

***Case No COMP/M.4581 -
IMPERIAL TOBACCO /
ALTADIS***

Only the English text is available and authentic.

**REGULATION (EC) No 139/2004
MERGER PROCEDURE**

Article 6(2) NON-OPPOSITION
Date: 18/10/2007

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COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 18/10/2007

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In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

PUBLIC VERSION

MERGER PROCEDURE
ARTICLE 6(2) DECISION

To the notifying party:

Dear Sir/Madam,

Subject: Case No. COMP/M.4581 – Imperial Tobacco / Altadis
Case Notification of 30/08/2007 pursuant to Article 4 of Council Regulation No 139/2004¹

- (1) On 30 August 2007, the Commission received a notification of a proposed concentration pursuant to Article 4 of Council Regulation (EC) No 139/2004 (the Merger Regulation), by which Imperial Tobacco Group plc (“Imperial”, United Kingdom) intends to acquire sole control of Altadis S.A. (“Altadis”, Spain) by means of a public offer announced on 18 July 2007.

I. THE PARTIES AND THE TRANSACTION

- (2) Imperial is a UK-based listed public company which manufactures and sells cigarettes and other tobacco products including roll-your-own tobacco, pipe tobacco, and cigars in more than 130 countries worldwide. Its cigarette brands include *Davidoff*, *West*, *JPS* and *Lambert & Butler*.
- (3) Altadis is a Franco-Spanish group that was formed following the merger of the former French and Spanish tobacco monopolies, Seita and Tabacalera.² It manufactures and

¹ OJ L 24, 29.1.2004, p. 1.

² Case COMP M. 1735 *Seita/Tabacalera*

sells cigarettes and other tobacco products including roll-your-own tobacco, pipe tobacco and cigars on a worldwide basis. Its main cigarette brands include *Gauloises Blondes*, *Fortuna*, *Ducados* and *Gitanes*. Altadis also provides wholesale distribution and logistic services that cover both tobacco and non-tobacco products in France, Italy, Spain and Portugal via its Logistics Division³. In 2006, cigarettes accounted for 43% of group revenues, cigars 22% and wholesale/logistics 30%. Altadis also has joint control of Aldeasa S.A. which is mainly active in retail services at airports in Spain, Portugal and other non-EU countries.

II. THE CONCENTRATION

- (4) On 18 July Imperial announced that it had reached agreement with Altadis regarding a non-recommended public offer in cash for the outstanding share capital of Altadis at €50 per share and that it had filed a draft offer document with the Comisión Nacional del Mercado de Valores⁴. A successful bid for Altadis will give Imperial sole control of Altadis and will therefore result in a concentration within the meaning of Article 3(1)(b) of the Merger Regulation.

III. COMMUNITY DIMENSION

- (5) The undertakings concerned have a combined aggregate worldwide turnover in excess of EUR 5 000 million (€ 17,081 million for Imperial, € 12,708 million for Altadis). The aggregate Community-wide turnover of Imperial and Altadis is more than EUR 250 million. Moreover, they do not achieve more than two-thirds of their respective aggregate Community-wide turnover within one and the same Member State. The notified operation therefore has a Community dimension within the meaning of Article 1(2) of the EC Merger Regulation.

IV. COMPETITIVE ASSESSMENT

- (6) The present transaction will combine the parties' activities in the manufacture and sale of factory made cigarettes (FMCs), roll-your-own (RYO) tobacco products, pipe tobacco and cigars, thus giving rise to horizontal overlaps. Both parties are also active in the wholesale distribution of third party tobacco products although it is the vertical aspects of distribution that are notably affected. The transaction also concerns the market for travel retail services in view of Altadis' interest in Aldeasa although Imperial is not active in the provision of travel retail services.

³ Altadis' Logistics Division comprises the Logista Group, which is controlled by Altadis and which operates in Spain, Italy and Portugal and a Distribution Division in France, which was contributed to a new subsidiary – Altadis Distribution France (ADF) – as of 1 August 2007. ADF is 100% owned by Altadis' subsidiary, Seita.

⁴ Altadis has confirmed to Imperial that it considers the offer is attractive and that in the absence of a competing offer at a higher price being filed with the CNMV, it will recommend the offer to its shareholders. At the time of notification, the offer document had not been approved by the CNMV.

(a) Relevant markets

Relevant product markets

Cigarettes

- (7) The notifying party submits that there is a single relevant product market for the so-called "white sticks" which would encompass FMC, RYO and cigarette papers. From a demand-side perspective, it is argued that FMCs and RYO cigarettes perform the same basic function and are close substitutes. From a supply-side perspective, it has been submitted that there is a high degree of substitutability between RYO and FMCs since most large tobacco manufacturers supply both FMCs and RYO, the same sales and distribution system can be used for both, the technical expertise and knowledge required to manufacture RYO is virtually identical to that required to produce tobacco for FMCs and, with minor modifications, the same machinery can be used for the primary processing of RYO tobacco and FMC tobacco.
- (8) In the *BAT/Rothmans* case, the Commission found that the physical and technical characteristics of RYO cigarettes are different from FMCs and that RYO cigarettes are generally taxed at a lower level than FMCs. It was also found that the degree of substitutability between the two products seems to be limited in most Member States. However, the question whether FMCs and RYO cigarettes constitute separate product markets was ultimately left open as it was in the more recent *JT/Gallaher* decision⁵.
- (9) In the course of the market investigation carried out by the Commission, the overwhelming majority of the responding competitors and customers confirmed that cigarette products cannot be equated with "white sticks". Some respondents noted that for very price sensitive consumers some switching may occur at the higher price end of RYO and the lower price end of the FMC market but significant excise tax discrepancies exist, and thus FMC and RYO prices are considerably different. Moreover, the products appeal to different consumer groups, the external and internal characteristics of the products affecting the smoking habits of the consumer (a RYO cigarette is prepared by the consumer himself when he puts the tobacco into the cigarette paper) as well as the manner of presentation differ (FMC are supplied in packs whereas RYO tobacco is generally presented in pouches). This distinction is clearly more pronounced than between different products within the FMC market.

1. FMC

- (10) In previous decisions, the Commission has considered that FMCs constitute one single relevant product market⁶. It has taken the view that any other division of the FMC market according to factors such as brand image, price, taste etc. would be "*arbitrary and not meaningful*"⁷.
- (11) The notifying party acknowledges that the Commission may again find that the

⁵ Case COMP/M.4424 *JT/Gallaher*

⁶ For example Case M.2779, *Imperial Tobacco/Reemtsma Cigarettenfabriken*

⁷ Case M. 1415, *BAT/Rothmans*; Case M.2779, *Imperial Tobacco/Reemtsma Cigarettenfabriken*; Case M.3191, *Philip Morris/Papastratos*.

relevant market is narrower than "white sticks" and provides its views on a further segmentation of the FMC market. It agrees that division of the FMC market by factors such as price and image would be arbitrary and not meaningful. However, the notifying party suggests that a distinction should be made between dark and blond cigarettes in view of supply and demand-side considerations.

- (12) Based on the market investigation in this case it seems that there are no reasons to depart from the Commission's previous practice and sub-divide the FMC market as suggested by the notifying party. The market investigation has shown that tobacco producers for internal purposes subdivide the market into different segments according to blend, taste, image and other physical characteristics. Consumers on the other hand have preferences for certain blends, but price is also important. The question whether the FMC market should be further sub-divided between dark and blond cigarettes as suggested by the notifying party can in any case remain open as this would not alter the competitive assessment⁸.

2. RYO

- (13) As was set out above, the majority of competitors and customers in the market investigation concurred with the view that FMC and RYO products constitute distinct product markets. As to a further distinction within the RYO market, consumers may have preferences regarding blends in different national markets, but the market investigation did not indicate that any further subdivision of the RYO market is appropriate.

3. Pipe tobacco

- (14) The Commission has previously taken the view that the pipe tobacco market should be separated from the RYO market on the basis of different uses on the demand side and different methods of consumption⁹. The notifying party submits that from the consumer's point of view, RYO is not substitutable with pipe tobacco and that the existence of different tobacco cuts for each indicates separate product markets from the supply side. In addition, pipe tobacco and RYO are subject to different levels of excise.
- (15) The Commission's market investigation revealed that competitors and customers broadly agree that pipe tobacco forms a market separate from other tobacco products. The Commission received some comments that producers are taking advantage of the differential in excise levels between pipe and RYO tobacco to market tobacco under the RYO heading that can in fact be used as a pipe tobacco. The market investigation was not, however, conclusive on this point and the Commission therefore retains the market definition corresponding to the classification made by the parties.

4. Cigars

- (16) The Commission has identified a separate relevant product market for cigars but has in

⁸ Imperial is not active in dark FMC. In blond FMC, Altadis' share would be lower than on the overall market for FMC due to the significant share of its sales in dark FMC in the countries where this distinction is more pertinent for the assessment of the present case (France and Spain).

⁹ Case COMP/M.3248 *BAT/ETI*

previous cases always left open the question whether the cigar market should be further segmented on the basis of criteria such as size, weight, method of production, tobacco type, quality or image¹⁰. In BAT/ETI the Commission stated that it had not identified any decisive elements in favour of a clear segmentation of the cigar market.

