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General Court backs European Commission in Altice gun jumping case – confirming strict standard for standstill obligation

On 22 September 2021, the General Court dismissed Altice's action against the European Commission's 2018 decision imposing two fines totalling EUR 124.5 million for "gun jumping" in connection with Altice's acquisition of PT Portugal, confirming the Commission's findings regarding the infringements and only correcting the amount of the fine by 10%. The judgment provides important clarifications regarding the interpretation and the application of the notification obligation and the standstill obligation for transactions subject to EU merger control.

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Background

In December 2014, the international telecommunications operator Altice signed a share purchase agreement (SPA) to acquire PT Portugal, the incumbent telecoms operator in Portugal. The transaction was subject to EU merger control, notified to the European Commission in February 2015 and cleared in April 2015 with conditions and obligations. However, the Commission later became aware of press reports that Altice and PT Portugal had intensive contacts prior to the clearance decision and launched an investigation to determine whether Altice had infringed obligations under the EU Merger Regulation, which require that transactions falling under the regulation are notified to the Commission (notification obligation) before they are implemented and prohibit their implementation before they are notified and cleared (standstill obligation).

Based on the results of this investigation, the Commission concluded that:

- certain veto rights in the SPA gave Altice the right to exercise decisive influence over PT Portugal as of the signing of the SPA.
- Altice had actually exercised decisive influence over aspects of PT Portugal's business, such as by giving PT Portugal instructions on how to carry out a marketing campaign.
- Furthermore, Altice had asked for and received commercially sensitive information about PT Portugal before closing, outside the framework of any confidentiality agreement.

In consequence, the Commission in April 2018 imposed two fines totalling EUR 124.5 million on Altice for breaching EU merger control rules and controlling PT Portugal before obtaining merger approval, so-called "gun jumping". Altice then filed an action seeking annulment of that decision before the General Court.

On 22 September 2021, the court dismissed most of this action, confirming the Commission's findings regarding the infringements and only correcting the amount of the fine by 10%.

The judgment provides important clarifications regarding the interpretation and the application of the notification obligation and the standstill obligation for transactions subject to EU merger control. This concerns the questions:

- when do pre-closing covenants contained in transaction agreements amount to an early implementation of the transaction?
- under what circumstances must contacts between the parties in the period before clearance and closing be qualified as "decisive influence" by the acquirer over the target?

Pre-closing covenants in transaction agreements

In transactions, which are subject to regulatory approval, often a significant period of time passes between signing and closing. In this period, the purchaser is already bearing the financial and commercial risk of the target's business, while the target is still an independent operator on the market. In such situations, transaction agreements normally contain pre-closing covenants in the form of "ordinary course of business" clauses, which prevent the target from taking decisions or making investments outside the ordinary course.

The Court acknowledged that the standstill obligation does not prohibit pre-closing covenants, which are necessary:

- to ensure that the value of the target is preserved; or
- to avoid compromising the commercial integrity of the target.

Unfortunately, the Court did not provide any further general guidance on these two aspects. In particular, it provided no specific criteria, which could be used by companies to draft pre-closing covenants in the future.

Still, the Court upheld the Commission's strict stance regarding the pre-closing covenants in the Altice / PT Portugal SPA. In particular, the Court found that the agreement of pre-closing covenants for the following three areas as such violated the gun-jumping prohibition (regardless of whether the covenants were implemented)

1) Senior management and its appointment, dismissal or changes to the contracts

The Altice / PT Portugal SPA foresaw that Altice had a veto-right over the appointment and dismissal of, or changes to the terms of employment to, any officer or director at PT Portugal. While the Court found that the wording of the provision had to be construed narrowly so that it would cover only the "management of PT Portugal", it still considered the clause as illicit because it enabled Altice to co-determine the structure of the senior management of PT Portugal. The Court referred to the Commission's Jurisdictional Consolidated Notice, which indicates that the power to co-determine the structure of the senior management of a company usually confers control. The Court did not engage in any assessment as to whether Altice's veto-right could have been justified with respect to the preservation of PT Portugal's value or its commercial integrity.

