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Memorandum

EU Court Affirms That Parent Companies, Including Private Equity Firms, May Be Held Jointly and Severally Liable With Less Than Full Share Ownership of Portfolio Companies That Breach EU Competition Laws

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On July 12, 2018, the General Court of the European Union dismissed Goldman Sachs's appeal of a decision finding it jointly and severally liable for the cartel conduct of a portfolio company held by funds controlled by Goldman Sachs. The General Court confirmed that the presumption that a parent company "exercises decisive influence" over a subsidiary, and therefore can be held jointly and severally liable for a subsidiary's conduct, may apply even when a parent holds less than 100% of the share capital of its subsidiary. The General Court also held that the presumption of parental liability can also extend to portfolio companies of private equity firms when a private equity firm exercises such decisive influence. The decision also outlined the type of de jure or de facto board governance rights that could lead to a finding of decisive influence regardless of the quantum of shares or voting rights held.

The judgment highlights the need for private equity and other investment companies to pay close attention to potential exposure to liability for competition law violations by portfolio companies and the importance of pre-acquisition diligence and post-acquisition monitoring to prevent competition law breaches.

Summary of the European Commission Decision

On April 2, 2014, the Commission announced fines totalling €302 million on 11 producers of underground and submarine high voltage power cables for participating in a market allocation cartel from 1999 to 2009.

The Commission imposed the largest fine (almost €105 million) on Prysmian Group, headquartered in Italy. The Commission held Goldman Sachs jointly and severally liable for €37 million of Prysmian's total fine under the doctrine of parental liability, covering the time that the Commission found that Goldman Sachs exercised decisive influence over Prysmian (July 2005 to January 2009). The Commission found that

Goldman Sachs held such decisive influence during this period even though Goldman Sachs held 100% of Prysmian's share capital for less than 50 days between 2005 and 2007, and held significantly less than 50% of its share capital from 2007 to 2009.

Goldman Sachs's Appeal

Goldman Sachs appealed the decision arguing that: (i) it could not be presumed to have exercised decisive influence when it held less than 100% of the share capital in Prysmian, (ii) the Commission did not present adequate evidence that Goldman Sachs had the ability to or actually did exercise decisive influence following the 2007 IPO of Prysmian which reduced Goldman Sachs's shareholding to less than 50%, and (iii) Goldman Sachs was a financial investor and therefore should not be held liable for Prysmian's conduct.

The European Commission and its overseeing courts have long held that a shareholding of 100% or close to 100% gives rise to a rebuttable presumption that a parent company exercises decisive influence over its subsidiary or portfolio company, and therefore can be held jointly and severally liable for competition law violations under the doctrine of parental liability.[1] Here, the General Court confirmed that it is not only the *share capital* that is relevant to a presumption of decisive influence but also the voting rights held. The General Court also affirmed the European Commission's extension of parental liability to a situation where a parent owns far less than even 50% of a portfolio company but where there are other indicia of decisive influence.

First, although Goldman Sachs held 100% of the equity of Prysmian for only 41 days following its initial purchase of the company, the General Court focused on the fact that from 2005 up until the 2007 IPO Goldman Sachs held 100% of the voting rights in Prysmian. The General Court affirmed the Commission's decision that this placed Goldman Sachs in a similar situation to that of the sole owner of a subsidiary and therefore the Commission had appropriately applied the presumption that Goldman Sachs could exercise decisive authority.

Second, the General Court affirmed the Commission's finding that although Goldman Sachs held less than 33% of Prysmian's shares following the 2007 IPO and no longer controlled a majority of the voting rights, which negated a presumption of decisive control, there was sufficient evidence that Goldman Sachs exercised decisive control over Prysmian. In particular, the General Court noted:

i. Goldman Sachs's ability to appoint members of the various boards of Prysmian,

ii. Goldman Sachs's power to call shareholder meetings and propose the revocation of directors or entire boards,

[1] Judgment of 10 September 2009, *Akzo Nobel and Others v Commission*, C-97/08 P.

iii. the presence on Prysmian's boards and strategic committees of employees with connections to Goldman Sachs,

iv. Goldman Sachs's receipt of regular updates and monthly reports,

v. measures Goldman Sachs took to ensure control over five of Prysmian's six board members (*e.g.*, amending Prysmian's by-laws to introduce a slate system for the nomination/appointment of new boards, securing a commitment from Prysmian's second-largest shareholder not to propose any candidates for director), and

vi. evidence Goldman Sachs acted as an industrial owner by favoring cross-selling between Prysmian and its other portfolio companies.

The General Court also rejected Goldman Sachs's argument that it did not have decisive influence because Prysmian's management proposed board members and put forth business proposals, finding that Goldman Sachs still had the authority to affirmatively approve any such proposals, which the General Court held amounted to decisive influence. The General Court also noted that the same board of directors that was put in place by Goldman Sachs before the 2007 IPO remained unchanged until after the date the cartel ended, and therefore concluded that Goldman Sachs continued to exercise decisive influence over the board of directors.

Finally, the General Court upheld the principle that "pure financial investors" that hold shares to make a profit but refrain from *any* involvement in its management or control cannot be held liable for an infringement of a subsidiary.[2] However, the General Court found that Goldman Sachs was not a pure financial investor in Prysmian. The General Court rejected Goldman Sachs's arguments that (i) its funds that held its share in Prysmian did not have the expertise or resources to determine Prysmian's market conduct, (ii) management of portfolio companies did not fall under the mandate of the Goldman Sachs division that managed the funds, (iii) Goldman Sachs's employee directors were simply in place to monitor the investment, and (iv) Prysmian was not perceived externally to be part of the Goldman Sachs group, either finding these points irrelevant or that there was evidence to the contrary.

Implications for Private Equity Firms

The General Court's decision in *Goldman Sachs v. Commission* extends the presumption of the exercise of decisive influence and the joint and several liability for parent companies to parents that hold less than 100% of the share capital of a portfolio company, but still control 100% of the voting rights of that company. The decision also outlines the types of governance rights or other actions by an investor that can give rise to a finding of decisive influence even in a publicly held company where a firm controls less than 50% of voting

[2] Judgment of 12 December 2012, 1. *garantovaná v Commission*, T-392/09.

rights. Given the General Court's willingness to transform the decisive influence test into a fact-specific inquiry and away from clear cut guidelines that provide certainty for investors, we expect that the Commission will consider the application of parental liability in future cases involving investors and sponsors. In light of these circumstances, this could warrant undertaking increased antitrust due diligence before acquisitions and ongoing monitoring of portfolio companies following the closing of transactions.

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