provides:

> A product relevant market includes all the products/services considered substitutable among themselves by the consumer due to its characteristics, prices and utilization. A relevant market of the product eventually could be composed by a certain number of products/services that present physical, techniques or business characteristics that recommend the grouping.

Resolution 15/98 of Aug. 19, 1998, Exhibit IV, *available at* http://www.mj.gov.br/cade.

focus on the preferences and decisionmaking of consumers. This approach conforms with the United States' focus on demand substitution.[118]

Resolution 15 merely defines the concept of a product market and does not set forth a test, as the U.S. Horizontal Merger Guidelines, for assessing the degree of demand substitution. It does not ask whether substitution would occur in response to a "small but significant and nontransitory increase in price" or a five percent price increase.[119] Nor does it describe in detail, like the U.S. Horizontal Merger Guidelines, the type and nature of the evidence it will consider on various factors affecting the demand substitution analysis. Thus, Resolution 15 does not represent complete guidelines for the analysis, but rather a general definition setting forth the key concept underlying CADE's product market definition.

Unlike the U.S. antitrust agencies, CADE publishes thorough decisions explaining its antitrust analysis, including market definition. These decisions provide further guidance for understanding CADE's market definition analysis and other matters. With the enactment of the Competition Act in 1994, CADE has been forced to address difficult issues of market definition in the earliest cases of merger enforcement. In September 1994 CADE reached its decision in connection with the Rhone-Poulenc S.A./Sinasa transaction. CADE performed a two-step analysis. First, it expressly defined the relevant product market as chemical fibers, which resulted in a combined firm share of only 24 percent. Second, it analyzed two segments or submarkets of the chemical fibers market consisting of acrylic fibers and polyester fibers. Based on these segments or submarkets, the combined firm share increased to 76 percent and 88 percent, respectively. On that basis, CADE ordered a divestiture of manufacturing assets.[120]

CADE's use of submarkets finds some support in U.S. antitrust law. In Brown Shoe Co. v. United States, the U.S. Supreme Court held that "within [a] broad product market, well defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes."[121] The Court identified various factors that could indicate the presence of submarkets,

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[118] U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines § 1.11 (1992), *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 13,104.

[119] *Id*.

[120] *See Rhondia and Sinas Plan to Divest Certain Polyester and Acrylic Fiber Production Assets in Brazil*, PR NEWSWIRE, June 28, 1995.

[121] Brown Shoe Co. v. United States, 370 U.S. 294, 325 (1962).

similar to those used in defining markets. Several lower courts in the United States have followed this approach in considering whether the competitive effects of a merger should be analyzed in submarkets.[122]

Although some lower courts have followed a submarket analysis approach, the Horizontal Merger Guidelines do not.[123] The Horizontal Merger Guidelines outline a single-step inquiry to define the relevant product market, rather than a two-step analysis involving the definition of a product market followed by the identification of any submarkets.[124] In the case of price discrimination by merging firms, U.S. antitrust authorities will consider additional relevant product markets and define them by the particular use or uses that groups of buyers have for the product in question. In other cases, however, U.S. antitrust authorities will not take a second step involving the identification of any submarkets based on the qualitative differences between the products in the relevant market, as CADE did in identifying submarkets for acrylic and polyester fibers in Rhone-Poulenc S.A./Sinasa.

The two-step submarket analysis has been widely criticized in the United States as unprincipled and biased toward merger enforcement.[125] Opponents of the submarket analysis argue that proper definition of product markets should be based on an economic evaluation that focuses on elasticity of demand. Such analysis does not entail identification of submarkets within a relevant product market. The use of submarkets may create a risk that a market will be defined too narrowly, resulting in opposition to a procompetitive or competitively neutral transaction.

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[122] *See* cases cited in ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS 520 n.112 (4th ed. 1997).

[123] Horizontal Merger Guidelines, *supra* note 116, at § 1.1 (1992).

[124] *Id.*

[125] Gregory J. Werden, *Market Delineation under the Merger Guidelines: A Tenth Anniversary Retrospective*, 48 ANTITRUST BULL. 517, 543-44 (1993) (criticizing Supreme Court's use of submarkets); William F. Upshaw, *The Relevant Market in Merger Decisions: Antitrust Concept or Antitrust Device?*, 60 N.W. U. L. REV. 424, 425 (1965) (describing the submarket concept as "a sort of universal solvent to be used to dissolve all forms of corporate consolidations"); *The Supreme Court, 1963 Term*, 78 HARV. L. REV. 143, 274-75 (1964) (the *Brown Shoe* court "appears to have taken a result-oriented approach to definition of the market, gerrymandering the boundaries 'so as to maximize the prospect of invalidating the challenged acquisition.")

CADE has not always used the two-step approach for defining relevant markets and submarkets since enactment of the Competition Act in 1994. In September 1996, approximately two years after Rhone-Poulenc S.A./Sinasa, CADE criticized its earlier two-step approach in its decision on Colgate-Palmolive's acquisition of Kolynos. It asserted that the use of submarkets conflicts with economic principles of market definition.[126] CADE's one-step analysis to define the relevant product market in the Colgate case aligned merger enforcement in Brazil more closely with the practices of the antitrust authorities in the United States.

Moreover, CADE expressly has described the product market analysis as including a review of the market's elasticity of demand, an approach which considers the change in the quantity of a product demanded by consumers in response to a change in prices. It is also an approach that corresponds with the economic focus of the U.S. Horizontal Merger Guidelines. In Colgate-Palmolive Co./Kolynos, CADE stated that "it would be better to calculate cross-elasticities of such lines of product than simply postulate its substitutability."[127] In the same decision, however, CADE emphasized the difficulty of obtaining data to measure demand elasticity given the inflationary instability in Brazil.[128] It indicated that measuring demand elasticity should become more feasible as prices become more stable.

