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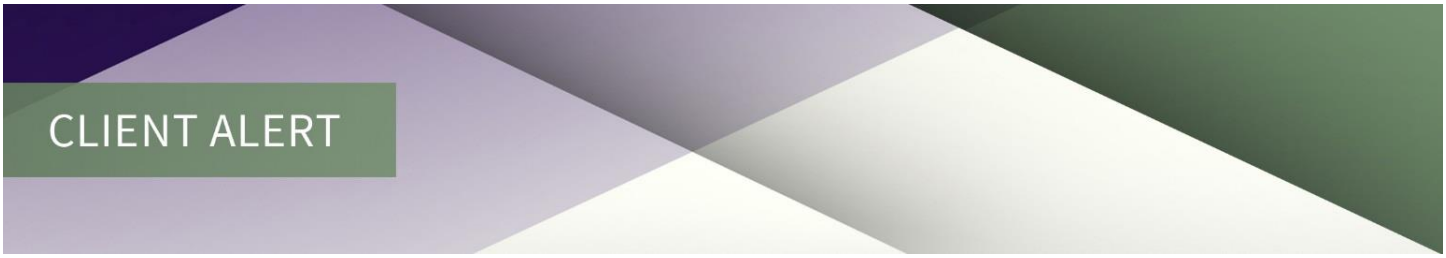

The General Court Clarifies Application of the EU Merger Regulation to Acquisitions by Joint Ventures and Other Jointly Controlled Companies

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On 5 October 2020, the General Court of the European Union (the "General Court")[1] confirmed the 2017 decision by the European Commission (the "Commission") to prohibit the proposed acquisition by HeidelbergCement and Schwenk of Cemex Croatia (the "*Cemex* case"). In its judgment, the General Court confirmed that the Commission had jurisdiction to review the transaction.

The judgment provides important clarification on how to apply the turnover thresholds under the EU Merger Regulation[2] ("EUMR") to acquisitions by joint ventures ("JVs") and other transactions where a target is acquired by a business which is controlled by two or more enterprises (such as several private equity firms). Among other things, a key question for the merger filing assessment of such acquisitions is who are the "*real players*" driving the acquisition?

1 Case T- 380/17, *HeidelbergCement AG / Schwenk Zement KG v. European Commission*, judgment of the General Court of 5 October 2020.

2 Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings, Official Journal L 24, 29.01.2004, p. 1-22.

Key Practical Takeaways

- Where a jointly controlled company (e.g. a company controlled by two private equity firms) acquires a business, companies need to consider with great care whether the involvement of the parent entities make them the "*real players*" on the purchaser side. This assessment can be decisive for whether the Commission has jurisdiction under the EUMR to review the transaction.

- Key to this assessment is the involvement of the parents, or even one parent, in the initiation, organization and financing of the transaction (and the involvement of the JV in the transaction, alongside its parents, may not be enough to dismiss them as the real players behind the transaction).

- Unless it is self-evident that the parents played no active role in the transaction, the parties should consider consulting the relevant Commission merger unit at an early stage if the issue who are the "real players" driving the transaction may be decisive for whether the transaction needs to be notified to the Commission. Such consultation can take several months.

- If the parties take the view that the parent entities played no role in the transaction, it is important to clearly document the basis of this analysis.

- Getting the analysis wrong, can be costly. The Commission has the power to impose 'gun jumping' fines on parties which implement a transaction without a required Commission clearance of up to 10% of the relevant companies' worldwide annual turnover.

- These principles may also apply to an assessment of whether filings are required in certain EU Member States, as a number of Member States apply the same jurisdictional principles as those in the EUMR.

More specifically, the judgment clarifies which businesses should be considered as the "undertakings concerned" for the purposes of the EUMR's turnover thresholds where a JV acquires a target. In the present case, the merger parties had argued that the "undertakings concerned" were only the JV itself and the target and the turnover of these two businesses was insufficient to trigger a Commission review under the EUMR. The Commission disagreed, holding that the undertakings concerned were each of the two JV parents and the target. On this basis, the EUMR turnover thresholds were met and the Commission reviewed the *Cemex* case, ultimately prohibiting it (the "Commission Decision").[3]

The General Court has now confirmed the Commission's assessment, holding that, in addition to the target, the two parents of the JV–HeidelbergCement and Schwenk–should be considered as the "undertakings concerned", rather than

[3] Case M.7878 – *HeidelbergCement/Schwenk/Cemex Hungary/Cemex Croatia*, 5 April 2017.

the JV itself. The General Court noted in this regard that: *"parent companies which are in fact the real players behind the transaction are regarded as undertakings concerned, in particular if their participation in the transaction amounts to significant involvement in its initiation, organisation and financing."*[4]

