On your mark, get set, go:

How companies might accidently jump the gun in the transactional race

By Dr. Michael Holzhäuser and Ansgar Hoffmann

The Cambridge Dictionary defines the phrase "jump the gun" as follows: "To do something too soon, especially without thinking carefully about it." With its origin in track and field races, gun jumping in competition law refers to a violation of what is known as the standstill obligation – the implementation of a transaction before the required regulatory clearance is obtained.

The wide-ranging variations of possible "gun jumping" conduct and the inhomogeneous decision practices of European authorities create a significant risk for companies' transactional practice.

For M&A transactions subject to a regulatory pre-closing merger review, in most jurisdictions a standstill obligation exists for the transaction parties that also requires them to continue acting as independent parties. An infringement of the standstill obligation constitutes gun jumping in the legal sense, which can have severe consequences.

The EU Merger Regulation (EUMR) contains two provisions on the subject of gun jumping. Article 4 (1) states that all transactions must be notified before they are implemented, which preserves the European Commission's ability to detect transactions. Article 7 (1) states that transactions may not be implemented before they are cleared, which prevents potential harm to competition while the outcome of the Commission's review is still pending. In the event of a violation – whether intentional or the result of negligence – the company concerned faces a fine of up to 10% of its aggregated global turnover. Fundamentally, it is never a good idea to start relevant processes too soon, but if financial interests are at stake, utmost caution should be exercised. However, the EUMR does not define which measures constitute a premature "implementation" of the transaction. →

This leaves parties working to maintain a very difficult balance between preserving the value and independence of the target until closing and planning for the target's integration into the acquirer's activities to ensure a smooth start of the combined business.

In general, parties are conscious of the fact that closing the transaction before clearance can be penalized with a fine.

>> **However, the EUMR does not define which measures constitute a premature "implementation" of the transaction** <<

However, the risks of gun jumping when engaging in pre-clearance integration planning are far less obvious and have to be assessed carefully. The measures concerned can be grouped into three categories.

The first category of measures that are generally prohibited includes: the transfer of shares or assets, the reappointment of management bodies, the organizational merger of business units, relocating employees, and other forms of implementing reporting or organizational structures, among others. Furthermore, the withdrawal of the target from certain business segments in anticipation of the closing of the acquisition, the coordination or adjustment of products, and joint marketing and distribution efforts are not permissible.

By contrast, there is a second category of measures that are generally permissible, such as: entering into an agreement (for example, the signing of an SPA), development of a joint business plan for the future, informing employees about the transaction, joint press releases, and meeting with customers to explain the intended transaction, among others.

In transactional practice, the main risks originate from the third area, which comprises a complex gray area of measures that have to be carefully assessed in each individual case, such as: the conditions for payment of the purchase price, financing of the target (by means of loans, for example) before closing, joint client visits and trade fair appearances. Particular care should be taken when drafting ordinary course of business clauses, material adverse effect clauses and warranties in the SPA.

Antitrust risks can also arise from the exchange of sensitive business information during due diligence and integration planning. The exchange of information without the necessary safeguards, provided it exceeds the limits of legitimate risk assessment and valuation of the target, might constitute a breach of the standstill obligation. Furthermore, provided the parties are competitors, such concerted practice is likely to be subject to a separate claim of infringement of the cartel prohibition of article 101 of the Treaty on the Functioning of the European Union.

Unfortunately, no official guidelines for integration planning and information exchange exist, which makes it difficult for companies to prepare for their businesses to combine. Major uncertainties have also arisen in recent years as a result of the increased enforcement activities of European competition authorities regarding gun jumping. On the other hand, analysis of the recent string of relevant decisions helps provide a better picture of the gun jumping do's and don'ts.

Jumping the gun by means of a de facto change of control

Generally, change of control (CoC) over a target is achieved by obtaining the majority of votes. The EU General Court's (GC) Marine Harvest/Morpol decision of 2017 shows that a CoC can also occur in de facto circumstances, thus constituting a potential gun jumping violation.

On October 26, 2017, the GC dismissed the appeal by Marine Harvest and confirmed the fine of €20 million for infringing the standstill obligation under the EUMR. Marine Harvest, a salmon farmer and processor, acquired its rival Morpol in three stages. In December 2012, Marine Harvest acquired a 48.5% stake in its competitor Morpol, thereby securing de facto control over the company. Marine Harvest gained a solid majority of the votes because the remaining shares were distributed very broadly and the attendance rate at shareholder meetings was persistently low. Subsequently, Marine Harvest acquired a further 38.6% stake in a public takeover bid in March 2013 and increased its total stake to 87.1%. Finally, the acquisition of the remaining shares was completed in November 2013.

However, the Commission was not formally notified of the transaction until August 2013. In July 2014, the Commission held that Marine Harvest had implemented the transaction by taking control in a de facto manner in December 2012, thereby violating both the notification requirement and the standstill →

obligation. The GC confirmed the Commission's view that a de facto CoC already took place in December 2012.