In some decisions, CADE has departed from a purely economic approach to market definition by placing undue weight on product characteristics and insufficient weight on consumer preferences. In Miller Brewing Co./Cervejaria Brahma, CADE identified several important differences between pilsener beer and premium beer, yet found a single product market -- beer.[129] Average prices for premium beers exceeded pilsener prices by 20 to 40 percent. Middle and upper-income consumers tended to purchase premium beers, while lower income consumers tended to purchase pilsener beer. CADE found a significantly higher degree of particular brand loyalty among the premium beers and less price elasticity.[130] In contrast, pilsener

[126] Colgate-Palmolive Co./Kolynos, Concentration 27/95 (Sept. 1996).

[127] *Id.*

[128] *Id*.

[129] Miller Brewing Co./Cervejaria Brahma, CADE Concentration 58/95 (June 11, 1997).

[130] *Id.*

beers exhibited poor brand loyalty and greater price elasticity.[131] Despite these important differences suggesting separate product markets, CADE found one broad relevant product market consisting of beer, reasoning that while distinctive "organoleptic characteristics" (taste, color, and fragrance) may exist among premium beers, usually such characteristics are not detected by the majority of consumers.[132] Concentrating not on consumer preferences and demand, but upon the qualitative characteristics of products and the ability of consumers to tell them apart, CADE adopted a single product market consisting of beer. A more economic approach to market definition would have placed greater weight on consumer preference and less weight on product characteristics. This would have led to a narrow product market focusing on premium beer.

The recent Miller Brewing Co./Cervejaria Brahma decision might suggest that CADE still has not fully implemented an economic approach to market definition. CADE has embraced the concept of analyzing product markets on a dynamic basis and focused on the elasticity of demand, but may need to develop more experience and expertise needed for consistent application of the economic concepts. The use of economics is becoming more important in CADE's analysis of product markets. As CADE gains more experience, it is likely to place more emphasis on a product's demand elasticity and less on the more simplified review of the product's physical characteristics or attributes.

CADE's antitrust analysis continues to evolve in its consideration of supply substitution. Both supply substitutability and entry relate to the ability of producers not currently selling a particular product to start doing so. The U.S. Horizontal Merger Guidelines distinguish between entry and supply substitutability.[133] Entry analysis focuses on whether there is potential for significant new investment in production or distribution and whether such investment could be accomplished in less than one year; supply substitution examines whether there is a likelihood that firms will make a quick and low cost entry into the market in response to a small nontransitory increase in prices.[134]

Consideration of supply substitution in this manner avoids excessive segmentation of a market. A pure demand-side substitution analysis, without

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[131] *Id.*

[132] *Id*.

[133] Horizontal Merger Guidelines, *supra* note 116, §§ 1.3, 3.0.

[134] *Id.*

any recognition of supply substitution, would lead to unduly narrow product markets, such as separate markets for size ten and size eight shoes.[135] In this shoe example, demand-size substitution cannot be established because the size ten user will not switch to size eight. But supply-side substitution likely exists based on the ability of producers to shift rapidly from the manufacture of one size shoe to another, without incurring significant plant and equipment costs.

CADE used supply substitution in Gerdau Group/Pains to define the relevant product market as non-flat steel. In this industry, at least five different types of non-flat steel are used without any possible demand substitution. Different types of non-flat steel may include light structurals, reinforcing bar, wide flange beams, and rod. Based on supply substitution, CADE defined the product market as non-flat steel, including the various different types and sizes. Had CADE employed solely demand substitution in its analysis of Gerdau Group/Pains, it would have defined the market too narrowly based on the different types of non-flat steel.

While Gerdau Group/Pains demonstrates that CADE has recognized the relevance of supply substitution, a secondary question is how CADE will use supply substitution in its analysis of future cases. The United States and the European Union treat supply substitution differently. Under the U.S. Horizontal Merger Guidelines, principles of supply substitution are used to identify market participants, but not to define the product market itself. For example, consider a merger of two firms that manufacture metal hubcaps using stamping machines. Under the U.S. Horizontal Merger Guidelines, metal stamping firms not currently producing hubcaps would be included in the relevant market and would be assigned shares based on their capacity to produce hubcaps. Although these potential suppliers are included, their products are not; the relevant product would be stamped metal hubcaps rather than all products made with stamping machines.[136] In this respect, supply substitution principles may lead to identification of additional competitive firms, but they will not result in a delineation of different markets. In contrast, the European Union has recently chosen to recognize supply

[135]Gregory J. Werden, *The History of Antitrust Market Delineation*, 76 MARQ. L. REV. 123, 197 (1992) ("A size eight model in a particular shoe is a poor substitute for a size ten from the point of view of consumers, but essentially a perfect substitute from the point of view of producers.").

[136]*Id*.

substitution when delineating the product market, which could lead to a broader market consisting of all products made with stamping machines.[137]

In Colgate-Palmolive Co./Kolynos, CADE denied arguments in favor of using supply substitution to delineate a broader product market.[138] It cited the U.S. Horizontal Merger Guidelines in concluding that demand substitution must be given paramount weight in delineating the relevant market. Since Colgate-Palmolive Co./Kolynos, however, CADE has used supply substitution more expansively to delineate the relevant markets, consistent with the approach followed by the European Union.[139]

Geographic Markets

In its published decisions, CADE, has not routinely applied a dynamic geographic market analysis consist with Resolution 15, which defines geographic markets based on supplier response to a "small, but substantial elevation of the practiced prices."[140] Like the U.S. Horizontal Merger Guidelines, Resolution 15 focuses on the likelihood consumers will switch to other suppliers in different regions.[141] Defining geographic markets under

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[137]Commission Notice on the Definition of the Relevant Market for the Purposes of Community Competition Law, 97/C372/03 (1998); Simon Baker & Lawrence Wu, *Applying the Market Definition Guidelines of the European Commission*, 19 EUR. COMP. L. REV. 273, 275 (June 1998).

[138]Colgate-Palmolive Co./Kolynos, Concentration 27/95 (Sept. 1996).