- (17) The notifying party argues on the basis of demand and supply-side considerations that distinct product markets exist for hand-made or 'premium' cigars and factory made cigars. Respondents to the market investigation have generally confirmed that factory made and hand made cigars appeal to different consumer profiles. Hand made cigars also require certain temperature and humidity levels to be kept in good condition, they are generally distributed via specialist distributors and to a more limited number of outlets than factory made cigars. However, a number of market players indicated that there is a certain overlap between expensive factory-made cigars and hand-made cigars competing with each other, thereby making it difficult to delineate separate markets for hand-made and factory made cigars respectively. Considering that the competitive assessment would not change given the parties' respective market shares on both overall and potentially further divided markets, the exact market definition can be left open for the purposes of the present transaction.

5. Wholesale distribution of tobacco products

- (18) In considering the distribution of manufactured tobacco products, the Commission takes into account the specific nature and characteristics of each relevant national market, but has so far in previous cases always come to the conclusion that there is a separate market for the wholesale distribution of manufactured tobacco products at the wholesale level based on regulatory issues, price and value of the product and the fact that tobacco manufacturers normally require specialised distributors¹¹. The notifying party argues that distributors for non-tobacco products could easily be involved in the distribution of tobacco products since no specific know-how is required and there is no significant cost, if any, for any distributor of products for retail to start distributing tobacco products.
- (19) The Commission's market investigation has shown that tobacco distribution remains a specialised activity compared to the distribution of other products. It requires specific knowledge about regulatory and tax issues. Tobacco manufacturers normally require specialised distributors and in many countries regulation results in specialised outlets selling tobacco. The Commission therefore considers that the relevant product market in this case is the market for the wholesale distribution of tobacco products.

6. Travel retail services

- (20) The Commission has considered the travel retail services market on two occasions¹². In the most recent of these cases, *Autogrill/Altadis/Aldeasa*, the Commission found that products sold in retail outlets at airports may be classified into duty-paid and duty-

¹⁰ Case COMP/M.1735 *SEITA/Tabacalera*

¹¹ Case No. COMP/M3553 *Logista/Etinera/Terzia* (with regard to Italy). See also, Case No. COMP/M.1735 *SEITA/Tabacalera* (with regard to France and Spain).

¹² Case No. IV/.782 *Swissair/Allders International*, decision of 17 July 1996 and Case No. COMP/M.3728 *Autogrill/Altadis/Aldeasa*, decision of 23 March 2005.

free products. Since 30 June 1999, duty-free products have only been available to customers travelling to destinations outside the EU. In the present case, the precise product definition may be left open in the absence of competition concerns.

Relevant geographic markets

- (21) The notifying party submits that the markets for tobacco products are national in scope although it draws attention to increasing levels of cross-border trade. The notifying party does, however, submit that for Spain a further geographic separation is appropriate as specific conditions (fiscal and regulatory) apply in the Canary Islands. In this case the question whether Spain should be further sub-divided can be left open as it does not affect the competitive assessment.
- (22) The notifying party also submits that the market for the wholesale distribution of tobacco products is national in scope. This is in line with previous decisional practice and broadly confirmed by the Commission's market investigation.
- (23) As regards the market for travel retail services, the notifying party submits that it is at least EEA-wide in scope, if not global, as considered in previous Commission decisions. In fact, in *Swissair/Alders International* the Commission indicated that in intra-Community travel, for a large number of travellers there are a variety of routes between any two non-adjacent countries. Consumers can purchase the same kind of products at most travel retail outlets, regardless of their geographic location. From the supply side, the same retailers are active in many different regions. However, the Commission in this case and subsequently in the *Autogrill/Altadis/Aldeasa* left the market definition open. Also for the purpose of this case, the exact geographic definition of the travel retail services market can be left open because the concentration would not give rise to competition concerns irrespective of the market definition.

(b) Assessment

A. Horizontal issues

- (24) The market investigation confirmed competition concerns which would arise from the parties' combined high market shares in the following markets: roll-your-own tobacco (RYO) in the Canary Islands, France, Italy, Portugal and Spain, pipe tobacco in Finland and France and cigars in Greece.

FMC

- (25) The proposed concentration would result in a number of affected FMC markets¹³ as shown in the following table.

Country	Imperial	Altadis	Combined entity	PM*	BAT*	JT/Gallaher
Belgium	[5-10]	[5-10]	[15-20]	[40-45]	[30-35]	[0-5]
Finland	[0-1]	[15-20]	[15-20]	[65-70]	[10-15]	[0-5]
France	[0-5]	[20-25]	[25-30]	[40-45]	[15-20]	[10-15]
Germany	[20-25]	[5-10]	[25-30]	[35-40]	[15-20]	[0-5]
Ireland	[25-30]	[0-1]	[25-30]	[5-10]	[15-20]	[45-50]
Luxembourg	[10-15]	[10-15]	[20-25]	[30-35]	[15-20]	[15-20]
Poland	[10-15]	[5-10]	[20-25]	[40-45]	[15-20]	[0-5]
Slovenia	[55-60]	[0-5]	[60-65]	[25-30]	[0-5]	[0-5]
Spain	[0-5]	[30-35]	[35-40]	[30-40]	[5-10]	[15-20]
United Kingdom	[45-50]	[0-1]	[45-50]	[5-10]	[5-10]	[35-40]
Italy (vertical)	[0-5]	[0-5]	[0-5]	[55-60]	[25-30]	[10-15]

* PM = Philip Morris; BAT = British American Tobacco; Source: Notifying party

- (26) The proposed transaction is not likely to change the competitive structure of the market to any significant degree in any of the above-mentioned affected markets. In Finland, Ireland and the United Kingdom, the increment in market share is insignificant at less than [0-1%]. In Italy, which is vertically affected because of Altadis' distribution activities, the parties' combined market share is only [0-5%]. In Belgium, Luxembourg and Poland, the combined market shares of the parties are below the 25% threshold identified in the Commission's horizontal merger guidelines as the point where typically competition concerns are unlikely to arise.
- (27) In the remaining markets (France, Germany, Slovenia and Spain) there are a number of large international competitors such as Philip Morris, BAT and Japan Tobacco that are able to exert competitive pressures on the combined entity. At the same time, there are additional factors to suggest that the transaction will not result in any significant impediment to effective competition. In Germany, the combined market share of the merged entity at [25-30%] with an increment of [5-10%]. The merged entity will continue to face strong competitive pressure from the market leader, Philip Morris ([35-40%]) and other international players such as BAT and JT.

¹³ Source: Notifying party estimates for 2006 based on value.

- (28) Imperial's relatively high market share in Slovenia is historical as Reemtsma, which it acquired in 2002, incorporated the former state monopoly. In this market, Imperial's market leading position has been steadily eroded from [70-75%] in 2003 to [55-60%] in 2006 during which period Philip Morris has increased its market share from [10-15%] to [25-30%] in 2006. Due to the fact that other global players have since Imperial's entry successfully entered the Slovenian market, for example Japan Tobacco in 2005, the merged entity's market share is likely to continue to decrease. As regards any risk of coordinated effects caused by the merger, this can also be excluded as, in view of the very weak position of Altadis in the Slovenian market for FMC, the merger which would result in a minor increment only, would not bring about any significant change in the competitive landscape which would render the market more susceptible for coordination than it would be absent the merger.
- (29) In France and Spain, the notifying party argues that its brands cannot be viewed as close substitutes to Altadis' as the latter sells a significant volume of dark FMC in both countries that are not sold by Imperial, and which are not substitutable for blond FMC from the consumer's perspective. In addition, many of Altadis' brands are said to have a strong local appeal whereas Imperial's brands are more 'international'.
- (30) The Commission's market investigation confirmed that the parties' brands are not viewed as close substitutes. In this light the relatively small increment ($[<5]\%$) which would result from this transaction in the French and Spanish FMC markets will not lead to significant changes of the market structure and the transaction is therefore unlikely to raise significant competition concerns.

