



COMMERCE COMMISSION

Decision No. 699

Determination pursuant to the Commerce Act 1986 in the matter of an application for a merger transaction between

Scandinavian Tobacco Group A/S

and

Swedish Match AB

The Commission: Dr Mark Berry
Mr Gowan Pickering
Dr Stephen Gale

Summary of Application: The merger of Scandinavian Tobacco Group A/S's cigar, pipe tobacco and accessories business with that of Swedish Match AB.

Determination: Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for Scandinavian Tobacco Group A/S to merge its cigar, pipe tobacco and accessories businesses with that of Swedish Match AB subject to the divestment undertaking dated 22 September 2010 provided by Scandinavian Tobacco Group A/S to the Commission pursuant to section 69A of the Commerce Act 1986.

Date of Determination: 22 September 2010

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THE PROPOSAL

1. On 21 June 2010, the Commerce Commission (Commission) received a Notice pursuant to s 66(1) of the Commerce Act 1986 (the Act). The notice sought clearance for Scandinavian Tobacco Group A/S to merge its cigar, pipe tobacco and accessories businesses with that of Swedish Match AB.
2. The Notice includes a proposal to undertake to divest certain assets (Divestiture Package) if required.

PROCEDURE

3. Section 66(3) of the Act requires the Commission either to clear or to decline to clear a notice given under section 66(1) within 10 working days, unless the Commission and the person who gave the notice agree to a longer period. In this instance, the Applicant agreed to an initial extension through to 6 August 2010. However, the Applicant sought two further extensions in order that it could have more time to harmonise its Australian and New Zealand divestment packages.
4. As stated in the Commission's Mergers & Acquisitions Merger Process Guidelines, the Commission aims to complete its consideration of most clearance applications within an average of forty working days; however, the further extensions suspended the Commission's process for a number of weeks, in accordance with the wishes of the Applicant.

DECISION

5. Absent the divestment, there would be considerable aggregation of market share and the proposed acquisition would be likely to raise significant competition concerns in the relevant cigar market.
6. The Commission has found no significant risks associated with the Divestiture Package and considers that it would remedy the competition concerns by providing sufficient constraint on the combined entity.
7. Accordingly, the Commission is satisfied that the proposed acquisition with the Divestiture Package in place will not have, or would not be likely to have, the effect of substantially lessening competition in the relevant cigar market.
8. With regard to the relevant pipe tobacco market, the Commission considers that there would be no material difference between the factual and the counterfactual. The Commission is therefore satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the relevant pipe tobacco market.

ANALYTICAL FRAMEWORK

9. The Commission applies a consistent analytical framework to all its clearance decisions.¹ The first step is to determine the relevant markets. As acquisitions considered under section 66 are prospective, the Commission uses a forward-

¹ Commerce Commission, *Mergers and Acquisitions Guidelines*, January 2004.

looking type of analysis to assess whether a lessening of competition is likely in the defined market(s). Hence, an important subsequent step is to establish the appropriate hypothetical future with and without scenarios, defined as the situations expected:

- with the acquisition (the factual); and
 - in the absence of the acquisition (the counterfactual).
10. The impact of the acquisition on competition is then viewed as the prospective difference in the extent of competition in the relevant markets between those two scenarios. To analyse the extent of competition in the factual and counterfactual, the Commission considers:
- existing competition;
 - potential competition;
 - other competition factors, such as the countervailing market power of buyers and suppliers; and
 - the potential for coordinated behaviour – whether the acquisition would enhance the ability of market participants to collude either tacitly or explicitly.
11. Under section 69A of the Act, the Commission, in giving a clearance, may accept undertakings to dispose of assets or shares. Under section 69A(2) of the Act the Commission is only able to accept structural undertakings. The Commission is not permitted to accept behavioural undertakings. If divestment undertakings are accepted by the Commission, they are deemed to form part of the clearance.
12. The Commission's analytical framework for assessing divestment undertakings is set out in the Mergers & Acquisition Divestment Remedies Guidelines² (Divestment Guidelines). The Commission's assessment of the market and divestment undertakings will be on a case by case basis to ensure that the divestment undertakings are sufficient to remedy the specific competitive harm. As set out in the Divestment Guidelines, the Commission assesses the risks associated with divestment undertakings within the analytical framework that comprises:
- composition risks;
 - asset risks; and
 - purchaser risks.
13. Overall, the Commission must be satisfied that the Divestiture Package remedies the competitive harm, absent the divestment found above.

² <http://www.comcom.govt.nz/assets/Business-Competition/Mergers-and-Acquisitions/Mergers-and-Acquisitions-Divestment-Remedies-Guidelines-June-2010.pdf>

PARTIES

Scandinavian Tobacco Group (STG)

14. STG is a privately owned Danish company involved in the manufacture and supply of tobacco and tobacco-related products including cigars and pipe tobacco. It has a number of manufacturing facilities located throughout the world, which it uses to supply its products to various countries including New Zealand and Australia.
15. At present, STG has no physical presence in New Zealand. Rather, STG has an arrangement with an independent distributor, Stuart Alexander Pty Limited, to distribute STG's cigar products in New Zealand. STG's cigar brands in New Zealand include Café Crème; Henri Wintemans; Schimmelpennick; and Van Hartog. STG's pipe tobacco brand, "Erinmore" is distributed in New Zealand by SM.³

Swedish Match (SM)

16. SM is a publicly listed company based in Sweden. Like STG, it manufactures and supplies tobacco and tobacco-related products including cigars and pipe tobacco globally from various manufacturing plants located around the world.
17. Its local subsidiary, Swedish Match New Zealand Limited, distributes SM products in New Zealand. SM's cigar brands in New Zealand include Wee Willem, Willem II and White Owl. It also supplies Borkum Riff and Erinmore pipe tobacco in New Zealand.

Tobacco Manufacturers

18. There are no cigar manufacturing facilities in New Zealand. International tobacco manufacturers distribute their products in New Zealand either through their New Zealand-based subsidiary or via local third party distributors who import tobacco products independent of the manufacturer. International tobacco companies based in New Zealand are predominately focused on cigarettes and roll-your-own tobacco. The three main international tobacco companies with a significant presence in New Zealand are:
 - British American Tobacco (New Zealand) Limited (BAT), a tobacco manufacturer that sells cigarettes, roll-your-own tobacco and a small number of its Dunhill branded cigars;
 - Imperial Tobacco New Zealand Limited (Imperial) which sells cigarettes, roll-your-own tobacco, and pipe tobacco; and
 - Philip Morris International, (PMI) a tobacco manufacturer that sells cigarettes and roll-your-own tobacco. While it sells cigars and pipe tobacco in a number of countries, it does not currently supply these products in New Zealand.