[139] Mahle/Metal Leve, Concentration 84/96 (Aug. 12, 1998).

[140] Resolution 15/98 of Aug. 19, 1998, Exhibit IV, *available at* http://www.mj.gov.br/cade.

[141] CADE defined the relevant geographic market as follows:

> A geographic market includes the area in which the companies offer and seek products/services in sufficiently homogeneous conditions of competition, regarding the prices, consumers' preferences, products/services characteristics. The definition of a geographic relevant market also demands the identification of the obstacles to the entrance of the products offered by companies placed out of that area. The companies capable to begin the offer of the products/services in the area considered after a small, but substantial elevation of the practiced prices, are part of the geographic relevant market…

Id. This definition incorporates principles on geographic market definition from the U.S. Horizontal Merger Guidelines. *See* Horizontal Merger Guidelines, *supra* note 116, § 1.21.

Resolution 15 requires asking and answering the question whether firms currently outside a region will begin supplying products or services to the region in response to a small, but substantial elevation of the practiced prices.[142] This analysis corresponds the analysis under the U.S. Horizontal Merger Guidelines focusing on likely supplier response to a "small but significant and nontransitory" increase in price.[143]

In its enforcement decisions, CADE's geographic market analysis has been more static compared to its product market analysis. CADE has not consistently asked the question, for purposes of defining the relevant geographic market, whether a hypothetical monopolist in the region can successfully impose a small but significant and non-transitory increase in price. In the United States and the European Union, geographic markets are defined by determining where substitution likely will occur in the event of such a price increase.[144] So far, CADE has relied on a more legalistic approach. But Resolution 15 suggests future use of a more dynamic, economic approach to defining geographic markets.

Empirical evidence shows that CADE has been extremely reluctant to define geographic markets as worldwide. In 87 transactions evaluated by CADE from June 1994 until May 1998, CADE adopted a world market just once and a Mercosur market just once.[145] In all other cases, CADE used a national market or smaller geographic market. A Mercosur market consists of Argentina, Brazil, Paraguay, and Uruguay. These four countries entered into an agreement, referred to as Mercado Common de Sul, providing for some economic integration among them.

CADE's common use of national geographic markets overlooks the importance of trade liberalization in Brazil. Since 1994, Brazil has implemented tariff rate reductions, and foreign-based firms have developed distribution systems to facilitate imports. In the past several years, imports in

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[142]Resolution 15/98 of Aug. 19, 1998, Exhibit IV, *available at* http://www.mj.gov.br/cade.

[143]Horizontal Merger Guidelines, *supra* note 116, § 1.21.

[144]Horizontal Merger Guidelines, *supra* note 116, § 1.2; Commission Notice on the Definition of the Relevant Market for the Purposes of Community Competition Law, 97/C372/03 (1998).

[145] CADE adopted a world market in Verolme-lshibrás, Concentration 15/94 (Mar. 1994), Revista do IBRAC Vol. 3, No. 7 (July 1996). CADE adopted a Mercosur market in Cia Petroquĩmica do sul-Copesul/Opp Petroquĩmica Concentration 54/95 (Feb. 11, 1998), Revista do IBRAC Vol. 5, No. 4 (1998).

Brazil have grown dramatically. Increasing trade liberalization in the region suggests greater use of world markets, yet national and more local markets have prevailed in CADE's definition of relevant geographic markets.

Even when considering imports, CADE has often adopted a static approach of looking solely at current import levels, overlooking prior and projected levels and the price elasticity of imports. In several cases, CADE refused to adopt a world market because of a low import rate or a small volume of current imports. But an absence or low level of current imports does not indicate that the market is a national or smaller geographic market, nor does it mean that local sellers could exercise market power. Imports could enter rapidly into the area as soon as prices increased even slightly. CADE's geographic market analysis would be improved by looking beyond current imports and considering the price elasticity of imports. Resolution 15, with its consideration of supplier reaction to a "small but substantial" price increase, may lead precisely in that direction.

An article by Lucia Helenda Salgado, a CADE board member, reveals CADE's basic approach in the past to geographic markets. It states that "the concept of relevant market is an economic and legal hybrid" and that the focus should be "where the operation has its effects."[146] The article further states, without detailed explanation, that the use of a world market should be the exception.[147] Geographic markets, however, should not be defined "where the operation has its effects," but rather by looking at the location of the current and potential competitors that constrain the competitive behavior of the merging firms. Current and potential competitors may operate in separate geographic areas, and often do. Considering only the area where the parties' operations produce effects currently may overlook firms located in other areas that nonetheless act as competitive constraints. To conduct a dynamic economic analysis based on a product's elasticity of demand, CADE should look beyond the area where the operations of a party have an immediate effect.

CADE's published decisions further reveal its static approach to geographic markets. In one transaction, CADE used a national market even though the

[146]Lucia Helenda Salgado, "O concerto de Mercado; Relevante," Revista de Direito Econômico 26, CADE (1997).

[147]*Id*.

main competitor of the merging firms resided outside Brazil.[148] In several cases, CADE adopted a national market while recognizing the important competitive effect of imports. For example, CADE adopted a national market while acknowledging growing competition from Uruguay and Argentina.[149] Perhaps the most striking result comes from the Exxon Corp./Nalco Chemical Co. joint venture.[150] CADE adopted a national market despite the fact that Exxon participated in the Brazilian market exclusively through imports. CADE measured the change in concentration in the so-called national market by counting Exxon's imports but not the imports of any other firms.[151]

In CADE's initial decision opposing the Anheuser-Busch Inc./Antarctica joint venture, a dissenting board member pointed to evidence of decreasing beer prices in Brazil.[152] The commissioners who opposed the transaction dismissed this evidence of declining prices as merely the result of imported beer.[153] A critical element underlying the decision to restrict the joint venture was the use of a national geographic market. But the evidence that beer prices declined because of imports compels the conclusion that CADE's geographic market should not have been limited to Brazil. A dynamic and less legalistic approach to geographic market definition would recognize the importance of imports and consequently, firms situated outside Brazil's borders.