(31) The proposed transaction would result in the following affected markets:

Country	Imperial	Altadis	Combined entity	BAT	JT/Gallaher	Others*
Belgium	[10-15]	[0-5]	[15-20]	[50-55]	[0-5]	[25-30]
France	[25-30]	[15-20]	[45-50]	[25-30]	[5-10]	[20-25]
Germany	[25-30]	[0-1]	[25-30]	[20-25]	[5-10]	[45-50]
Italy	[50-55]	[0-5]	[55-60]	[10-15]	[15-20]	[10-15]
Luxembourg	[35-40]	[0-5]	[40-45]	[5-10]	[10-15]	[35-40]
Netherlands	[55-60]	[0-1]	[55-60]	[20-25]	[0-1]	[20-25]
Portugal	[60-65]	[5-10]	[65-70]	[5-10]	[20-25]	[0-1]
Spain (mainland)	[65-70]	[0-5]	[65-70]	[5-10]	[0-5]	[15-20]
Spain – Canary Islands	[75-80]	[0-5]	[75-80]	[0-5]	[5-10]	[10-15]
United Kingdom	[60-65]	[0-1]	[60-65]	[5-10]	[25-30]	[0-1]

* Others includes Philip Morris, Gryson, Poeschl, De Jaegher and Heintz van Landewyck; Source: Notifying party

- (32) The increment in Germany, the Netherlands and the UK is negligible and there will be no change to the competitive structure of the market post transaction. Although the increment is more significant in Luxembourg, the market investigation has not raised any significant concerns. The merged entity will be subject to competition from not only smaller players such as Gryson and De Jaegher with shares of [5-10%] and [0-10%] respectively but also from larger competitors such as Philip Morris which entered the market in 2005 and secured nearly [0-5%] market share within a year.
- (33) In Belgium, the combined market share of the parties post transaction will be significantly less than the 25% threshold identified in the Commission's horizontal merger guidelines as the point where typically competition concerns are unlikely to arise.
- (34) The transaction would lead to competition concerns regarding the markets in France, Italy, Portugal and Spain, including Canary Islands. The transaction would create a strong market leader in France, combining the largest and the third-largest player on the market. In Italy, Portugal and Spain (including Canary Islands) the transaction would consolidate Imperial's market-leading position and increase the distance between the merged entity and the other competitors present in each market. On these markets, the merger would arguably strengthen the existing dominant position enjoyed by Imperial. In Italy, the relatively small market share increment of Altadis to be added to Imperial's [55-60%] has to be seen in the context of Altadis' new entry, as

this company only *de facto* entered the RYO market in 2006 (before it had only a [0-1%] market share) and the merger would actually prevent it from further expanding and bringing more competitive pressures into the market.

- (35) It should also be noted that the merged entity will have a significant position in the wholesale distribution of tobacco products in France, Italy and Spain via its interest in Logista (Logista is also active in Portugal but does not have a *de facto* monopoly). In addition to the vertical issues explained below, Logista's strong position in distribution adds a qualitative element to Altadis market position reflected in its moderate market shares, which will be combined with Imperial's significant market position in the countries concerned.

Pipe tobacco

- (36) In the pipe tobacco markets in Finland and France the merged entity will consolidate its leading position on the market as shown in the following table:

	Imperial	Altadis	Combined	Others
Finland	[10-15]	[40-45]	[55-60]	[40-45]
France	[5-10]	[80-85]	[85-90]	[10-15]

Source: Notifying party

- (37) In Finland, the new entity would have a combined market share of [55-60%] with Imperial adding [10-15%] to Altadis' current market leading position ([40-45%]). Other competitors in the Finnish market are smaller players such as Petteroes, Swedish Match and Mac Baren. In France, the arguably current dominant position of Altadis, which has [80-85%] market share, would be strengthened by the addition of Imperial's [5-10%] share. In addition, in these markets competitive constraints from other leading tobacco companies is much weaker than in other markets. The fact that the pipe market accounts for a relatively minor part of overall tobacco consumption, 0.4% by value in 2006 according to the notifying party, does not diminish concerns that the parties' high market shares in Finland and France would result in competition problems.

Cigars

- (38) The parties' cigar activities are to a large extent complementary as Imperial is active only in factory made cigars and a large part of Altadis' cigar sales by value are of hand made cigars Altadis is active in the production and supply of premium Cuban cigars via its 50% equity investment in Corporación Habanos¹⁴.
- (39) The market investigation focused mainly on the Greek market where on the basis of information contained in the notification, the parties' combined market share would be very high. During the investigation the notifying party changed its view on the market shares several times (indicating originally in the Form CO a market share of ([75-

¹⁴ Corporación Habanos owns the largest and most internationally well-known Cuban brands including Montecristo, Cohiba, Romeo y Julieta and Partagas. It also controls an extensive global distribution network covering some 90 countries.

80%]). It also during the investigation informed the Commission that, due to the fact that the majority of its cigar sales in Greece are originating from a third party's brand, i.e. Davidoff cigars, the market share that Davidoff cigars capture on the Greek cigar market should not be allocated to Imperial but to Davidoff. However, because Imperial buys and resells Davidoff cigars for its own account and is entitled to freely determine the retail prices of the products in Greece (Davidoff does not issue recommended retail price lists for the cigars supplied to Imperial) on an ex-factory price basis, Imperial's sales stemming from Davidoff brand cigars actually add to its market power and, consequently, cannot be disregarded for the purposes of the competitive assessment.

- (40) Ultimately the Commission had to reconstruct the market seeking the best available information. Accordingly, it is apparent that the combined entity has a strong position on the Greek cigar market with a market share of [55-60%] in value terms (Altadis [50-55%], Imperial [0-5%]) and [30-35%] in volume terms (Altadis [25-30%], Imperial [0-5%]). The difference in market shares between volumes and values is primarily explained by the fact that Altadis is active in hand made cigars, whereas Imperial is not.
- (41) As indicated above the notifying party submitted that hand made cigars should be considered as a separate product market, but a number of market players indicated that there is a certain overlap between expensive factory-made cigars and lower-end hand-made cigars competing with each other, thereby making it difficult to delineate separate markets for hand-made and factory made cigars respectively. Nevertheless, even if it would be possible to distinguish between factory and hand made cigars, the Commission investigation concludes that the combined entity would still have a strong position on the factory made segment on the Greek market with a market share of [40-45%] in value terms (Altadis [40-45%], Imperial [0-5%]). In addition, the Commission's investigation suggested, on the basis of retail price information, that the brands sold by the parties in the factory made segment are positioned towards the higher end of this segment and therefore appear to compete more closely. Therefore, the transaction raises concerns in the Greek cigar markets, as market shares are high on both overall and segmented factory made market.

B. Vertical issues

- (42) In addition to the horizontal aspects discussed above, the proposed concentration also has vertical aspects resulting from the parties' wholesale distribution activities. Imperial is active in the wholesale distribution of third party manufactured tobacco products in the Czech Republic, Estonia, Hungary, Ireland, the Netherlands, Norway, Slovenia and the United Kingdom. Altadis, via its Logista subsidiary, is active in France, Italy, Portugal and Spain.

1. Imperial's wholesale distribution

- (43) In [...], the only third party products Imperial distributes are Altadis'. In [...], the parties do not have more than 25% of any upstream market. The only vertically affected markets as regards Imperial's distribution activities are therefore Ireland and the United Kingdom. All countries in which Altadis is active are vertically affected markets (Spain, France, Italy and Portugal).
- (44) In Ireland and the United Kingdom, all major cigarette manufactures with the exception of Philip Morris, distribute their own products. As Imperial has the

distribution contracts for Philip Morris in both countries, it has over [90-95%] of the third party distribution market. However, the horizontal overlap in the tobacco product markets brought about by the merger is minimal (Altadis brands add less than [0-1%] share), the transaction therefore does not change the situation as regards Imperial's abilities and incentives to foreclose. In addition, these contracts are vigorously competed for by other competitors so that the likelihood of foreclosure can be excluded.

- (45) The market investigation did not bring any elements suggesting that Imperial's distribution activities would raise any anti-competitive problems.

2. Wholesale distribution of Altadis

- (46) In France, Italy and Spain, Altadis distributes practically all major third party tobacco products, including Imperial's brands, and has market shares of about [95-100%]. Its market share in Portugal is estimated to be [15-20%].
- (47) The market investigation examined possible vertical effects in France, Spain and Italy, where Altadis has a near monopoly on the market for distribution of tobacco products via its subsidiary Logista (Seita in France). Two competitors raised concerns that the merged entity might change its behaviour in relation to tobacco distribution and might start to discriminate against other manufacturers. One of these competitors argued that post merger, Imperial might discriminate against certain upstream competitors by raising prices for the distribution services and/or decreasing service levels (to disrupt supplies or hinder launches of new products). Although admitting that it has not suffered any discrimination from Logista/Seita in the past (this was confirmed by all other responding tobacco producers), this competitor put forward that post-merger the behaviour of Logista/Seita is likely to change due to changing incentives of the merged entity viewed in the relative importance of distribution business for the combined entity in comparison to Altadis (arguing that Altadis alone is a relatively weaker competitor with a different, less aggressive culture).

No substantial change of the existing situation through the transaction

- (48) First, it has to be noted that Altadis already pre-merger was vertically integrated being active in both the manufacturing and distribution of tobacco products. Furthermore the market investigation confirmed that the merger would not bring about any major change to the present situation on both the downstream market for tobacco distribution (Logista's/Seita's position would not be strengthened in any way as a result of the transaction, as it already now distributes all Imperial's tobacco products in Spain, Italy and France), nor on the upstream FMC market (which, is the dominating tobacco product market).
- (49) Logista's/Seita's tobacco distribution sales derive to a large extent from distributing FMC. On the FMC markets the addition brought by Imperial to the current position of Altadis would be as follows: [0-5%] in France (in addition to [20-25%] from Altadis), [0-5%] in Spain (in addition to Altadis' [30-35%]) and in Italy Imperial would bring [0-5%] to the current [0-5%] for Altadis. In fact, given that Altadis market shares have slightly declined in France and Spain, the current position of the combined entity on the FMC market would be comparable or even weaker than the position of Altadis three or four years ago. Therefore, the change caused by the merger would not make any significant difference to the structure of the FMC market, which is by far the most important for Logista's/Seita's distribution activities.

