1. Introduction

1. This is the response of CompetitionRx to the White Paper of DG Competition entitled “Towards more effective EU merger control” on minority shareholdings dated 9 July 2014 (the “White Paper”).

2. As expert advisors in the fields of competition law, merger remedies and compliance, we are pleased to contribute our experience of substantive merger control in several jurisdictions including the EU, US, China and South America.

3. Our comments particularly focus on section 3.2.3 and paragraphs 50-52 of the White Paper which presents details of the procedure foreseen to implement the “targeted transparency system”\(^1\) which includes the possibility for the Commission to investigate a transaction, whether or not it has been implemented, for up to 4 to 6 months after the filing of an information notice and potentially to issue interim measures including hold separate orders. Based upon our experience of implementing and monitoring hold separate arrangements, assuming the Commission is minded to pursue its preferred option, we would like to outline some issues that should be considered in designing the legal framework for such a procedure.

4. If the Commission is minded to implement the targeted transparency system in the scenario in which the Commission investigates a transaction up to 4 to 6 months after filing of an information notice, careful consideration should be given to the types of ring-fencing and hold separate measures that are established in order to prevent action being taken that might impede the adoption of a Commission decision. We consider is it important to draw a clear distinction between acquisitions of control and acquisitions of minority shareholdings and that any interim measures should be proportionate in scope to the potential harm identified. Moreover, while we agree with that there should be no requirement to maintain a standstill obligation beyond 15 days, the scope for unwinding any actions and decisions taken during a period of 4-6 months after Closing is a serious issue and may be difficult to resolve.

5. These comments are structured as follows:

- Section 2 describes the procedure foreseen by the White Paper;
- Section 3 considers the circumstances in which interim measures or hold separate orders might be appropriate; and

\(^1\) Option 3 in the Executive Summary of the Impact Assessment and the "preferred option."
Section 4 discusses the elements such measures could include and highlights some potential consequences of the proposal in its current form.

2. Procedure foreseen by the White Paper

6. Pursuant to paragraph 50 of the White Paper, an undertaking would be required to submit an information notice to the Commission if it proposes to acquire a minority shareholding that qualifies as a “competitively significant link.” The Commission will decide whether further investigation of the transaction is warranted and Member States would consider whether to request a referral on the basis of the information notice. The Commission could consider proposing a waiting period 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 have to decide whether to request a referral. The White Paper suggests that such a waiting period could last 15 working days to align the procedure with the deadline under Article 9 for a Member State referral request. Such a system would ensure that a referral to Member States who could handle such cases could take place under their normal procedure, as they might foresee a stand-still obligation and not be equipped to deal with consummated transactions.

7. The Commission would also be free to investigate a transaction, whether or not it has been implemented, within a period of 4 to 6 months, as this would allow the business community to come forward with complaints. Paragraph 52 proposes that in the event that the Commission initiates an investigation of a transaction which was already (fully or partially) implemented, it should have the power to issue interim measures in order to ensure the effectiveness of a decision under Articles 6 and 8 of the Merger Regulation. Such power could take the form of a hold separate order, for example.

3. Are interim measures or hold separate measures necessary?

8. The purpose of issuing interim measures would be to prevent action being taken which might prejudice the outcome of the Commission’s investigation or impede the Commission from adopting a decision under Article 6 or 8 of the Merger Regulation. We consider there are two important distinctions to be made when considering the appropriate hold separate measures. First, it is necessary to distinguish between acquisitions of minority shareholdings where these are fully or partially implemented or not implemented. Clearly where the acquisition is not implemented, a hold separate order will be straightforward to execute: the appropriate order would be to prevent the acquirer from acquiring any interest in the shares of the target company. Where transactions have been partially or fully implemented, some further hold separate measures may be necessary.
9. Second, acquisitions of minority shareholdings should be distinguished from acquisitions of control where full integration of businesses may be likely to occur. In our view, the standard toolkit of hold separate and ring-fencing mechanisms that are foreseen in the Commission’s standard texts for divestment commitments in merger cases, may not be appropriate to apply to acquisitions of minority shareholdings which are subject to a Commission investigation. In our view, in minority shareholding cases, any hold separate mechanism should respect the general principle of proportionality and be tailored to safeguard against the specific types of harmful conduct that may potentially occur.

