

The New German Digitalization Act: An Overview

The Digitalization Act, which entered into force on January 19, 2021, substantially extends the scope of German antitrust law to tackle presumed enforcement challenges in the digital economy and raises merger control thresholds across all industries.

The Digitalization Act is the 10th amendment of the German Competition Act (GWB), the so-called GWB10. The most prominent changes include:

1. A new quasi-regulatory tool to prohibit certain conduct patterns of platforms on multi-sided markets and networks (§ 19a). This new tool is combined with a shortening of the judicial review process (§ 73(5)) — appeals can now only be heard by the Federal Court of Justice (FCJ).
2. A new ex ante tool that, in essence, prohibits conduct that may amount to a tipping of the market as “unfair impediment of competitors” (§ 20(3a)).
3. Higher merger control thresholds that will significantly reduce the number of notifiable transactions across all industries (§ 35(1)).

This *Client Alert* provides an overview of these three major changes. Latham & Watkins will discuss additional changes in GWB10 that are highly relevant in practice, especially new and extended rules on access to data (e.g., § 19(4), §20(1a)), in upcoming *Alerts*.

New Tool to Control Platform Conduct

The heart of GWB10 is arguably the Federal Cartel Office’s (FCO’s) new power to tackle certain patterns of conduct of companies with “paramount importance for competition across markets” (*PICAM*). This new power is primarily targeted at large digital platforms and tech companies. However, it is applicable to all companies, B2B, and B2C platforms active on multi-sided markets and networks that have a strong market position on two or more markets. The legislative reasoning indicates that there will be approximately three cases in the next five years, and the FCO has publicly announced that it is already working on initiating such investigations.

The two-pronged instrument introduces (i) an unprecedented concept of market power of companies active on multi-sided markets and networks and, (ii) an extensive list of patterns of conduct that the FCO may prohibit if it has found *PICAM*. While these two determinations are to be made separately, in

practice, they can and likely will be synchronized and adopted as one decision (as provided for by § 19a(2) last sentence).

This new set of rules may aim to protect non-platform/smaller tech companies. However, the new procedures and ex ante test may negatively impact rights of defense. The scope of the broad and far-reaching blacklist of conduct is yet to be defined. Pro-competitive behavior, innovation, and pro-consumer products that are introduced to the market (also) by large digital platforms should not be overlooked when interpreting and applying the new rules.

Paramount importance for competition across markets (PICAM)

The FCO must first determine a company's PICAM based on a non-exhaustive list of criteria set out in § 19a(1), including financial strength, access to competitively relevant data, and intermediation power. Market dominance is one of the factors to be considered, but is not a prerequisite for finding PICAM. It follows that the threshold of the new tool is below that of market dominance. A finding is limited to five years (pursuant to § 19a(1) last sentence).

Blacklisted conduct

Once the FCO has found a company's PICAM, it can, in a second step, prohibit certain types of conduct as abusive, including:

- Self-preferencing (a company giving preferential treatment to own offers over competitors' offers)
- Foreclosure (impeding other companies in their activities on upstream and downstream markets)
- Leveraging market power (impeding competitors on a market, on which the company can rapidly develop its position even without being dominant)
- Processing and combining data from different sources (and thereby creating or raising market entry barriers)
- Denying or hindering interoperability or portability of data
- Creating information deficits vis-à-vis providers of services (providing the companies with insufficient information on the scope, quality, or success of services)
- Requesting a disproportionate advantage for the treatment of another company's offers

While relevant conduct cannot be prohibited if objectively justified, the company concerned carries the burden of proof for the justification.

Potential limiting principles to blacklisted conduct

There is no case law to guide the application of the unprecedented concept of the new § 19a by the FCO. The blacklisted conduct is specified by examples, both in the provision itself and in the legislative reasoning, which apparently aim at capturing current practices of digital platforms that have already been assessed in pending cases or upcoming investigations. The FCO and the courts will, therefore, have to consider limiting principles for the application of the new provision. These may include:

- The prohibition of self-preferencing should be limited to favoring own products, e.g., a more prominent placement of its own products on a shopping site's search page while demoting rival products, as opposed to self-promotion — e.g., a company's use of its inventory as advertising space for its products.
- Pro-competitive conduct that facilitates (a) entry into markets lacking effective competition or (b) innovation should not be considered an abusive leveraging of market power.
- Data processing should be permissible if (i) the data is aggregated and anonymized and therefore cannot be attributed to individual users (or businesses) or (ii) users have sufficient choice as to the circumstances, the purpose, and the manner of use of the processing.
- The far-reaching prohibition to deny or hinder interoperability should not be interpreted as creating a positive obligation to enable interoperability. Such an interpretation would promote free-riding and stifle innovation and the launch of new services.