- (50) On the RYO market, the picture is different. As shown above, Imperial is much stronger on the RYO market and brings about a more significant change in the national markets concerned. However, the complete removal of the parties' overlap in the RYO markets in all three countries concerned through a brand divestiture, as proposed in the remedies offered, will ensure that the transaction as modified by the commitments proposed by the parties will not lead to a change on the RYO markets either.

No ability to foreclose

- (51) Second, the investigation has indicated that despite the near monopoly position of Logista/Seita, it is likely that the merged entity would not have the ability to foreclose the access of its competitors to the final consumers as these competitors would be in a position to find alternative distribution channels in these countries. In Spain the company Conway (part of the Lekkerland group which already is a major distributor of tobacco products in Germany and Netherlands) possesses a bonded warehouse and distribution near Madrid from which it services approximately 7,000 licensed tobacconists (*estancos*) throughout Spain. Conway believes that it has "*all the necessary know-how, infrastructure and national outreach to start distributing cigarettes on a larger scale and it estimates that it would take 4-6 months to expand its facilities to deal with the distribution of one of the cigarette majors*"¹⁵. Comet¹⁶ is another distributor of tobacco products in Spain with national coverage¹⁷.
- (52) In France, the Société Pipière Française (SPF), which is composed of eight regional subsidiaries with logistic centres and a sales force of 180 persons, already distributes a number of less-well known tobacco products (with about 25.000 other articles) to tobacconists throughout France. SPF believes it has the necessary infrastructure and know-how to start distributing large volumes of tobacco products in the event it were to secure a distribution from a large manufacturer¹⁸.
- (53) In Italy, the market investigation suggested that alternative distribution solutions may exist. It can also be mentioned that in Austria, a tobacco producer with a less than 10% market share on the FMC market was in the past able to find alternatives to the former distribution monopoly by way of helping an existing smaller distributor to expand its activities, and even increased its own market share by using this alternative distribution channel¹⁹. In addition, many of the large tobacco manufacturers have their own tobacco distribution arms in other countries, which witnesses the fact that logistic know-how is available to those manufacturers to be used in providing assistance to emerging alternatives (in-house or sponsored new entrant) in Spain, France and

¹⁵ Agreed minutes of telephone conference with Conway of 21 September 2007.

¹⁶ [...]

¹⁷ Legislation in Spain concerning the wholesale distribution of tobacco products originally implied that licences were national with the obligation to cover all Spanish territory (except the Canary Islands). Modifications to the law in 2000 and 2007 have removed the obligation to ensure nationwide coverage and have opened the possibility of regional licences for the wholesale distribution of tobacco products.

¹⁸ Agreed minutes of telephone conference with SPF of 2 October 2007

¹⁹ Case M.4424 *JT/Gallaher*, para 37.

Italy²⁰.

No incentives to foreclose

- (54) The notifying party has submitted an economic analysis aimed at evaluating the incentives the merging parties would have to adopt vertical foreclosure strategies²¹. This analysis evaluates the increase in sales of its own tobacco products that the merged entity would need to realise in order to compensate the loss of revenue of the logistic business resulting from losing one of more competitors due to foreclosure strategies. The study is based on the assumptions that (i) the market shares attributable to the businesses proposed for divestiture no longer belong to the merged entity (and therefore are not counted) and more importantly that (ii) alternative distribution channels are available. On the latter, the investigation has provided sufficiently strong indications, as discussed above.
- (55) The study essentially argues that a foreclosure strategy would be profitable for the merged entity only under very extreme conditions, namely a very big increase in sales that is extremely unlikely in a market whose size is relatively stable. Furthermore, considering that rivals would be able to set up competitive distribution networks or rely on existing alternative distributors, the merged entity would still have to compete with those rivals for the sales lost by foreclosed rivals. This would make the big increase in sales necessary to make the foreclosure strategy profitable (and justify the potential losses in the distribution business) even less likely. Therefore, foreclosure attempts are highly unlikely to arise and to lead to a reduction in the availability of rival tobacco products to retailers and final consumers. Even if foreclosure resulted in somewhat higher costs (perhaps in case foreclosure is targeted at small rivals that could have more difficulty to find alternative distribution channels in view of their lower scale), it would still be unlikely that the demand for the merged entity's products will be increased enough to justify the potential losses in the distribution business.
- (56) The Commission considers that the figures and conclusions as put forward by the study provide indications that a foreclosure strategy adopted by merged entity would indeed not be profitable and that it would thus not have the incentives to foreclose its upstream rivals.

No significant detrimental effect on consumers

- (57) Finally, it should be noted that the importance of distribution costs in the final retail price of the tobacco products is limited given the incidence of excise duties and other taxes²². Arguably, the price offered by the near monopoly distribution company appears to be, due to economies of scale, more beneficial than prices which could be

²⁰ All large FMC manufacturers including Phillip Morris, Japan Tobacco/Gallaher and British American Tobacco own distribution companies in certain European countries.

²¹ Study ("An analysis of potential vertical effects from the Imperial Tobacco/Altadis merger") prepared by CRA International and submitted on 4 October 2007.

²² The notifying party submits that in the three countries concerned, taxation represents 70-80% of the final retail price, while manufacturing makes up to 7-10% and the retail margin, which is fixed by legislation, accounts to 8-10% of the retail price.

offered by alternative distributors, which might have been one of the reasons why main tobacco manufacturers up till now kept on relying on Logista/Seita (apart from the fact they were apparently satisfied with their services, as none of them indicated any problems in that respect during the market investigation). In this regard, a potential increase of the wholesale distribution costs due to setting-up alternative distribution channels ('sponsoring' entry or setting up own distribution) is not likely to lead to a significant impact on the retail prices for tobacco products.

- (58) In the view of the above, there is no reason to believe that a vertical foreclosure of upstream competitors due to the merger is likely and that the possible vertical effects would give rise to competition concerns.

3. Travel Retail services of Altadis

- (59) Altadis has joint control of Aldeasa, which operates 251 retail outlets in 14 countries worldwide, primarily at airports in Spain. Aldeasa sells a range of goods including tobacco products. The market investigation has not revealed any concerns on the part of competitors regarding possible foreclosure post-transaction from the retail outlets operated by Aldeasa, except for one smaller competitor, which claimed that the merged entity would be inclined to prefer its own brands.

- (60) In Spain, the sales of tobacco products by Aldeasa account for not more than [0-5%] of the national market. On the possible market for travel retail services in the EEA Aldeasa would have approximately [5-10%] market share (and below 15% of EEA travel retail services limited to sales of tobacco products)²³.

- (61) It has to be noted that the transaction does not significantly change the situation pre-merger, as Aldeasa is already jointly controlled by Altadis, which is one of the few bigger players in the tobacco industry. The other controlling shareholder, Autogrill (owning the remaining 50% in Aldeasa), is not active on the upstream markets for tobacco products and would likely not adhere to any attempt by the merged entity's to foreclose competitors. Aldeasa's brand portfolio includes mainly major international brands which are demanded by international travellers and Aldeasa is therefore obliged to hold a multi-brand portfolio to satisfy customers' needs. The decision to limit other producers' sales in Aldeasa's outlets would not be profitable for Aldeasa, as this would mean losing customers and revenues, which arguably could not completely be offset by a hypothetical increase in sales of Imperial/Altadis products. Aldeasa will thus very unlikely to change its policy as a result of the present transaction, this view being largely supported by the responding market participants.

V. COMMITMENTS SUBMITTED BY THE NOTIFYING PARTY

(a) Procedure

- (62) In order to render the concentration compatible with the common market, the notifying party has offered some commitments pursuant to Article 6(2) of the Merger Regulation, which are annexed to this Decision. A first commitment package was proposed by Imperial on 27 September 2007. After examination and market testing of

²³ Page 87 of Form CO.

this commitment package, the notifying party amended the latter and submitted on 11 October 2007 its final Commitments, which were deemed suitable to remedy the competition concerns identified. These commitments are attached to this decision and form an integral part thereof.

(b) Description of the commitments

- (63) The commitments proposed by the notifying party essentially consist of the divestment, by Imperial or by Altadis, of one or more brands (the "divestment brands") in each market where competition concerns were identified. The divestment brands in each of these markets are shown below²⁴.

1. Roll-your-own tobacco

France	<i>Interval (I), Bergerac(A), Wervicq(I), Santoya(A)</i>
Italy	<i>Van Nelle (I)</i>
Portugal	<i>Amsterdamer (A)</i>
Spain	<i>Interval (I), Picadura (A)</i>
Canary Islands	<i>Van Nelle (I)</i>

2. Pipe tobacco

Finland	<i>Kilta (A)</i>
France	<i>Bergerac (A)</i>

3. Cigars

Greece	<i>Backwoods (A)</i>
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- (64) The divestment brands essentially include all tangible and intangible assets (including intellectual property rights such as trademarks and know-how in particular the blends) which contribute to its current operation or are necessary to ensure its viability and competitiveness. The divestment brands also include the possibility for the purchaser to enter into arrangements by which Imperial would provide the following:
- production capacity by way of a toll manufacturing agreement with Imperial at cost price for a period of up to 5 years;
 - distribution support by way of a wholesale distribution agreement or assignment of any existing distribution contracts with third parties;
 - transfer of key personnel

²⁴ The 'A' or 'I' indicates whether the brand belongs to Altadis or Imperial respectively.

