(SECA) European Commission's merger control reform proposal to include the acquisition of certain non-controlling minority shareholdings: What consequences for investors and private equity firms?

This summer the European Commission released a White Paper presenting several proposals aimed at making EU merger control more effective. The consultation on these proposals is open until October 3rd, 2014. One of the main proposal would be to extend the Commission's merger control competence to allow it to review certain acquisitions of non-controlling minority interests. Currently, the Commission can only review operations resulting in the acquisition of the control over the target company (alongside with mergers and the creation of full-function joint ventures). Under this regime, the acquisition of a minority stake can already be reviewed, but only if it gives the acquiring firm(s) the control over the target (be it because of extended voting rights, special board representation rights or in connection with other contractual provisions). An existing minority shareholding of a participating firm in a third company can also be reviewed by the Commission when assessing the impact on competition of a concentration (which quite frequently leads to divestiture requirements).

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The acquisition of a minority interest that does not give the acquirer(s) control, i.e. the possibility to exercise a determinant influence, over the target, however, cannot be reviewed by the Commission (unlike in the U.K., Germany, Austria, Canada, Japan and the U.S.). The Commission might still intervene if the operation also qualifies as a restrictive agreement under Article 101 TFUE (especially in very concentrated markets with high barriers to entry) or as an abuse of a dominant position under Article 102 TFUE, but this is most of the time not the case (especially for staggered acquisitions on the stock exchange for example). Consequently, the Commission considers that there is a gap in EU competition law that needs to be filled, as the acquisition of minority interests, first and foremost in competitors, can sometime seriously harm competition.

The potential harm to competition feared by the Commission includes the higher risk of collusion between firms that may not be competing that much anymore, but also unilateral effects, such as the possibility for a firm to raise its prices above competitive level while recapturing resulting losses through its participation in a competitor. Or the possibility to use exclusive shareholders' information and influence to stifle competition by the target. The poster child for this latter risk is the Ryanair / Aer Lingus case: Ryanair had progressively acquired a 29.4% participation in his rival Aer Lingus. The Commission twice blocked Ryanair's attempts to take full control of Aer Lingus, but was not competent to review alleged anticompetitive effects of the minority shareholding. It is finally the U.K. authorities who jumped in and ordered the divestiture of the participation down to 5%. Finally, the risk of foreclosure of competitors is also cited in the case of "vertical" participations, i.e. in suppliers or customers.

The Commission's proposal would introduce a "targeted transparency system" for the review of the acquisition of minority interests. Under such system the acquiring firm would not have to file a full notification, but would be required to submit an information notice informing the Commission about certain types of transactions. Based on this notice, the Commission would then decide whether a transaction warrants an investigation and should be properly notified or not. The transactions concerned would be those presumptively creating a “competitively significant link”, meaning acquisitions of minority shareholdings in a competitor or a vertically related company. Moreover, acquisitions leading to a post-transaction shareholding of less than 5% would not be concerned, while those leading to a post-transaction shareholding of 5% to 20% would be concerned only if certain rights attach to the shareholding, such as rights giving the acquirer a de facto blocking minority, the right to nominate a member of the board, exert influence, or obtain access to the target’s competitively sensitive information.

At first sight, private equity firms and other investors should not be as affected by the proposed amendment of the EU merger regulation as this was feared a year ago when the Commission launched its first consultation on the subject. Indeed, the limitation of this extension of the merger control regime to shareholdings in competitors or vertically related companies should shield them from additional burdensome filing requirements in most cases. In this sense, it takes into accounts some of the concerns raised by the European Private Equity and Venture Capital Association during the first consultation in 2013. However, the day-to-day application of such new regulation could well prove to be tricky in certain circumstances. This is because the notion of “competitor” will not always be as easy to define as it may seem, as markets are often hard to delimit precisely. And what if the investor owns interests (majority or minority) in a third company that is a competitor of the target? Will this investor then be considered as a “competitor” within the meaning of the proposed regulation? This seems to be the intention of the Commission, as one of the footnote (!) in its Staff Working Document states that “this approach would also capture an acquisition of a minority shareholding by one company which itself does not compete with the target, but already holds a minority stake (or more) in one or more other firm(s) competing with the target. In light of the facts that there will be a true “safe harbor” only for participations below 5%, respectively 20% if there are no special rights attached – which is extremely low – and that the required “information” might well be quite burdensome in some cases (without definitively shielding the acquirer from the necessity to file a full notification later), there will certainly be a number of cases where investors will face some consequent delays and additional costs (not to mention confidentiality issues) that could well have a negative impact on their activities.

As far as the situation is Switzerland is concerned, an extension of the merger control competence of the Competition Commission (Comco) would also require the amendment of the Cartel Act. Indeed, article 4 III clearly only includes in the notion of “concentration” the acquisition of the control of an undertaking. This excludes non-controlling minority shareholdings. To the author’s knowledge, such amendment is not on the agenda. As it is the case in the EU, the acquisition of non-controlling minority shareholdings may however be analyzed as agreements restraining competition under article 5 of the Cartel Act (which the Comco did in the *JC Decaux/Affichage* case, see DPC 2001/2 p. 306), or as an abuse of a dominant position under article 7 of the Cartel Act (which the Comco did in the *Minderheitsbeteiligungen der Publigroupe SA an Zeitungsverlagen* case , see DPC 2006/3 p. 449, and in the *CS/Bank Linth* case, see DPC 2003/3 p. 514).

It remains to be seen how the Commission will take into accounts the comments that the industry and other interested stakeholders will formulate during the consultation. In any case, Swiss private equity firms and investors will have to keep on monitoring closely the adoption and implementation of the new European rules, as well as their concrete application by the EU Commission and EU Courts, bearing in mind that Switzerland often ends up following the developments on the European stage. Particularly in cases where the investor may possibly be considered as a competitor of the target due to special circumstances, extra caution will be necessary to assure a full compliance with merger regulations.