

MINORITY SHAREHOLDING ACQUISITIONS AND THE UK MERGER CONTROL REGIME

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On 5 July 2019, the UK's Competition and Markets Authority (the "**CMA**") announced that it had opened an investigation under the UK merger control regime into the acquisition by Amazon.com NV Investment Holdings LLC ("**Amazon**") of a minority shareholding and certain rights in Roofoods Limited ("**Deliveroo**").

In the context of its investigation, the CMA has imposed a so-called initial enforcement order ("**IEO**") upon Amazon's parent company and Deliveroo,^[1] which prevents action being taken by the parties that may prejudice the outcome of the investigation.

The CMA's announcement follows Deliveroo's own announcement on 17 May 2019 that Amazon would be acquiring shares in the company as a part of a wider funding round of \$575 million (c. £450 million), which also saw existing investors acquiring further shares in Deliveroo.

Against the background of the CMA's intervention, this update considers:

- the CMA's ability to investigate completed acquisitions, and the risks this presents for parties;
- the CMA's use of IEOs in completed acquisitions, and what this means for parties;
- the CMA's approach to the assessment of acquisitions of minority shareholdings; and
- what companies can do to mitigate legal and commercial risks where planned investments in minority shareholdings would be capable of investigation under the UK merger control regime.

The CMA's ability to investigate completed

transactions

Under the UK merger control regime, while parties can notify transactions and obtain clearance from the CMA before completion, there is no legal requirement to do so.

However, if parties do not obtain clearance before completion, the CMA remains able to investigate. In this context, the CMA has a statutory period of four months from the material facts of the completed transaction being publicised (or otherwise being brought to its attention), within which to open a Phase 1 investigation and decide whether to refer the transaction for a Phase 2 investigation.^[2]

Importantly, the CMA is able to exercise a wide ambit of discretion when deciding whether to investigate. For example, the CMA is able to open a Phase 1 investigation where it has **reasonable grounds** for suspecting that two or more "enterprises"^[3] have ceased to be distinct;^[4] the CMA is not required to reach a definitive conclusion that it has jurisdiction to investigate the transaction.^[5]

As a consequence, a completed transaction is potentially "at risk" of investigation during the four month statutory period, with the opening of an investigation giving rise to certain legal and commercial risks for the parties, as outlined below.

Risks arising from IEOs

If the CMA decides to open a Phase 1 investigation into a completed transaction, it will generally impose an IEO.^[6]

As considered further below, the imposition of an IEO may be expected to have a material impact upon the parties' activities, and gives rise to (i) commercial risks, including in relation to the extent to which the acquirer's business and the target business are prevented from integrating while the IEO is in force; and (ii) legal risks, including in relation to ensuring compliance with the IEO.

Risks arising from the duration of the investigation

An investigation under the UK merger control regime is time consuming and resource-intensive, both in the context of the CMA's involvement, as well as the parties' involvement.

The duration of the CMA's investigation may have significant commercial implications for

the parties (particularly where an IEO is imposed), and the investigation is also likely to result in unexpected costs being incurred (including with regard to any merger fee^[7] that becomes payable to the CMA).

By way of example:

- in a Phase 1 investigation, the CMA will typically spend **several weeks** gathering information from the parties (as well as potentially third parties) before confirming the start of a statutory investigation period at Phase 1 of **up to 40 working days** (which may be extended in only limited circumstances);^[8]
- at the conclusion of a Phase 1 investigation, subject to limited exceptions, the CMA is under a statutory duty to refer a completed transaction for a Phase 2 investigation where it believes that it "is or may be the case"^[9] that the completed transaction (i) satisfies the relevant jurisdictional criteria under the UK merger control regime;^[10] and (ii) has resulted, or may be expected to result, in a substantial lessening of competition in any market in the UK (an "**SLC**"); and
- at Phase 2, the CMA then has a period of **up to 24 weeks** from the date of the reference to undertake its investigation (with this time period capable of extension in limited circumstances).

Risks associated with remedial action

At Phase 2, the CMA is required to determine whether on the "balance of probabilities"^[11] the transaction: (i) satisfies the relevant jurisdictional criteria under the UK merger control regime; and (ii) has resulted, or may be expected to result, in an SLC.