2) Entering, terminating or modifying certain types of contracts

The Altice / PT Portugal SPA further stipulated that Altice had a veto-right over any material contract (as defined in the SPA) and over all other contracts and commitments above a certain value. For the first month from the date of the signing of the SPA, this threshold amounted to EUR 5 million, and for the period afterwards to EUR 1 million.

The Court held that the provisions were "so numerous and broad and the monetary thresholds so low" that they went beyond what was necessary to preserve the value of PT Portugal. Unfortunately, the judgment does not contain guidance on a monetary threshold, which would have been legitimate, or the general criteria to calculate such a threshold. The Commission had made reference in its decision to the purchase price of EUR 7.4 billion and PT Portugal's turnover of EUR 2.5 billion in 2014. Based on these two parameters, the monetary threshold of EUR 1 million accounted for 0.0135% of the purchase price and for 0.04% of PT Portugal's 2014 turnover, whereas the monetary threshold of EUR 5 million accounted for 0.0676% of the purchase price and for 0.2% of PT Portugal's 2014 turnover. Apparently, these ratios were too low in the view of the Court (and the Commission), but the question remains: which ratio would be high enough to ensure that it is necessary for the purchaser's legitimate interest to have its investment protected? This question leaves companies with a considerable degree of uncertainty and in the absence of further guidance the general rule for any purchaser should be stick to thresholds, which might appear high. (The Court explicitly noted that the seller of PT Portugal had initially proposed "much higher" thresholds, but these were negotiated downwards).

3) Changes to the pricing policies & standard terms and conditions

Moreover, the Altice / PT Portugal SPA conferred a veto-right on Altice regarding any modification of PT Portugal's pricing policies, standard offer prices or standard terms and conditions. The Court agreed with the Commission that the provision was "extremely broad" and obliged PT Portugal to obtain consent from Altice for "a very wide range of decisions on prices and client contracts". Moreover, the provision lacked a definition of "pricing policies" and "standard offer prices" and therefore captured "any changes to prices" in the Court's view.

The Court also made it clear that pre-closing covenants, which oblige the seller to obtain the purchaser's consent to specific measures (with consent not to be unreasonably withheld), and entail compensation rights for the purchaser in case of a violation, amount to *de-facto* veto-rights and not merely consultation rights.

Contacts with the target company prior to clearance

The judgment further deals with contacts between the purchaser and the target in the interim period between signing and closing. The Court clarified that such contacts are considered an early implementation of the transaction in breach of the standstill obligation if they amount to the **exercise of decisive influence** by the purchaser.

The Court explained that the same standard applies to the assessment of such involvement by the purchaser in the management of the target's business. In other words, the involvement is only justified if it is necessary to ensure that the value of the target is preserved, or to avoid compromising the commercial integrity of the target.

In its decision, the Commission set out seven instances demonstrating that Altice had exercised decisive influence over PT Portugal by interfering in PT Portugal's ordinary course of business. These instances of involvement in the management of the target included:

- **Participation in a marketing campaign:** Altice had participated in a conference call concerning a new product promotion campaign by PT Telecom, later gave PT Telecom written instructions concerning this campaign and received reports by PT Portugal. The Court noted that there was "nothing to suggest that the campaign could have had a negative impact on the integrity of PT Portugal’s business". Rather, the aim of creating business was a normal objective for a company.

- **Intervention in negotiations with a business partner:** The Court held that the negotiation of contracts, also with important business partners (in this case, a football club), are generally considered the ordinary business of a company. In the case of PT Portugal, the value of one contract was also "very small" (and below the thresholds of the SPA) compared to the purchase price and the target's turnover. Another contract related to a type of service already offered by PT Portugal and therefore did not relate to a new offering. Also, the judges noted that Altice failed to bring forward any evidence to demonstrate that PT Portugal had materially changed its business strategy which would have justified the intervention.

- **Involvement in choice of suppliers:** According to Altice, PT Portugal had consulted it regarding the selection of a technical equipment supplier to ensure that that selection was prepared and carried out "under the best possible conditions" so as to avoid any disruption in the functioning of PT Portugal's network. However, the Court found that the background of the selection process was that PT Portugal wished to rationalise procurement and simplify its network, part of the ordinary course of business.

