Response to the European Commission’s consultation on the White Paper and Staff Working Document on “Towards More Effective EU Merger Control”

Submission by Cisco, Qualcomm and Samsung Electronics
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Cisco, Qualcomm and Samsung Electronics welcome the opportunity to comment on the European Commission's consultation on the White Paper and Staff Working Document on “Towards more effective EU Merger Control”. This letter seeks to focus on a few critical points in relation to minority shareholdings.

Cisco, Qualcomm and Samsung Electronics are innovative companies that regularly notify transactions or provide information in merger reviews undertaken by competition agencies around the world. Our companies also have, as part of our respective business strategies, significant corporate venture capital activities in Europe with allocated funds or active portfolios running to the hundreds of millions of Euros. We regularly seek out and invest in promising disruptive technology start-ups or small and medium size enterprises, which entail the acquisitions of minority shareholdings.

The European start-up and SME community is an important source of innovation and job creation in the region. Given the state of traditional access to finance in Europe, Europe needs to attract capital investment. This is particularly true for its technology SMEs, given that the funding gap causes European companies in need of early stage or expansion funding to be at a competitive disadvantage. And very often, corporate venture capital is a key way for smaller companies not only to receive capital injections but also seek support to grow in a complex ecosystem.

Yet competition for venture capital is fierce and takes place at a global level. Over the years the Commission’s industrial policies has sought to ensure that Europe has a regulatory environment that attracts inflow of corporate investment. It would therefore appear to contradict this important goal if proposed changes requiring the notification of minority shareholder acquisitions caused corporate venture groups to reconsider their European investment strategies and seek less burdensome or risky opportunities elsewhere. Unfortunately, for the reasons stated below, we believe that the proposals actually risk making Europe a less attractive market for venture capital funding given the disproportionate approach taken in the proposals.

The Commission proposal will represent a significant burden on investors in Europe and elsewhere

We are concerned that the Commission proposal to require ex-ante notifications of minority shareholdings will have the effect of disincentivising capital investment, as
the proposal is both “unnecessary” and imposes a “disproportionate administrative burden on companies”.

The Commission proposes to require ex-ante approval of minority acquisitions that trigger the low ownership thresholds contained in the White Paper. This process will be burdensome and costly, requiring substantial resources and time, as well as causing market uncertainty. Companies will be required to prepare and submit a substantive information notice related to the parties, their turnover, a description of the transaction, the level of shareholding before and after the transaction, any rights attached to the minority shareholding and market share information.

While this is a lighter burden than a full Form CO, supplying such information may well be difficult. The target’s information may neither be easily accessible nor be readily available, which will delay filing. After submission parties will have to wait for the 15 working day suspensory period (at least three weeks) before closing the acquisition that will further delay transactions. The Commission would then have between 4 and 6 months to decide whether it wishes to investigate the transaction. This will increase uncertainty, and discourage pro-competitive investments. Corporate venture capital, like most other forms of investment, factors in cost and risk in taking investment decisions. Neither increased cost or increased uncertainty will promote increased investment.

The Commission should also be conscious of the likely effect of its proposal on national competition authorities in Europe and elsewhere. Other antitrust agencies, which may lack the Commission’s expertise and its focus on consumer welfare effects, may follow the Commission lead by scrutinizing minority investments. This will only increase the burden and uncertainty faced by investors and the often small and undercapitalized companies in which they invest.

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1 White Paper at paragraph 42 “A system for controlling acquisitions of non-controlling minority shareholdings should take into account the following three principles: (i) it should capture the potentially anti-competitive acquisitions of non-controlling minority shareholdings; (ii) it should avoid any unnecessary and disproportionate administrative burden on companies, the Commission and NCAs; and (iii) it should fit with the merger control regimes currently in place at both the EU and national level.”
The Commission does not show sufficient evidence to support the adoption of an ex-ante notification mechanism; its proposals are therefore disproportionate

The Commission identifies three theories of harm which purportedly justify the imposition of this ex-ante control mechanism: first, the ability of the acquirer to influence the target’s competitive decisions; second, the acquirer’s financial incentive to compete less aggressively; and third, the acquirer’s access to the competing target’s sensitive information. We will look at each in turn.

(i) The ability of the acquirer to influence the target’s competitive decisions

The Commission appears to be concerned about a degree of “influence” whereby the acquirer will be capable of influencing the target’s prices or ability to compete. The Commission cites four cases (Siemens/ VA Tech; Toshiba/ Westinghouse; IPIC/ MAN Ferrostaal; and Ryanair/ Aer Lingus)

First, the Commission provides little evidence that, prior to the transactions that were notified to the Commission, the minority investment that these companies had undertaken previously had caused any anti-competitive harm. Second, cases that may fall under this theory of harm could have fallen under the Commission’s jurisdiction if they had required notification based on the concept of “decisive influence” under the European Union Merger Regulation (EUMR). To the extent that the Commission considers that this notion should be clarified or revised it should consider revising its Consolidated Jurisdictional Notice, rather than seeking to extend notification requirements more broadly. Third, as we will explain below, the Commission Paper does not explore more proportionate ways of identifying potentially problematic acquisitions of minority interests, such as a voluntary notification system.