³ In the past, a small amount of STG's other pipe tobacco brands, Skandinavik and WO Larsen was exported to New Zealand via Charles Vella Australia. []

Distributors/Importers

19. In addition to STG and SM, a number of companies import cigars and pipe tobacco into New Zealand from international manufacturers. The significant importers of cigars and pipe tobacco include:
- Stuart Alexander Pty Limited (Stuart Alexander), which as noted above, is responsible for the distribution of STG's cigars in New Zealand and Australia;
 - The Pacific Cigar Company (New Zealand) Limited, a distributor and retailer of premium Cuban cigars;
 - Moderna Trading Co Limited, a distributor which is the New Zealand agent for Koninklijke Agio Sigarenfabrieken N.V., which is based in the Netherlands and manufactures the Agio range of cigars. Moderna also distributes a small amount of pipe tobacco products;
 - N.Z Tobacco Group Limited, a distributor which is the New Zealand agent for Von Eicken's Candlelight brand of cigars.

Retail outlets

20. Cigars and pipe tobacco are sold through a number of different retail outlets including supermarkets, dairies and convenience stores, liquor outlets, traditional tobacconists, and the four main service station chains.
21. These outlets acquire cigars and pipe tobacco either directly from the manufacturer/distributor or via a wholesale distributor such as James Gilmour, Toops Wholesale and Trents Wholesale (together "GTT").
22. Appendix 2 outlines the industry structure and relationships between the international tobacco manufacturers, wholesalers and importers, and retail outlets.

INDUSTRY BACKGROUND

23. The volume of cigars sold in New Zealand increased by only 2% during the period 1999 to 2009. Industry participants advised the Commission that there was unlikely to be any significant growth in the relevant market in the future. Sales of pipe tobacco, mirroring global trends, have significantly declined in New Zealand. Between 2005 and 2009, consumption of pipe tobacco fell by 22%.
24. New Zealand tobacco companies are predominately focused on sales of cigarettes and roll-your-own tobacco. Cigars and pipe tobacco combined generally represent only about []% of retail sales of all tobacco products.
25. Low end machine-made cigars represent about 90% of the cigar market. It is quite common for these low end machine made cigars to be contract manufactured (or toll manufactured) by other tobacco manufacturers. These retail for about \$3-4 per 'stick' or about \$15 for a packet of five cigar sticks. This type of cigar is smoked by customers on a regular basis. Low end cigars are sold direct to supermarkets, through the GTT channel to dairies and convenience stores, and through service stations. The Foodstuffs Group (in particular through the GTT distribution channel)

and service stations are [] of STG and SM. Progressive Enterprises informed the Commission that it no longer retails cigars or pipe tobacco.

26. High end Cuban cigars are hand rolled and account for the remaining 10% of the cigar market. A single stick retails between \$20 and \$100. These are special occasion cigars typically smoked to celebrate birthdays, weddings or the births of children. There are about five importers of high end cigars.
27. Intermediate quality cigars are imported from other Caribbean nations such as the Agio brand from the Dominican Republic. These types of cigars, although hand rolled, retail for significantly less than Cuban cigars.
28. Excise duty accounts for about 40% of the retail price of cigars and pipe tobacco. Regular increases in duty occur on 1 January every year with other ad hoc duty increases imposed from time to time. Thus, retail prices of cigars and pipe tobacco are influenced by excise duty as well as other factors such as manufacturing costs, retailers' margin expectations, customer demand and competitors' pricing.
29. The advertising and retail display of tobacco products is heavily regulated in New Zealand. Advertising (and sponsorship) is banned completely. Regulations restrict both the amount of retail display space and the display position. Industry participants advised the Commission that this means the only way to gain market share for tobacco brands is by attempting to obtain additional display shelf space. This may be achieved by the fostering of direct relationships between sales representatives and retailers. Even then, the major cigarette brands provide free display racks and stands to retailers, on the basis that their particular brand is most prominently displayed.

MARKET DEFINITION

30. The Applicant submitted that two separate markets should be defined; the national markets for the importation and wholesale supply of: (i) cigars; and (ii) pipe tobacco.
31. This is consistent with the Commission's Decision 614 (ST Cigar Group and British American Tobacco) of 17 August 2007. In that decision the Commission found a discrete cigar product market. It noted that cigarettes would not be readily substitutable for cigars; that cigars and cigarettes have very distinct characteristics including taste and image, and that cigar smoking tends to be more event related.
32. The European Commission (EC) concluded in *Imperial Tobacco/Altadis* (2007⁴) that competitors and customers broadly agree that pipe tobacco forms a market separate from other tobacco products. The EC also found a separate market for cigars. It noted that an argument had been made that a clear difference (but some overlap) existed between hand-made or 'premium' cigars and machine-made cigars, but it was not necessary in the circumstances of the case to consider whether that difference was sufficient to justify placing them in separate markets.