HERFINDAHL-HIRSCHMAN INDEX

Market concentration depends on the number of firms in the market and their market shares. As an aid in interpreting market share data, CADE has used the Herfindahl-Hirschman Index (HHI) of market concentration.[154] This follows the concentration analysis adopted in the U.S. Horizontal Merger Guidelines. The HHI, which is calculated by summing the squares of the

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[148] Electrolux/Oberdofer, Concentration 62/95 (Oct. 9, 1996), Revista do IBRAC Vol. 5, No. 2 (1998).

[149] Ficop/Alcan, Concentration 18/94 (Aug. 21, 1996).

[150] Exxon Corp./Nalco, Concentration 28/95 (June 19, 1996).

[151] *Id.*

[152] Anheuser-Busch Inc./Antarctica, CADE Concentration 83/96 at 46 (July 23, 1997), *available at* http://www.mj.gov.br/cade.

[153] *Id.*

[154] Horizontal Merger Guidelines, *supra* note 116, § 1.5.

individual market shares of each of the participants in the market, gives proportionately greater weight to the market shares of the larger firms, in accordance with their relative importance in competitive interactions.

In its Colgate-Palmolive Co./Kolynos decision, CADE expressly relied on an HHI analysis to evaluate the proposed transaction. The published decision contains the following table:

CADE HHI Chart, Colgate-Palmolive/Kolynos

product market	HHI before the operation	market structure	HHI after the operation	market structure	HHI change	likelihood of anticompetitive effect
toothpaste	644	highly concentrated	3750	highly concentrated	2691	presumed
tooth brush	1970	highly concentrated	2243	highly concentrated	272	presumed
dental floss	3720	highly concentrated	3782	highly concentrated	61	potential effects
tooth wash	1771	highly concentrated	1806	highly concentrated	35	unlikely

The CADE decision required a performance commitment or divestiture only with respect to the product market defined as toothpaste. As indicated by CADE's table, the HHI analysis reveals that other relevant product markets were highly concentrated, especially dental floss. But CADE focused on toothpaste, given the large change in HHI resulting from the proposed transaction. This approach aligns CADE with U.S. antitrust policy, as set forth in the Horizontal Merger Guidelines. Indeed, CADE used the same parameters as the U.S. Horizontal Merger Guidelines for classifying concentration levels. Under the U.S. Horizontal Merger Guidelines, markets are characterized as unconcentrated when the HHI falls below 1000, moderately concentrated when the HHI comes between 1000 and 1800, and

highly concentrated when the HHI exceeds 1800.[155] CADE used the same parameters and market characterizations in rendering its decision challenging Colgate-Palmolive's acquisition of Kolynos.

CADE also followed the U.S. Horizontal Merger Guidelines in analyzing the change in HHI as a result of the proposed transaction. Consistent with the Merger Guidelines, CADE found a presumption of an anticompetitive effect when the change in HHI exceeded 100 in a highly concentrated market. Likewise, CADE followed the Merger Guidelines and found that a change in the HHI between 50 and 100 in a highly concentrated market indicated that the transaction had a potential anticompetitive effect, but that even in a highly concentrated market, an increase in the HHI of less than 50 indicated that the transaction would not have an anticompetitive effect. Thus, CADE took no action with respect to the dental floss and mouthwash markets. But because the transaction produced a change in HHI over 100 in the toothbrush market, a highly concentrated market, it was necessary for CADE to find that other factors, especially ease of entry, overcame the presumption of an anticompetitive effect.

One of the CADE board members stated in Colgate-Palmolive Co./Kolynos that any HHI analysis should be used sparingly in Brazil, based on three observations: (1) modern economic theories of industrial organization and empirical evidence do not demonstrate a correlation between market concentration and anticompetitive conduct; (2) the Brazilian economy is much smaller than that of the United States, and thus should be analyzed differently; and (3) recent trade liberalization has created enormous industrial change and restructuring in the Brazilian economy.[156] These comments have shaped CADE's analyses in subsequent merger investigations.

The first observation reflects considerable accepted economic thought. It further reflects CADE's practice of looking beyond concentration indices to consider the role of other market characteristics, such as entry barriers and efficiencies. The second and third observations have caused some concern within CADE about the relevance of HHI to the Brazilian economy. This concern seems misplaced for several reasons. HHI analysis serves as an aid to evaluate market share data or concentration levels in a defined market. It does not represent a complete merger analysis, which should entail evaluation of entry barriers, efficiencies, and other factors. The HHI analysis may have

[155] *Id*.

[156] Colgate-Palmolive. Co./Kolynos, Concentration 27/95 (Sept. 1996).

limitations, but those limitations are the same for the Brazilian economy as for the U.S. economy. Characteristics of the Brazilian economy do not suggest that concentration indices such as HHI lack relevance.

The statement of the CADE board member in Colgate-Palmolive Co./Kolynos speaks more fundamentally to the role of efficiencies. The characteristics of the Brazilian economy may appropriately be considered in evaluating the nature and credibility of alleged efficiencies. In weighing the alleged impact of efficiencies that compensate for an increase in concentration, CADE has considered the Brazilian economy's smaller size relative to the U.S. economy. Moreover, CADE has also considered efficiencies in light of Brazil's industrial restructuring as a result of its trade liberalization. And it has recognized that local firms are seeking to become more efficient to compete better with foreign firms rapidly expanding into the Brazilian economy.

