Not The Best Solution: The European Commission's July 2014 Proposals to Reform the EU Merger Regulation to Review Minority Shareholding Cases

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A little over a year ago in the CPI Europe Column, we wrote on the state of play of reform efforts to extend the European Union Merger Regulation ("EUMR")[1] to non-controlling minority shareholdings,[2] and the background which had led to those efforts, as well as the treatment of minority shareholdings in the merger control laws of a number of other jurisdictions.

Now, almost four years since the then EU Competition Commissioner Joaquín Almunia first said there was "probably an enforcement gap,"[3] we take stock as the new Competition Commissioner, Margrethe Vestager, settles into office. The reform dossier is hers to pursue, the exercise having progressed as far as the publication of White Paper on 9 July 2014,[4] on which comment closed on 3 October 2014.[5]

To encapsulate the issue briefly, at the present time, under the EUMR, unless the acquisition of a minority shareholding amounts to a "change of control" such that the buyer has the possibility to exercise "decisive influence" over the target, the transaction will not qualify as a "concentration" and will not require review, even if the turnover thresholds are met so that the deal would have an "EU dimension." The long-running saga between Aer Lingus and Ryanair is the poster child of this debate.[6]

The Proposed "Targeted" Transparency System in the July 2014 White Paper

Following three options presented in 2013[7] and the first round of public consultation, in July 2014, the Commission put forward its preferred solution, which it terms a "targeted" transparency system:

- Acquirers of minority shareholdings that qualify as a "**competitively significant link**" would have to submit an "**information notice**" to the Commission in advance of closing the transaction;
- The Commission would then decide whether further investigation of the transaction is appropriate, and Member State competition authorities would have an

[1] Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation).
[2] Alec Burnside and Nandu Machiraju, An Emerging Consensus on Minority Shareholdings?, October 24, 2013.
[3] Speaking on 10 March 2011 at a conference to mark 20 years of the EU Merger Regulation.
[4] European Commission White Paper, *Towards more effective EU merger control*, Brussels, 9 July 2014, COM(2014) 449 final.
[5] The White Paper was accompanied by a further Commission Staff Working Paper, an Impact assessment, and an executive summary of the Impact assessment. At the time of going to press, comments received by DG COMP in response to the second consultation period have not yet been published on the Commission's website.
[6] The UK Competition Commission's August 2013 Report requiring Ryanair to sell down to 5% its nearly 30% stake is a significant discussion of some of the ways in which small stakes can and do cause very real harm to competition – and a demonstration that the 2007 EC prohibition decision had not been effective to ensure undistorted competition. Cadwalader, Wickersham & Taft LLP are advisers to Aer Lingus.
[7] See Commission Staff Working Document, *Towards more effective EU merger control*, Brussels, 25 June 2013, SWD(2013) 239 final.

opportunity to request a referral on the basis of the information notice. If the Commission decided to initiate an investigation, the acquirer would have to then make a full notification, which would lead, following the usual procedure, to a Commission decision; [8]

- In the interests of legal certainty, parties could choose to voluntarily submit a full notification in place of just the information notice;
- The Commission is considering whether there should be a statutory waiting period (e.g. 15 working days) once an information notice has been submitted, during which the parties would not be able to close the transaction and during which the Member States would have to decide whether to request a referral;[9]
- The Commission would still be able to investigate a transaction after the statutory standstill period had expired, whether or not the transaction was closed, within a set period of time following receipt of the information notice. The Commission is suggesting that that period could be 4 to 6 months, which would allow third parties to come forward with complaints, and also means that the Commission should feel less inclined to initiate an investigation on a precautionary basis during the initial standstill period.[10]
- If the Commission were to initiate an investigation of a transaction, which had already been implemented, it would need to have the power to issue interim measures in order to ensure the effectiveness of a decision under Articles 6 and 8 of the EUMR, such powers taking the form of a hold separate order, for example.[11]

What Is A "Competitively Significant Link?"

The definition of this concept is key since it would be the self-assessment test to be applied under the new system to enable parties to decide whether an information notice has to be filed.