- to the extent not covered by the transferred key personnel, sales and marketing support through entering into an agreement with Imperial to procure such services on reasonable commercial terms.

(65) The buyer will have a possibility to opt-out from any of the above arrangements. This is relevant in case of a trade buyer, who will himself likely have the above elements in-house.

(c) Suitability for removing the serious doubts

(66) Under the first sentence of the second subparagraph of Article 6(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.

(67) As explained above, under the proposed undertakings the notifying party commits to sell one or more divestment brands (the relevant IP rights and know-how in combination with all elements necessary for the production and marketing of the products concerned), in each of the market where competition concerns were identified. The sales of the products marketed under these divestment brands in all the respective markets correspond, in terms of market shares, to the overlap which would be brought about by the notified transaction, or are in some cases even higher than the overlap (see the following tables). The divestiture would thus entirely eliminate the increment resulting from the transaction on all the markets where serious doubts have been identified.

Roll-your-own tobacco

Member State	Brand	Decrease of market shares (%)
France	Interval(I), Bergerac(A), Wervicq(I), Santoya(A)	- [15-20]
Italy	Van Nelle(I)	- [0-5]
Portugal	Amsterdamer(A)	- [5-10]
Spain	Interval(I), Picadura(A)	- [0-5]
Canary Islands	Van Nelle(I)	- [0-5]

Pipe tobacco

Member State	Brand	Decrease of market shares (%)
Finland	Kilta(A)	- [40-45]
France	Bergerac(A)	- [10-15]

Cigars

Member State	Brand	Decrease of market shares (%)
Greece	Backwoods(A)	- [0-5]

Source: Notifying party

- (68) It has to be noted that a remedy consisting of brand divestiture without the divestment of the whole stand-alone business, is generally considered to be suitable only in exceptional circumstances. However, the particularities of the present case justify such approach, which is in line with previous Commission practice in the tobacco industry²⁵. Indeed, the market investigation confirmed that for tobacco products, the most important criteria for consumer's choice are, alongside price, the brand image and the taste (blend) of the products²⁶. The brand is key for the customers not only to identify the products, but the image of the brand plays a very strong role for targeting the customer groups which feel attracted by a certain appeal. Given the advertising bans and restrictions imposed on promoting of tobacco products, the brand is the key communicator with the final customer. In the absence of traditional marketing, and considering the regulated nature of the tobacco distribution together with a very low degree of technical innovations of the products, the access to IP (brand) and know-how (mainly related to blend composition) are most important factors for the ability to compete effectively on the these markets.
- (69) As regards the manufacturing of the products, which are arranged by way of a 5-year toll-manufacturing agreement, virtually all respondents to the Commission market test which gave a position on this point, regard these arrangements as sufficient to enable the potential buyer to secure the manufacturing of the divestment brands²⁷. Generally, toll manufacturing agreements are quite common in the tobacco industry. For example, Imperial itself is outsourcing the manufacturing of a number of factory made cigarette brands in [...] from [...] and it is also outsourcing the production of [...] to [...]. On the other hand, Imperial is itself manufacturing one cigarette brand [...] for [...] in [...]. One competitor noted that the purchaser should have the flexibility to manufacture the products himself, which reflects the fact that if the purchasers of the divestiture brands are established players in the tobacco sector with sufficient in-house production capacities, they would not need the toll-manufacturing arrangements. As explained above, the opt-out included in the commitments assures that the purchaser is free not to enter into the manufacturing arrangements if not needed.
- (70) The market test also confirmed that the proposed 5-year arrangements regarding wholesale distribution and sales support, which Imperial commits to provide, are seen as

²⁵ M.2779 *Imperial Tobacco/Reetsma Cigarettenfabriken*

²⁶ Answers to question 19 of Commission questionnaire to customers of 9.8.2007 and to question 20 of questionnaire to competitors of 7.8.2007.

²⁷ Question 9 of Commission questionnaire of market testing the proposed remedy. Out of 20 respondents, 14 gave a position on that point and 13 of them generally see the 5-year toll-manufacturing arrangement as sufficient.

sufficient to enable the potential purchaser of the divestment brands to establish himself on the market, if not yet established²⁸.

- (71) The majority of the market participants also indicate that the fact that the divestment brands are offered on a national basis (plus separately for Canary Islands) would not negatively affect the viability of the brands in this case²⁹, although a number of manufacturers mentioned that the image and positioning of the brands may be affected by the brands from other, mainly neighbouring countries (one competitor stated that such shared brands may be less attractive, but this is less problematic in larger geographic markets). Despite their comments on geographic brand splitting, some of these manufacturers indicated that they might themselves be interested in buying the divestiture brands, or they at least not exclude it. The market investigation further revealed that such geographic brand splitting is not uncommon in tobacco industry, as there are a number of examples³⁰. In the light of the above and given that serious doubts were identified only in a limited number of geographic markets (which are clearly separate as was concluded in earlier in the part of the decision on geographic market definition), the divestiture of national brands appears suitable in this case
- (72) Overall, the results of the market test gave a positive feedback on the divestment package. Even though most of the divestment brands have limited market shares (with the exception of the pipe brands and *Interval* in the French RYO market) the results of the market test of the remedies are generally positive with a number of respondents indicating that most of the divestment brands are likely to attract interest from buyers. Four manufacturers explicitly expressed potential interest and three others did not exclude that they would be interested in acquiring the brands (incl. major players). Even brands which have relatively small sales might be interesting for players with existing market presence, who would like to expand their portfolio.

(d) Conclusion on the commitments

- (73) The Commission therefore considers the commitments suitable for remedying the serious doubts on the compatibility of the concentration with the Common Market and the EEA, which have been established in the previous sections of this Decision.

VI. CONDITIONS AND OBLIGATIONS

- (74) Under the first sentence of the second subparagraph of Article 6(2) of the Merger Regulation, the Commission may attach to its decision conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they

²⁸ Answers to question 11 of Commission questionnaire of market testing the proposed remedy. Out of 16 market participants who provided an answer, 14 generally agree that the arrangements are sufficient.

²⁹ Answers to question 5 of Commission questionnaire of market testing the proposed remedy. Out of 13 market participants who provided an answer, 8 think that this splitting would have no impact on the viability, whereas 4 mentioned that the image and positioning of the brands could be affected in particular from neighbouring countries. One competitor stated that shared brands are less attractive, but that this is less problematic in larger geographic markets.

³⁰ Imperial mentions 12 examples of such brand splitting and other market participants also mention a number of additional brands.

have entered into vis-à-vis the Commission with a view to rendering the concentration compatible with the common market.

- (75) The achievement of the measure that gives rise to the structural change of the market is a condition, whereas the implementing steps which are necessary to achieve this result are generally obligations on the parties. Where a condition is not fulfilled, the Commission's decision declaring the concentration compatible with the common market no longer stands. Where the undertakings concerned commit a breach of an obligation, the Commission may revoke the clearance decision in accordance with Article 8(5) of the Merger Regulation. The undertakings concerned may also be subject to fines and periodic penalty payments under Articles 14(2) and 15(1) of the Merger Regulation. In accordance with the basic distinction described above, the decision in this case is conditioned on the full compliance with Section B, points 1-3 and point 5, a-d of the Commitments submitted by the notifying party on 11 October 2007.
- (76) The remaining requirements set out in the other Sections of the Commitments submitted by the notifying party on 11 October 2007 are considered to constitute obligations.

VII. OVERALL CONCLUSION

- (77) For the above reasons the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement pursuant to Article 2(2) of Council Regulation (EC) No 139/2004, subject to full compliance with the Commitments annexed to this Decision that forms an integral part to this decision.
- (78) Consequently, the Commission has decided not to oppose the notified operation and to declare it compatible with the common market and with the EEA Agreement. This decision is adopted in application of Article 6(1)(b) and Article 6(2) of Council Regulation (EC) No 139/2004.

For the Commission,
signed
Meglana KUNEVA
Member of the Commission

Annex 1 A – Commitments offered to resolve any horizontal issues the Commission may have

European Commission – Merger Task Force
DG Competition
Rue Joseph II 70 Jozef-II straat
B-1000 BRUSSELS

CASE COMP/M.4581 (IMPERIAL TOBACCO/ALTADIS)

COMMITMENTS TO THE EUROPEAN COMMISSION RELATING TO POTENTIAL HORIZONTAL ISSUES

Pursuant to Article 6(2) of Council Regulation (EC) No. 139/2004 (the “*Merger Regulation*”), Imperial Tobacco Group PLC (“*Imperial*”) hereby provides the following Commitments (the “*Commitments*”) in order to enable the European Commission (the “*Commission*”) to declare Altadis, S.A. (“*Altadis*”) by Imperial compatible with the common market and the EEA Agreement by its decision pursuant to Article 6(1)(b) of the Merger Regulation (the “*Decision*”).

The Commitments shall take effect upon the date of adoption of the Decision.

This text shall be interpreted in the light of the Decision to the extent that the Commitments are attached as conditions and obligations, in the general framework of Community law, in particular in the light of the Merger Regulation, and by reference to the Commission Notice on remedies acceptable under Council Regulation (EEC) No 4064/89 and under Commission Regulation (EC) No 447/98.