After the Colgate-Palmolive Co./Kolynos, CADE's use of HHI has increased substantially. But the use of the U.S. Horizontal Merger Guidelines' HHI parameters (e.g., an HHI from 1000 to 1800 equals moderate concentration) for characterizing concentration levels and evaluating the change in concentration has become less commonly accepted, largely as a result of the CADE board member's comments concerning application of HHI to the Brazilian economy. The underlying problem likely stems from CADE's approach to geographic markets. Because geographic markets have been defined narrowly, application of the U.S. Horizontal Merger Guidelines' HHI parameters would lead too often to presumptions that a transaction will create an anticompetitive effect. Unduly narrow geographic markets improperly raise the HHI levels and lead to unjustified presumptions about likely competitive effects. This has contributed to criticism of CADE's use of HHI analysis.

B. ENTRY

In the early days of the Competition Act, CADE did not routinely consider entry conditions. In fact, CADE ordered performance commitments in two

cases without even considering entry.[157] CADE has assumed, in some cases, the existence of entry barriers merely because the market was characterized by high levels of concentration. In the cases of Rhone-Poulenc S.A./Sinasa and Gerdau Group/Pains, CADE stated that the main barrier to entry was the high level of concentration itself.[158]

CADE's linkage of high market concentration levels and barriers to entry has confused the antitrust analysis. Economists often dispute the degree of linkage between high concentration and competitive performance. But economists widely accept the principle that high concentration does not correspond with anticompetitive market performance when entry is easy.[159] In these circumstances, any anticompetitive behavior of the incumbents (such as higher prices, reduced quality, and under-investment in new technology) creates profit opportunities for potential entrants. The potential for entry may deter the anticompetitive behavior in the first instance. Rather than associate concentration with barriers to entry, CADE must evaluate, as it has done recently, the factual circumstances relating to entry conditions in the affected industry.

Colgate-Palmolive Co./Kolynos marked a turning point in the importance of CADE's entry analysis. A third party, Proctor & Gamble, informally assisted CADE with an analysis of potential entry barriers, which CADE relied on in formulating its decision. Analyzing entry factors in a more exhaustive way than it had done before, CADE determined that competitive conditions in a highly concentrated product market (toothpaste) necessitated large-scale and relatively high-cost entry.[160] CADE found that the main barrier to entry was brand name, which required sunk costs associated with advertising and marketing.[161] Large-scale entry would be necessary to dilute the fixed costs of advertising and marketing.

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[157] Eternit/Brasilit, Concentration 6/94 (Nov. 1994), Revista do IBRAC Vol. 2, No. 3 (Sept. 1995); Rockwell Corp./Albarus, Concentration 01/94 (Dec. 1, 1994), Revista do IBRAC Vol. 2, No. 4 (Oct. 1995).

[158] Rhone-Poulenc S.A./Sinasa, Concentration 12/94 (Nov. 16, 1994); Gerdau Group/Pains, Concentration 16/94 (1995).

[159] *See, e.g.*, Jonathan B. Baker, *The Problem with* Baker Hughes *and* Syufy*: On the Role of Entry in Merger Analysis,* 65 ANTITRUST L.J. 353, 362 (1997).

[160] CADE, RECENT JURISPRUDENCE, *supra* note 3; Page, *supra* note 1, at 1124-26 (1998).

[161] Page, *supra* note 1, at 1124-26 (1998).

Without the detailed entry analysis in Colgate-Palmolive Co./Kolynos, CADE likely would have ordered a total divestiture, given the high concentration levels in several product markets affected by the transaction. But CADE did not base its decision solely upon the perceived correlation between high market share and barriers to entry, as it had done in past cases. Rather, detailed entry analysis narrowed CADE's focus on the impact of brand loyalty in the toothpaste market. CADE did not order a divestiture of any manufacturing assets, because it did not view any manufacturing requirements as barriers to entry. Instead, CADE offered the parties three alternatives: (1) suspension of the Kolynos brand for four years, (2) licensing of the Kolynos brand for twenty years, and (3) total divestiture.[162] Colgate-Palmolive agreed to suspend the Kolynos brand for four years. CADE sought suspension of the Kolynos brand name on the theory that firms would find entry opportunities more attractive in its absence.[163]

Since the cases immediately following enactment of the Competition Act, CADE has engaged in a more thorough, economic-oriented entry analysis. No longer does CADE associate barriers to entry with concentration levels alone. Some conceptual problems concerning entry remain, however. In Miller Brewing Co./Cervejaria Brahma, CADE ranked as an important barrier to entry, the "competition of imported beers."[164] It seems obvious that competition itself should not be regarded as a barrier to entry. If foreign competition presents such a threat to incumbent firms in Brazil, the better approach is to define the geographic market as worldwide rather than national, as CADE had done.

C. EFFICIENCIES

Efficiencies are a critical element of antitrust analysis in Brazil. Article 54 of the Competition Act provides that a transaction should ordinarily be authorized by CADE if it meets three or four of the following requirements: (1) the transaction will lead to an increase in productivity, improve the quality of a product or service, foster technological or economic development, or create efficiencies; (2) the resulting benefits shall be allocable to consumers in addition to the firms involved in the transaction; (3) only acts that are strictly

[162] *Id.*

[163] *Id*. at 1125-26.

[164] Miller Brewing Co./Cervejaria Brahma, Concentration 58/95 (June 11, 1997).

required to attain these objectives shall be performed for that purpose; and (4) the transaction will not drive competition out of a substantial portion of the relevant market.[165] According to the Competition Act, the parties must satisfy only three of these requirements if the transaction serves "the public interest" or operates "to the benefit of the Brazilian economy," terms in the law that remain unclear.[166] If the transaction does not serve the public interest or important interests for the Brazilian economy, the Competition Act requires the parties to satisfy all four requirements.

