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Resurgence of Protectionism – Can European Member States Really Do Whatever They Want to Foreign Takeovers?

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EU Competition Commissioner Joaquín Almunia recently cited the French initiatives to block the GE-Alstom deal as an example of "*worrying signals of protectionist threats*" in Europe.[1] France is not, however, to be singled out. EU Member States have sought to protect their national champions for decades, relying, among others, on an EU merger provision which allows Member States to take measures to protect their legitimate interests.

France's Extended Powers to Intervene in Foreign Takeovers

In May 2014, the French government adopted a decree extending its powers to block foreign investments in strategic activities relating in particular to energy supply, water supply, transport networks, electronic communication services, and public health. This measure cannot be detached from the government's initial opposition to GE's bid for Alstom's power and grid businesses. After lengthy discussions, an update to GE's offer received support from the French government at the end of June. Under the terms of the agreement, France would purchase a 20 per cent stake in Alstom to ensure, in particular, that the State would retain a say in job-related decisions and decision-making at the company.

Commenting on the French measure, Mr. Montebourg, the then *Economy and Industry Minister*, said that the new decree was a "*choice of economic patriotism*"

1 "*Almunia voices concern over rising protectionism, cites debate over GE-Alstom deal*," MLex, 24 June 2014, referring to Joaquín Almunia's speech delivered at the Forum Observatory on Europe in Brussels, on 24 June 2014.

and that blocking sales was "*an essential rearmament of public power*."[2] Such a stand gives the impression that EU Member States can take the steps they wish to protect their national champions. This is not the case however. EU merger rules do allow Member States to take certain measures to protect their legitimate interests, but these powers are not unlimited.

Merger Control in the European Union

The EU Merger Regulation ("EUMR") is articulated around the principle that mergers with an EU dimension, i.e., meeting certain turnover thresholds, have to be cleared by the Commission. Article 21 EUMR provides that the Commission has sole competence to review such mergers and that EU Member States shall not apply their national competition rules in respect of these transactions.

The allocation of jurisdiction between the Commission and the Member States is, however, subject to a number of exceptions, and Member States may review transactions which initially fell under the exclusive competence of the Commission.

Thus, pre-notification, the parties may opt for a case referral to a national competition authority instead of notifying their operation to the Commission. Similarly, post-notification, notified cases may be referred from the Commission to a national competition authority.

Another exception is Article 21 EUMR. This clause provides that Member States can adopt measures which could prohibit, submit to conditions, or in any way prejudice transactions with an EU dimension in order to protect legitimate interests in so far as they are compatible with the general principles and other provisions of EU law.

The "Legitimate Interests" Clause

The "legitimate interests" clause does not create new rights for Member States. Member States have the ability to intervene on grounds other than those covered by the EUMR in order to prohibit a transaction or make it subject to additional conditions and requirements. However, they are not allowed to authorize concentrations which the Commission has prohibited under the EUMR. It is also essential that prohibitions or restrictions placed on transactions do not amount to any form of discrimination or any disguised restriction in trade between Member States. Finally, in application of the EU general principles of necessity and proportionality, the measures taken by Member States must be limited to the minimum of action necessary to ensure the protection of the legitimate interests in question.

A distinction is drawn between two types of legitimate interests.

The "Recognized" Interests

Three categories of legitimate interests are expressly recognized by the EUMR and may be freely invoked by Member States: public security, plurality of the media, and prudential rules.