- **Involvement in M&A activities**: Altice was informed by the seller that a third party intended to purchase PT Portugal's shares in a joint venture, which also triggered pre-emption rights and the decision that it did not intend to sell the shares or to exercise pre-emption rights. After requesting and obtaining further information, Altice had informed PT Portugal that it wished PT Portugal to buy as many shares from other shareholders as possible and to establish contacts to purchase further shares. While the Court found that the information by the seller could be justified by the need to preserve the business acquired by Altice, it found that by asking PT Portugal to contact the third party, it "had overstepped the boundaries of what could be considered necessary to preserve the value of PT Portugal" and "acted as if it had already formally acquired control of PT Portugal".

- **Approval of investments:** The seller sent Altice a formal request in accordance with the SPA, seeking its approval for certain investments to be made in connection with an outsourcing project. Altice then asked for additional information and what the payback period for the investment would be. According to Altice, this was justified in light of low profitability and the nature of the contract. The Court rebutted this argument, pointing out that the contract formed part of PT Portugal's day-to-day business since "it concerned the renewal of an existing contract and a level of revenue comparable to that of the pre-existing contract". Furthermore, the Court was concerned that PT Portugal shared confidential information regarding expected customer revenues with Altice, a competitor.

The Court therefore confirmed that Altice had in fact breached the notification obligation and standstill obligation in all the above instances. However, the Court considered that the involvement of Altice in the management of the target's business was justified in one instance:

- **Intervention regarding "unusual" new product launch:** This concerned the envisaged launch of a new TV channel not aimed at human beings but at dogs, in which Altice intervened in the light of the novelty of the contract and the negative effects, which this content might have on PT Portugal's image. The Court agreed that the planned dog channel could affect PT Portugal's image and that Altice's intervention was therefore necessary to preserve this image and the value connected with this image or at least the integrity of the business.

The judgment further addressed the issue of the **exchange of commercially sensitive information of the target** before clearance and closing. According to the finding of the Commission, Altice and PT Portugal had exchanged information regarding PT Portugal which was "highly sensitive both commercially and competitively", even though subsidiaries of Altice were in direct competition with PT Portugal. As the Court

points out, this could not be justified by Altice's need to assess the value of the business, as the exchanges continued after the signing of the SPA. As a result, Altice had access to information "to which it should not have had access". Also, the fact that PT Portugal replied to Altice’s requests demonstrated in the court's view that Altice had exercised decisive influence over certain aspects of PT Portugal’s business. According to the Court, it was sufficient that the information exchanges contributed to the decisive influence. It was not necessary to find that they directly established an infringement of the notification obligation and standstill obligation.

Conclusions

The Altice judgment touches upon significant legal questions, but more importantly provides several key conclusions for the M&A and merger control practice:

- Pre-closing covenants in transaction agreements should be carefully reviewed whether they are necessary to preserve the target's value (taking into account the Court's conservative approach as to an appropriate monetary threshold) or to protect the commercial integrity of the target.

- Veto-rights regarding the direct market strategy (e.g. pricing policies) and senior management are particularly sensitive. The willingness by competition authorities and courts to accept these veto-rights is limited, so that such clauses should only be considered it there is a clear and demonstrable basis that the veto-right is necessary to preserve the target's value (which appears more difficult in case of employment contracts) or to protect the commercial integrity of the target (which appears more likely in case of key managers who cannot be easily replaced due to their specific business or knowledge of the company).

- An involvement in the management of the target company is only permitted to a limited extent. The purchaser must be able to demonstrate that such involvement is required to protect the value or the commercial integrity of the target. The Court made clear that a strict standard must be applied in this respect. Normally, if the value limits of the covenant are complied with and the target's behavior is in line with the previous and ordinary course of business, intervention is not justified.

- Parties must avoid the impression that the purchaser already takes over control in the interim period between signing and closing. In this respect, reports (sometimes extensive) from the target to the purchaser and an exchange of commercially sensitive information of the target must also be viewed critically – keeping in mind that this can also lead to an additional violation of the cartel prohibition under Art. 101 TFEU.

- The Court also emphasised in its judgment that parties should request from the Commission a derogation from the standstill obligation if they want to partially implement a notified transaction, rather than just carrying out the partial implementation relying on "unusual nature" of the intended measures.