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Private Equity Funds - Antitrust Liability for their Portfolio Companies Cartel Infringements

1. The Single Economic Unit: notion

European Competition Law cannot go after 27 different corporate laws across the Union to ascertain antitrust liability, as it would trigger the *effet utile* of the Treaty. Thus, it is settled EU case law that parent companies can be held liable for antitrust infringements if it forms "one single economic entity" or "unit" with the subsidiary within the meaning of art.101(1) TFEU, regardless of the concrete way of control and corporate law structure implemented. It means:

- Subsidiary's antitrust infringement can be imputed to the parent company where the former does not decide independently upon its own conduct on the market, but carries out, in all material respects, the instructions given to it by the latter, account being taken in particular of the economic, organizational and legal links between those two legal entities[1].
- If parent companies and their subsidiaries form a "single economic entity" and therefore a single "undertaking" within the meaning of art.101 TFEU, the Commission may address a decision imposing fines to the parent company, without having to establish the personal involvement of the latter in the infringement. Thus, in EU competition law the term "undertaking" (in Italian misleadingly translated in "*imprese*" i.e. "*companies*") must be understood as designating an economic unit for the purposes of the subject-matter of the TFEU, even if in domestic law that economic unit consists of several persons, natural or legal[2].

Antitrust Authorities must ascertain if the parent company actually exercises in the concrete case at stake a decisive influence over the subsidiary by any economic, organizational or legal means. The burden of proof lays therefore upon the Authorities' shoulders but there is no an exhaustive

[1] See ECJ *Akzo Nobel NV v Commission of the European Communities* (C-97/08 P) [2009] E.C.R. I-8237 at [58], [72] and [74]; *General Química SA v European Commission* (C-90/09 P) [2011] 4 C.M.L.R. 13; [2011] 5 C.M.L.R. 1 at [37]; *Alliance One International Inc v European Commission* (C-628/10 P) [2012] 5 C.M.L.R. 14 at [43] and [45]; *EI du Pont de Nemours & Co v European Commission* (C-172/12 P) [2014] 4 C.M.L.R. 7 at [41] and [43], and *Dow Chemical Co v European Commission* (C-179/12 P) [2014] 4 C.M.L.R. 6 at [52]; *European Commission v Siemens AG Österreich* (C-231/11 P) [2014] 5 C.M.L.R. 1 at [46], and *Areva SA v European Commission* (C-247/11 P & C-253/11 P) [2014] 4 C.M.L.R. 31 at [30]; see also already *AEG Telefunken AG v Commission of the European Communities* (107/82) [1983] E.C.R. 3151 at [49f] and General Court, *Sasol v European Commission* (T-541/08) [2014] 5 C.M.L.R. 16 at [31] et seq. with further references.

[2] See cases *Akzo Nobel* [2009] E.C.R. I-8237 at [59], and *Alliance One International* [2012] 5 C.M.L.R. 14 at [44]; see also for instance *Elf Aquitaine v Commission* (C-521/09 P) [2011] E.C.R. I-8947 at [55], ECJ, *Hydrotherm Gerätebau GmbH v Compact del Dott Ing Mario Andreoli & CSAS* (170/83) [1984] E.C.R. 2999 at [11]; *Confederación Española de Empresarios de Estaciones de Servicio v Compañía Española de Petróleos SA* (C-217/05) [2006] E.C.R. I-11987 at [40]; *Akzo Nobel* [2009] E.C.R. I-8237 at [55]; *Knauf Gips KG v European Commission* (C-407/08 P) [2010] 5 C.M.L.R. 12 at [64].

list of requisites to look for to be held responsible of the subsidiary's infringement[3]. Nonetheless, case law may provide some guidance of the most relevant indicia.

- *Very strong presumption of liability for fully-own subsidiary*. The ECJ held that where a parent company fully own a subsidiary there is a presumption of decisive influence on the part of the parent company which has the heavy burden of rebutting that presumption[4].
- *100 % voting rights and notion of "decisive influence".* In the Power Cables case, the EU General Court confirmed that the Commission is entitled to hold a large international private equity investor partially liable for a cartel fine imposed on its former portfolio company. The decision deserves the focus of the next paragraphs.

2. The Power cable case: Commission decision

Between 29 July 2005 and 16 January 2007, a private equity division of one of the largest investment funds held between 84 and 91% of the shares in a power cable company and 100% of the voting rights. On 16 January 2007, a part of the stock in the company became publicly listed through an initial public offering ('IPO'), which reduced the Private equity fund's shareholding, leaving nonetheless the Private equity fund by far the largest shareholder.

Seven years later, the Commission issued a decision where the company and some of its major competitors were found part of a market and customer allocation cartel between February 1999 and January 2009, for which it imposed a fine. The subsidiary received the highest fine. The Private equity fund was held jointly and severally liable for this fine for an amount equivalent to the period of its shareholding in the company. The decision was challenged in Court.