⁴ Case No COMP/M.4581 – Imperial Tobacco/Altadis

33. During its investigation of this application, the Commission has discussed issues relevant to the market definition with other importer/wholesalers of tobacco products and with distributors and retailers. There is broad industry consensus that cigars and pipe tobacco are in discrete product markets and that cigarettes are not generally substitutable for either. These views are consistent with those of the Applicant and with those of the Commission at the time of Decision 614.
34. The Commission notes that some industry participants consider that machine made cigars and handmade Cuban cigars are not in the same product market. [] stated that the price differences and production processes are very different for low end machine made and handmade Cuban cigars. In the Commission's view there is some evidence that these form separate markets because:
- there is a large price difference between handmade Cuban cigars (perhaps retailing at \$80 a cigar) and less expensive machine-made cigars (possibly around \$12 for a pack of 10 cigarillos - short, narrow cigars wrapped in whole-leaf tobacco) and there is unlikely to be significant demand-side substitution between the cigars at these extremes; and
 - less expensive machine-made cigars tend to be smoked regularly while handmade Cuban cigars are mostly for one-off special occasions.
35. However there is some price overlap between top-of-the-range machine-made cigars and the less expensive hand-made cigars. In this market segment premium and machine-made cigars are more likely to be satisfactory substitutes. As the Commission noted in Decision 614, this overlapping substitutability between cigars at adjacent quality/price levels would result in a chain of substitutability stretching from the premium cigars to the less expensive machine-made cigars.
36. The Commission considers that it may be possible to define separate markets for hand-made and machine-made cigars. However, in this instance, it is not necessary as:
- the competitive assessment would not change if cigars were distinguished in this manner because the significant aggregation of market share occurs only in respect of less expensive machine-made cigars which account for about 90% of all cigar sales by volume which are sold in New Zealand; and
 - while SM imports a small quantity of handmade cigars into New Zealand, STG does not so there would be no aggregation if the Commission were to find a separate product market for hand made cigars.
37. The Commission, therefore, sees no reason to depart from the product markets defined in Decision 614 as separate product markets for cigars and pipe tobacco.
38. The Applicant submitted that the geographic markets are national in scope. The Commission found that suppliers sell their products to wholesalers who distribute nationwide or sell direct to supermarkets nationwide. Therefore, the Commission considers the geographic markets to be national in scope.

39. The Commission concludes that the relevant markets are the national markets for the import and wholesale supply of: (i) cigars (the cigar market); and (ii) pipe tobacco (the pipe tobacco market).

COUNTERFACTUAL

40. In the absence of any other proposed transactions between either STG or SM, and other tobacco companies, the counterfactual appears to be the status quo in both relevant markets. []

COMPETITION ANALYSIS

The Pipe Tobacco Market

41. STG exports its Erinmore branded pipe tobacco to Swedish Match (Australia) Ltd (SM Australia). SM Australia then distributes Erinmore pipe tobacco in Australia and also re-exports Erinmore pipe tobacco to its New Zealand subsidiary for distribution and retailing in New Zealand. The Applicant advised the Commission that STG has no involvement in setting the wholesale price of its pipe tobacco brand, Erinmore, in New Zealand.
42. The Applicant therefore submits that there is no difference between the factual and counterfactual in the pipe tobacco market.
43. The Commission agrees with the Applicant. Essentially, there would be no competition between Erinmore and SM's Borkum Riff brand either in the counterfactual or the factual. As such, the Commission is satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the pipe tobacco market.

The Cigar Market

44. The Applicant has included a divestment undertaking as part of its application. The Commission will first consider whether, absent the divestment, the proposed acquisition is likely to result in a substantial lessening of competition in the relevant market(s). If this is the case, then the Commission will then consider whether the proposed divestment undertakings would be sufficient to remedy that likely substantial lessening of competition.

Table 1: 2009 Market Shares by Volume in the Cigar Market (Without the Divestment)

Market Shares based on Volume

Supplier	Units	%
Scandinavian Tobacco	5,202,384	55
Swedish Match	3,526,947	38
Merged Entity	8,729,331	93
NZ Tobacco	227,915	2
Other	456,395	5
Total	9,413,641	100

* Source: Ministry of Health Tobacco Returns 2009.

45. The Applicant, as well as industry participants, consider that calculating market shares by volume is the most appropriate measure. This is because of the differentiated nature of the cigar market. Low end cigars sold in high volumes are significantly cheaper than high end Cuban cigars which are sold in much smaller volumes. In addition, the Commission understands that it is difficult to accurately calculate market share by value due to differing annual increases and ad hoc excise duties applied to different tobacco products.
46. Table 1 indicates that, absent the divestment, the merged entity would have a market share of 93%.
47. The Applicant argued that post-acquisition it would, absent the divestment, be constrained by existing competitors who have the capacity and capability to increase supply in response to any attempt by the merged entity to increase prices or reduce supply. In addition, the Applicant argued that likely entry by potential competitors (given the ease of entry) would provide further constraint, as would large customers who hold and exercise a significant degree of countervailing power.
48. The Commission interviewed a number of key industry participants and found quite the opposite.
49. The Applicant submitted that large international cigar manufacturers could increase their supply in New Zealand either directly, or through third party distributors. While there are some small distributors supplying small amounts of cigars from large international tobacco companies, these products and their brands are not well known in New Zealand. The market shares of the remaining 7% have not changed significantly over the last three years. All industry participants advised the Commission that having an established brand is an important requirement in the New Zealand market.
50. NZ Tobacco began importing and selling the Candlelight cigar brand in 2007. To date, it has only achieved 2% market share. NZ Tobacco has obtained a small presence in some Foodstuffs supermarkets in the South Island, []
51. Moderna, imports and distributes the Agio brand of cigars and has only 0.43% market share but has been distributing the Agio brand for over twenty years. []

52. The Commission has gathered evidence that suggests it is very difficult for small wholesalers to expand or to introduce new cigar brands into New Zealand in order to gain access to large retailers or the GTT wholesale channel. This is because:
- tobacco consumers appear to be loyal to established brands;
 - due to strict government regulations there is almost no ability to advertise and market a new cigar brand; and
 - due to government regulation, there is very limited ability to display new cigar products because there are strict rules around how a retailer can display those products.
53. The Applicant also submitted that large tobacco companies with established overseas cigar brands could easily enter New Zealand if the combined entity were to increase prices. The Commission agrees with the Applicants that international tobacco companies with no current presence in New Zealand but with an established international brand would be unlikely to have difficulty establishing warehousing, employing a sales force or setting up nationwide distribution.
54. []
55. []
56. []
57. The Applicant submitted that new brands have been introduced in New Zealand. For example, SM's Café Crème brand was introduced in 2003 and now has market share of around 15%. The Commission notes, however, that this is a scenario quite different to that of de novo entry or the expansion of a small existing wholesaler as these were new products launched by an established industry player with the sales and distribution infrastructure already in place within the GTT channel, the oil channel and supermarkets.
58. Stuart Alexander, STG's New Zealand distributor, informed the Commission that it attempted to introduce Hamlet, a leading cigar brand in the United Kingdom, into New Zealand. []
- []
59. STG and SM informed the Commission that they compete with each other on product range, service and price. Both were aware of the retail price points of the other. Large customers such as [] advised the Commission that there is a considerable degree of competitive tension between STG and SM and that this would be lost as a result of the proposed acquisition.
60. []
61. []
62. Overall, customers considered that they would have virtually no bargaining power post merger, as there were no credible alternative suppliers to STG or SM. []
63. Overall, the Commission considers that, absent the divestment, there would be few constraints on the combined entity because:

- the combined entity would have 93% of the cigar market and would be the only supplier to key retail and wholesale channels.
 - the small existing competitors with only 7% of the market have not gained access to important retail and wholesale channels;
 - even if the small existing competitors wanted to expand, the lack of an established brand and regulatory advertising and display restrictions would limit such expansion;
 - [] and
 - the lack of any countervailing power from large customers who would have no credible alternative, and even if they could source alternative supply, would have difficulty promoting a new brand due to regulatory restrictions.
64. Accordingly, the Commission considers that absent the divestment, it cannot be satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the cigar market.

The Divestiture Package

65. The Applicant proposes to divest the Wee Willem and Willem II (together, Willem) cigar brands owned by SM (the Divestiture Package). The Applicant argued that the Divestiture Package would either significantly enhance an existing competitor's position in the market or alternatively create a new competitor such that there would be no substantial lessening of competition. The Divestiture Package is attached as Appendix One.

Table 2: Market Shares by Volume in the Cigar Market Post-Divestment

Supplier / Brand	Units	%
Scandinavian Tobacco		
- Café Crème	1,371,715	15
- Schimmelpennick	1,719,430	18
- Van Hartog	1,852,920	19
- Other	258,319	3
ST Total	5,202,384	55
Swedish Match		
- White Owl	270,460	3
- Other	356,725	4
SM Total	627,185	7
Merged Entity	5,829,569	62
Divested Brand		
- Willem	2,899,762	31
NZ Tobacco	227,915	2
Other	456,395	5
Total	9,413,641	100

* Source: Ministry of Health Tobacco Returns 2009.

66. Table 2 indicates that the merged entity would have a market share of 62% and the new owner of the divested brand would have a market share of 31%.

Table 3: Sales by Volume in the Cigar Market of Willem Branded Cigars

	2005 (units)	2006	2007	2008	2009
Willem	3,955,043	3,735,457	3,579,070	3,157,201	3,069,718

* Source: Ministry of Health Tobacco Returns 2009.

67. Table 3 shows that Willem brands have declined in volume by about 22% since 2005. The Applicant advised the Commission that the loss of volume was the cumulative effect of:

- []
- []
- []

68. The Applicant submitted that:

- []
- []

69. []
[]
70. Industry participants confirmed to the Commission that the Willem brand is well established in New Zealand. [] stated that the Willem cigar brands are long established brands with “a high degree of brand loyalty”.
71. Willem is recognised as being the top selling or number one brand in New Zealand over all retail outlets. [] advised the Commission that Willem is one of its major brands and “its second biggest seller”. [] would be willing to support a new owner so long as it could ensure nationwide distribution. [] advised the Commission that Willem is “the biggest single seller for []”. [] stated that it would support the new owner so long as the new owner has nationwide distribution and sales force.
72. []
73. []
74. Overall, the Commission considers that the Divestiture Package is likely to create a viable long term competitor to the merged entity due to:
- its 31% market share of the cigar market;
 - it being the top selling cigar brand by volume in New Zealand; and
 - the strong on-going support by large customers such [].
75. The Commission assesses the risks associated with divestments by analysis of composition risks, asset risks, and purchaser risks. These are discussed in turn below.

Composition Risks

76. These are risks that the configuration of a divestment proposal may be too constrained, or not appropriately configured, to either attract a suitable purchaser or to allow a successful business to be operated in competition with the merged entity.
77. As discussed above, the Commission considers that the brand in the Divestiture Package is a well established brand and a leading market share brand that will be supported by large customers. In particular, the divested brand is well represented by the service station channel and by the Foodstuffs Group.
78. Accordingly, the Willem brand is likely to attract a suitable buyer. Currently, [] have expressed interest in acquiring the divested brands, []
79. The Commission is also satisfied that the Divestiture Package contains all the relevant trademarks, recipes and corporate knowledge necessary for a new owner to manufacture the products.
80. Overall, the Commission is satisfied that there are no significant composition risks based on:
- the 31% market share of the divested brand;
 - the fact that Willem is the top selling cigar brand by volume in New Zealand;

- the strong future support indicated by large retailers; and
- the fact that all relevant intellectual property, recipes and corporate knowledge is included.

Asset Risks

81. Asset risks are risks that the competitive capability of a divestment package will deteriorate prior to completion of the divestment.
82. The Commission considers that the Divestiture Package is unlikely to contain any significant asset risks because:
- the Applicant must divest within [] of the date of the clearance;
 - clause 5.1(a)(i) of the Divestiture Package states that the Applicant will take all reasonable steps to preserve and maintain the business including goodwill, maintenance of supply and standards of manufacturing;
 - clause 5.1(a)(ii) states that the Applicant will maintain the supply of products to existing distributors and retailers in a manner consistent with its current arrangements; – this is likely to ensure consistency of supply;
 - clause 3.1(b)(iv) and clause 10 of the Divestiture Package gives the purchaser the option of acquiring the merged entity’s staff that are necessary for the operation of the divested business; and
 - the apparent ease and ubiquity of toll manufacturing (contract manufacturing independent of the supplier of the brand but using the standard recipe) will ensure that stock and supply is maintained.
83. The Commission notes that BAT sold the Schimmelpennick cigar brand to STG in 2007 and that since then, Schimmelpennick has not lost significant market share. This illustrates that cigar brands can be smoothly transferred between businesses. The Applicant also provided two other examples of acquisitions of cigar brands where the transfer of cigar brands was undertaken efficiently and expeditiously.⁵

Purchaser Risks

84. The Commission analyses two main purchaser risks, namely that:
- a purchaser acceptable to the Commission may not be available; and/or
 - the Applicant has an incentive to sell to a weak competitor, albeit for a low price, rather than to a strong competitor for a high price.