The Commission states that "a "competitively significant link" would arise where there is a "*prima facie* competitive relationship between the acquirer's and the target's activities, either because they are active in the same markets or sectors or they are active in vertically related markets. In principle, the system would only be triggered when the minority shareholding and the rights attached to it enable the acquirer to influence materially the commercial policy of the target and therefore its behaviour in the marketplace or grant it access to commercially sensitive information."[12]

It goes on to say that "above a certain level, the shareholding itself might result in a change in the acquirer's financial incentives in a way that the acquirer would adjust its own

[8] July 2014 White Paper at paragraph 49.
[9] July 2014 White Paper at paragraph 50.
[10] July 2014 White Paper at paragraph 51.
[11] July 2014 White Paper at paragraph 52.
[12] July 2014 White Paper at paragraph 46.

behaviour in the market place, irrespective of whether it gains material influence over the target."[13]

The following cumulative criteria would have to be satisfied by a transaction for it to fall within the definition of a "competitively significant link:"

- acquisitions of a minority shareholding in a competitor or vertically related company (i.e. there needs to be a competitive relationship between acquirer and target); and
- the competitive link would be considered significant if the acquired shareholding is (1) around 20% or (2) between 5% and around 20%, but accompanied by additional factors such as rights which give the acquirer a "de-facto" blocking minority, a seat on the board of directors, or access to commercially sensitive information of the target.[14]

A Lighter, Voluntary Alternative System

The authors take the view that the Commission's proposed system of "targeted transparency" is not the optimal solution. They agree that the EUMR should be extended to problematic non-controlling minority shareholdings but not in the way the Commission proposes in the July 2014 White Paper.

Although the Commission purports to want to avoid "any unnecessary and disproportionate administrative burden on companies," in fact there is considerable burden inherent in what is proposed. The self-assessment required to determine whether a filing is required is based on uncertain concepts of competitive impact.

Approximately 20-30 minority shareholding cases per year would, the Commission estimates, meet the criteria of the targeted transparency system as well as the turnover thresholds of the EUMR, roughly 7-10 percent of the merger cases reviewed each year.[15] The authors submit, however, that the proposed system would in all likelihood mean that many more information notices would be filed than are objectively necessary, because parties involved in innocuous transactions would want to err on the side of caution. There is a studied ambiguity, not clarified in public discussions on the proposal, as to whether there would be sanctions for failing to submit an information notice if it later emerged that the Commission viewed the acquisition as one which fell within the definition of "competitively significant link."

Parties who do proceed to the preparation of an information notice will face additional work on top of the initial self-assessment. The Commission states that the information notice "would contain information relating to the parties, their turnover, a description of the transaction, the level of shareholding before and after the transaction, any rights

[13] Ibid.
[14] July 2014 White Paper at paragraph 47.
[15] July 2014 Commission Staff Working Document, paragraph 85.

attached to the minority shareholding and some limited market share information."[16] This is reminiscent in many respects of what is currently required in a Form RS, or indeed a Short Form notification. Practitioners and businesses that have had to submit those documents to DG COMP in the past know that they can be major exercises. It has to be hoped that there would be no "pre-notification phase" for information notices.

Problematic Shareholdings Often Arise in Adversarial Circumstances

One element neglected in the White Paper is that a large number of potentially problematic minority shareholdings have arisen in adversarial circumstances, where the shareholding has been acquired against the wishes of the target company. This provides a simple and ultra-efficient mechanism for them to come to the attention of the Commission: the targeted company can be relied upon to come running. Prominent examples include:

a) *BSkyB/ITV* – a minority stake that was built with apparent intent to frustrate ITV's own strategic initiatives.
b) *Ryanair/Aer Lingus* – a stake that was built as part of a takeover bid but which has been retained after its failure and has served to frustrate the competitor's strategic initiatives.
c) *Xstrata/Lonmin* – a stake that was built as a prelude to a takeover but retained despite the decision not to bid.
d) *LVMH/Hermes*– a stake that was built up secretively at first, as a first step in a possible consolidation move.

Commission Sidesteps Article 101 and 102 Debate

In 2013, a number of stakeholders argued that Articles 101 and 102 TFEU could be used as tools to catch anti-competitive acquisitions of minority shareholdings, so that an amendment to the EUMR was not required. Before the EUMR was introduced, the European Court of Justice found that the acquisition of a (controlling or minority) stake in, for instance, a competitor can, under certain circumstances, be construed as an anti-competitive agreement (*Philip Morris*)[17] or an abuse of a dominant position (*Continental Can*).[18]

The Commission's brief response to this in the 2014 White Paper is that Articles 101 and 102 cannot cover all the problematic cases, and even when they could be applied, they are not the best way of addressing the purchase of minority stakes. Consequently, it concludes that there is still an enforcement gap in the EUMR itself.[19] But leaving aside the adversarial situations looked at above, almost inevitably other minority shareholdings will be established by way of consent. A much fuller discussion of Article 101 is therefore called for than appears in the White Paper. At §40 the White Paper seeks to sidestep the relevance of

[16] July 2014 White Paper at paragraph 49.
[17] Joint Cases 142 and 156/84 *BAT and Reynolds v Commission* [1987] ECR, 4566.
[18] Case 6/72 *Continental Can v Commission* [1973] ECR 215.
[19] July 2014 White Paper at paragraphs 39 to 41.