10. It is worth recalling the main theories of harm of acquisitions of minority shareholdings identified by the White Paper as follows:²

- horizontal unilateral effects due to an increase in the parties’ ability and incentive to unilaterally raise prices or restrict output;
- enabling the acquirer to gain a competitive advantage in the market by increasing its rival’s costs;
- enabling the acquirer to use its position to limit the competitive strategies available to the target firm, thereby weakening it as a competitive force;
- enhancing the availability and incentive of market players to coordinate in order to achieve supra-competitive profits (due to increased transparency and threat of retaliation);
- leading to foreclosure, particularly input foreclosure, given that the acquirer only internalises a part, rather than all, of the loss in the target firm’s profits.

11. It is also necessary in our view to differentiate between silent stakes and minority shareholdings giving rise to material influence. This important difference is highlighted at point 3 of the Commission’s Competition Policy Brief on minority shareholdings.³ Our understanding of the distinction is that in the case of the former, the minority shareholder does not have control over the decisions of the target and therefore no rights to board representation or voting powers. As a result, a silent shareholder cannot influence decisions, will not have access to commercially sensitive information and has merely a financial interest in the target.

12. By contrast, a minority shareholder with rights that confer a material influence will have a right to board representation, may gain access to commercially sensitive information and may influence the commercial strategy of the company, but does not have control over it.

13. In our view, it should be acknowledged that silent stakes are less likely to require the issuance of interim measures. The theories of harm identified in the White Paper would in our view be most

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² Paragraph 4 of the White Paper.
likely to disappear if the silent stake were to be subsequently divested if the Commission were to adopt a decision requiring the stake to be sold as illustrated by the following examples:

- **Example 1:** the theory of a unilateral effects, that a buyer might raise its prices if enough customers that are lost as a result will switch to the target thereby reducing the costs of the buyer associated with the price increase (as it will recover its costs partly through dividends from the target), does not apply if the buyer does not receive the dividends if the acquisition is not completed because the Commission ultimately objects to the acquisition and the stake must be subsequently sold;

- **Example 2:** the theory underpinning the potential concern of coordinated effects due to alignment of financial interests may only be an issue if the silent stake is a long term investment and not if there is a risk that acquisition may ultimately not occur due to concerns raised by the Commission.

14. The UK’s Competition and Markets Authority (“CMA”) has issued detailed guidance on Interim measures[^4] which describe the circumstances in which interim measures may be adopted where a merger has been referred by the OFT. The CMA notes that the acquirer will often wish to negotiate Undertakings to clarify precisely what action it may carry out pending the final determination of the case. The CMA further allows the parties to agree upon the terms of interim Undertakings speedily. However, if appropriate Undertakings cannot be agreed on a timely basis, the CMA may decide to impose an Interim Order. The CMA has a template set of interim Undertakings and associated compliance statements for completed mergers. In appropriate cases the CMA may require regular compliance reporting from the senior management of the acquirer to confirm that the hold separate measures are respected.

15. Our recommendation is that the parties should be able to propose hold separate undertakings to the Commission within a reasonable time and the power to issue interim measures should be available where such measures are not agreed in a timely manner. From the perspective of businesses, it will be important for the Commission to issue clear guidance and standard templates on the types of hold separate measures that will be required so that businesses can know what to expect.

4. **What should the hold separate or interim measures include?**

16. Divestiture commitments offered in merger control proceedings usually include hold-separate obligations on behalf of the acquirer in relation to the divested assets in order to ensure the

complete commercial separation between the acquirer and the divested assets. The standard hold-separate obligations include the appointment of (i) a HSM and (ii) a Monitoring Trustee.

