Antitrust Concerns From Partial Ownership Interest Acquisitions: New Developments in the European Union and United States

Samuel R. Miller, Marc E. Raven, & David Went

Sidley Austin LLP
Antitrust Concerns From Partial Ownership Interest Acquisitions: New Developments in the European Union and United States

Samuel R. Miller, Marc E. Raven, & David Went

I. INTRODUCTION

This article will focus on recent developments in the European Union and the United States relating to antitrust issues arising from the acquisition of partial ownership interests in an entity. An important distinction exists in the treatment of partial ownership acquisitions between the European Union and the United States. While the European Commission (the “EC”) does not (currently at least) have competence under its merger control rules to review partial ownership acquisitions that do not confer control on the purchaser, the U.S. authorities (and certain EU Member States) have broader jurisdiction.

II. EU MERGER CONTROL RULES REGARDING MINORITY SHAREHOLDINGS

The question of whether minority shareholdings that do not confer control should be subject to merger control review is once again being debated in Europe. EU Competition Commissioner Joaquín Almunia said earlier this year that there might be an enforcement gap at the EU level, with the EC unable properly to regulate anticompetitive effects arising from minority shareholdings. As a result, Commissioner Almunia has commissioned a study to establish whether a solution is required.

The debate has no doubt been sparked in part by the ongoing and acrimonious saga involving Ryanair’s acquisition of a minority shareholding in rival “no-frills” Irish air carrier Aer Lingus. While the acquisition of the minority shareholding took place in 2007, the European merger control proceedings (including appeals) relating to a proposed hostile takeover concluded only in July 2010. Although the EC was able to prohibit the hostile takeover, it could not take action under the EU Merger Regulation against Ryanair’s minority shareholding since it did not confer control.

After the European proceedings had concluded, the U.K.’s Office of Fair Trading (the “OFT”) initiated its own merger control review of the minority shareholding. That review is currently stayed pending the outcome of further appeals before the English courts. The fact that certain EU Member States (including the United Kingdom) apply a lower standard under their national merger control rules for review of acquisitions of minority shareholdings as compared

---

1 Samuel R. Miller is a partner in Sidley Austin’s San Francisco office, focused in the areas of antitrust, intellectual property, and white-collar criminal matters. Marc E. Raven is a partner in Sidley’s Chicago office whose practice focuses on antitrust analysis of mergers and acquisitions and on premerger notification and investigations under the Hart-Scott-Rodino Act. David Went is a partner in Sidley’s London office, where he focuses on EU and U.K. competition law.

with the EC complicates the situation in Europe and can lead to regulatory uncertainty for parties involved.

**III. THE FOCUS OF RELEVANT EU MERGER CONTROL RULES ON “DECISIVE INFLUENCE”**

The EU Merger Regulation applies to so-called “concentrations.” Concentrations arise where there is a change in control over an undertaking\(^3\) on a lasting basis. A change in control can arise either where two previously independent undertakings merge or where one or more undertakings acquire control over the whole or part of a previously independent undertaking. Control is defined as the possibility of exercising decisive influence on an undertaking and can be acquired through purchase of securities or assets or by rights, contracts, or any other means (either separately or in combination). There is no prescribed minimum level of shareholding above which minority shareholding acquisitions will necessarily be caught by the EU Merger Regulation. It is a question of law and fact in each case.

Sole control is acquired on a legal basis where an undertaking acquires a majority of the voting rights of a company.\(^4\) This typically (though not always) arises where an undertaking acquires more than 50 percent of the shares in a company. However, acquisition of a minority shareholding can also give rise to control on a legal basis depending on the rights attached to the shareholding. For example, preferential shares might enable a minority shareholder to appoint more than half of the members of the supervisory or administrative board of the target company.

Legal control for merger control purposes can also arise where one or more shareholders have the power to veto strategic commercial decisions of the target company (so-called “negative control”). Strategic decisions are those relating to matters such as the budget, business plan, and appointment of senior management. One situation in which joint negative control might arise in the merger context is where two shareholders each own 50 percent of the target company. Equally, a minority shareholder can have sole negative control for merger control purposes where there is a supermajority required for strategic decisions and this means that the shareholder alone can in effect veto such decisions. In *CCIE/GTE*, a 19 percent share of the voting rights was found to give rise to control where the shareholder’s prior written approval was required for all significant decisions and the shareholder had the right to appoint senior management.\(^5\) Conversely, normal minority shareholder protection rights do not typically confer control.