Where the CMA answers these questions affirmatively, it must then decide what (if any) remedial action should be taken in the circumstances to remedy, mitigate, or prevent the SLC.^[12]

The possibility of remedial action being required therefore represents a clear risk. For example, depending upon the circumstances of the case, appropriate remedial action could include the CMA ordering that the completed transaction is undone.^[13]

Use of IEOs in completed transactions

Where the CMA opens an investigation into a completed transaction, it will generally impose an IEO.^[14] In addition, the CMA is able to impose IEOs in the context of planned

transactions, but anticipates that it will do so relatively rarely in practice.^[15]

In the context of a completed transaction, an IEO is intended to ensure that the acquired business (i) continues to compete with the acquiring business, and (ii) is maintained as a going concern, during the course of the CMA's investigation.^[16]

Pre-emptive action

As such, an IEO prevents "pre-emptive action" being taken, which might prejudice the outcome of the CMA's investigation, and/or impede appropriate remedial action at a later date. In addition, an IEO can require any pre-emptive action that has already taken place to be unwound.^[17]

While there is no exhaustive list of the types of conduct that would constitute pre-emptive action, the CMA's published guidance provides that, depending upon the nature of the transaction, pre-emptive action could include closing or selling sites; selling or failing to maintain equipment; degrading service levels; failing to retain key employees; integrating IT systems; failing to compete at arm's length for tenders; integrating customer-facing functions; weakening the independence of brands; discontinuing competing products; and/or exchanging confidential commercially sensitive information.^[18]

IEO template and penalties for failures to comply

As a general rule, the CMA will use its standard template when imposing an IEO imposed in relation to completed acquisitions.^[19]

Where an IEO is imposed, the parties able to request the CMA's consent to specific derogations from the IEO (e.g. to enable specific actions or activities to be undertaken), with consents published by the CMA on its website (together with the IEO).

An IEO will remain in force (subject to variation, revocation, or release by the CMA) until the conclusion of the CMA's Phase 1 investigation. Where a transaction is referred for a Phase 2 investigation, the IEO will be replaced with an interim order ("IO"); this will remain in force (subject to variation, revocation, or release by the CMA), until the conclusion of the Phase 2 investigation.

The CMA may require the appointment (at the parties' cost) of a monitoring trustee, and/or a so-called "hold separate manager" to ensure compliance with, and the

appropriate implementation of, an IEO or an IO.^[20]

Significantly, if an addressee fails to comply with an IEO or an IO without reasonable excuse, the CMA may impose a penalty of up to 5% of the group worldwide turnover of the person(s) concerned.^[21]

Thus far, CMA has imposed financial penalties ranging from £100,000 to £200,000 in respect of failures to comply with IOs without reasonable excuse, with these penalties being substantially lower than the statutory maximum.^[22]

However, the CMA's recently updated guidance indicates that the larger penalties may be considered appropriate in future cases:

"[t]o date the penalties imposed have been significantly less than the 5% cap. However, given the importance of [IEOs and IOs] to the functioning of the regime, the CMA will not hesitate to make full use of its fining powers. ***The CMA will therefore impose proportionately larger penalties in future cases should this prove necessary in the interests of deterrence***"^[23] (emphasis added).

Acquisitions of minority shareholdings under the UK merger control regime

As outlined above, the CMA may open an investigation and impose IEOs where it has reasonable grounds for suspecting that two or more enterprises have ceased to be distinct.

This includes circumstances in which the acquirer only purchases a minority shareholding in the target business. This is as, under the UK merger control regime, two or more enterprises cease to be distinct where they are brought under "common ownership or common control",^[24] with three different levels of control being recognised:

- **de jure control:** which generally arises where the acquirer has a shareholding conferring a majority of the voting rights in the target business;^[25]
- **de facto control:** where the acquirer controls the commercial policy of the target business in the marketplace, despite not having a majority of voting rights (e.g. where the acquirer controls more than half of the voting rights that are actually exercised);^[26] and
- **material influence:** where the acquirer is able to influence materially the commercial policy of the target business in the marketplace^[27] (e.g. as a result of a minority

shareholding).

In practice, the CMA will treat de facto control and material influence as de jure control for the purposes of a Phase 1 investigation.^[28]

In assessing material influence, the CMA will consider all of the circumstances of the case, including: (i) the extent of any voting rights conferred by any shareholding held by the acquirer; (ii) the acquirer's ability to influence the board of the target business; and (iii) any other aspects considered relevant by the CMA.