⁵ SM’s acquisition of the brands Hajenius and Oud Kampen from the Burger Group, and SM’s acquisition of the Bogart Group

85. In some cases there may be little or no interest from potential purchasers. This might indicate that the assets are unattractive to potential purchasers which may cast doubt on the effectiveness of the undertaking.
86. A buyer acceptable to the Commission may need to have certain attributes that enable it to be an effective competitor in the relevant market. If a buyer is not acceptable, the Commission may find that the proposed divestment does not remedy the substantial lessening of competition in the market. Examples of attributes that may make a buyer acceptable are:
- it is independent of the merged entity;
 - it possesses or has access to the necessary expertise, experience and resources to be an effective long term competitor in the market; and
 - the acquisition of the divested shares or assets by the proposed buyer does not raise competition concerns.
87. []
[]
[]
[]
88. []
89. []
90. [], the Commission considers that there are no significant purchaser risks.

OVERALL CONCLUSION – THE CIGAR MARKET

91. Having considered the proposed divestment, the Commission considers that the Divestiture Package is likely to remedy the competition concerns in the cigar market by providing sufficient constraint on the combined entity. The Commission has found no significant risks associated with the Divestiture Package.
92. Accordingly, the Commission is satisfied that the proposed acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the cigar market.

DETERMINATION ON NOTICE OF CLEARANCE

93. Pursuant to section 66(3)(a) of the Commerce Act 1986, the Commission determines to give clearance for Scandinavian Tobacco Group A/S to merge its cigar, pipe tobacco and accessories businesses with that of Swedish Match AB subject to the divestment undertaking dated 22 September 2010 provided by Scandinavian Tobacco Group A/S to the Commission pursuant to section 69A of the Commerce Act 1986.

Dated this 22 day of September 2010

Dr Mark Berry
Chair

Appendix One – Divestiture Package

Commerce Act 1986

Divestment Undertaking to the New
Zealand Commerce Commission by
Scandinavian Tobacco Group

22 September 2010

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Parties

Scandinavian Tobacco Group A/S, a Danish privately owned company, on its own behalf and on behalf of its subsidiaries (STG).

The Commerce Commission, a body corporate established by section 8 of the Commerce Act 1986 (Commission).

Background

- A On 23 April 2010, STG and Swedish Match (SM) entered into an agreement to create a company to be held and controlled by STG. STG will hold 51% of the shares in the company and the remaining 49% of the shares will be held by SM (Proposed Merger).
- B On 22 June 2010, STG gave notice to the Commission pursuant to section 66(1) of the Commerce Act 1986 (Act) seeking clearance for the proposed global merger of STG and SM (Clearance Application).
- C STG offers the Commission the divestment undertaking in the form of this Deed, pursuant to section 69A of the Act.

BY THIS DEED STG undertakes to the Commission as follows:

1 Defined terms and interpretation

1.1 Definitions in the Dictionary

A term or expression starting with a capital letter which is defined in the Dictionary in Schedule 1 has the meaning given to it in the Dictionary.

1.2 Interpretation

The Interpretation clause in Schedule 1 sets out rules of interpretation for this Deed.

2 Commencement and termination of Deed

2.1 Commencement

This Deed comes into effect when it is executed by STG.

2.2 Termination

- (a) Subject to clause (b), this Deed terminates on the Divestiture Date, unless the transfer, grant, or provision of license, agreements, Transitional Services or the fulfilment of any other obligations continue after the Divestiture Date, as the case may be, in accordance with this Deed, in which case the Deed only terminates once any such license, agreement, Transitional Services or other obligations are transferred, granted, provided or fulfilled.
 - (b) Notwithstanding clause 2.2(a), this Deed terminates on the date the Commission consents in writing to the withdrawal of the undertakings given by this Deed in accordance with the Act.
-

3 Sale of Divestiture Business

3.1 Divestiture

- (a) STG must, within the Divestiture Period and in accordance with this Deed, divest, or cause the divestiture of, the Divestiture Business to the Approved Purchaser.
- (b) STG must divest the Divestiture Business on terms which include:
 - (i) the sale, assignment, transfer or perpetual licence to the Approved Purchaser of all trademarks relating to the products that form part of the Divestiture Business;
 - (ii) interim arrangements for the supply or toll manufacturing of the products that form part of the Divestiture Business which are described further in clause 3.2(a);
 - (iii) at the option of the Approved Purchaser, the provision by STG of Transitional Services and/or Technical Assistance that the Approved Purchaser requires subject to the services and Technical Assistance being:
 - (A) provided on a transitional basis;
 - (B) provided on arm's length terms; and
 - (C) notified to the NZCC; and
 - (iv) at the option of the Approved Purchaser, the transfer to the Approved Purchase of employees employed in New Zealand in the operation of the Divestiture Business at the time of the sale (**Transferred Personnel**) who are, in each case, necessary for the operation of the Divestiture Business and who agree to the transfer, other than the Excluded Employee; and
 - (v) that STG must:
 - (A) not directly or indirectly discourage any Transferred Personnel from continuing or seeking employment with, or providing services to, the Approved Purchaser; and
 - (B) release those Transferred Personnel from their employment or service contracts,in accordance with clause 10.
- (c) STG must assist the Approved Purchaser to apply for all licences, permits and/or other regulatory approvals that are required for the operation of the business in New Zealand.
- (d) STG must:
 - (i) obtain any Third Party Consents as soon as practicable after entering into a Sale and Purchase Agreement with the Approved Purchaser;
 - (ii) comply with all requirements necessary to obtain any Third Party Consents including providing necessary information promptly to the third party;

- (iii) promptly pay the costs and expenses of any third party reasonably incurred in providing the Third Party Consents; and
 - (iv) act in good faith in its negotiations to obtain any Third Party Consents.
- (e) If, before the Divestiture Date:
- (i) the Approved Purchaser fails to obtain or is unable to obtain a licence, permit or other regulatory approval referred to in clause 3.1(c); or
 - (ii) STG fails to obtain or is unable to obtain any Third Party Consents,

then STG must provide the Commission, at least seven Business Days prior to the Divestiture Date, with details of those licences, permits, approvals or Third Party Consents (including reasons why approval, consent or transfer could not be given prior to that date, and what is required to obtain the approval, consent or transfer).