While the parties and the antitrust enforcers cannot easily determine for a given transaction whether three of these four statutory conditions have been satisfied, or whether the parties must satisfy only three rather than four of them, it is clear that efficiencies play an important role in the analysis under the Competition Act. The Competition Act requires a weighing of all cognizable efficiencies against any anticompetitive effects likely to result from the transaction.[167] It also asks whether the efficiencies claimed by the firms can be achieved through less restrictive means.[168]

Resolution 15 defines efficiencies as any cost reduction that could not be obtained through internal means.[169] The claimed efficiencies must be "intrinsic" to the transaction.[170] This corresponds with the U.S. policy that "the Agency will reject claims of efficiencies if equivalent or comparable savings can reasonably be achieved by the parties through other means."[171] A firm asserting efficiencies consistent with CADE's Resolution 15 definition must show (1) that the transaction will likely result in cost reductions, and (2) that these cost reductions could not be obtained by the firm alone.[172]

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[165] Competition Act, art. 54, ¶¶ 1-2.

[166] *Id.* ¶ 2.

[167] *Id.* ¶ 1.

[168] *Id.*

[169] Resolution 15 states: "Efficiencies means the reductions of costs of any nature, quantitatively esteemed and intrinsic to the transaction type related, that could not just be obtained by means of internal effort." Resolution 15/98 of Aug. 19, 1998, Exhibit IV, *available at* http://www.mj.gov.br/cade.

[170] *Id.*

[171] Horizontal Merger Guidelines, *supra* note 116, § 4.

[172] Resolution 15/98 of Aug. 19, 1998, Exhibit IV, *available at* http://www.mj.gov.br/cade.

Efficiencies might appear easier to prove under Resolution 15 compared to the U.S. Horizontal Merger Guidelines. Resolution 15 does not express any disfavor with efficiencies related to general selling, administrative, and overhead expenses, as do the U.S. Horizontal Merger Guidelines.[173] But Resolution 15's requirement that the claimed efficiencies be intrinsic to the transaction may reduce the importance of these types of efficiencies, and align CADE with U.S. antitrust policy toward efficiencies.

Neither Resolution 15 nor the U.S. Horizontal Merger Guidelines requires firms to prove that efficiencies will be passed on to consumers, but nor does the. The policies of both Brazil and the United States reflect the view that merger-specific efficiencies are those that are most likely to benefit consumers. Accordingly, for CADE's review and approval, firms must be prepared to show that the transaction will create cost savings or other benefits, which likely will flow to consumers.

In its published decisions, CADE has distinguished between private and public efficiencies, referring to public efficiencies as those likely to extend beyond the parties to the transaction. The so-called public efficiencies include benefits to consumers, but also other matters that would not be accounted for as efficiencies under the U.S. Horizontal Merger Guidelines. In one case, CADE required the buyer to invest in pollution control programs.[174] In Colgate Palmolive Co./Kolynos, CADE required the firms to invest in programs relating to dental health. These two cases demonstrate CADE's use of public efficiencies to benefit a much broader segment of the general population than just consumers. In other cases, CADE has directed its decisions more directly toward the relevant consumers. For example, in Norton/Carborundum and Rockwell Corp./Albarus, CADE required quality improvements and price decreases respectively, which were designed to benefit consumers in the relevant markets.[175]

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[173]Horizontal Merger Guidelines, *supra* note 116, § 4 ("The Agency may also consider claimed efficiencies resulting from reductions in general selling, administrative, and overhead expenses . . . although, as a practical matter, these types of efficiencies may be difficult to demonstrate"); U.S. Department of Justice and Federal Trade Commission, Revisions to Horizontal Merger Guidelines (1997) (efficiencies "related to procurement, management, or capital cost are less likely to be merger-specific or substantial, or may not be cognizable for other reasons").

[174] Yolat/Parmalat, Concentration 11/94 (Nov. 23, 1994), Revista do IBRAC, Vol. 2, No. 3 (Sept. 1995).

[175] Norton/Carborundum, Concentration 5/94 (Oct. 19, 1995), Revista do IBRAC Vol. 3, No. 4 (Apr. 1996); Rockwell Corp./Albarus 01/94 (Dec. 1, 1994), Revista do IBRAC Vol. 2, No. 4 (Oct. 1995).

CADE's consideration of efficiencies has weighed heavily in several decisions since the Competition Act became effective in 1994. In its review of the joint production and marketing agreement between the Miller Brewing Co. and Brahma in 1995, CADE made a detailed appraisal of the efficiencies, or what it entitled "the benefits of the operation."[176] The joint venture agreement provided for the production and sale of the Miller Genuine Draft brand of beer in Brazil. By December 1996, after notification, but before CADE's decision, Miller and Brahma jointly had attained a leadership position in the premium beer market in Brazil. CADE in its analysis found that Miller and Brahma had improved their positions while consumers of beer had not. CADE found that the joint venture enhanced Brahma's market power to such an extent that it was in a position to restrain competition within the domestic market for beer.[177] As part of its analysis, CADE further examined whether the benefits or the efficiencies generated by the joint venture sufficiently counterbalanced the resultant restraints to competition within the national beer market.[178] In balancing the efficiencies against the joint venture's market control, CADE determined that the venture, as proposed, violated the Competition Act and should not be approved.

CADE determined that all of the efficiencies claimed by the two breweries were not, in fact, likely, and that those that did result from the joint venture flowed to the firms involved rather than the consumer. Specifically, CADE found that the parties' mere adaptations of existing Brahma breweries failed to contribute to the expansion of production capacity as the parties under review had claimed.[179] Moreover, CADE found that the prerequisites for approval under Article 54 of the Competition Act were not satisfied because Miller failed to invest significantly in new production facilities and distribution networks in Brazil.[180] Considering whether the claimed efficiencies could have been achieved in a less restrictive manner, CADE determined that all benefits resulting from the joint venture could have been achieved through Miller's independent entry into the Brazilian beer market.[181] This course of action would have resulted in increased competition in the

[176]Miller Brewing Co./Cervejeria Brahma, Concentration 58/95 (June 11, 1997).

[177]*Id*.

[178]*Id*.