Voting rights conferred by a minority shareholding

While the CMA does not apply a list of exhaustive criteria, in relation to voting rights conferred by a minority shareholding:

- **shareholder voting rights of more than 25%:** as a general rule the CMA is likely to view the acquisition of shareholder voting rights of more than 25% as conferring material influence, given that this level of minority shareholding would typically allow the acquirer to block decisions requiring a special resolution;^[29]
- **shareholder voting rights of 15% to 25%:** the CMA may examine acquisitions of shareholder voting rights of 15% to 25% in order to consider whether these might enable the acquirer to exercise material influence over the commercial policy of the target business (e.g. by reference to the distribution of the remaining voting rights,^[30] patterns of voting at recent shareholder meetings, and/or any special voting or veto rights attaching to the minority shareholding^[31]); and
- **shareholder voting rights of less than 15%:** at levels below 15% of shareholder voting rights, the CMA may exceptionally choose to examine acquisitions, where other factors indicate that material influence may arise.

Board of the target business

With regard to the board of the target business, depending upon the circumstances of the case, board representation alone may be sufficient to confer material influence, or otherwise may be considered amongst other factors when assessing material influence.

When considering the significance of board representation, the CMA is likely to examine aspects including the expertise and experience of the acquirer's board nominee.^[32]

Other relevant aspects

In terms of other relevant aspects, the CMA may consider a range of factors, including:

- the financial dependency of the target business upon the acquirer;^[33]
- the possibility that the parties may become more closely involved in the future;^[34] and
- the extent to which the acquirer's status and expertise more generally may enable it to influence the commercial policy of the target business (e.g. where the target business is reluctant to pursue strategies that would be likely to cause conflict with the acquirer).^[35]

Consequently, parties can anticipate that the CMA will take a holistic approach when considering whether the acquisition of a minority shareholding would give rise to (at least) material influence, and result in "two or more enterprises ceasing to be distinct" for the purposes of the UK merger control regime.

Investment planning: factoring in the UK merger control regime

Where the acquisition of a minority shareholding (which satisfies the jurisdictional criteria under the UK merger control regime) is completed without obtaining clearance, this presents a range of legal and commercial risks for the parties, including that the CMA could ultimately order the acquisition to be undone.

Identifying and understanding risks

To seek to identify and understand the extent of these risks, the parties may choose to undertake an initial assessment of the "risk profile" of the transaction, so as to determine:

- whether the CMA would be likely to be able to establish jurisdiction to conduct a Phase 1 investigation (e.g. having regard to either of the value of turnover test, or the so-called "share of supply test", under section 23 of the Enterprise Act 2002); and
- if so, whether the CMA would be likely to identify any material competition concerns, and how any such concerns could realistically be addressed by the parties while ensuring that the transaction remains commercially viable (e.g. by offering undertakings in lieu of reference for a Phase 2 investigation), together with the implications in terms of timing if an IEO (or an IO) was to be imposed.

Mitigating risks

Where this "risk profile" is acceptable to the parties, they may opt to consider possible strategies in relation to engaging with the CMA in respect of the acquisition.

These may include, for example:

- informing the CMA of the acquisition by way of an informal briefing note setting out why the parties do not intend to notify and obtain clearance from the CMA (e.g. on the basis that the acquisition does not give rise to competition concerns);^[36] or
- engaging with the CMA in advance to seek to obtain derogations from any IEO that may be imposed in respect of the acquisition once completed.

Alternatively, if this "risk profile" raises concerns, the parties may wish to consider:

- whether it would be commercially viable to restructure the acquisition, so as to seek to mitigate the identified risks (including, for example, reducing the shareholding and associated rights to be acquired, and/or introducing CMA clearance as a condition to be satisfied prior to completion); and
- if not, whether the parties are minded to continue with the transaction in view of the risks identified to this stage.

In this regard, forewarned is forearmed, and consideration in advance of the likelihood (and likely outcome) of a CMA investigation is central to ensuring that the contemplated investment has (at least) the opportunity to deliver the envisaged returns.