*De facto* control can occur in a number of situations. One common situation is where a minority shareholder has a large shareholding compared with other shareholders such as to give it a majority of the votes at shareholder meetings. For example, in *Arjomari/Wiggins*, a 39 percent shareholding was found to give rise to a controlling interest given that there were 107,000 shareholders in total, with no others owning more than 4 percent.\(^6\) Exceptionally, a minority shareholder might have joint control with other minority shareholders where strong common interests exist between them to the effect that they would not act against each other in exercising their rights.

---

3 An undertaking is a natural or legal entity active in economic activity.


5 Case No IV/M.258.

6 Case No IV/M.25.
While this is the position at the EC level, a number of EU Member States (notably Germany and the United Kingdom) have a lower standard. In the United Kingdom, for example, the relevant test is the ability to exercise material influence. There is a presumption of material influence above a 25 percent shareholding, and the U.K. competition authorities will examine whether material influence arises in shareholdings above 15 percent and, in exceptional cases, even below 15 percent. Accordingly, even where acquisition of a minority shareholding is not notifiable to the EC because it does not confer control, one or more EU Member States might have jurisdiction to review it under their national merger control rules.

IV. RYANAIR/AER LINGUS CASE

Towards the end of 2006, Ryanair launched a hostile public takeover bid for the entirety of Aer Lingus. Before announcing its bid on October 5, 2006, Ryanair had built up a 19.16 percent shareholding in Aer Lingus, which it had increased to 25.17 percent by November 28, 2006. Ryanair’s bid for Aer Lingus was notified to the EC for merger review on October 30, 2006. After an in-depth investigation, the EC prohibited the transaction on June 27, 2007, having found that it would create and/or strengthen a dominant position on 35 routes from, and 15 routes to, Irish airports. The EC’s prohibition decision was upheld on appeal by the General Court on July 6, 2010. Notwithstanding that the EC concluded in its decision that the acquisition of the minority shareholding in Aer Lingus was part of Ryanair’s plan to acquire control of Aer Lingus, and therefore should be viewed as a single concentration with the public bid, the decision did not require Ryanair to divest its 25.17 percent shareholding in Aer Lingus. During August 2007, Ryanair increased its shareholding to 29.3 percent.

Following the EC’s prohibition decision, Aer Lingus lobbied the EC to require Ryanair pursuant to Article 8(4) and/or Article 8(5) of the EU Merger Regulation to divest its minority shareholding. Under the EU Merger Regulation, the EC can issue binding orders to dissolve concentrations (including through divestiture of shares or assets) so as to restore the status quo prevailing prior to the concentration in circumstances where a concentration has already been implemented but is prohibited by the EC. On October 11, 2007, the EC issued a decision rejecting Aer Lingus’ request on the basis that Ryanair had never obtained a controlling interest in Aer Lingus and therefore no concentration had been implemented. The EC noted in its decision that Ryanair’s 25.17 percent shareholding in Aer Lingus did not grant Ryanair de jure or de facto control but Ryanair merely had minority shareholder protection rights.

The decision rejecting Aer Lingus’ request for the EC to order divestiture of the minority shareholding was upheld on appeal by the General Court on July 6, 2007. In its judgment, the General Court pointed out that, while Aer Lingus considered that the shareholding gave Ryanair substantial opportunities to seek to interfere with the management and commercial strategy of Aer Lingus, Aer Lingus accepted that Ryanair had not obtained a controlling interest in Aer Lingus (even when it increased its shareholding to 29.3 percent in August 2007).

After the end of the European process in July 2010, the U.K.’s OFT decided to initiate a merger investigation into the shareholding on October 29, 2010. As mentioned, the OFT has a lower standard for the review of minority shareholdings as compared with the EC. The OFT determined that it had been prevented from reviewing the acquisition of the minority shareholding while the European proceedings were ongoing and, therefore, the normal four

---

7 Case T-411/07 Aer Lingus Group plc v European Commission.
month statutory period by which it must decide whether or not to refer a transaction for in-depth investigation to the U.K.’s Competition Commission had been suspended.