Significantly, the GC held that the exception to the standstill obligation under article 7 (2) of the EUMR was not applicable. This exception states, inter alia, that the standstill obligation shall not apply to a public bid if control is acquired "from various sellers." Marine Harvest claimed the scope of article 7 (2) of the EUMR should be extended, as the first two stages of the transaction in December 2012 and March 2013 should qualify as a "single concentration." The GC, however, did not follow this argumentation. Hence, the exception did not apply, as Marine Harvest acquired de facto sole control over the target as of December 2012. The GC added that if a company is able to exercise decisive influence, that alone is sufficient to count as a de facto assumption of control and thus a breach of the standstill obligation.

The judgment also confirmed the Commission's view that Marine Harvest's breaches of the notification and standstill obligations constituted two separate infringements, justifying two distinct fines in a single decision. This did not violate the *ne bis in idem* principle, as it was issued by the same authority. An appeal against this decision is pending.

In 2018, in the Ernst & Young/KPMG DK case, the Court of Justice of the European Union (CJEU) also dealt with the conditions under which a de facto CoC constitutes gun jumping.

» **In principle, warehousing consists of a complex two-step transaction** «

The CJEU handed down a highly anticipated judgment on the preliminary ruling request brought by the Danish Commercial Court. In the Court's view, the merger between Ernst & Young (EY) and KPMG DK did not constitute a breach of the EUMR's standstill obligation. Gun jumping, in the view of the CJEU, requires a CoC over the target. Ancillary or preparatory transactions that do not represent a direct functional link with the implementation of a concentration do not, in principle, fall under the scope of the standstill obligation.

Shortly after the signing of the merger agreement, KPMG DK announced that it intended to withdraw from the KPMG international network effective as of September 30, 2014, at the latest, acting in accordance with the terms of the SPA. This was considered to be a breach of the Danish standstill obligation by the Danish Competition Office (DCC). In the DCC's view, the termination of the cooperation agreement was, inter alia, transaction-specific, irreversible and likely to have market effects prior to regulatory clearance.

EY filed an appeal against the DCC's decision before the Danish Commercial Court, which, in turn, submitted a request to the CJEU for a preliminary ruling on the approach under the EUMR. The CJEU followed a more pragmatic approach, defining the scope of the standstill obligation in light of the concept of concentration as defined in article 3 of the EUMR.

The CJEU stated that only steps that "in whole or in part, in fact or in law contribute to the change in control of the target undertaking" can be considered as implementing a transaction. The Court did not evaluate the termination of the KMPG cooperation agreement by KMPG DK as an integration step within the scope of article 7 (1) of the EUMR, despite being necessary for the transaction as such and having effects on the market. The termination of the cooperation agreement did not grant EY the possibility of exercising any influence over KPMG DK. Therefore, the termination was not regarded as a breach of the standstill obligation.

Gun jumping in connection with warehousing structures

The most recent decision issued by the Commission dealt with a breach of the standstill obligation in connection with a "warehousing" structure (Canon/Toshiba Medical Systems).

In principle, warehousing consists of a complex two-step transaction. In the first step, the shares of the target are acquired by a third company (an interim buyer). Following clearance, the shares are then transferred by the interim buyer to the final buyer in a second step. The potential gun-jumping risk of warehousing structures results from the premature assumption of the commercial risk of the target, which may be viewed as a CoC.

On June 27, 2019, the Commission issued a fine of €28 million against the Japanese camera manufacturer Canon. The Commission accused Canon of "partial implementation" of the acquisi- →

tion of Toshiba Medical Systems (TMSC) without the required notification and clearance. Canon has already announced it is appealing the decision.

In August 2016, Canon notified the Commission of its intended acquisition of TMSC. The transaction was approved by the Commission in September 2016. Prior to the notification, the interim buyer had already acquired 95% of TMSC's shares for €800 in step one. At the same time, Canon paid €5.25 billion for the remaining 5% and the purchase option for the interim buyer's share package in step two. The Commission held that these steps form one single notifiable transaction, as step one was essential and necessary for Canon to gain control over TMSC. In the Commission's view, step one constituted a "partial implementation" of the transaction. Even though the purchase option did not formally lead to a CoC prior to stage two, the payment of the full purchase price meant that Canon effectively assumed all TMSC's commercial risk. The case was also aggravated by a few other facts, namely that the interim buyer served solely as a transaction vehicle, that Canon had already paid the full purchase price in the first step and that the transaction was cleared unconditionally.

It remains to be seen whether the Commission will take an equally restrictive view cases of less extreme warehousing. For example, the interim buyer may continue to hold the target's shares after clearance is denied, or the final buyer may not assume the target's commercial risk in the first step. In any case, parties should carefully consider at which step the final buyer might assume commercial risk, and they should exercise utmost caution in using transaction vehicles for the sole purpose of warehousing.