3.2 Interim supply and toll arrangements

- (a) In relation to the arrangements in clause 3.1(b)(ii), STG must ensure the reasonable and continuous supply of the products that form part of the Divestiture Business for the term of the arrangements and that the supply or toll manufacturing is:
- (i) for a reasonable period to enable the establishment of the business as a competitive, viable and independent business, which period is to be:
 - (A) nominated by the Approved Purchaser; and
 - (B) approved by the Commission;
 - (ii) provided at a reasonable price;
 - (iii) on such other terms which are no less favourable to the Approved Purchaser than arm's length terms; and
 - (iv) notified to the Commission.
- (b) For the avoidance of doubt, the arrangements in clause 3.1(b)(ii) are able to be renewed by the parties in respect of some or all of the products that form part of the Divestiture Business subject to the requirements of clause 3.2(a) being satisfied.

4 Sale of Divestiture Business to Approved Purchaser

4.1 Sale only to Approved Purchaser

STG must sell the Divestiture Business to an Approved Purchaser.

4.2 Proposed Purchaser Notice

- (a) If STG seeks to have a Proposed Purchaser approved by the Commission, STG must give the Commission written notice (**Proposed Purchaser Notice**), containing:
- (i) the name, address, telephone number and any other available contact details of the Proposed Purchaser;

- (ii) a copy of the proposed Sale and Purchase Agreement;
 - (iii) a description of the business carried on by the Proposed Purchaser including the locations in which the Proposed Purchaser carries on its business;
 - (iv) details of the Proposed Purchaser's experience in the relevant market; and
 - (v) the names of the owner and the directors of the Proposed Purchaser.
- (b) A Proposed Purchaser Notice must be given to the Commission at least 20 Business Days prior to the Divestiture Date.

5 Divestiture Business protection

5.1 Protection of the Divestiture Business

- (a) Until the Divestiture Date, STG will take all reasonable steps within its power and control as are necessary to:
- (i) preserve the reputation and goodwill of the Divestiture Business;
 - (ii) maintain the supply of products that form part of the Divestiture Business to existing distributors and retailers in a manner consistent with the supply of those products as at the date of this Deed; and
 - (iii) maintain the standards of manufacture, distribution, promotion and sale of the products that form part of the Divestiture Business as at the date of this Deed.
- (b) Until the Divestiture Date, STG will not terminate the employment or change the terms of employment of any person involved in the operation of the Divestiture Business.

6 Information

- (a) STG must notify the Commission in writing of:
- (i) the date which STG anticipates will be the Completion Date at least 5 Business Days before that date; and
 - (ii) the date of the Completion Date at least 1 Business Day before the Completion Date.
- (b) STG must notify the Commission in writing of the occurrence of:
- (i) the completion of the Proposed Merger within one Business Day of the Completion Date; and
 - (ii) the divestiture of the Divestiture Business within one Business Day of the Divestiture Date.
- (c) STG must provide the Commission with a copy of the executed Sale and Purchase Agreement, and any other agreements between STG and the Approved Purchaser relating to the sale of the Divestiture Business, within one Business Day of that agreement being executed.

- (d) STG must respond in a timely manner to any queries or requests for information or documents made by the Commission about this Deed.
 - (e) The Commission may request information from STG and STG must respond in a timely manner to any queries or requests for information or documents made by the Commission which specifically relate to the Divestiture Business.
 - (f) Any request made by the Commission under clause 6(e) will be notified in accordance with clause 12.1(b).
 - (g) Nothing in this clause 6 requires the provision of information or documents in respect of which STG has a claim of legal professional privilege.
-

7 Disclosure of Deed

- (a) STG and the Commission agree that:
 - (i) Schedule 2; and
 - (ii) any confidential information disclosed,will remain confidential at all times.
 - (b) STG acknowledges that the Commission may, subject to clause 7(a):
 - (i) make this Deed publicly available;
 - (ii) publish this Deed on its mergers register; and
 - (iii) from time to time publicly refer to this Deed.
 - (c) Nothing in the confidential parts of this Deed prevents the Commission from disclosing such information as is required by law.
 - (d) Nothing in the confidential parts of this Deed prevents the Commission from using the information contained in this Deed for any purpose consistent with its statutory functions and powers.
-

8 Obligation to procure

Where the performance of an obligation under this Deed requires a Related Body Corporate of STG to take or refrain from taking some action, STG will procure that Related Body Corporate to take or refrain from taking that action, as the case may be.

9 No Derogation

- (a) This Deed does not prevent the Commission from taking enforcement action at any time whether during or after the period of this Deed in respect of any breach by STG of any term of the Deed.
 - (b) Nothing in this Deed is intended to restrict the right of the Commission to take action under the Act for penalties or other remedies in the event that STG does not fully implement and/or perform its obligations under this Deed or in any other event where the Commission decides to take action under the Act for penalties or other remedies.
-

10 Release of personnel

- (a) The obligations in clause 10(b) apply if the Divestiture Business or Unsold Business is divested as contemplated by this Undertaking.
- (b) Subject to clause 10(a), STG must release the Transferred Personnel, with effect from the Divestiture Date, from:
 - (i) any obligation to provide services to STG; and
 - (ii) any non-compete or similar restraint of trade obligation, to the extent that such obligation would otherwise prevent the person from performing his or her contemplated role in relation to the Divestiture Business or Unsold Business.
- (c) STG must not procure, promote or encourage the transfer of any of the Transferred Personnel from the Approved Purchaser to STG for a period of 6 months from the Divestiture Date.

11 Costs

STG must pay all of its own costs incurred in relation to this Deed.

12 Notices

12.1 Giving Notices

- (a) Any notice or communication to the Commission pursuant to this Deed must be sent to:

Name: Commerce Commission
Address: 44 The Terrace
PO Box 2351
Wellington 6140
New Zealand
Fax number: (04) 924 3700
Email: registrar@comcom.govt.nz
Attention: The Registrar

- (b) Any notice or communication to STG pursuant to this Deed must be sent to:

Name: Gilbert + Tobin Lawyers
Address: Level 37, 2 Park Street
Sydney, NSW 2000
Fax number: (02) 9263 4111
Attention: Simon Snow, Partner

13 Miscellaneous

13.1 Binding and enforceable

STG confirms that in entering into the obligations recorded in this Deed it intends to create binding and enforceable legal obligations for the benefit of the Commission.