Ryanair challenged this decision before the U.K.’s Competition Appeals Tribunal. On July 28, 2011, the Competition Appeals Tribunal upheld the OFT’s decision, concluding that the OFT’s proceeding with its merger review prior to conclusion of the European proceedings would have risked inconsistent outcomes and a conflict of jurisdiction contrary to EU Member States’ duty of sincere cooperation laid down in Article 4 of the Treaty on the Functioning of the European Union (“TFEU”). Ryanair is now appealing to the English Court of Appeal and the hearing is expected to take place between February and June next year. The OFT’s merger review has been stayed pending the outcome of this appeal. The saga therefore continues.

V. WHAT’S NEXT IN THE EUROPEAN UNION

Sometime next year, we will learn the results of the EC’s study on the economic importance of minority shareholdings and whether it might be appropriate to close the alleged enforcement gap, including through a change in the EU Merger Regulation.

One of Aer Lingus’ complaints before the General Court was that Ryanair could use its shareholding to seek access to confidential Aer Lingus strategic plans and business secrets (although there was no evidence that Ryanair had actually done so). The General Court considered that, had there been an exchange of competitively sensitive information, this would be subject to review under Article 101 TFEU (dealing with restrictive agreements between undertakings) rather than the EU Merger Regulation. The European Court of Justice has equally confirmed that Article 102 TFEU can apply to acquisitions of minority shareholdings where they result in “effective control of the other company or at least in some influence on its commercial policy.”8 The EC applied Article 102 TFEU to Gillette’s acquisition of “some influence” over the Wilkinson Sword wet-razor business.9

While there may be difficulties in applying Articles 101 and 102 TFEU to acquisitions of minority shareholdings, expanding the scope of the EU Merger Regulation would subject a large number of previously immune transactions to review under the EU Merger Regulation and the administrative burden this entails. It may be difficult to justify such an expansion given that most acquisitions of minority shareholdings do not raise competition concern.

VI. PARTIAL ACQUISITIONS UNDER U.S. LAW

In the United States, Section 7 of the Clayton Act, 15 U.S.C. § 18, prohibits acquisitions that “may” substantially lessen competition, and theoretically applies to the acquisition of “any part” of the equity of a company. While the acquisition of a majority or controlling interest in a company clearly suffices, the Supreme Court has held that the acquisition of control is not necessary to violate Section 7.10

As a general matter, cases in which a court has held an acquisition of a minority interest to be in violation of Section 7 have involved acquisitions resulting in holdings of at least 15 percent. Such a partial acquisition may raise competitive concerns if the buyer acquires a minority interest in a competitor or in a competitor of one of the buyer’s subsidiaries. A partial

---

8 Joined Cases 142 and 156/84 British-American Tobacco Co Ltd v Commission.
9 Cases IV/33.440 and IV/33.486.
acquisition may lessen competition by either (a) enabling the acquiring firm to raise prices or decrease output by controlling or influencing the second firm; or (b) altering the incentives of the acquiring firm to compete with the second firm.

The revised Horizontal Merger Guidelines issued jointly in 2010 by the U.S. Department of Justice (“DOJ”) and Federal Trade Commission (“FTC”) also recognize the possibility that the acquiring firm may gain access to the competitively-sensitive information of the target firm, which “can lead to adverse unilateral or coordinated effects.”\(^\text{11}\) An example of a DOJ challenge to a partial acquisition is the 2005 decision in *United States v. Dairy Farmers of America*,\(^\text{12}\) where the court ruled that there were factual issues regarding the ability of the proposed acquirer of a 50 percent interest in one dairy to limit competition in the relevant market (for the provision of milk to school districts) in light of the proposed acquirer’s 50 percent non-voting interest in the only other dairy in the market. The court held that, “even without control or influence, an acquisition may still lessen competition” in violation of the Clayton Act. In so ruling, the court noted the testimony of the DOJ’s expert that the partial ownership interest, coupled with other business dealings between the acquired plant’s respective owners, created “an incredibly strong incentive” for the elimination of competition.

