

Legal Updates & News

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European Commission Imposes Record-Setting Fine for Failing to Notify Acquisition of Minority Ownership Interest

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On June 10th, 2009, the European Commission imposed a fine of €20 million on electricity producer Electrabel for acquiring control of electricity producer Compagnie Nationale du Rhône (CNR) without seeking prior approval from the European Commission under the EC Merger Regulation (“ECMR”).

The Commission held that by acquiring close to 50% of CNR’s shares in December 2003, Electrabel was “by far CNR’s largest shareholder” and had acquired *de facto* sole control of the company. Closing the transaction without notifying and obtaining clearance from the Commission amounted to “gun-jumping” and therefore constituted a breach of the “standstill obligation” contained in the ECMR.

This decision is significant for two reasons, namely the broad interpretation of the notion of “control” by the European authorities and the size of the fine imposed.

Background

In December 2003, Electrabel acquired shares of CNR held by EDF that amounted to approximately 22.22% of the share capital and 20% of the voting rights of CNR. Due to Electrabel’s existing holdings in CNR, the transaction with EDF resulted in CNR holding 47.88% of the share capital in CNR and 46.06% of the voting rights.

Electrabel’s press release announcing the deal to acquire CNR’s shares also notes that the transaction “fits with Electrabel’s strategy of pursuing its activities on the French market and reinforces the strategic cooperation agreement between Electrabel and CNR. It also consolidates the role of the Suez group - as an important actor – on the French electricity market.” (Electrabel belonged to the Suez group - now GDF Suez).

Commission Decision

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The Commission found that this acquisition resulted in Electrabel obtaining *de facto* control of CNR for two principal reasons.

- First, due to the wide dispersion of the remaining shares and the past attendance rates at CNR's shareholders' meetings, the Commission concluded that Electrabel enjoyed a stable majority of the votes at such meetings.
- Second, the Commission also stated that its finding of an acquisition of control was reinforced by the fact that Electrabel was the sole industrial shareholder of CNR and had taken over the operational management of the power plants and marketing of electricity of CNR from a prior shareholder (EDF, the leading electricity producer in France). The Commission's press release, however, does not provide significant analysis or insight into the precise nature of Electrabel's rights and ability to manage CNR's electricity business.

Because the transaction resulted, in the Commission's view, in an acquisition of control of another company, it qualified as a notifiable "concentration" under the ECMR. Given the size of the parties involved, the transaction also satisfied the relevant ECMR revenue thresholds that determine when a "concentration" has a "Community dimension" and therefore requires a pre-closing notification to the Commission.

Key Implications

The Commission's decision is notable in two respects.

First, it illustrates that minority share acquisitions of less than 50% can give rise to merger notification requirements if the transaction is deemed to result in the *de facto* acquisition of control of the target company. This may not always be obvious or clear to the parties involved.

The Commission's *Jurisdictional Notice* contains a detailed explanation of how the ECMR notification rules are applied by the Commission. It specifically notes that a minority shareholder may be deemed to have *de facto* sole control of an undertaking where the shareholder was "highly likely" to achieve a "stable majority" of the votes at shareholders' meetings. The *Jurisdictional Notice* also makes clear that control can be acquired on a contractual basis in certain circumstances.

While these Commission rules are transparent, it often may be difficult to prospectively analyse the likelihood of attendance and voting patterns of other shareholders at future meetings based solely on historic voting patterns at prior meetings. Moreover, even in situations where there may be a wide dispersion of voting rights of other shareholders, it may not always be clear that a large minority shareholder will achieve a majority of the actual votes cast at subsequent meetings.

As a result, parties to transactions may not be able to easily predict when the Commission will consider a failure to notify an acquisition of a minority ownership position to be a violation of the ECMR rules. An acquiring party that becomes the largest shareholder due to an acquisition will need to carefully review the voting rights and records of other shareholders to determine whether the Commission would deem it to have *de facto* control of the target company.

Second, this is a record-setting fine for "gun-jumping" violation by EU and international standards. The sheer size of the fine imposed by the European Commission for a procedural infringement of the EC Merger Regulation is striking. The fine far surpasses the fines previously imposed by the US Department of Justice, for example, the Qualcomm-Flarion fine of \$1.8 million in 2006. Moreover, while some national competition authorities in Europe, particularly the German Bundeskartellamt, have also taken an increasingly proactive stance against violations of national level merger notification requirements, the fine by the EC in this case substantially exceeds the fines of €4.5 million and €4.1 million that the German authorities recently imposed on several companies for gun-jumping violations.

In sum, this decision signals a more aggressive approach by the European Commission toward procedural violations of the ECMR. Commissioner Neelie Kroes maintains that the decision will send a

“clear signal” to companies to “respect scrupulously” their notification obligations under the ECMR.