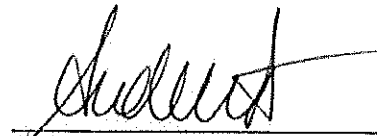
13.2 Governing law

This Deed is governed by New Zealand law and the parties accept the exclusive jurisdiction of the New Zealand Courts.

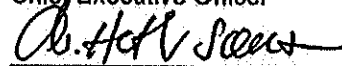
13.3 Counterparts

This Deed may be executed in any number of counterparts each of which is deemed an original, but all of which together are to constitute an instrument. It is acknowledged that this Deed may be executed by an exchange of facsimile copies and executing of this Deed by that means is valid and sufficient execution.

Signed by **Scandinavian Tobacco Group**
A/S by its authorised signatories:



Anders C. Friis,
Chief Executive Officer



Christian Høther Sørensen
Executive Vice President

22 September 2010

Date

Schedule 1: Dictionary

In this Deed:

1 Dictionary

Act means the New Zealand Commerce Act 1986;

Approved Purchaser means a Proposed Purchaser approved by the Commission in accordance with section 4.

Business Day means a day on which banks are open for business excluding Saturdays, Sundays and public holidays in Wellington, New Zealand.

Completion Date means the date on which the Proposed Merger is completed.

Clearance Date means the date on which the Commission grants clearance to STG for the proposed transaction under the Act.

Commission means the Commerce Commission;

Deed is a reference to all the provisions of this document including its schedules.

Divestiture Business means the brands and other assets set in Schedule 3.

Divestiture Business Sale means the transfer of the Divestiture Business to an Approved Purchaser.

Divestiture Date means the date on which STG no longer has ownership or control of the Divestiture Business and on which the Commission confirms in writing to STG that it is satisfied that the divestiture has been completed in accordance with this Deed.

Excluded Employee means the person listed in Schedule 2.

Intellectual Property includes all rights in relation to copyright, trademarks, inventions (including patents, innovation patents and utility models), confidential information, trade secrets, technical data, information, know-how, formulae, specifications, drawings, data, manuals and instructions which are owned by STG and used for the operation of the Divestiture Business and are necessary for the viability, marketability and competitiveness of the Divestiture Business.

Proposed Purchaser means a person who proposes to acquire the Divestiture Business.

Proposed Purchaser Notice is defined in clause 4.2.

Related Body Corporate has the meaning given to the term "related company" in section 2(3) of the Companies Act 1993 (NZ), provided that to be a "company" for that purpose it shall not be necessary for a body corporate to be a company registered in New Zealand.

Sale and Purchase Agreement means an agreement or agreements in respect of the sale and purchase of the Divestiture Business.

Third Party Consents means any consents (including by any governmental agency or authority) required for the assignment, novation, sale, sub-licensing or transfer of any assets, licences, contracts (including those agreements, licences or sub-licences, as the case may be), permits or approvals:

- (a) used by or in, the Divestiture Business at the date of this Deed;
- (b) which will be subject in each case to STG obtaining the relevant written consent of the third party to the continuation of the use, after the sale of such business in accordance with this Deed, of such asset, licence, contract, permit or approval by the Divestiture Business; and
- (c) without which STG would not be able to effect the divestiture of the Divestiture Business in accordance with this Deed,

on no less favourable terms than enjoyed by the Divestiture Business at the date of this Deed.

Technical Assistance includes advising on technical knowledge documentation, supporting the Approved Purchaser in acquiring specific equipment, providing staff with suitable experience and skills to assist and/or advice on technical issues, assisting in training for the Approved Purchaser's staff, and providing guidance on regulatory and legal aspects relating to the application for licences.

Transferred Personnel has the meaning given in clause 3.1(b)(iv).

Transitional Services means such services as the Approved Purchaser reasonably requires pursuant to clause 3.1(b)(iii) for operation of the Divestiture Business in the period immediately after completion of the sale, which may include:

- (a) contract manufacturing, warehousing and shipment services relating to Divestiture Business products;
- (b) management of any relevant intellectual property (such as attending to renewals of trade marks); and
- (c) account management (such as invoicing) and debtor management (such as receipt of payment) for Divestiture Business products supplied to a local distributor.

Unsold Business has the meaning given in Schedule 2.

2 Interpretation

In the interpretation of this Deed, the following provisions apply unless the context otherwise requires:

- (a) a reference to 'this Deed' includes all of the provisions of this document including its schedules;
- (b) headings are inserted for convenience only and do not affect the interpretation of this Deed;
- (c) if the day on which any act, matter or thing is to be done under this Deed is not a Business Day, the act, matter or thing must be done on the next Business Day;
- (d) a reference in this Deed to any law, legislation or legislative provision includes any statutory modification, amendment or re-enactment, and any subordinate legislation or regulations issued under that legislation or legislative provision;
- (e) a reference in this Deed to any company includes its Related Bodies Corporate;
- (f) a reference in this Deed to any agreement or document is to that agreement or document as amended, novated, supplemented or replaced;

- (g) a reference to a clause, part, schedule or attachment is a reference to a clause, part, schedule or attachment of or to this Deed;
- (h) an expression importing a natural person includes any company, trust, partnership, joint venture, association, body corporate or governmental agency;
- (i) where a word or phrase is given a defined meaning, another part of speech or other grammatical form in respect of that word or phrase has a corresponding meaning;
- (j) a word which denotes the singular also denotes the plural, a word which denotes the plural also denotes the singular, and a reference to any gender also denotes the other genders;
- (k) a reference to the words 'such as', 'including', 'particularly' and similar expressions is to be construed without limitation;
- (l) a construction that would promote the purpose - or object - underlying the Deed (whether expressly stated or not) will be preferred to a construction that would not promote that purpose or object;
- (m) material not forming part of this Deed may be considered to:
 - (i) confirm the meaning of a clause is the ordinary meaning conveyed by the text of the clause, taking into account its context in the Deed and the competition concerns intended to be addressed by the Deed and the clause in question; or
 - (ii) determine the meaning of the clause when the ordinary meaning conveyed by the text of the clause, taking into account its context in the Deed and the purpose or object underlying the Deed, leads to a result that does not promote the purpose or object underlying the Deed;
- (n) the operation of this Deed is subject to the Act, and for the avoidance of doubt the Commission may accept a variation of the Deed in accordance with the Act on receipt of an application by STG;
- (o) in performing its obligations under this Deed, STG will do everything reasonably within its power to ensure that its performance of those obligations is done in a manner which is consistent with promoting the purpose and object of this Deed;
- (p) a reference to:
 - (i) a thing (including, but not limited to, a chose in action or other right) includes a part of that thing;
 - (ii) a party includes its successors and permitted assigns; and
 - (iii) a monetary amount is in New Zealand dollars.