[179]*Id.*

[180]*Id.*

[181]*Id.*

marketplace and considerably less market concentration than the joint venture between the two brewers. CADE contrasted Miller's attempted expansion into Brazil with that of the small brewer Schincariol, which obtained a small but impressive share of the Brazilian beer market after persistent investment produced efficiencies in the form of increased production and improved quality.[182] Additionally, CADE found that Miller Genuine Draft's classification as "draft beer in a bottle," was merely a product differentiation factor, which did not provide the Brazilian beer drinker with a sufficient taste differential, and therefore consumers received no tangible benefit from the joint venture.[183]

In its analysis of the Miller Brewing Co./Cervejeria Brahma joint venture, CADE considered the efficiencies listed under Article 54 of the Competition Act, but also expressed its intent to consider efficiencies and factors not specifically identified by the Competition Act.[184] At times, CADE has turned to international case law for its analysis of efficiencies affecting domestic markets. In assessing efficiencies relating to the 1996 joint production agreement between Anheuser-Busch and the Brazilian brewing company, Antarctica, CADE referred to case law of both the European Union and the United States, in addition to Article 54 of the Competition Act.[185] CADE reviewed the European Commission's consideration of a similar case involving brewing companies in Europe.[186] It further highlighted the fact that European Union law generally permits joint ventures when they present likely efficiencies, such as expanding research and development activities, generating new products, or expanding production capacity.[187] Also, CADE emphasized that the U.S. Supreme Court has held that a joint venture is little more than a naked restriction on trade if it is not characterized by integrative

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[182] *Id.*

[183] *Id.*

[184] *Id.*

[185] Anheuser-Busch Inc./Antarctica, CADE Concentration Act 83/96 at 18-21, Vote of Reporting Board Member Lucia Helena Salgado e Silva (doscissopm at §I-4 "Introduction: Competition Policy as a Pillar of Non-Exclusive Development – Recent Case Law"), *available at* http://www.mj.gov.br/cade.

[186] *Id.* at 18 (discussing Commission's investigation of license agreement between Carlsberg and Interbrew).

[187] *Id.*

efficiencies.[188] CADE indicated that integrative efficiencies may include the sharing the risks through joint activity, such as in creating new products and constructing new marketing distribution channels.[189]

Thus, in addition to considering those efficiencies defined by Article 54, CADE has also considered efficiencies that are not expressly described in the Competition Act and has used international sources to identify other such efficiencies. Indeed, a former CADE official has observed that other efficiencies besides those in the Competition Act should be taken into consideration.[190] She has argued that when using the generic term "efficiency," the Competition Act allows for the inclusion of scale economies, the integration of facilities, the specialization of plants, and other benefits related to production and distribution.[191]

In Miller Brewing Co./Cervejeria Bruhma and other decisions, CADE has required firms to show by specific evidence that the alleged efficiencies are likely to benefit consumers. This conforms with Article 54's requirement that efficiencies be "allocated" to consumers or end-users.[192] CADE has not focused as much on the Article 54 provision regarding alternative means for obtaining the efficiencies.[193] So far, CADE has not strictly required that the transaction be the only mechanism to achieve the asserted efficiencies, although Article 54 appears to require that. CADE Resolution 15, by requiring that the efficiencies be intrinsic to the transaction, should cause greater attention to be focused on the question whether the benefits can be achieved through other, less restrictive means.[194]

Performance Commitments

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[188] *Id.* at 19 ("In the United States, when an alleged joint venture does not involve the integration of resources and is nothing more than an attempt on the part of competitors to restrict competition, the Supreme Court has dealt with a joint activity as a 'naked restraint of trade and invalidated such as illegal per se.'")

[189] *Id*. at 19-20.

[190] Niede T. Mallard, Integraçao de Empresas: Concentraçao, Eficiência e Controle (presented at the International Seminar of Competition Defense (1994)).

[191] *Id*.

[192] Competition Act, art. 54, ¶ 1 § 2.

[193] Mallard, *supra* note 188 ("only the acts strictly required to attain an envisaged objective shall be performed for that purpose").

[194] *See* CADE Resolution 15/98, Exhibit IV, *available at* http:/www.mj.gov.br/cade.

The term performance commitment comes directly from the Competition Act.[195] Like consent decrees in the United States, performance commitments are agreed alterations to the proposed transaction that are designed to reduce or eliminate an anticompetitive or other improper market effect. Specifically, CADE issues performance commitments to ensure that the firms comply with the efficiencies and conditions established in Article 54.[196]

Performance commitments in Brazil are described as either structural or behavioral. Structural performance commitments usually involve a one-time sale of assets, such as a manufacturing plant. Behavioral performance commitments usually involve conditions placed upon the ongoing business conduct or behavior of the surviving firm.

The Competition Act provides that in drafting performance commitments, CADE will consider international competition, domestic employment levels, and other relevant circumstances.[197] Thus, the Competition Act expressly directs CADE to take into account domestic employment in fashioning performance commitments. CADE has exercised this authority by issuing performance commitments relating to employment in several transactions. In Oriento/Ajinomoto, CADE simply required that the merging firms maintain existing employment levels.[198] In several other cases, CADE has required the merging firms to invest in training for employees who were to be laid-off or dismissed. [199]

In addition to issues of employment, the Competition Act expressly gives CADE authority to consider international competition in the relevant market and all other "relevant circumstances" in its formulation of performance commitments.[200] "Relevant circumstances" is a catch-all phrase which conceivably gives CADE an expansive license to evaluate matters beyond efficiencies or other competitive concerns. CADE has used this broad

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[195]Competition Act, Title VII, chapter II. The Competition Act refers to performance commitments, but does not define that term.

[196]*Id*. art. 58.

[197]*Id*. ¶ 1.

[198]Oriento/Aginomoto, Concentration 19/94 (Feb. 28, 1996).

[199] Santista/Carfepe, Concentration 25/95 (Aug. 7, 1996); Grace/Crown, Concentration 24/95 (July 10, 1997); Verlome/Ishibras; Colgate-Palmolive.Co./Kolynos, Concentration 27/95 (Sept. 1996).