Veto rights and access to sensitive information

On April 24, 2018, the Commission issued a fine of €124.5 million against Altice, a multinational cable and telecommunications company headquartered in the Netherlands. Altice allegedly gained control over PT Portugal prior to clearance by obtaining veto rights and access to sensitive business data.

Altice notified the Commission in February 2015 of its intended acquisition of PT Portugal. The transaction was conditionally cleared by the Commission on April 20, 2015, subject to the divestment of Altice's businesses in Portugal. In May 2017, the Commission sent a statement of objections to Altice, alleging that Altice had implemented its acquisition of PT Portugal before obtaining clearance. The Commission claimed that Altice had already gained decisive influence over PT Portugal's business activities, for example by granting Altice veto rights over day-to-day business proceedings. Altice had been enabled to exercise significant influence over PT Portugal's business beyond the necessary influence to preserve the value of the target. For instance, Altice gave PT Portugal specific instructions on how to carry out a marketing campaign. Altice also received detailed commercially sensitive information outside of the framework of a confidentiality agreement and without providing necessary safeguards, such as "clean teams." A clean team generally consists of an impartial third party, typically a consulting firm or external lawyers, that is bound by strict impartibility and confidentiality protocols. It protects the merging parties' competitively sensitive and confidential information and ensures the information can be shared in accordance with applicable antitrust laws, while simultaneously allowing the parties to complete due diligence and plan for integration.

Altice has already filed an appeal before the GC. This decision is eagerly awaited, especially in the light of the CJEU's judgment regarding EY/KPMG DK.

Enforcement trends of national competition authorities in the EU

At the national level, too, competition authorities in the EU have recently increased their focus on compliance with merger control procedural rules. Despite the existence of a relatively coherent statutory framework, the administrative practice of national authorities varies and further complicates planning a cross-border transaction subject to merger control in various jurisdictions:

- Germany: In the Edeka/Tengelmann case, the German Federal Court of Justice confirmed that independent of a CoC, preparatory measures that relate to a merger and anticipate its effects infringe the standstill obligation. This rather broad approach by the German authorities means even more caution is required when doing business in Germany.
- France: In the Altice/SFR OTL case, the French Competition Authority held that Altice's involvement in the operational management of SFR and OTL before the closing of the acquisition was a breach of the standstill obligation, leading to a fine of €80 million. In particular, Altice had intervened in strategic decisions and the definition of business policies.

→

- The UK: In the Electro Rent case, the Court upheld the first-ever fine issued for a breach of the standstill obligation by the UK Competition and Markets Authority (CMA), pointing out that gun jumping is not merely a theoretical risk under UK law. Following the CMA's approach, it appears that a CoC is not a necessary condition for gun jumping sanctions. This will be of particular interest in a post-Brexit world.
- Spain: In the Gestamp/Essa Bonmor case, the High Spanish Court annulled the relevant authority's decision regarding a breach of the standstill obligation resulting from a two-step acquisition. Contrary to the authority's opinion, the scope of the veto rights granted by the first stage and the 10% shareholding did not establish a CoC, while the second stage did respect the standstill obligation.

Lessons learned from recent enforcement activities

The Ernst & Young/KPMG Denmark decision has helped clarify the red line for parties' integration planning efforts in a transaction: Any integration steps before clearance that, in whole or in part, in fact or in law, lead to a CoC over the target will be considered gun jumping. Practices such as the acquisition of a company through warehousing, the attainment of a de facto CoC despite minority shareholding, the granting of veto rights, and the exchange of sensitive business data prior to clearance should be treated with particular caution. The Commission's Altice/PT Portugal decision shows that veto rights granted to the buyer may constitute a gun jumping infringement if they are either not necessary for safeguarding the target's value during the interim period or they are too extensive without having the purpose of preventing material changes in the business.

Furthermore, the decision clarified that the exchange of detailed commercially sensitive information may enable the buyer to gain decisive influence. Besides information exchange during the due diligence, parties to a M&A transaction should exchange such information for the purpose of integration planning on a need-to-know basis through clean team structures.

The wide variety of conduct that might constitute gun jumping and the inhomogeneous decision practices of the European authorities together create a significant risk for companies' transactional practice. In light of increasing enforcement activities, the integration planning approach with the lowest risk should be chosen. As parties currently often operate in a legal gray zone, it would be helpful if the authorities were to publish detailed official guidelines for integration planning and information exchange. For the time being, however, it is of utmost importance for parties to involve competition experts at the earliest stages of the transaction. <-

Dr. Michael Holzhäuser
Rechtsanwalt, Partner
Ashurst
Frankfurt am Main

michael.holzhaeuser@ashurst.com

Ansgar Hoffmann
Rechtsanwalt, Wissenschaftlicher Mitarbeiter
Ashurst
Frankfurt am Main
ansgar.hoffmann@ashurst.com

www.ashurst.com