The Commission's 2017 prohibition decision

The Commission prohibited, on 5 April 2017, the takeover of Cemex Croatia by HeidelbergCement and Schwenk, two construction material producers based in Germany. Following an in-depth investigation, the Commission had identified strong concerns that the transaction would have significantly reduced competition in grey cement markets and increased prices in Croatia. The Commission considered that the behavioral remedies offered by the parties were insufficient to address its concerns. (The Commission had previously referred the analysis of the takeover of Cemex Hungary and the deal's potential local effects to the Hungarian competition authority.[5])

Importantly, the takeover was to be carried out, not by the two parents themselves, but via a full-function JV equally owned and jointly controlled by HeidelbergCement and Schwenk, i.e. Duna Dráva Cement ("DDC").

Under the EUMR, at least two parties (or "undertakings concerned") must meet the turnover thresholds specified in the EUMR,[6] to trigger a Commission review. Here, the target's turnover did not meet these thresholds (only the JV's did, so that "two parties" did not trigger the thresholds separately, as required under the EUMR). In contrast, both HeidelbergCement's and Schwenk's respective turnovers were above the thresholds, which would have been sufficient to trigger a Commission review (irrespective of the fact that the target's turnover was below the thresholds).

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4 General Court judgment, paragraph 257.

5 Concerning Cemex Hungary, the parties decided to re-notify their acquisition of only Cemex Hungary shortly after the prohibition decision, and the Commission referred that acquisition again to the Hungarian competition authority, which cleared the transaction subject to conditions.

6 Article 1, EUMR : *"2. A concentration has a Community dimension where: (a) the combined aggregate worldwide turnover of all the undertakings concerned is more than EUR 5000 million; and (b) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than EUR 250 million, unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State. 3. A concentration that does not meet the thresholds laid down in paragraph 2 has a Community dimension where: (a) the combined aggregate worldwide turnover of all the undertakings concerned is more than EUR 2500 million; (b) in each of at least three Member States, the combined aggregate turnover of all the undertakings concerned is more than EUR 100 million; (c) in each of at least three Member States included for the purpose of point (b), the aggregate turnover of each of at least two of the undertakings concerned is more than EUR 25 million; and (d) the aggregate Community-wide turnover of each of at least two of the undertakings concerned is more than EUR 100 million, unless each of the undertakings concerned achieves more than two-thirds of its aggregate Community-wide turnover within one and the same Member State."*

The Commission's guidance on how to apply the turnover thresholds under the EUMR to JV transactions, which is set out in its Commission's Consolidated Jurisdictional Notice[7] ("CCJN"), notes the following:

"Whereas, in principle, the undertaking concerned is the joint venture as the direct participant in the acquisition of control, there may be circumstances where companies set up 'shell' companies and the parent companies will individually be considered as undertakings concerned. In this type of situation, the Commission will look at the economic reality of the operation to determine which are the undertakings concerned."

"Where the acquisition is carried out by a full-function joint venture (…), and already operates on the same market, the Commission will normally consider the joint venture itself and the target undertaking to be the undertakings concerned (and not the joint venture's parent companies)."

"Conversely, where the joint venture can be regarded as a mere vehicle for an acquisition by the parent companies, the Commission will consider each of the parent companies themselves to be the undertakings concerned, rather than the joint venture, together with the target company. This is the case in particular where the joint venture is set up especially for the purpose of acquiring the target company or has not yet started to operate, where an existing joint venture has no full-function character (…) or where the joint venture is an association of undertakings. The same applies where there are elements which demonstrate that the parent companies are in fact the real players behind the operation. These elements may include a significant involvement by the parent companies themselves in the initiation, organisation and financing of the operation. In those cases, the parent companies are regarded as undertakings concerned." (emphasis added)

In the *Cemex* case, the Commission relied on the last part of the above guidance to assert its jurisdiction, noting that:*"because of their significant involvement in the initiation, organisation and financing of the Transaction, HeidelbergCement and Schwenk are the real players behind the Transaction and thus "undertakings concerned"."*[8] Analyzing the substance of the case, the Commission then decided to prohibit the transaction.[9]

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7 Commission consolidated jurisdictional notice of 16 April 2008 under Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (2008/C 95/01) (the "CCJN"), paragraphs 145-147.

8 Commission Decision, paragraph 58.

9 We will not detail further the Commission's competitive reasoning in the present note in order to focus on the procedural and jurisdictional questions raised.