Footnotes

[1] See, www.gov.uk/cma-cases/amazon-deliveroo-merger-inquiry

[2] See, section 24 of the Enterprise Act 2002. This statutory period may be extended in limited circumstances.

[3] With an "enterprise" being "the activities or part of the activities of a business" (see, section 129(1) Enterprise Act 2002).

[4] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, footnote 97.

[5] It is therefore possible (although relatively unusual) for the CMA to open a Phase 1 investigation into a completed transaction (including imposing an IEO), before deciding that the transaction does not satisfy the relevant jurisdictional criteria. See, for example, ME/50693 Completed acquisition by Headlam Group Plc of Ashmount Flooring Supplies Ltd, CMA decision of 11 February 2019.

- [6] Read, CMA108 Interim measures in merger investigations, 28 June 2019, paragraph 2.26.
- [7] Depending upon the UK turnover of the target business, a merger fee of up to £160,000 may be payable to the CMA following its Phase 1 decision in relation to whether to refer the transaction for a Phase 2 investigation.
- [8] This 40 working day period may be extended in limited circumstances, including where the parties fail to respond to a request for information made by the CMA under section 109 of the Enterprise Act 2002.
- [9] See, section 22 of the Enterprise Act 2002.
- [10] Including, for example, either of the value of turnover test, or the so-called "share of supply test" (see, section 23 of the Enterprise Act 2002).
- [11] See, for example, CC2 OFT1254 Merger Assessment Guidelines, September 2010, paragraph 2.12, and CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 3.7.
- [12] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 3.5.
- [13] See, [for example, Intercontinental Exchange / Trayport merger inquiry](#)
- [14] See, CMA108 Interim measures in merger investigations, 28 June 2019, paragraph 2.26.
- [15] See, CMA108 Interim measures in merger investigations, 28 June 2019, paragraph 2.15.
- [16] See, CMA108 Interim measures in merger investigations, 28 June 2019, paragraph 1.7.
- [17] See, for example, CMA108 Interim measures in merger investigations, 28 June 2019, section 5.
- [18] See, CMA108 Interim measures in merger investigations, 28 June 2019, footnote 1.
- [19] [Standard IEO template](#)
- [20] See, CMA108 Interim measures in merger investigations, 28 June 2019, section 4.
- [21] See, section 94A of the Enterprise Act 2002.
- [22] See, for example, Case ME/6676-17 Notices of penalty pursuant to section 94A of the Enterprise Act 2002 - addressed to Electro Rent Corporation, dated 11 June 2018 and 12 February 2019.
- [23] See, CMA108 Interim measures in merger investigations, 28 June 2019, paragraph 7.6.
- [24] See, section 26 of the Enterprise Act 2002.
- [25] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 4.30.

[26] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 4.28.

[27] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 4.14.

[28] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 4.13.

[29] See, for example, Ryanair / Aer Lingus merger inquiry in relation to which Ryanair's acquisition of a 29.8% stake in Aer Lingus was investigated under the UK merger control regime, with Ryanair subsequently required to sell its stake in Aer Lingus down to 5%.

[30] See, for example, ME/2811/06 Acquisition by British Sky Broadcasting Group plc of a 17.9 per cent stake in ITV plc, OFT decision of 27 April 2007, paragraph 59.

[31] See, for example, ME/1316/03 Completed acquisition by VB Autobatterien GmbH, in which Robert Bosch GmbH has material influence, of Optima Batterien AB and certain assets and companies constituting Johnson Controls Batterien, OFT decision of 26 September 2003, which provides that "Bosch's existing 20 per cent shareholding in VB, and the fact that Bosch has the ability to veto strategic commercial decisions, is in our view sufficient to confer on Bosch the ability to materially influence VB".

[32] See, for example, ME/1459/04 Completed acquisition by First Milk Limited of a 15 per cent stake in Robert Wiseman Dairies Plc, paragraph 5.

[33] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 4.27.

[34] See, for example, ME/1459/04 Completed acquisition by First Milk Limited of a 15 per cent stake in Robert Wiseman Dairies Plc, OFT decision of 7 April 2005, paragraph 6.

[35] See, CMA2 Mergers: Guidance on the CMA's jurisdiction and procedure, January 2014, paragraph 4.22.

[36] See, CMA56 Guidance on the CMA's mergers intelligence function, 5 September 2017, paragraph 11.

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