EXTENDING THE SCOPE OF THE EU MERGER REGULATION TO THE ACQUISITION OF NON-CONTROLLING MINORITY SHAREHOLDINGS

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In June 2013, the European Commission launched a three-month public consultation on possible improvements of the EU Merger Regulation (EUMR). Among the issues on which the Commission consulted stakeholders, the most significant one concerns the possibility to amend the Merger Regulation in order to extend its scope to the acquisition of non-controlling minority shareholdings (also called “structural links”).

The following paragraphs summarize the content of the consultation documents on this topic focusing on: possible anti-competitive effects of structural links (section 1); options for interventions against anti-competitive structural links (section 2).

1. HARM TO COMPETITION FROM NON-CONTROLLING MINORITY SHAREHOLDINGS

From the outset, a distinction is made in the consultation paper between: passive minority shareholdings which entitle the minority owner merely to a share of the profits of the target company, and structural links which confer some degree of influence although not “decisive” on the target firm’s decisions.

It is argued that both situations can give rise to competitive concerns. In particular, this assessment rests on the analysis of: i) the impact that structural links may have on the firms’ incentive to compete when the competitor’s strategy is taken as given (horizontal unilateral effects); ii) the role of structural links with respect to coordination among competitors (coordinated effects); iii) the implications of vertical structural links for market access (vertical effects).

i) Unilateral effects

As far as the unilateral effects of structural links are concerned, the consultation documents argue that, under appropriate assumptions concerning the nature of firms’ strategic interaction, financial interests among rival firms may soften competition. Even when minority shareholdings do not confer to their owners any influence on the target firms’ decisions, they may nevertheless decrease firms’ incentive...
to compete aggressively, given that firms benefit financially from the market success of the competitors in which they have invested. More specifically, the acquisition of a minority stake in a competing company increases the acquirer’s incentives to raise prices, since the acquirer internalizes some of the commercial benefits that said conduct will bring to the participated company. On the basis of the same reasoning, the acquirer has less incentives to lower prices, since the same would bear some of the losses inflicted on the competitor. The consultation documents acknowledge that the magnitude of these effects may be small, since minority owners only partly internalize the externalities of their price strategies. However, said effects may become more significant when the acquisition of a minority stake confers the possibility to exert some influence on the target firm’s strategy. In fact, it is argued that, under these circumstances, the acquirer may induce the target firm to compete less aggressively (for example by raising prices) because this would enable said acquirer to benefit from the positive externalities of the competitor’s conduct, without bearing the full cost of it.

ii) Coordinated effects

Turning to the question of whether structural links may facilitate firms’ coordination, the consultation documents consider how minority shareholdings may affect market transparency and retaliation effectiveness. With regard to transparency, it is maintained that even passive minority shareholdings can give access to rivals’ sensitive information. Moreover, it is argued that transparency is likely to be further enhanced when structural links are associated with some degree of involvement in competitors’ corporate governance. Since increased transparency facilitates the achievement of an agreement among undertakings and the detection of deviations, structural links are deemed to facilitate collusion. Moreover, the consultation documents consider other ways in which structural links affect collusive agreements’ sustainability. In particular, it is argued that, under some circumstances, namely in markets with intense competition in the absence of collusion, minority shareholdings weaken companies’ incentives to deviate from collusion. Firms with financial interests in rival companies are aware that if they deviate they will have to bear part of the losses suffered from competitors: that is, losses of customers during the deviation phase as well as costs entailed by the punishment strategies following after the deviation has been detected.

iii) Vertical effects

Finally, as far as vertical structural links are concerned, the consultation documents argue that minority shareholdings, either forward (if an upstream firm owns shares of a downstream firm) or backward (if a downstream firm owns shares in an upstream firm), may give rise to competitive concerns if the target company can discriminate between customers. More specifically, backward partial integration could result in input foreclosure if, after the acquisition, the downstream minority owner is able to induce the upstream target firm to rise input prices to downstream competitors. Analogously, forward partial integration might lead to customer foreclosure if the target company is an important customer and is
induced to acquire its input predominantly from the supplier to which it is linked.

Interestingly, the consultation documents argue that if the minority owner can influence the target company’s decisions, the likelihood of a foreclosure strategy is higher than in a full merger context. In fact, the minority owner benefits from rivals’ foreclosure without bearing all the costs incurred by the target firm to pursue this strategy.

Finally, the consultation documents consider whether minority share acquisitions may entail efficiency benefits. It is acknowledged that vertical structural links may favor the alignment of firms’ incentives along the vertical chain, particularly with regard to prices and the quality of supply in downstream markets, and may reduce information asymmetries. On the other hand, it is affirmed that synergies seem to be limited for horizontal structural links.

2. OPTIONS FOR THE REFORM OF THE EU MERGER REGULATION

Against this background, the Commission argues that structural links have competitive implications which are similar to the ones that arise in the context of mergers. Hence, from a substantive point of view, the potential adverse effects of acquisitions of minority shareholdings could be assessed by applying the “substantial lessening of competition” test which is used to evaluate the impact of full mergers.

In order to empower the Commission to investigate structural links along the above lines and to intervene if necessary, the consultation paper contemplates an “upgrading” of the EUMR. In particular, two basic options are put forward:

a) to extend the current system of merger notification and control to relevant minority shareholdings (notification system); this would imply that companies should ex ante notify the Commission concerning all the acquisitions of relevant minority shareholdings and wait for clearance before implementing them;

b) to circumscribe investigations on minority shareholdings to a selected number of cases, which are to be identified either through self-assessment, or by obliging companies to provide the Commission with a set of basic information in cases of prima facie problematic structural links. Then, the Commission would make discretionary decisions concerning which cases deserve further investigation (selective system).

The consultation paper maintains that the system to be designed must strike an appropriate balance between increased administrative burden - entailed by extending the merger control system - and enhanced effectiveness of the EU merger control regime. To this end, it is important to take into account that, according to empirical analyses, the expected number of problematic cases should be limited.

This factual consideration seems to point towards the selective system rather than the notification system. However, several commentators have noticed that the former may raise issues of legal certainty. It has been argued that under the selective system, firms should perform the self-assessment of potentially problematic structural links, without the necessary precedent which would ensure
legal certainty. The latter would also be prejudiced by the possibility that companies, after implementing a transaction, may be subject to the Commission’s investigation, which is not constrained by any period of limitation.

3. Next steps

Although replies to the Commission’s consultation paper are not yet available, it is not difficult to foresee that further efforts will be needed to tackle the issues above mentioned, possibly through the identification of clear criteria to select problematic cases upfront. Moreover, should the Commission, on the basis of the public consultation, decide to proceed with a legislative proposal in order to extend the scope of the EUMR to the acquisition of minority shareholdings, it remains to be seen whether such proposal may win parliamentary agreement before the European Parliamentary session expires, early next year.

Certainly, the future publication on the Commission’s website concerning the outcome of the public consultation and the imminent Commissioner’s decision whether or not to proceed with a legislative proposal, will provide further elements to appreciate the likelihood and possibly the main features of the much debated extension of the scope of the EU Merger regime to the acquisition of minority shareholdings.