The General Court's 2020 ruling

HeidelbergCement and Schwenk contested the Commission Decision before the General Court on various substantial and procedural grounds; in our comments we will focus only on the jurisdictional questions. The principal procedural argument was that the Commission erred when concluding that, on the purchaser side, each of HeidelbergCement and Schwenk should be considered to be undertakings concerned instead of just DDC.

More specifically, the applicants first argued that the Commission had improperly interpreted the CCJN. The applicants submitted that the "significant involvement by the parent companies" prong may serve as an indication that the parent companies are using a JV as a mere acquisition vehicle, but is not sufficient in and of itself for dismissing the JV as the undertaking concerned. As a result, according to the applicants, a JV that is *full-function* (i.e. has a largely independent presence on the market) could not be classified as a mere acquisition vehicle if it has its own strategic interest in the transaction, even though the parent companies may also share a broader strategic interest. It is only where the acquisition does not concern the economic activity of the JV, but serves *only* the interests of the parent companies, that the parent companies may be considered as the undertakings concerned. (It was undisputed, in the present case, that DDC was a full-function JV–active in Hungary, Croatia and in the Western Balkans in the areas of cement, ready-mix concrete and aggregate–and was one of the target's close competitors.)

The General Court did not accept the applicants' reasoning and confirmed that the Commission had been correct in relying, on a stand-alone basis, on the significant involvement of the parent companies in the transaction, in spite of DDC's own clear involvement and strategic interest.

In this regard, the General Court recalled that the fact that a JV is full-function and, therefore, economically autonomous from an operational stand point, does not mean that it enjoys autonomy as regards the adoption of its strategic decisions; otherwise joint control would never be possible.[10] It follows, according to the General Court, that, *"in order to ensure the effectiveness of merger control, it is necessary to take into account the economic reality of the real players behind a concentration in accordance with the circumstances of fact and law specific to each case. Therefore, the identification of the undertakings concerned is necessarily connected to the way in which the acquisition process was initiated, organised and financed in each individual case."*[11]

In the present case, the General Court considered that it was clear from the wording of the CCJN that the "*mere vehicle for acquisition*" scenario is not the only situation in which parent companies may be regarded as the undertakings concerned. Conversely, according to the General Court, there are several distinct alternative scenarios covered in the CCJN, i.e. (i) when parent companies are in fact the real players behind the operation, and (ii) when the JV is simply a

[10] General Court judgment, paragraph 112.

[11] General Court judgment, paragraph 116.

mere acquisition vehicle. The General Court concluded that: *"it is not only when the parent companies use a 'shell company' for the acquisition or in circumvention scenarios that it may be necessary to consider the parent companies to be the undertakings concerned, but also when they are the real players behind the transaction."*[12] (emphasis added) In the *Cemex* case, the Commission chose to rely on the latter scenario to assert its jurisdiction, and the General Court confirmed that the Commission was entitled to do so.

The applicants also disagreed with the Commission's assessment that HeidelbergCement and Schwenk initiated the transaction, arguing that DDC took an active part in it and that one of the parents (Schwenk) did not in fact participate actively in the transaction.

This separate, factual argument was also rejected by the General Court, which put forward a series of considerations pointing in the opposite direction: (i) HeidelbergCement's representatives attended negotiations with the seller and prepared detailed documentation, deal valuation, negotiated the non-disclosure agreements, organised and conducted the due diligence, decided on the planning, engaged with banks and agreed on the final purchase price; (ii) DDC strictly adhered to all decisions taken by HeidelbergCement, while DDC did not have the capacity, on account of its lack of personnel and experience, to negotiate such a large transaction; and (iii) on its side, Schwenk indicated at a kick-off meeting that it was in favor of the deal, and was then kept regularly informed by weekly updates about the transaction and never opposed, and also discussed with HeidelbergCement the potential structure of the transaction.

Therefore, while the General Court accepted that DDC did play an active role in the transaction (including in dealings with the banks and its participation in the steering committee) and that one of the two parent companies (Schwenk) took a more passive role than the other parent company, the court agreed with the Commission that this did not preclude the conclusion that the parents were the real players behind the transaction. In this regard, the General Court noted *"that DDC might have participated in the transaction does not preclude the applicants from being significantly involved in the initiation, organisation and financing of the transaction."*[13] (emphasis added)

Significantly, the General Court noted that DDC had financed 80% of the purchase price via bank loans and the remaining 20% out of its own funds, but concluded nonetheless that this was not determinative as the financing structure was in fact authorized by the parents and DCC's own funds in fact came from an increase in capital provided by the parents to finance the purchase price.

For these reasons, the General Court confirmed the Commission's assessment that it had jurisdiction to review the *Cemex* transaction.

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[12] General Court judgment, paragraph 124.

[13] General Court judgment, paragraph 205.

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