Section A. Definitions

For the purpose of the Commitments, the following terms shall have the following meaning:

Affiliated Undertakings: undertakings controlled by the Parties and/or by the ultimate parents of the Parties, whereby the notion of control shall be interpreted pursuant to Article 3 Merger Regulation and in the light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004.

Closing: the transfer of the legal title of the Divestment Brands to the Purchaser.

Control: control within the meaning of Article 3 Merger Regulation and in the light of the Commission Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004.

Divestment Brands: the brands and all associated assets and Key Personnel, as defined in Section B and the Schedule, that Imperial commits to divest. With regard to *Interval* RYO France and *Van Nelle* Canary Islands, their inclusion in the Divestment Brands is conditional upon clearance under Art. 6(1)(b) of Council Regulation (EC) No. 139/2004.

Divestiture Trustee: one or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by Imperial and who has received from Imperial the exclusive Trustee Mandate to sell the Divestment Brands to a Purchaser at no minimum price.

Effective Date: the date of adoption of the Decision.

First Divestiture Period: the period of [...].

Hold Separate Manager: the person appointed by Imperial for Imperial's Divestment Brands and by Altadis for Altadis' Divestment Brands to manage the day-to-day business under the supervision of the Monitoring Trustee.

Imperial: Imperial Tobacco Group PLC, incorporated under the laws of England and Wales, with its registered office at PO Box 244, Upton Road, Bristol BS99 7UJ and registered with the Company Register at Companies House under number 03236483.

Key Personnel: all personnel necessary to maintain the viability and competitiveness of the Divestment Brands, as listed in the Schedule.

Monitoring Trustee: one or more natural or legal person(s), independent from the Parties, who is approved by the Commission and appointed by Imperial, and who has the duty to monitor Imperial's compliance with the conditions and obligations attached to the Decision.

Parties: Imperial and Altadis.

Personnel: all personnel currently employed by the Parties who are dedicated to the Divestment Brands, including Key Personnel, staff seconded to the Divestment Brands, and the additional personnel listed in the Schedule.

Purchaser: one or several entities approved by the Commission as acquirer(s) of any or all of the Divestment Brands in accordance with the criteria set out in Section D.

Reasonable Terms and Conditions: terms commensurate with agreements Imperial already has in place, including but not limited to the relevant elements of the agreement currently in place with [...] as regards the [...] market, as well as with general industry practice.

Schedule: the annex to these commitments.

Trustee(s): the Monitoring Trustee and the Divestiture Trustee.

Trustee Divestiture Period: the period of [...] from the end of the First Divestiture Period.

Section B. The Divestment Brands

Commitment to divest

1. In order to restore effective competition, Imperial commits to divest, or procure the divestiture of the Divestment Brands by the end of the Trustee Divestiture Period to a Purchaser and on terms of sale approved by the Commission in accordance with the procedure described in paragraph 15. To carry out the divestiture, Imperial commits to find a Purchaser and to enter into a final binding sale and purchase agreement for the sale of the Divestment Brands within the First Divestiture Period. If Imperial has not entered into such an agreement at the end of the First Divestiture Period, Imperial shall grant the Divestiture Trustee an exclusive mandate to sell the Divestment Brands in accordance with the procedure described in paragraph 24 in the Trustee Divestiture Period.
2. Imperial shall be deemed to have complied with this commitment if, by the end of the Trustee Divestiture Period, Imperial has entered into a final binding sale and purchase agreement, if the Commission approves the Purchaser and the terms in accordance with the procedure described in paragraph 15 and if the closing of the sale of the Divestment Brands takes place within a period not exceeding 3 months after the approval of the Purchaser and the terms of sale by the Commission.
3. In order to maintain the structural effect of the Commitments, the Parties shall, for a period of 10 years after the Effective Date, not acquire direct or indirect influence over the whole or part of the Divestment Brands, unless the Commission has previously found that the structure of the market has changed to such an extent that the absence of influence over the Divestment Brands is no longer necessary to render the proposed concentration compatible with the common market.
4. In relation to paragraphs 6 to 13, prior to the acquisition of Control of Altadis by Imperial, Imperial shall endeavour to cause Altadis to adhere *mutatis mutandis* to the commitments mentioned in these paragraphs.

Structure and definition of the Divestment Brands

5. Divestment Brands, described in more detail in the Schedule, include:
 - (a) all tangible and intangible assets (including intellectual property rights and blend formulas), which contribute to the current operation or are necessary to ensure the viability and competitiveness of the Divestment Brands;
 - (b) to the extent assignable, all licences, permits and authorisations issued by any governmental organisation for the benefit of the Divestment Brands; Imperial will undertake all acts and provide all information and other support that may be necessary for the transfer of such licences, permits and authorisations to the Purchaser;
 - (c) all contracts, leases, commitments and customer orders of the Divestment Brands; all customer, credit and other records of the Divestment Brands;
 - (d) the Key Personnel;
 - (e) the benefit for a period of up to five years after Closing and on Reasonable Terms and Conditions of arrangements under which Imperial or Affiliated Undertakings supply

brand marketing services for the Divestment Brands, as detailed in the Schedule, unless otherwise agreed with the Purchaser; such benefit will only be included in the Divestment Brands to the extent that the relevant brand marketing services are not covered by paragraph 5(d) of these Commitments or the Purchaser chooses not to acquire the Key Personnel;

- (f) the benefit, for a period of up to five years after Closing and on Reasonable Terms and Conditions of arrangements under which Imperial or Affiliated Undertakings supply sales support and wholesale distribution services for the Divestment Brands, as detailed in the Schedule, unless otherwise agreed with the Purchaser; and
- (g) the benefit, for a period of up to five years after Closing and on cost based commercial terms, of arrangements under which Imperial or Affiliated Undertakings supply toll manufacturing services for the Divestment Brands, as detailed in the Schedule, unless otherwise agreed with the Purchaser (items referred to under (a)-(g) hereinafter collectively referred to as “*Assets*”).

Section C. Related commitments

Preservation of Viability, Marketability and Competitiveness

6. From the Effective Date until Closing, Imperial shall preserve the economic viability, marketability and competitiveness of the Divestment Brands, in accordance with good business practice, and shall minimise as far as possible any risk of loss of competitive potential of the Divestment Brands. In particular Imperial undertakes:
 - (a) not to carry out any act upon its own authority that might have a significant adverse impact on the value, management or competitiveness of the Divestment Brands or that might alter the nature and scope of activity, or the industrial or commercial strategy or the investment policy of the Divestment Brands;
 - (b) to make available sufficient resources for the development of the Divestment Brands, on the basis and continuation of the existing business plans including the provision of the necessary support services;
 - (c) to take all reasonable steps, including appropriate incentive schemes (based on industry practice), to encourage all Key Personnel to remain with the Divestment Brands.

Hold-separate obligations of Parties

7. Imperial commits, from the Effective Date until Closing, to keep the Divestment Brands separate from the businesses it is retaining and to ensure that the Hold Separate Manager has no involvement in any business retained and vice versa. Imperial shall also ensure that the Personnel does not report, in relation to any Divestment Brand, to any individual outside the Divestment Brands save through and with the authorisation of the Monitoring Trustee.
8. Until Closing, Imperial shall assist the Monitoring Trustee in ensuring that the Divestment Brands are managed as a distinct and saleable entity separate from the businesses retained by the Parties. Imperial shall appoint a Hold Separate Manager who shall be responsible for the management of the Divestment Brands, under the supervision of the Monitoring Trustee. The Hold Separate Manager shall manage the Divestment Brands independently and in the best interest of the business with a view to ensuring its continued economic viability, marketability and competitiveness and its independence from the businesses retained by the Parties.

Ring-fencing

9. Imperial shall implement all necessary measures to ensure that it does not after the Effective Date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to the Divestment Brands. In particular, the participation of the Divestment Brands in a central information technology network shall be severed to the extent possible, without compromising the viability of the Divestment Brands. Imperial may obtain information relating to the Divestment Brands which is reasonably necessary for the divestiture of the Divestment Brands or whose disclosure to Imperial is required by law.

Non-solicitation clause

10. Imperial undertakes, subject to customary limitations, not to solicit, and to procure that Affiliated Undertakings do not solicit, the Key Personnel transferred with the Divestment Brands for a period of 12 months after Closing.

Due Diligence

11. In order to enable potential purchasers to carry out a reasonable due diligence of the Divestment Brands, Imperial shall, subject to customary confidentiality assurances and dependent on the stage of the divestiture process:
 - (a) provide to potential purchasers sufficient information as regards the Divestment Brands;
 - (b) provide to potential purchasers sufficient information relating to the Personnel and allow them reasonable access to the Personnel.

Reporting

12. Imperial shall submit written reports in English on potential purchasers of the Divestment Brands and developments in the negotiations with such potential purchasers to the Commission and the

Monitoring Trustee no later than 10 days after the end of every month following the start of the First Divestiture Period (or otherwise at the Commission's request).