(ii) The acquirer’s financial incentive to compete less aggressively since it would partially internalize, via its financial interest in the competing target, the positive effects that its softened competition has on the target

The harm from minority investments the Commission identifies is entirely theoretical. Based on our collective experiences as investors, the likelihood that a company’s sales force would choose to lose sales to a target in which the investor owns a 20 percent interest is remote. If the Commission has real-world, not theoretical, counter-examples, it should identify them.

2 Staff Working Document at paragraphs 51-54.
(iii) The acquirer’s access to the competing target’s sensitive information would facilitate coordination in the market as well as the monitoring of that coordination and the detection of deviations.

The Commission fails to explain in its White Paper why its current powers under Art 101 TFEU are insufficient to deal with unlawful exchanges of confidential information or concerted practices between an investor and the company in which it invests.

The theories of harm raise valid antitrust concerns, but as the Commission itself acknowledges, the economic literature regarding non-controlling shareholdings “is mainly based on theoretical considerations as there is currently only a limited empirical literature on the effects of structural links.” Theories should first be tested against observable facts, as seeking solutions to theories will inevitably lead to unintended consequences.

Before addressing these theoretical concerns by the imposition of a burdensome notification regime, the Commission should first explore (i) whether these theories are borne out by observable fact and (ii) whether its current powers under Article 101, 102 TFEU and the EUMR are not sufficient to deal with such cases. Many of the concerns outlined above constitute some form of collusion, concerted practice or exchange of confidential information. Article 101 TFEU gives the Commission sufficient powers to sanction these conducts. Furthermore, other concerns identified (e.g. influencing a rival to raise prices) that would materialize only if the acquirer enjoys a substantial amount of market power can be dealt with by Art 102 TFEU. To the extent there is a gap, the Commission should consider how best to review any anti-competitive concerns ex post, including through the imposition of fines to sanction past illegal conduct and deter others.

The Commission ex ante control of minority shareholdings is at odds with EU and European national merger control regimes

Our companies recognize that merger control rules requiring ex ante notifications are justified where there is evidence that if unchecked, companies would engage in anti-competitive acquisitions and that the conduct, if found anti-competitive, cannot be brought effectively to an end once it has taken place. However, we believe that these considerations do not apply to acquisitions of minority shareholdings. As mentioned above, the antitrust concerns raised by minority shareholdings are theoretical and research undertaken by the Commission has not yielded statistically significant numbers to warrant intervention. The likelihood of anti-competitive effect occurring in transactions relating to acquisitions of minority shareholdings is reflected in the fact that only 2 countries of the 31 EEA countries have felt the need to impose an obligation to notify such acquisitions. Contrary to the statement in the

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3 Annex 1 to the Commission Staff Working Document at paragraph 23.
Commission's White Paper, then, the Commission's proposal does not "fit with the merger control regimes currently in place at both the EU and national level."5

Rather than following the position taken in the great majority of EEA countries, the Commission is following the view of a small minority that the competitive harm that minority shareholdings can cause is sufficiently certain to justify the imposition of the substantial burden and uncertainty for investors and investment recipients that a notification regime will create. We urge the Commission to reconsider this position.

The proposed system is not targeted

The Commission proposal seeks to limit the impact of its proposals. However, the “targeted transparency system” as developed in the Commission Staff Working Document does not limit the impact of the proposal. As currently drafted, it would require notification for every acquisition of a minority shareholding that has a "competitive significant link". The document describes such a link arising where there is a “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."6

Based on our history of investments we predict that this definition of “competitive significant link” will require the notification of almost every minority investment. Companies almost invariably invest only in businesses active in areas they know well. Those areas are likely to be areas where the investor competes, or where its suppliers or customers compete. This is particularly the case in high tech markets which continuously evolve, connecting previously unconnected markets (e.g. mapping data and cell phones) and where the role of venture capital funding is to help create future ecosystems. The inclusion of vertical relationships is particularly mystifying: as noted previously, the evidence of anti-competitive harm from the acquisition of minority investments in competitors is theoretical, but, at least in theory, it exists. The evidence of anti-competitive harm from acquisitions of minority interests in customers or suppliers is non-existent.

Furthermore, the Commission considers that an investment will be considered “significant” if the acquired shareholding is:

(i) around 20% or
(ii) 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.