The FTC has taken enforcement action involving partial acquisitions by private equity firms where the partial acquisition was deemed likely to lead to potential anticompetitive activity or improper sharing of competitively sensitive information. In the *Kinder Morgan, Inc.* (“KMI”) case, the FTC challenged the acquisition of a 22.6 percent equity interest in KMI by private equity funds managed by the Carlyle Group (“Carlyle”) and Riverstone Holdings LLC (“Riverstone”).\(^\text{13}\) The FTC challenged the proposed acquisition under Section 7 of the Clayton Act because investment funds controlled by Carlyle and Riverstone would hold interests in both KMI and a major competitor of KMI, Magellan. The FTC asserted that, as a result of the acquisition of the interest in KMI, Carlyle would likely be in a position to reduce competition between KMI and Magellan through its ability to appoint board members at both companies and by exchanging competitively sensitive non-public information between the two competitors.

Importantly, Section 7 does include an exception for stock acquisitions made “solely for investment.” Similarly, the Hart-Scott-Rodino Act (“HSR Act”) includes a related provision exempting from the Act’s premerger notification requirements acquisitions resulting in holdings of 10 percent or less of a company’s outstanding voting securities made “solely for the purpose of investment.”\(^\text{14}\) This exemption, however, is narrowly construed, and the FTC’s Premerger Notification Office applies a rebuttable presumption against its use where the issuer whose stock is being acquired is a competitor of the acquirer. Further, there is no categorical exemption for acquisitions resulting in holdings of more than 10 percent of an issuer’s outstanding voting

---


\(^\text{12}\) *United States v. Dairy Farmers of America*, 426 F.3d 850 (6th Cir. 2005).


securities unless the acquirer is in one of certain specified categories of “institutional investors,” and even then the acquirer cannot hold more than a 15 percent stake.\textsuperscript{15}

\textbf{VII. RECENT EXPANSION OF HSR REPORTING REQUIREMENTS THAT MAY AFFECT INVESTMENT FIRMS}

In August 2011, the FTC made significant changes to the premerger notification and report form used by parties seeking antitrust approval from the FTC and DOJ under the HSR Act to consummate a merger or acquisition. The most significant change involves the introduction of the concept of an “associate” of an “acquiring person” (i.e., of an “ultimate parent entity” of an entity making an acquisition). The term “associate” is defined in Section 801.1(d)(2) of the HSR Rules as follows:

\textit{Associate.} For purposes of Items 6 and 7 of the Form, an associate of an acquiring person shall be an entity that is not an affiliate of such person but: (A) has the right, directly or indirectly, to manage the operations or investment decisions of an acquiring entity (a “managing entity”); or (B) has its operations or investment decisions, directly or indirectly, managed by the acquiring person; or (C) directly or indirectly controls, is controlled by, or is under common control with a managing entity; or (D) directly or indirectly manages, is managed by, or is under common operational or investment management with a managing entity.

According to the FTC, the new definition of “associate” was implemented to provide the antitrust agencies with relevant information regarding entities that are under common investment or operational management with, but are not “controlled” by, an acquiring person.

Though the recent changes have no bearing on whether or not any particular transaction is reportable under the HSR Act, the new “associate” concept can have a notable impact where an acquisition is made by one of the family of investment funds under common management or by a limited partnership (such as a master limited partnership in the energy industry) that is one of multiple limited partnerships managed by the same general partner. The new rules regarding “associates” require these and other similarly situated acquiring persons to check for possible revenue code overlaps involving “associates” and, where such overlaps exist, provide information about them when making HSR filings.

\textsuperscript{15} 16 C.F.R. § 802.64. Neither this exemption nor the one provided by § 802.9 applies to acquisitions of what are classified for HSR Act purposes as “non-corporate interests” (e.g., partnership interests or limited liability company membership interests). On the other hand, an acquisition of non-corporate interests is not reportable under the HSR Act unless it confers “control” of the target, 16 C.F.R. § 801.13(c)(2) which, in the case of an unincorporated entity, is defined as “having the right to 50 percent or more of the profits of the entity, or having the right in the event of dissolution to 50 percent or more of the assets of the entity,” 16 C.F.R., 801.1(b)(1)(ii).