13. Imperial shall inform the Commission and the Monitoring Trustee on the preparation of the data room documentation and the due diligence procedure and shall submit a copy of an information memorandum to the Commission and the Monitoring Trustee before sending the memorandum out to potential purchasers.

Section D. The Purchaser

14. In order to ensure the immediate restoration of effective competition, the Purchaser, in order to be approved by the Commission, must:
 - (a) be independent of and unconnected to the Parties;
 - (b) have the financial resources, proven expertise and incentive to maintain and develop the Divestment Brands as a viable and active competitive force in competition with the Parties and other competitors;
 - (c) neither be likely to create, in the light of the information available to the Commission, *prima facie* competition concerns nor give rise to a risk that the implementation of the Commitments will be delayed, and must, in particular, reasonably be expected to obtain all necessary approvals from the relevant regulatory authorities for the acquisition of the Divestment Brands (the before-mentioned criteria for the Purchaser hereafter the "**Purchaser Requirements**").
15. The final binding sale and purchase agreement shall be conditional on the Commission's approval. When Imperial has reached an agreement with a purchaser, it shall submit a fully documented and reasoned proposal, including a copy of the final agreement(s), to the Commission and the Monitoring Trustee. Imperial must be able to demonstrate to the Commission that the purchaser meets the Purchaser Requirements and that the Divestment Brands are being sold in a manner consistent with the Commitments. For the approval, the Commission shall verify that the purchaser fulfils the Purchaser Requirements and that the Divestment Brands are being sold in a manner consistent with the Commitments. The Commission may approve the sale of the Divestment Brands without one or more Assets or parts of the Key Personnel, if this does not affect the viability and competitiveness of the Divestment Brands after the sale, taking account of the proposed purchaser.

Section E. Trustee

I. Appointment Procedure

16. Imperial shall appoint a Monitoring Trustee to carry out the functions specified in the Commitments for a Monitoring Trustee. If Imperial has not entered into a binding sales and purchase agreement one month before the end of the First Divestiture Period or if the Commission has rejected a purchaser proposed by Imperial at that time or thereafter, Imperial shall appoint a Divestiture Trustee to carry out the functions specified in the Commitments for a Divestiture Trustee. The appointment of the Divestiture Trustee shall take effect upon the commencement of the Trustee Divestiture Period.

17. The Trustee shall be independent of the Parties, possess the necessary qualifications to carry out its mandate, for example as an investment bank or consultant or auditor, and shall neither have nor become exposed to a conflict of interest. The Trustee shall be remunerated by the Parties in a way that does not impede the independent and effective fulfilment of its mandate. In particular, where the remuneration package of a Divestiture Trustee includes a success premium linked to the final sale value of the Divestment Brands, the fee shall also be linked to a divestiture within the Trustee Divestiture Period.

Proposal by the Parties

18. No later than one week after the Effective Date, Imperial shall submit a list of one or more persons whom Imperial proposes to appoint as the Monitoring Trustee to the Commission for approval. No later than one month before the end of the First Divestiture Period, Imperial shall submit a list of one or more persons whom Imperial proposes to appoint as Divestiture Trustee to the Commission for approval. The proposal shall contain sufficient information for the Commission to verify that the proposed Trustee fulfils the requirements set out in paragraph 17 and shall include:
- (a) the full terms of the proposed mandate, which shall include all provisions necessary to enable the Trustee to fulfil its duties under these Commitments;
 - (b) the outline of a work plan which describes how the Trustee intends to carry out its assigned tasks;
 - (c) an indication whether the proposed Trustee is to act as both Monitoring Trustee and Divestiture Trustee or whether different trustees are proposed for the two functions.

Approval or rejection by the Commission

19. The Commission shall have the discretion to approve or reject the proposed Trustee(s) and to approve the proposed mandate subject to any modifications it deems necessary for the Trustee to fulfil its obligations. If only one name is approved, Imperial shall appoint or cause to be appointed, the individual or institution concerned as Trustee, in accordance with the mandate approved by the Commission. If more than one name is approved, Imperial shall be free to choose the Trustee to be appointed from among the names approved. The Trustee shall be appointed within one week of the Commission's approval, in accordance with the mandate approved by the Commission.

New proposal by the Parties

20. If all the proposed Trustees are rejected, Imperial shall submit the names of at least two more individuals or institutions within one week of being informed of the rejection, in accordance with the requirements and the procedure set out in paragraphs 16 and 19.

Trustee nominated by the Commission

21. If all further proposed Trustees are rejected by the Commission, the Commission shall nominate a Trustee, whom Imperial shall appoint, or cause to be appointed, in accordance with a trustee mandate approved by the Commission.

II. Functions of the Trustee

22. The Trustee shall assume its specified duties in order to ensure compliance with the Commitments. The Commission may, on its own initiative or at the request of the Trustee or Imperial, give any orders or instructions to the Trustee in order to ensure compliance with the conditions and obligations attached to the Decision.

Duties and obligations of the Monitoring Trustee

23. The Monitoring Trustee shall:

- (i) propose in its first report to the Commission a detailed work plan describing how it intends to monitor compliance with the obligations and conditions attached to the Decision.
- (ii) oversee the on-going management of the Divestment Brands with a view to ensuring its continued economic viability, marketability and competitiveness and monitor compliance by Imperial with the conditions and obligations attached to the Decision. To that end the Monitoring Trustee shall:
 - (a) monitor the preservation of the economic viability, marketability and competitiveness of the Divestment Brands, and the keeping separate of the Divestment Brands from the business retained by the Parties, in accordance with paragraphs 6 and 7 of the Commitments;
 - (b) supervise the management of the Divestment Brands as a distinct and saleable entity, in accordance with paragraph 8 of the Commitments;
- (i) in consultation with Imperial, determine all necessary measures to ensure that Imperial does not after the effective date obtain any business secrets, know-how, commercial information, or any other information of a confidential or proprietary nature relating to the Divestment Brands, in particular strive for the severing of the Divestment Brands' participation in a central information technology network to the extent possible, without compromising the viability of the Divestment Brands, and (ii) decide whether such information may be disclosed to Imperial as the disclosure is reasonably necessary to allow Imperial to carry out the divestiture or as the disclosure is required by law;
- (c) monitor the splitting of assets and the allocation of Personnel between the Divestment Brands and Imperial or Affiliated Undertakings;
- (iii) assume the other functions assigned to the Monitoring Trustee under the conditions and obligations attached to the Decision;
- (iv) propose to Imperial such measures as the Monitoring Trustee considers necessary to ensure Imperial's compliance with the conditions and obligations attached to the Decision, in particular the maintenance of the full economic viability, marketability or

competitiveness of the Divestment Brands, the holding separate of the Divestment Brands and the non-disclosure of competitively sensitive information;

- (v) review and assess potential purchasers as well as the progress of the divestiture process and verify that, dependent on the stage of the divestiture process, (a) potential purchasers receive sufficient information relating to the Divestment Brands and the Personnel in particular by reviewing, if available, the data room documentation, the information memorandum and the due diligence process, and (b) potential purchasers are granted reasonable access to the Personnel;
- (vi) provide to the Commission, sending Imperial a non-confidential copy at the same time, a written report within 15 days after the end of every month. The report shall cover the operation and management of the Divestment Brands so that the Commission can assess whether the business is held in a manner consistent with the Commitments and the progress of the divestiture process as well as potential purchasers. In addition to these reports, the Monitoring Trustee shall promptly report in writing to the Commission, sending Imperial a non-confidential copy at the same time, if it concludes on reasonable grounds that Imperial is failing to comply with these Commitments;
- (vii) within one week after receipt of the documented proposal referred to in paragraph 15, submit to the Commission a reasoned opinion as to the suitability and independence of the proposed purchaser and the viability of the Divestment Brands after the sale and as to whether the Divestment Brands are sold in a manner consistent with the conditions and obligations attached to the Decision, in particular, if relevant, whether the sale of the Divestment Brands without one or more Assets or not all of the Personnel affects the viability of the Divestment Brands after the sale, taking account of the proposed purchaser.

Duties and obligations of the Divestiture Trustee

- 24. Within the Trustee Divestiture Period, the Divestiture Trustee shall sell at no minimum price the Divestment Brands to a purchaser, provided that the Commission has approved both the purchaser and the final binding sale and purchase agreement in accordance with the procedure laid down in paragraph 15. The Divestiture Trustee shall include in the sale and purchase agreement such terms and conditions as it considers appropriate for an expedient sale in the Trustee Divestiture Period. In particular, the Divestiture Trustee may include in the sale and purchase agreement such customary representations and warranties and indemnities as are reasonably required to effect the sale. The Divestiture Trustee shall protect the legitimate financial interests of Imperial, subject to the Parties' unconditional obligation to divest at no minimum price in the Trustee Divestiture Period.
- 25. In the Trustee Divestiture Period (or otherwise at the Commission's request), the Divestiture Trustee shall provide the Commission with a comprehensive monthly report written in English on the progress of the divestiture process. Such reports shall be submitted within 15 days after the

end of every month with a simultaneous copy to the Monitoring Trustee and a non-confidential copy to the Parties.

