

HOW POST-MERGER DISPOSALS ALLEVIATE COMPETITION FEARS

The Competition Commission is proposing new guidelines for divestiture remedies in merger inquiries referred to by the Office of Fair Trading.

A consultation document, *Application of Divestiture Remedies in Merger Inquiries: Competition Commission Guidelines*, deals with situations where the Commission believes a merger has resulted, or may result, in a substantial lessening of competition (SLC) and the action it may require. In general, the Commission prefers structural remedies, such as divestiture or prohibition, to behavioural remedies because structural remedies generally require less monitoring or enforcement of compliance.

The risks

The consultation paper identifies three broad categories of risk that can impair the effectiveness of divestiture remedies:

- 1) Composition risks – that the scope of the divestment package may be too constrained or inappropriate to attract a suitable purchaser or to allow a purchaser to operate effectively.
- 2) Purchaser risks – that a suitable purchaser is not available, or that the merger parties will select a weak or inappropriate purchaser.
- 3) Asset risks – that the competitive capability of a divestiture package will deteriorate before completion of the sale, for example, due to loss of customers or key personnel.

Scope of divestiture packages

The Commission says that the starting point for defining a divestiture package is “identifying that minimum package of assets or substantive business which, if

successfully divested, would *prima facie* remedy the SLC”. Other assets or business segments may be added to ensure ongoing ability to compete. Merger parties may request approval for the addition of further assets to the specified package in order to secure a sale.

The Commission will generally prefer the sale of an existing business able to operate on a standalone basis, independent of the merger parties rather than the sale of a part of a business or collection of assets. If sale of a set of assets or parts of a business is proposed, the assets should all be provided by one of the merging parties. A ‘mix-and-match’ approach, combining a mixture of assets from both merging operations, is seen as increasing the risk that the divestiture package will not function effectively.

The consultation document also contains an incentive – in the form of a stick rather than a carrot – to encourage merging companies to complete required divestitures promptly. It does this by proposing that the Commission could require the merging companies to sell off some of their crown jewels – ie, a broader, more valuable group of assets – if a proposed divestiture is not completed within a specified time. However, the Commission says it will generally only consider use of such packages when other effective options are not available.

Suitable purchasers

The draft guidance stresses that the identity and capability of a purchaser is important for effective sale remedies and the Commission must approve the prospective purchaser. When assessing

suitability, the Commission will consider criteria that include:

- Independence – the purchaser should have no significant connection to the merging parties.
- Capability – the purchaser must have the necessary financial resources, incentives and access to appropriate expertise, and assets to enable the divested business to compete effectively in the market.

The Commission may require a suitable purchaser to be identified and contractually committed to the purchase up front before permitting a proposed merger to proceed. This may be the case where there is some doubt about the viability or attractiveness of a proposed divestiture package, or where there may be a limited pool of suitable purchasers. In some cases – ie, where there is a risk the divestment package could deteriorate pending the sale – the Commission may require the sale’s completion before the merger proceeds.

Effective divestiture process

The Commission states that an effective divestiture process will “protect the competitive potential of the divestiture package prior to disposal and will enable a suitable purchaser to be secured in an acceptable timescale”.

The draft guidance says the Commission will generally seek undertakings from merging companies, imposing a general duty of care to maintain the assets to be sold in good order and not to undermine their competitive position. Where the risk to the assets is seen as significant, the Commission may require ‘hold-separate’ undertakings – requiring the divestiture package to be held

and managed separately from the retained business. In this case, the Commission will normally require the appointment of an independent monitoring trustee to oversee the ongoing management of the divestiture package.

The Commission will set the timescale in which the sale of assets should take place to a suitable purchaser. If the assets cannot be sold to a suitable purchaser within this initial divestiture period, an independent divestiture trustee may be mandated to handle the disposal.

Employment of trustees

Monitoring or divestment trustees can be proposed by the merging companies, but must be approved by the Commission. Trustees must act in accordance with a trustee mandate approved by the Commission and must not accept instructions from the merging parties. A trustee may be part of an accounting firm, consultancy or other professional organisation. The Commission may set a timetable for the appointment of a trustee. Merger parties are responsible for the trustee’s remuneration, but the structure must not compromise the trustee’s independence. The Commission must therefore approve the remuneration agreement.

**Responses to the consultation are requested by 17 September 2004.*

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A wide range of Briefings can be found at www.financialdirector.co.uk/briefing

Useful links

- Details are available at www.competition-commission.org.uk/rep_pub/consultations/current/divestiture_remedies.htm