3. The Power cable case: the judgment

In its judgment dated 12 July 2018, the General Court of the European Union dismisses the Private equity fund's appeal in its entirety. With regard to the period preceding the IPO, the private equity fund argues that the Commission could not rely on a mere assumption that the private equity fund exercised decisive influence over the company before the IPO but had to prove it. In this respect, the fund recalled the well-known rebuttable presumption that a shareholder has a decisive influence over its subsidiary only where its shares are (nearly) 100%. The Court however concludes that since the private equity fund did have 100% of the voting rights in the company, its position was equivalent to that of a 100% shareholder.

The Court also finds that the Commission was correct to conclude that the private equity fund exercised decisive influence over the company between the IPO on 16 January 2007 and the end of the cartel on 28 January 2009. The Court bases this finding on the following circumstances:

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[3] See already *AEG* [1983] E.C.R. 3151 at [50] and *Sasol* [2014] 5 C.M.L.R. 16 at [43f.] with reference to General Court *General Technic-Otis Sarl v European Commission* (T-141/07, T-142/07, T-145/07 & T-146/07) [2011] 5 C.M.L.R. 28 at [69].

[4] See *Akzo Nobel* [2009] E.C.R. I-8237 at [61] See for instance ECJ, *L'Air Liquide société anonyme pour l'étude et l'exploitation des procédés Georges Claude v European Commission* (T-185/06) [2013] 4 C.M.L.R. 35 at [65] and [79], and *Edison SpA v European Commission* (T-196/06) [2013] 4 C.M.L.R. 36 at [58] and [87], as well as decision *Koninklijke Grolsch v Commission* (T-234/07) [2011] E.C.R. II-6169 at [77f.], where the European Commission had, in the General Court's findings, infringed its obligation to give a detailed statement of reasons for imputing the infringement to the parent companies.

1. The Private equity fund's representatives on the Company's board of directors enjoyed the broadest possible management powers.
2. The Private equity fund had the right to (indirectly) appoint and dismiss all members of the various boards of the Company.
3. Representatives of the Private equity fund held at least 50% of the positions in these boards.
4. The Private equity fund also played an important role in several of the Company's committees.
5. The Private equity fund received regular updates and monthly reports on the Company's business activities.
6. The Private equity fund had taken several measures to ensure the continuation of its control over the Company after the IPO. Prior to the IPO, the fund appointed the members of the board of directors until 9 April 2009 and changed the Company's by-laws, so that it would remain able to nominate at least five of its six directors even with a smaller shareholding. In addition - after the IPO – the Private equity fund successfully convinced other shareholders not to increase their interests above 10%. Finally, minutes of the Company's board of directors explicitly referred to the Private equity fund's controlling interest.

The Court also confirms the Commission's finding that the Private equity fund behaved like an 'industrial owner', also after the IPO. In particular, the private equity fund attempted to broker business relationships between the Company and other of its portfolio companies[5].

In view of the above, the Court also rejects the Private equity fund's plea that it acted as a purely financial investor in the power cable company.

To sum up, we may assume that where the private equity fund may influence decisively the economic and business strategy of its subsidiary, it will not be considered as a purely financial investor and be held potentially liable of any antitrust infringement[6]. The way for ascertain its influence may vary dramatically and it will be a case-by-case approach.

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[5] This point of law recalls a debate quite new within the antitrust community, about the potential antitrust concern for horizontal and minority cross shareholding held by investment funds in competing undertakings. See *ESSAY - HORIZONTAL SHAREHOLDING*, *Einer Elhauge* , *WHY COMMON OWNERSHIP IS NOT AN ANTITRUST PROBLEM* posted by *Douglas H. Ginsburg* (U.S. Court of Appeals), on Tuesday, December 4, 2018 at Harvard Law School Forum on Corporate Governance and Financial Regulation; *THE CASE FOR DOING NOTHING ABOUT INSTITUTIONAL PRIVATE EQUITY FUNDS' COMMON OWNERSHIP OF SMALL STAKES IN COMPETING FIRMS, Thomas A. Lambert & Michael E. Sykuta*

[6] The Purely financial investor (immune to antitrust liability for subsidiary's behavior) is limited to companies whose sole purpose is to acquire holdings or shares in other undertakings without involving themselves directly or indirectly in the management of those undertakings, the foregoing without prejudice to their rights as shareholders. Such investment companies must be further structured in a way that compliance with these limitations can be supervised by an administrative or judicial authority. Such companies may be able to prove that they exercise the voting rights in the other undertakings only to maintain the full value of those investments and not to determine directly or indirectly the strategic commercial conduct of the controlled undertaking. Noteworthy, this operation falls out also to merger control. In the EU, see Consolidated Jurisdictional Notice under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings, OJ C95, 16.04.2008, p. 1. In the US see Clayton Act Section 7; 18 U.S.C. Section 18. To Sum up, the merger control is tempered by an exemption from the statute for acquisition of such stock or assets "*solely for investment*," which is defined as "*...not using the same by voting or otherwise to bring about or attempting to bring about, the substantial lessening of competition*." (see also Dubrow, Challenging the Economic Incentives Analysis of Competitive Effects in Acquisitions of Passive Minority Equity Interests, 69 ABA Antitrust Law Journal