One instance appeals process

As a truly last-minute introduction into the pending legislation, § 73(5) stipulates the FCJ as the first and only instance for legal proceedings regarding the FCO's decisions under § 19a. However, the need for this acceleration seems doubtful, particularly in light of the already immediately enforceable nature of the FCO's orders. A "delay" in proceedings can only occur if a qualified and specialized court has found "serious legal doubts" as to the legality of an FCO order. Additionally, the FCO can apply interim measures, and the prerequisites for applying these measures have been reduced by § 32a.

Further, the new system only provides for one instance of judicial review despite the legal uncertainty surrounding § 19a and the expertise of the Düsseldorf Higher District Court as standing court of appeals against FCO orders. It remains to be seen how the FCJ — traditionally a pure appellate court — will assess the factual basis of a case and comprehensively review the FCO's factual findings.

New Tool Against the Tipping of Markets

GWB10 introduces a new tool to prevent "tipping" of multi-sided (particularly digital) markets into monopolistic or highly concentrated markets. The tool enables the FCO to intervene against non-dominant companies already at an early stage, as the legislator (the German Parliament) anticipates irreversible consequences once a market has tipped.

Companies with superior market power

The new tipping provision targets companies with superior market power active on multi-sided markets. This allows the FCO to intervene before the company has reached a position of dominance. According to the bill's reasoning, "superior market power" must be assessed in relation to all competitors active on the affected markets and not just small- and mid-sized companies (unlike in § 20(3) GWB).

Impediment of competitors' independent attainment of network effects

The provision prohibits impeding competitors from independently realizing network effects. The provision is drafted broadly and lacks examples, but appears principally aimed at obstruction of (i) multi-homing and (ii) switching platforms. Refusal of interoperability, on the other hand, is explicitly excluded as relevant conduct in the legislative reasoning.

No evidence on competitive effects required

The provision only requires a risk for a tipping of the market. The FCO does not have to wait until exclusionary conduct actually harms competition. In practice, it will likely be difficult for the FCO to accurately predict the tipping of a market. Premature intervention may have the opposite effect and slow down innovation to the detriment of consumers.

Increase of Merger Control Thresholds

In another last-minute change, the current merger control thresholds have been substantially raised in order to relieve (mid-sized) companies from notifying transactions of minor economic importance. This change aims at reallocating and focusing the FCO's resources on other enforcement priorities, including use of the new tools and powers discussed above:

- The turnover test is amended by increasing the domestic turnover threshold of at least one company concerned to more than €50 million and that of another company concerned to more than €17.5 million (§ 35(1) no. 2, rather than previously €25 million and €5 million).
- The thresholds for the value of the transaction — i.e., the consideration for the acquisition exceeds €400 million, and the requirement of substantial operations in Germany of the target — remain unchanged (§ 35(1a)).
- As a consequence of the increased domestic turnover thresholds, the de minimis exemption (acquisition of an independent company with less than €10 million worldwide turnover) is now redundant and has been abolished (former § 35(2) sentence 1).

GWB10, which is expected to reduce the number of notifiable cases by 20% to 30%, applies to all transactions that close on or after January 19, 2021. This is also true for cases that were notified before the amendment entered into force (under the old thresholds). Those notifications can be withdrawn.

Even if a transaction must be notified, the so-called exemption for “de minimis markets” (*Bagatellmarktklausel*) has been increased to €20 million. That said, several related affected de minimis markets must be assessed together under the new provision, thereby reducing the threshold for intervention in those cases.

Finally, the period for a Phase II review has been extended from four to five months (§ 40(2), second sentence).

Sector-Specific Expansion of Notification Obligation

The FCO may obligate a company, for a limited three-year-period, to notify every acquisition in a given industry, even if the domestic turnover thresholds are not met. This provision is perceived to also target “killer acquisitions” of small or the smallest companies.

The expansion of the company's formal obligation to notify is subject to further requirements, most prominently a sector inquiry with findings of competitive concerns in the respective industry, post-dating the entry into force of the new law. The risk of significant impediment of effective competition must relate to Germany. As a result, in practice, only very few companies are likely to be subject to such an obligation. The criteria for the substantive assessment of acquisitions under review remains unchanged.

Outlook

With GWB10, the German Parliament is aiming to take a leading role in international efforts to address the perceived under-enforcement of competition law in the digital economy. Germany is the first country in the world to introduce rules specifically tailored to address certain patterns of conduct of large digital platforms in a quasi-regulatory manner. Meanwhile, the European Commission proposed enacting similar tools for digital gatekeepers in the Digital Markets Act. Given that legislation, the new German tools bear the risk of a diverging national legal standard in the European Union.

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