5 See footnote 1.
6 White Paper at paragraph 46.
Here too, the Commission’s definition may sweep quite broadly. Minority stakes will very often include some of the additional rights listed above. Some of these rights, such as “access to commercially sensitive information” or the existence of a “de-facto” blocking minority, are not defined clearly, raising the specter that in the future the Commission – or a national authority that chooses to follow the Commission’s lead – will interpret them as a “catch-all”. Furthermore, in light of our experience as investors, we are concerned that the existence of “additional factors” could catch legitimate terms that are part of last minute negotiations (e.g. some terms are renegotiated at closing to reflect the risks identified during the period of due diligence that takes place after the negotiation of the investment agreement). In this situation, parties would then have to start the notification process before the European Commission (and elsewhere) which may significantly delay closing. Finally, these “additional factors” may change during the course of an investment cycle. For example, observer rights may come to include access to commercially sensitive information, shifting coalitions among investors may create de facto blocking minorities that did not exist at the time the investment was first made or a new investor may have corporate governance requirements that involve giving minority shareholders greater visibility.

We are also concerned that the proposed merger review for minority investments misunderstands some of the essential elements of corporate venture capital. For example, it is common practice for an investor to seek a ‘seat at the table’ to monitor his investment. More importantly, companies invested in very often seek active input from the investor to advise them in growing their business. These are typical activities of many investors such as business angels. Where European merger review requirements to chill this, it would make investments in small European companies less efficient (or attractive).

Finally, the Commission states “SMEs and micro-enterprises are not directly affected by the proposals as the Merger Regulation would continue to apply only to transactions where parties meet the turnover thresholds set out in Article 1 [EUMR]”. While certainly a welcome statement, the Commission must further clarify that it considers ‘the parties’ to be only the acquirer’s and the target’s revenues for the purpose of turnover calculation. Given that start-ups are often funded by a group of co-investors (including venture funds, corporate venture units, and the start-up’s founders), consideration of the turnover of other minority shareholders would force companies to notify investments that could not possibly raise any antitrust concern given the target’s minimal turnover. Moreover, such a rule would force co-investors to exchange turnover information to determine whether notification was required. Our experience in evaluating whether investments are notifiable in Germany, for example, confirms that obtaining information from corporate venture arms and venture capitalists regarding revenues from other investments can be difficult, particularly as some of those investments may not be publicly disclosed. Corporate venture arms tend to only be possible where companies have reached a certain size to afford venture activities; in other words their turnover is likely to be large. If the rules are understood to discriminate
against large co-investors, it will affect the vast majority of corporate venture funds.

**The Commission proposal is contrary to its wider efforts on Smart Regulation**

At a time when the “European Council has called for further efforts to reduce the overall regulatory burden at EU and national level”7 the current proposal ignores the principle of proportionality. Imposing a notification burden on companies before fully evaluating less burdensome alternatives is the opposite of Smart Regulation.

There is in fact a better way of addressing any potential antitrust concern. Before creating an ex-ante notification regime for minority shareholdings that does not now exist at EU level, before diverging from the merger control regime that exists in the vast majority of the EEA countries, before imposing a new burden on companies in Europe, before creating market uncertainty that will discourage venture capital and chill pro-competitive investments, and before other less sophisticated enforcement agencies around the world follow the Commission’s lead by adopting similar notification regimes, the Commission should consider starting with a voluntary system. Such a system would be closer to those 29 EEA jurisdictions that do not require ex-ante notification of acquisitions of minority shareholdings. Furthermore, a voluntary system will allow the Commission to gather more evidence to assess whether it has sufficient powers under Article 101, 102 TFEU or the EUMR to review acquisitions of minority shareholdings, which would lead to a more informed decision as to whether it is indeed indispensable to impose the burden of notifying on investors.

**Conclusion**

Given that the risks of harm are theoretical and the evidence of actual harm is scarce, while the negative impact is significant, we submit that it is disproportionate to expand the scope of the EUMR to allow for the ex-ante notification of acquisitions of minority shareholdings.

We encourage the Commission to abandon the proposal to create an ex-ante notification regime. If however the Commission ignores these arguments, it should at least consider the following suggestions to minimize its impact:

- Consider clarifying the notion of “decisive influence” in the Commission jurisdictional notice to include cases where an acquisition of a minority shareholding can determine the company’s strategy;

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- Consider an ex-post voluntary system which will allow the Commission to gather more evidence in relation to minority shareholdings;
- Clarify that in the current proposal only the acquirer’s and the target’s sales will be taken into account for the purpose of turnover calculation. The Commission will therefore not take into account sales by other co-investors;
- The ‘competitively significant link’ should exclude vertical relationships and minority stakes below 20%;
- If the Commission still takes into account “additional factors” to require notification of acquisitions of minority shareholdings between 5-20%, this list of factors should be streamlined to ensure these can be clearly defined, tracked and avoid undermining some of the benefits of venture capital funding. For example, having a full board member is easier to track than understanding whether one gains access to commercially sensitive information;

We thank the Commission for the opportunity to comment on its proposal. We hope that this letter together with the submissions by other stakeholders serve to better evaluate the impact of its proposal and consider a less interventionist approach to avoid imposing a disproportionate burden on businesses in Europe and elsewhere.

Cisco Systems                                Qualcomm                                Samsung Electronics

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