17. **HSM appointment.** The role of a HSM is to manage the divested assets independently and in the best interests of the business with a view to ensuring its continued economic viability, marketability and competitiveness and its independence from the businesses retained. In the case of undertakings or interim measures as a result of the acquisition of a minority shareholding, the role of a HSM is likely to be more limited than managing the entire business of the target, but would be principally concerned with the monitoring of the hold-separate undertaking rather than the independent management of the assets.

18. Based upon the theories of harm identified in the particular case, the separation measures will most likely need to be aimed at restricting information flows between the parties that may disclose commercially sensitive information of the target and require the ring-fencing of information. Decision-making processes may also need to be held separate (e.g. appointment of board members postponed, no exercise of voting rights in respect of board or other decisions affecting commercial strategy). Depending on the facts of the particular case, it may be necessary to establish additional ring-fencing mechanisms, for example, if there are individuals on the acquirer side that require information regarding the target during the Commission’s investigation for example, in order to fulfil financial reporting or fiduciary duties.

19. **Monitoring Trustee Appointment.** Monitoring trustees are routinely appointed in EC merger cases involving remedies to independently monitor the implementation of divestiture commitments. It is unclear under which circumstances monitoring trustee appointments would be required if the Commission decided to open a case concerning minority shareholdings. The CMA will normally consider the appointment of a hold-separate manager (“HSM”) and/or a monitoring trustee depending on where there are, inter alia, risks to the deterioration of the business or the pre-merger senior management of the acquired business is absent and/or strong incentives exist for the current senior management of the acquired business to operate the acquired business on behalf of the acquirer.5

20. The monitoring trustee would be tasked with monitoring that the hold-separate provisions are being upheld. Further, in the event that the minority shareholding carries with it “material influence”6 which could include representation on a board, the monitoring trustee could be appointed to serve as an independent board member and exercise the rights of the minority

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5 Appendix 2, paragraph 14 contains a list of risk factors. However, these should be read with care as the list may be more appropriate to acquisitions of control rather than minority shareholdings.

6 “with 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” - paragraph 46 EC White Paper

“Towards a more effective EU merger control.”
shareholder with the aim of acting in the best interest of the business, which shall be
determined on a stand-alone basis, as an independent financial investor.\(^7\)

21. However, given the low probability of harm occurring in cases of silent stakes we are unsure of
the need for inclusion of a routine requirement for a HSM or monitoring trustee appointment in
such instances.

22. In the scenario in which a transaction has been in place for 4-6 months prior to Commission
intervention, more stringent measures and the appointment of a monitoring trustee may be
more appropriate, than circumstances in which the transaction has recently been
consummated, and very little information has been exchanged and/or no key decisions have
been adopted.

23. **Ring-fencing measures.** Similar to divestiture commitments, in the event that the Commission
imposes hold-separate measures, it might be possible to ring-fence certain individuals on the
acquirer side and create a “clean team” so that information is only exchanged with the
individuals identified in that team who have signed a non-disclosure agreement committing not
to disclose the information to third parties (which includes non-clean team individuals of the
acquirer). The clean team could remain in place for as long as the Commission investigation is
ongoing and they could also help to seek to ensure that the hold-separate measures (non-
exercise of voting rights etc) are being respected. The formation of such a clean team would
mean that information is only exchanged with individuals on a “need to know” basis with a legal
obligation not to disclose and would ensure the effective continued operation of the target
business during the time that the Commission investigates.

24. **Historical information.** Another interesting issue raised by the proposal relates to historical
information. In the period of four to six months, a significant amount of commercially sensitive
information could have been exchanged between the acquirer and target. If interim hold-
separate measures are imposed six months into a completed transaction, it may be difficult or
impossible to reverse the communication of this information and to ensure that the acquirer
does not act on the information received. A similar situation is faced in divestiture commitments
with respect to ring-fencing where the seller of a divested business must not receive any
information related to that asset from the time of the Commission Decision. The commercially-
sensitive information related to that divested business (customers, prices etc.) is held by the
employees that previously operated and came into contact with that divested business. There is
no way of removing this historical knowledge, therefore employees are required to sign Non-
Disclosure Agreements committing not to disclose confidential information to third parties. The

\(^7\)The formulation at paragraph 12 of the Commission’s Standard Divestiture Commitments Template for cases in which a
company or a share in a company is to be divested and a strict separation of the corporate structure is necessary.
conclusion of non-disclosure agreements by employees having had access to information may be an appropriate remedial measure to ensure that commercially sensitive information is not used to the detriment of the target business.