III. Duties and obligations of the Parties

26. Imperial shall provide and shall cause its advisors to provide the Trustee with all such cooperation, assistance and information as the Trustee may reasonably require to perform its tasks. The Trustee shall have full and complete access to any of Imperial's or the Divestment Brands' books, records, documents, management or other personnel, facilities, sites and technical information necessary for fulfilling its duties under the Commitments and Imperial and the Divestment Brands shall provide the Trustee upon request with copies of any document. Imperial and the Divestment Brands shall make available to the Trustee one or more offices on their premises and shall be available for meetings in order to provide the Trustee with all information necessary for the performance of its tasks.
27. Imperial shall provide the Monitoring Trustee with all managerial and administrative support that it may reasonably request on behalf of the management of the Divestment Brands. This shall include all administrative support functions relating to the Divestment Brands which are currently carried out at headquarters level. Imperial shall provide and shall cause its advisors to provide the Monitoring Trustee, on request, with the information submitted to potential purchasers, in particular give the Monitoring Trustee access to the data room documentation and all other information granted to potential purchasers in the due diligence procedure. Imperial shall inform the Monitoring Trustee on possible purchasers, submit a list of potential purchasers, and keep the Monitoring Trustee informed of all developments in the divestiture process.
28. Imperial shall grant or procure Affiliated Undertakings to grant comprehensive powers of attorney, duly executed, to the Divestiture Trustee to effect the sale, the Closing and all actions and declarations which the Divestiture Trustee considers necessary or appropriate to achieve the sale and the Closing, including the appointment of advisors to assist with the sale process. Upon request of the Divestiture Trustee, Imperial shall cause the documents required for effecting the sale and the Closing to be duly executed.
29. Imperial shall indemnify the Trustee and its employees and agents (each an "*Indemnified Party*") and hold each Indemnified Party harmless against, and hereby agrees that an Indemnified Party shall have no liability to Imperial for any liabilities arising out of the performance of the Trustee's duties under the Commitments, except to the extent that such liabilities result from the wilful default, recklessness, gross negligence or bad faith of the Trustee, its employees, agents or advisors.
30. At the expense of Imperial, the Trustee may appoint advisors (in particular for corporate finance or legal advice), subject to Imperial's approval (this approval not to be unreasonably withheld or delayed) if the Trustee considers the appointment of such advisors necessary or appropriate for the performance of its duties and obligations under the Mandate, provided that any fees and other expenses incurred by the Trustee are reasonable. Should Imperial refuse to approve the advisors proposed by the Trustee the Commission may approve the appointment of such advisors instead, after having heard Imperial. Only the Trustee shall be entitled to issue instructions to the

advisors. Paragraph 29 shall apply *mutatis mutandis*. In the Trustee Divestiture Period, the Divestiture Trustee may use advisors who served Imperial during the Divestiture Period if the Divestiture Trustee considers this in the best interest of an expedient sale.

IV. Replacement, discharge and reappointment of the Trustee

31. If the Trustee ceases to perform its functions under the Commitments or for any other good cause, including the exposure of the Trustee to a conflict of interest:
 - (a) the Commission may, after hearing the Trustee, require Imperial to replace the Trustee; or
 - (b) Imperial, with the prior approval of the Commission, may replace the Trustee.
32. If the Trustee is removed according to paragraph 31, the Trustee may be required to continue in its function until a new Trustee is in place to whom the Trustee has effected a full hand over of all relevant information. The new Trustee shall be appointed in accordance with the procedure referred to in paragraphs 16-21.
33. Beside the removal according to paragraph 31, the Trustee shall cease to act as Trustee only after the Commission has discharged it from its duties after all the Commitments with which the Trustee has been entrusted have been implemented. However, the Commission may at any time require the reappointment of the Monitoring Trustee if it subsequently appears that the relevant remedies might not have been fully and properly implemented.

Section F. The Review Clause

34. The Commission may, where appropriate, in response to a request from Imperial showing good cause and accompanied by a report from the Monitoring Trustee:
 - (i) Grant an extension of the time periods foreseen in the Commitments, or
 - (ii) Waive, modify or substitute, in exceptional circumstances, one or more of the undertakings in these Commitments.

Where Imperial seeks an extension of a time period, it shall submit a request to the Commission no later than one month before the expiry of that period, showing good cause. Only in exceptional circumstances shall Imperial be entitled to request an extension within the last month of any period.

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duly authorised for and on behalf of
Imperial Tobacco Group PLC

SCHEDULE

1. Some of the Divestment Brands are owned and operated by Altadis whereas the others are owned and operated by Imperial. The Divestment Brands may be identified by reference to their relevant product and geographic market, brand name and current owner as follows:

Product market	Geographic market	Brand name	Owner at the time of the offering of the Commitments
RYO	Portugal	<i>Amsterdamer</i>	Altadis
RYO	Spain	<i>Interval</i>	Imperial
RYO	Spain	<i>Picadura</i>	Altadis
RYO	Canary Islands	<i>Van Nelle</i>	Imperial
RYO	France	<i>Interval</i>	Imperial
RYO	France	<i>Wervicq</i>	Imperial
RYO	France	<i>Bergerac</i>	Altadis
RYO	France	<i>Santoya</i>	Altadis
RYO	Italy	<i>Van Nelle</i>	Imperial
Pipe tobacco	Finland	<i>Kilta</i>	Altadis
Pipe tobacco	France	<i>Bergerac</i>	Altadis
Cigars	Greece	<i>Backwoods</i>	Altadis

2. Following paragraph 5 of these Commitments, the Divestment Brands include, but are not limited to:

- (a) All tangible assets exclusively related to the Divestment Brands, including the warehoused stock, finished products, raw and pack materials, outstanding product orders from suppliers and in-store advertising materials;

- (b) The following intangible assets used in the operation of the Divestment Brands:
- Trademarks: assignment wherever possible, otherwise an exclusive and irrevocable licence of the trademarks contained in **Annex 1A, Part I**;
 - Other intellectual property rights: where possible the assignment, otherwise the licence for all other intellectual property rights, including know-how, blend formulas and design rights relating to the packaging of the products;
- (c) Licences, permits and authorisations; Imperial will undertake all acts and provide all information and other support that may be necessary for the transfer of such licences, permits and authorisations to the Purchaser;
- (d) All purchase orders, contracts, agreements and other obligations exclusively related to the Divestment Brands. Imperial will use all reasonable efforts to obtain the consent of any third party to any purchase order, contract, agreement or other obligation exclusively used in the Divestment Brands, which consent is required for the assignment of any such purchase order, contract, agreement or other obligation from Imperial to the Purchaser;
- (e) Copies of all the books, records and other documents exclusively related to or necessary for the operation of the Divestment Brands (including, without limitation, customer and supplier lists and files, distribution lists, mailing lists, sales materials, operating, production and other manuals, plans, files, specifications, process drawings, computer programs, data and information, manufacturing and quality control records and procedures, market research and intelligence, advertising and promotional materials), provided that Imperial may redact from such copies any information that does not relate to the Divestment Brands;
- (f) The Key Personnel identified in **Annex 1A, Part II**, subject to labour law restrictions;
- (g) the benefit for a period of up to five years after Closing and on Reasonable Terms and Conditions of arrangements under which Imperial or Affiliated Undertakings supply brand marketing services for the Divestment Brands, unless otherwise agreed with the Purchaser; such benefit will only be included in the Divestment Brands to the extent that the relevant brand marketing services are not covered by paragraph 2(f) of this Schedule or the Purchaser chooses not to acquire the Key Personnel;
- (h) The benefit, for a period of up to five years after Closing and on Reasonable Terms and Conditions of arrangements under which Imperial or Affiliated Undertakings supply sales support and wholesale distribution services for the Divestment Brands, unless otherwise agreed with the Purchaser;
- (i) The benefit, for a period of up to five years after Closing and on Reasonable Terms and Conditions, of arrangements under which Imperial or Affiliated Undertakings supply sales support services for the Divestment Brands, unless otherwise agreed with the Purchaser;
- (j) The benefit, for a period of up to five years after Closing and on a cost based commercial terms, of arrangements between, on the one hand, Imperial or Affiliated Undertakings or Altadis or Affiliated Undertakings, and, on the other hand, third parties relating to the wholesale distribution of the Divestment Brands, unless otherwise agreed with the Purchaser; and

- (k) The benefit, for a period of up to five years after Closing and on cost based commercial terms, of arrangements under which Imperial or Affiliated Undertakings supply toll manufacturing services for the Divestment Brands, unless otherwise agreed with the Purchaser.

If there is any asset which would not be covered in the above list but which is both used exclusively in the operation of the Divestment Brands and necessary for the continued viability of the Divestment Brands, then that asset will be offered to potential purchasers. If there is any asset which would not be covered in the above list but which is both used (but not exclusively) in the operation of the Divestment Brands and necessary for the continued viability of the Divestment Brands (a "Shared Asset"), then Imperial will offer such Shared Asset or adequate substitute, unless otherwise agreed with the Purchaser.

3. The Divestment Brands shall not include:

- (a) Assignment of or license on future patents, trademarks and other intellectual property rights to be filed by Imperial after the Effective Date;
- (b) Trademark licences or assignments for geographic markets other than the geographic markets identified in paragraph 1 of this Schedule.

Annex 1A, Part I - Trademarks

Annex 1A, Part II – Key Personnel