Article 101 by a brief discussion of stake-building on a stock exchange where there may be no attackable agreement, but it omits any discussion of the (much more obvious) scenario where the stake is acquired by agreement. This is the *Philip Morris* situation in its simplest form. Many have argued that a statement of enforcement policy in relation to Article 101, in the light of the *Philip Morris* case, would be useful. Some insight into the Commission's position is provided in its October 2014 *Competition Policy Brief*, published just *after* the consultation deadline of 3 October 2014:[20]

> *Even where a share purchase agreement exists, these transactions are on the face of it competition-neutral, which makes it in most cases legally difficult to prove an anti-competitive object or effect. Alternatively, one would have to demonstrate that the articles of association or by-laws of a company were anti-competitive. This is far-fetched, as their purpose is to organise the corporate governance of a legal person. Also, it would affect parties to the agreement who have not pursued any anti-competitive objectives, such as the seller of a shareholding or the other shareholders of the target company*.

If this is Commission policy it needs better exposition centrally in the debate, not least the attempt to deny the application of Article 101 to the *effect* of agreements, even absent anti-competitive *object*.

A clear statement of enforcement policy in relation to Article 101 and potentially problematic minority shareholdings would go a long way to ensuring the effectiveness of a voluntary notification regime under an amended EUMR. The authors are not suggesting that consensual minority shareholdings should simply be left under a regime of Article 101 self-assessment. A customized and rapid review process is desirable. Undertakings would then be able to come forward voluntarily for clearance in cases potentially giving rise to a Significant Impediment to Effective Competition (SIEC). If they do not do so, their arrangements would in any event remain subject to Article 101 for the lifetime of their agreement; but all agreements remain, in the nature of modernization and self-assessment, exposed to that requirement.

Marrying a Voluntary EU System with the Compulsory German and Austrian Systems

It is true that a voluntary EU system would pose a challenge in relation to compatibility with existing national systems. It would sit uneasily with the existing compulsory German (and Austrian) system, since it would potentially remove from review a certain number of minority shareholding situations which at present require mandatory notification to those national competition authorities. But a way can probably be found to ensure review of those cases.

The introduction of a voluntary regime for minority shareholdings with a Union dimension could entail removing from national competition authorities' review a certain number of

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[20] European Commission, Competition Policy Brief, *Minority Power – EU Merger Control and the Acquisition of Minority Shareholdings*, Issue 15, October 2014, page 2.

cases presently subject to mandatory notification, particularly in Germany. But the scale of this issue should not be overstated: *Bundeskartellamt* statistics indicate that notifications of minority shareholdings in 2012 in Germany were no more than 13% of notifications received.[21] Of course, consistent with the view that minority shareholdings are a problem meriting attention, these cases cannot simply be abandoned. Indeed, a *Bundeskartellamt* speaker is reported as having said recently that cases of "*wettbewerblich erheblicher Einfluss*"[22] represent only around 1% of notifications but 10% of prohibitions.[23]

The *Bundeskartellamt* wants to be sure that it has the opportunity to examine cases not brought to the European Commission. That can be addressed by a mechanism requiring undertakings to make a notification to the German (or Austrian) authority, if they have not chosen the path of voluntary notification to the European Commission. This could be framed either by reference to the European Commission's exclusive jurisdiction, and as an exception in these limited circumstances; or as an extension of the case referral mechanisms already under discussion in the White Paper.

If viewed as a matter of jurisdiction, it could be expressed in terms that undertakings may elect whether to make notification to the European Commission, or to relevant NCAs. Exclusive jurisdiction would reside with the European Commission or the NCAs depending on the choice made, but always subject to the possibility of case referral. Undertakings would have an obvious incentive to begin with notification to the agency which is best placed,[24] and indeed pre-notification contacts could be used to assist in forming a view. Alternatively, the revised EUMR could be framed so that the European Commission has exclusive jurisdiction, but that where a notification obligation would otherwise exist at national level, the making of that notification is deemed to give rise to a case referral from the European Commission to the national authority. Again, undertakings will in practice have the incentive to make the notification from the outset to the agency, which is best placed, and to verify this in pre-notification where useful.

Conclusion

The road to reform of the EU Merger Regulation as it applies to the acquisition of minority shareholdings has been a long one, and the journey is far from complete. It is to be hoped that the Commission will reconsider the system it put forward in the July 2014 White Paper, in favour of a lighter, voluntary system.

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[21] *Bundeskartellamt* Activity Report 2011/2012, p. 129. These are the most recent figures available from the *Bundeskartellamt*.

[22] The subset of cases where the minority shareholding was below 25%.

[23] Andreas Bardong, quoted in *Minority acquisitions raise same competition concerns as other deals, BKartA finds*, PaRR report of 22 September 2014.

[24] Applying the principles of the Referral Notice.