25. **Absence of a standstill obligation.** An interesting issue raised by the proposal is the difficulty of reversing commercial decisions that may have been adopted during a period of up to 4-6 months between the Closing of a transaction and the Commission decision to investigate.

26. This may be a particular concern for example, in the case of a minority shareholder with rights that confer a material influence, those which allow a right to board representation, or to gain access to commercially sensitive information and may facilitate the horizontal and vertical theories of harm described by the White Paper to occur.

27. From the period in which interim measures are imposed and there is a hold-separate obligation in place, it is clear that a shareholder with material influence should have its corporate rights suspended while the Commission investigates the acquisition of the minority shareholding. This shareholder will not be able to engage in influencing key decisions relating to such matters as commercial strategy, M&A activity, investments, and the exchange of commercially sensitive information with the minority shareholder will be prohibited. What is not so clear is the effect on key business decisions which were taken (with the presence of the minority shareholder) in the time from the acquisition of the shareholding to the imposition of interim hold separate measures. Should these commercial decisions be allowed to stand given that hold-separate undertakings have been issued? The argument against the enforceability of such previous commercial decisions may be strengthened in the event that the Commission investigation identifies competition concerns and remedies are required in order for the transaction to be approved. The identification of a detrimental effect on competition may therefore imply a requirement to un-do (as far as possible) decision sand therefore any competitive harm that may have been caused by that decision. The extent to which a company is actually able to reverse a key commercial decision that has been taken, is an open question, notwithstanding the cost, time and resources required to do this.

28. The harm to competition resulting from the acquisition of a minority shareholding could have been experienced on the market for up to 6 months prior to the Commission intervention and imposition of hold-separate measures. The deterioration in competition during this period of time may be irreversible, regardless of whether or not strategic commercial decisions are capable of being undone.

29. On the contrary, in the event that no competition concerns are identified during the Commission investigation, it could be argued that previous commercial decisions taken should
be allowed to stand given the absence of a detrimental effect on competition. In this scenario, the hold-separate would apply immediately from its imposition and not retroactively.

30. In the written statement of the Bundeskartellamt on the White Paper dated 17 September 2014, the Bundeskartellamt argues in favour of a standstill obligation which would only allow implementation of the transaction once it has received Commission approval. The application of a standstill obligation for 4 to 6 months is arguably disproportionate to the harm that may be caused the small number of cases in which minority shareholdings require investigation. The options appear to be to either not intervene in past decisions or to do so on a selective basis. To the extent that the policy is to attempt to reverse past conduct, the task of unravelling such decisions and their consequences may well involve difficult assessments and be of limited effectiveness.

31. In conclusion, should the Commission decide to adopt its preferred option, our conclusions with respect to interim measures and hold separate measures are as follows:

- It may be preferable for the parties to be given reasonable time to propose hold separate measures prior to issuance of interim measures.
- The standard tool kit of hold separate and ring-fencing measures may not always be appropriate and the Commission should maintain some flexibility in the measures that are established. Hold separate measures should ideally be proportionate to safeguard against the theory of harm identified.
- The ability to appoint a monitoring trustee and/or a hold separate manager should be available but may not always be appropriate.
- The Commission should prepare guidelines and templates describing the types of hold separate measures it will accept.
- A distinction should be drawn between silent shareholdings and minority shareholdings giving rise to material influence.
- The task of unwinding any actions and decisions is a serious issue which may be best dealt with on a case by case basis.

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17 October 2014

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