

Private equity and competition law: liability for infringements by portfolio companies

On 2 April 2014, the European Commission fined eleven producers of underground and submarine high voltage cables a total of €301 million for participation in a cartel. In line with the Commission's established practice, the liability for these fines extended to parent companies that exercised decisive influence over the cartel participants, including Goldman Sachs, which was found to have exercised such influence on the cable producer Prysmian for several years when the infringement was committed.

This case acts as an important reminder that private equity houses may be held jointly liable for infringements of competition law by their portfolio companies. This may entail exposure not only to the risk of significant fines but also to private actions brought by those claiming to have suffered loss as a result of the cartel.

BACKGROUND

In July 2011, the European Commission sent a statement of objections to many of the world's largest high voltage power cable producers alleging that they had shared markets and allocated customers between themselves. At that time, Goldman Sachs confirmed that it had also received the statement of objections as a result of its interest in Prysmian, which had been held by certain of the GS Capital Partners Funds. Last week's decision imposed a fine of €104.6 million on Prysmian for this conduct, of which Goldman Sachs was held to be jointly and severally liable for €37.3 million.

This decision follows a judgment from the General Court of the European Union on 23 January 2014 which upheld the Commission's decision to hold Arcques AG (now Gigaset AG), a German private equity fund, jointly liable for a €13.3 million fine levied on one of Arcques' investments (SKW Stahl-Metallurgie) for its role in a cartel involving calcium carbide and magnesium based reagents for the steel and gas industries.

ANALYSIS

These cases reflect the application by the Commission in the private equity context of the long-established principle that one undertaking may be held jointly and severally liable for the anti-competitive conduct of another where they formed part of a single economic unit during the period of the infringement.

Whether two undertakings formed part of a single economic unit turns on whether one of the undertakings exercised decisive influence over the other's conduct on the market at the relevant time. In the case of a 100% shareholder (direct or indirect) the Commission will apply a rebuttable presumption that the shareholder exercised decisive influence over the market conduct of its investment and thus that the two formed part of a single economic unit. The Commission applied this presumption in the calcium carbide case to hold Arcques jointly liable for the infringement committed by SKW during a period when it was wholly owned by Arcques.

In the case of a shareholder with an interest of less than 100%, it will be for the Commission to show that the shareholder in fact exercised decisive influence over the conduct of the investment. In the calcium carbide case, the General Court upheld the Commission's findings that several elements showed that Arcques had also exercised decisive influence over SKW during a period when its shareholding was reduced to just over 57%. These elements included board representation, the regular reporting of information about the economic performance of SKW to Arcques and documents which showed that the approval of Arcques was required for strategic decisions directly affecting the profitability and growth of SKW.

Although the public version of the high voltage cables decision is not yet available, it appears that the Commission relied upon similar elements to establish decisive influence on the part of Goldman Sachs. The European Commissioner for Competition, Joaquín Almunia, noted that there was evidence that Goldman Sachs had been involved in the management decisions of Prysmian through voting rights and board representation. These elements were deemed sufficient by the Commission to impose joint and several liability even though, as publically noted by Goldman Sachs, there was no suggestion that "Goldman Sachs or its people had any knowledge or involvement in the purported collusive behaviour."

It should be noted that recent years have seen the Commission widely extend the net of liability for cartel infringements to minority shareholders and joint venture owners on the basis that they exercised decisive influence over the cartel participants. For example, on 26 September 2013, the European Court of Justice upheld the Commission's decision to hold the parents of a 50/50 full function joint venture liable for the participation of the JV in a chloroprene rubber cartel.

COMMENT

These cases highlight the fact that private equity houses may be held liable for the anti-competitive conduct of their investments where they are deemed to form part of a single economic unit during the period of the infringement, which may be the case even where they are a minority shareholder.

In the context of the Goldman Sachs case, Commissioner Almunia commented that investment companies "should take a careful look at the compliance culture of the companies they invest in." In addition to carrying out appropriate due diligence, private equity houses may seek protection through warranties and indemnities from the sellers to cover potential prior cartel conduct by acquisition targets. Further protection may also be sought by seeking to instil a competition compliance culture in acquired businesses through the maintenance of appropriate competition compliance programmes. Given the wider scope of the criminal cartel offence in the UK from 1 April and the possibility of director disqualification orders where a director's company has breached competition law, it is particularly important for private equity house representatives on the boards of acquired businesses to take steps to ensure that competition law compliance is taken seriously within the business in order to protect their personal positions.

Compliance programmes may include antitrust reviews post-acquisition to identify and assess the competition law risks facing the business, including identifying any possible competition infringements. Where potential cartel behaviour is identified, active consideration should be given to whether it is appropriate to be making applications for leniency. The review should also encompass the risk mitigation steps currently being undertaken by the business (such as procedures, policies and training) to assess whether these are fit for purpose or whether they need to be refreshed or re-engineered. An important part of this will be to establish whether the business has a commitment to compliance with competition law and, if not, steps will need to be taken to establish one and achieve behaviour change.

It would also be open to a private equity investor when exiting an investment to take contractual protection for liability for competition law infringements from the incoming purchaser, for example by a reverse indemnity. It could also take protection directly from the investee either at the time of investment or exit. However, since any form of protection may be difficult to achieve in practice, liability for cartel activity may in fact add to the list of liabilities that, as a legal matter, it is not necessarily possible to leave behind once an investment is realised.

Please contact your usual Slaughter and May contact if you would like to discuss any of the issues raised in this note or require further information.