[200]Competition Act, art. 58.

authority in several cases. While Article 54 does not explicitly address exports, CADE has required significant export increases in several transactions.[201] CADE also required investment in pollution control and in health programs. Thus, when ordering performance commitments, CADE has not restricted itself to considering only efficiencies and other competition matters.

Like consent decrees used by U.S. antitrust authorities, CADE has relied upon structural performance commitments to eliminate or reduce a transaction's potential harm to competition. Structural commitments have typically entailed the divestiture and the sale of assets, the licensing of technology, or the leasing of equipment. In Rhone Poulenc S.A./Sinasa, for example, CADE required the partial divestiture of manufacturing assets.[202] Similarly, in Gerdau Group/Pains, CADE required the refurbishment and divestiture of a steel plant and divestiture of a transportation company, leaving all other assets of the merged firms intact.[203] During the acquisition of Kolynos, not only did CADE order Colgate-Palmolive to suspend a brand name, but it also ordered the company to sell 14,000 tons of toothpaste for private labeling and sales.

Since the passage of the Competition Act, CADE has, in several cases, relied upon behavioral performance commitments. In Gerdau Group/Pains, for example, CADE required a mandatory disclosure to third party competitors of technical information developed through a research and development agreement with another firm. In fashioning performance commitments, CADE has occasionally sought to promote investment in Brazil, by requiring investment, often stipulating how much a corporation must invest over a defined period. For instance, CADE approved a transaction in 1995, upon agreement that the buyer invest U.S. $1.6 billion through the year 2000.[204] In

[201] Helios/Carbex, Concentration 13/94 (Nov. 20, 1996); Colgate-Palmolive Co./Kolynos, Concentration 27/95 (Sept. 1996); Rockwell Corp./Albarus, Concentration 01/94 (Dec. 1, 1994), Revisto do IBRAC, Vol. 2, No. 4 (Oct. 1995).

[202] *See* Rhondia and Sinasa Plan to Divest Certain Polyester and Acrylic Fiber Production Assets in Brazil, PR NEWSWIRE, June 28, 1995.

[203] CADE, RECENT JURISPRUDENCE, *supra* note 3 (CADE discussion of divestiture relating to acquisition between Gerdau Group and Korf GmbH involving steel).

[204] Helios/Carbex, Concentration 13/94 (Nov. 20, 1996).

other cases, CADE has required specific types of investment, such as in technology, or research and development.[205]

For the first two years under the Competition Act, CADE requested performance commitments to ensure efficiencies in almost all cases. In the case of Verolme/Ishibras, for example, CADE adopted a worldwide geographic market for the product market consisting of boats.[206] As a result of the broad geographic market, the firms involved had a trivial market share. CADE nevertheless insisted on a behavioral performance commitment to ensure efficiencies.[207]

Since 1996 CADE has required fewer efficiency-related, behavioral performance commitments in transactions that do not present a clear risk of anticompetitive effect. Between May 1996 and December 1997, CADE approved 78 percent of all transactions without imposing any form of performance commitment.[208] While CADE now issues much fewer behavioral performance commitments than it did during the 1994 to 1996 period, it still may consider behavioral performance commitments. Between May 1996 and December 1997, 14 percent of all transactions submitted and decided by CADE required performance commitments intended to promote efficiencies. In a decision from November 1997, for example, CADE required commitments to improve qualitative standards, to implement commercial policies for certain brands, and to develop certain technology.[209]

VI.CONCLUSION

In a short period of time, Brazil has implemented a comparatively sophisticated merger control program. While many nations have enacted antitrust laws providing for mandatory review of mergers, acquisitions, and joint ventures during the past several years, few of these nations have

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[205] Electrolux/Oberdofer, Concentration 62/95 (Oct. 9, 1996), Revista do IBRAC Vol. 5, No. 2 (1998).

[206] Verolme-Ishibras, Concentration 15/94 (Mar. 1994), Revista do IBRAC Vol. 3, No. 7 (July 1996).

[207] *Id.*

[208] CADE'S ANNUAL REPORT 1997 (published in Portuguese only).

[209] Panex/Alcan Aluminio de Brasil, Concentration 79/96 (Nov. 19, 1997).

advanced as far as Brazil in its merger control procedures and policies. In less than five years, Brazil has adopted a mandatory merger control law and implemented significant procedural and substantive improvements. Other new competition agencies can learn much from the Brazilian model.

Since its enactment of the Competition Act, Brazil has taken important steps to improve merger control procedures. CADE has adopted and published regulations clarifying and addressing various procedural issues. CADE, in its regulations, has adopted measures for reducing duplicative multi-agency oversight and shortening the merger review period. It has clarified the notification form and timing considerations concerning notification, and enumerated third party rights to participate. It has even adopted procedures for challenging or moving to reconsider CADE decisions. The regulations have been published, in English as well as Portuguese, on a CADE internet site.[210] These represent significant steps to advance the worthy goals of greater transparency and certainty in the merger review process.

Merger enforcement requires substantive antitrust analysis at the most sophisticated levels. CADE's substantive analysis has improved considerably since enactment of the Competition Act. CADE has reduced the use of behavioral performance commitments, and now seeks to tailor the performance commitments more narrowly in order to remedy the specific anticompetitive threat presented by the transaction. CADE's product market definition analysis now focuses more on consumer preference rather than product characteristics. Geographic market definition should become more dynamic, without the prejudice against world markets. CADE continues to place appropriate weight on the recognition of merger-specific efficiencies.

The policies adopted by CADE since enactment of the Competition Act have improved the merger control process and analysis in Brazil. But room for improvement exists in several areas. CADE's notification thresholds still create uncertainty by including a market definition test. The time period for clearance needs to be shortened, which CADE hopes to accomplish through Resolution 15. CADE should engage in a more economic analysis of entry and geographic markets. CADE's current leadership has significantly advanced merger control law, and indications are they will continue to make improvements.

[210] http://www.mj.gov.br/cade.