4. National Case Law: the Netherlands' experience

Private equity firms can be held liable for antitrust infringements by their portfolio companies in several EU jurisdictions, also in the Netherlands where many controlling entities are based. In the Netherlands the CMA follows the Commission's approach consistently. This was confirmed in a judgment dated 26 January 2017 of the Administrative Law Sector of the Rotterdam District Court.

The Court confirmed two earlier decisions by the Dutch Authority for Consumers & Markets dated 20 November 2014 and 11 December 2015. In these decisions, the CMA had imposed a fine of almost € 1.3 million on Private equity private equity fund Bencis for cartel infringements on the market for flour committed by Bencis' former portfolio company Meneba between 2001 and 2007. On the same date, Meneba's earlier indirect minority shareholder CVC received a fine of in total € 900,000 (imposed on two entities) for the same infringement.

Interestingly enough, the CMA's decisions do not suggest that Bencis was or should have been aware of Meneba's illegal conduct. Instead, the CMA merely established that Bencis was in a legal position to influence Meneba's strategic conduct. In its judgment, the court confirms that it is indeed sufficient that Bencis was merely capable of exercising decisive influence on Meneba's conduct for Bencis to be liable for the infringement. Consequently, the CMA does not need to demonstrate that a direct or indirect shareholder did actually use its powers to coerce its subsidiary to engage in illegal conduct.

In this respect, both the CMA and the court put great emphasis on the fact that Bencis:

- was entitled to nominate two members (out of four) in Meneba's supervisory board.
- the chairman had a casting vote in case of a tie.
- The chairman was also a director in the General Partner of the Bencis investment fund that held the shareholding in Meneba.
- Strategic issues such as commercial and pricing policy, general strategy and (contemplated) acquisitions were regularly discussed in the supervisory board. The latter was considered relevant, since one of the infringements committed by the cartel involved the joint purchasing of a redundant production facility with the objective of permanently removing its capacity from the market. It does not, however, follow from the CMA's decisions or the court's judgment that that that particular acquisition had been discussed in Meneba's supervisory board.

Another interesting feature of the case was that Bencis had been fined individually and separately, rather than being held liable for a portion of Meneba's fine. This implies that if Meneba were to pay its entire fine, the obligation for Bencis to pay its own fine in its entirety would still remain to exist and vice versa. Bencis contended that this constituted meant imposing two separate fines for one and the same infringement. The court however observed that Bencis was a controlling shareholder and a separate legal entity which had not been fined in the original cartel decision. In that capacity, Bencis had an own responsibility and liability for the fine and therefore the CMA was entitled to impose a separate fine on Bencis.

113, 115 (2001). The U.S. case law is tolerably clear that if you are not seeking representation on the target board of directors, and are not able or seeking to become able to exert operational influence over the target, then even substantial equity investments may qualify for exemption (See, e.g. Crane Co. v. The Anaconda Co., 411 F.Supp. 1210 (S.D.N.Y. 1975); United States v. Tracinda Investment Corp., 477 F. Supp. 1093 (C.D. Cal. 1979).

Notably, a separate fine on a parent rather than 'merely' holding it liable for its subsidiary's infringement marks a clear departure from the previous case law.

Conclusion

Albeit some Member State such as Germany had long and harsh discussion about parental liabilit[7], it can be considered settled case law in the EU and in most Member States that even Private equity funds may be deemed responsible for subsidiary antitrust infringement, although their acquisition had the sole objective of reselling the subsidiary within a limited number of years.

This is because to accomplish this mission, Private equity funds generally take control of the subsidiary and exercises decisive influence over it. It follows that at the EU level and in several EU jurisdictions, the private equity funds may be held liable for that company's infringement just like any 'normal' parental company, if its rights and involvement go beyond those of a purely financial investor.

It seems therefore highly recommended to undertake serious antitrust audit (even forensic and with mock dawn raid) over the target before the transaction. The main scope is to find out if antitrust violation is on-going, secondly to ascertain if the target enjoys extra profit because of antitrust violation, thirdly, to be fully aware of every possible option, such as leniency program.

Once the transaction is closed, it is highly recommended to undertake and enforce an antitrust compliance program where the subsidiary is under control of the fund.

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[7] Janka, S. *Parent liability and claims for recovery between joint and several debtors according to EU antitrust law,* European Competition Law Review, 2014, 35, 12; and *Parent Company Liability in German and EU Competition Law: Two Worlds Apart?* Journal of European Competition Law & Practice, 2016, Vol. 7, No. 9.