Schedule 2: Confidential

Schedule 3: Divestiture Business

The Divestiture Business consists of:

- 1 The assignment to the Approved Purchaser of the following trade mark registrations in New Zealand, subject to a licence-back to STG for a reasonable period (not to exceed 18 months from the Divestiture Date) to enable STG to remove the Willem II mark from packaging for its Amanda and Moments branded products within 6 months from the Divestiture Date and to sell off its stocks of those products in an orderly fashion:

Trademark	Country	Registration number	Owner
Willem II (word)	New Zealand	208309	Willem II Sigarenfabrieken BV.
Wee Willem (word)	New Zealand	797128	Willem II Sigarenfabrieken BV.

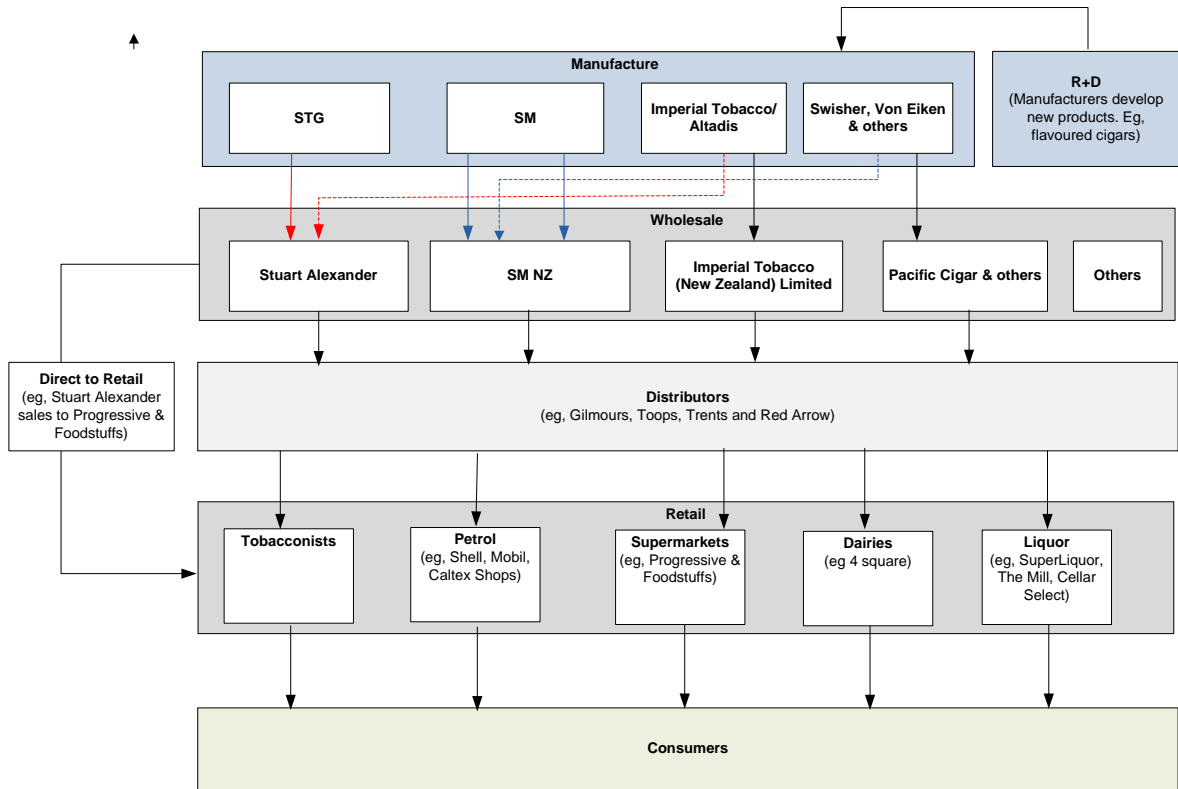
- 2 The assignment to the Approved Purchaser of all New Zealand copyright held by STG in relation to packaging, sales and marketing material relating to the products that form part of the Divestiture Business, as described in paragraph 4 below, subject to a licence-back to STG for a reasonable period (not to exceed 18 months from the Divestiture Date) to enable STG to remove the Willem II mark from any packaging and sales and marketing material relating to the Amanda and Moments branded products within 6 months from the Divestiture Date and to sell off its stocks of those products in an orderly fashion.
- 3 A perpetual licence of any other Intellectual Property rights held by STG necessary to give the Approved Purchaser a right to non-exclusively manufacture the products that form part of the Divestiture Business as set out in paragraph 4 below anywhere in the world and to exclusively market and sell these products in New Zealand. These Intellectual Property rights include existing product recipes, manufacturing know-how and secret processes and related copyright.
- 4 The products that form part of the Divestiture Business are:

Divestiture Brand	Variant
Willem II	Corona Optimum 5s
	DF Half Corona 25s
	Gold 5s
	Half Corona 5s
	Long Panatella 5s
	Short Panatella 5s
	Single 20s BLUE
	Single 20s Regular
	Slim Corona 5s
Wee Willem	Wee Willem Aromatic 10s
	Wee Willem Aroma Filter 10s
	Wee Willem Blue 10s
	Wee Willem Gold 10s
	Wee Willem 10s

- 5 Stock of finished products which form part of the Divestiture Business which have been packaged for sale in New Zealand.

- 6 Stock of packaging for products which form part of the Divestiture Business.
- 7 All books, records and other documents, including customer data, exclusively relating to or necessary for the operation of the Divestiture Business, provided that STG may redact from such copies any information that does not relate to the Divestiture Business.

Appendix 2 – Industry Structure



Source: STG application for clearance 21 June 2010, Public submission in support of application for formal merger clearance (16 June 2010) at page 5 <http://www.comcom.govt.nz/assets/Uploads/Supporting-Submission-Scandinavian-Tobacco-Group-Swedish-Match-Public.pdf>