Public security interests include internal and external military security. Other interests such as the protection of the population's health or the security of supply of a product that is of fundamental importance for a Member State may also be considered as a public security interest. However, the requirements of public security are to be interpreted

[2] "*France takes 'nuclear weapon' powers to block foreign takeovers*", Financial Times, 15 May 2014.

strictly. Thus, public security may be relied on "*only if there is a genuine and sufficiently serious threat to a fundamental interest of society*."[3]

The reference to the plurality of media recognizes the legitimate concern of maintaining diversified sources of information. In *Newspaper publishing*[4] and *NewsCopr/BSkyB*, the Commission did not oppose the additional review of media plurality issues by UK authorities. Thus, even if the Commission cleared the *NewsCorp/BSkyB* transaction without remedies, considering that NewsCorp's increased shareholding would not significantly impede effective competition, NewsCorp offered undertakings to the UK Secretary of State to "*remedy, mitigate or prevent the potential threats to media plurality identified by Ofcom*."[5]

Prudential rules can also be – and have regularly been – invoked by Member States. Attempts by some European banks to acquire credit institutions in other Member States have caused EU governments and national supervisory authorities to invoke prudential rules. Thus, for instance, when Banco Santander, a Spanish bank, announced that it would acquire joint control over a group of Portuguese financial institutions, the Portuguese government vetoed the deal, claiming that it was violating national prudential rules and was incompatible with the "national interest." The legitimate interest invoked by Portugal was not, however, communicated to the Commission. The Commission reviewed the deal under the EUMR and approved it in August 1999. In light of the inaction of the Portuguese government to reverse its veto, the Commission initiated infringement proceedings against Portugal, arguing that "*none of the reasons allegedly justifying Portugal's continued attempts to derail the operation ha*[d] *any factual or legal basis*."[6] The matter gained political attention from a number of countries, including France and Italy, which sided with Portugal in arguing that foreign meddling in national financial issues should not be allowed. Finally, changes were brought to the structure of the transaction to lift Portugal's concerns, and the Commission cleared the "revised" deal in January 2000.[7]

Measures genuinely aiming to protect one of these interests, which are liable to block, submit to conditions, or in any way prejudice transactions with an EU dimension, but which are in compliance with the principles of non-discrimination and proportionality, can be adopted by Member States without prior communication and approval by the Commission. Conversely, measures must be notified to the Commission when there are reasonable doubts that they genuinely aim to protect one of these interests or that they comply with the principles of non-discrimination and proportionality.

[3] Case COMP/M.4685, *Enel/Acciona/Endesa*, Commission decision of 5 December 2007, para. 57. In this case, Spain failed in justifying measures restricting Enel's and Acciona's freedom of establishment and the free movement of capital by referring to the risks or negative effects that the conversion of Endesa into a company jointly controlled by Enel, an international group, could bring to the Spanish public interest in the field of security of energy supply.

[4] Case COMP/M.423, *Newspaper Publishing*, Commission decision of 14 March 1994. The Commission acknowledged the power of the UK Secretary of State to grant formal consent under the UK Fair Trading Act as the transaction involved issues such as the accurate presentation of news and free expression of opinion. The Commission stressed, however, the need for the UK authorities to keep the Commission informed about the conditions which they might deem appropriate to attach to the transaction (see para. 22 and 24).

[5] See undertakings given by News Corporation pursuant to paragraph 3 of schedule 2 of the Enterprise Act (protection of legitimate interests) order 2003, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/72994/News_Sky_1_March_UIL_for_consultation.pdf

[6] "*Commission overrules Portuguese measures against BSCH/Champalimaud operation*", IP/99/774, 20 October 1999.

[7] Case COMP/M.1799, BSCH/Banco Tottay CPP/A. Champalimaud, Commission decision of 11 January 2000.

Other Legitimate Interests

Member States may also take measures to protect other legitimate interests. Before doing so, Member States are invited to communicate the interests invoked to the Commission. The Commission will assess the "legitimate" nature of these interests and decide whether the intervention of the Member State is justified. Upon approval by the Commission, Member States can implement the measure.[8] If a Member State breaches the "standstill" obligation, the Commission is empowered to issue a decision on the compatibility of the measure with Article 21(4) of the EUMR and, if need be, order the Member State to cancel the relevant measure.

In a number of cases, the Commission, but also sometimes the Court, made it clear that Article 21(4) of the EUMR did not allow Member States to intervene and block transactions in order to protect national champions.

This was the case, for instance, in *E.ON/Endesa*. After E.ON announced its intention to launch a bid for Endesa in February 2006, the Spanish government adopted new legislative measures aiming to increase the supervisory powers of the Spanish energy regulator and make the bid conditional upon the energy regulator's approval. E.ON notified the acquisition to the Commission on 16 March 2006 and requested the energy regulator to authorize the transaction on 23 March 2006. The Commission cleared the deal on 25 April 2006. A few months later, the energy regulator adopted a decision making the transaction subject to a large number of conditions. Subsequently, the Commission adopted a decision by which it declared that the energy regulator's decision breached Article 21(4) of the EUMR as (i) the decision was adopted without the prior communication of the legitimate interests and the approval by the Commission, and (ii) a number of conditions were contrary to the EU Treaty rules on free movement of capital and freedom of establishment.[9] The energy regulator reviewed its decision. Despite the modifications brought to the conditions, the Commission remained unsatisfied and brought the matter to the Court in Luxembourg. In March 2008, the Court confirmed that Spain breached its obligations under the EU Treaty by not withdrawing the decision imposing illegal conditions on the transaction.[10]

In the last few months, besides the GE-Alstom case, another case was likely on the Commission's surveillance radar. Indeed, after Pfizer walked away from the AstraZenaca takeover, UK Business Secretary Vince Cable told the press that the UK government's powers to intervene in a bid should be extended to cover takeovers of companies that own critical infrastructure and receive public funding to conduct research and development. He added that foreign bidders should also be forced to make legally binding commitments they offer during takeover negotiations when national interests are at stake.[11] In response, the House of Lords Economic Affairs Committee asked him to clarify his position as Vince Cable formerly indicated that such extended powers would be incompatible with EU law. No doubt the Commission will closely follow any legal initiative and ensure that the UK communicates the invoked legitimate interest to allow the Commission to check it complies with EU law.

8 In *Lyonnaise des Eaux/Northumbrian Water*, the Commission recognized the legitimate interest of the UK authorities in applying certain provisions of the Water Industry Act 1991 to ensure a sufficient number of independent water companies. The Commission also verified the proportionality and the non-discriminatory nature of the measures the UK intended to take. *Lyonnaise des Eaux/Northumbrian Water*, M.567, decision of 21 December 1995, para. 7-8; "*Commission approves takeover of Northumbrian Water by Lyonnaise*", IP/95/1469, 22 December 1995.

9 "*Commission rules against Spanish Energy Regulator's measures concerning E.ON's bid for Endesa*", IP/06/1265, 26 September 2006.

10 Case C-196/07, *Commission v. Spain*, para. 39.

11 Maintaining jobs is an example of such commitments.

No Reason for the Commission Adopting a Softer Approach

The first EUMR, dated 1989, represented a watershed improvement in the EU competition policy as the Commission became exclusively competent to review certain transactions. Through the existence of the "legitimate interests" clause, Member States arranged a way out. Governments finding their legitimate interests engaged can intervene and even prohibit – under certain conditions – transactions even if the Commission previously cleared them. EU Member States have sought to protect their national champions through this clause but have consistently faced the Commission's uncompromising position. Indeed, the Commission has only rarely recognized the legitimate nature of the interests invoked by the Member States (besides the three interests explicitly mentioned in Article 21(4) EUMR). Furthermore, the Commission does not hesitate to launch infringement proceedings in cases where Member States fail to communicate the legitimate interests allegedly engaged and/or block transactions without sufficient factual or legal basis to do so.

It is difficult to evaluate whether the approach defended by the Commission will – in the longer term – deliver "net benefits" to Europe. What is certain however is that jurisdictions such as the US or Canada have protectionists tools which go beyond what EU Member States have at their disposal and do not hesitate to block takeovers by foreign buyers when the independence of their national champions is deemed to be at risk.

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