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Minority Acquisitions under Merger Control Scrutiny in Norway – Key Learnings from the Recent Sector Alarm/Nokas Case

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1. **Abstract**

In its recent decision V2018-22 the Norwegian Competition Authority ('NCA') approved – subject to remedies – the acquisition by Sector Alarm AS ("Sector") of the small systems business of Nokas AS ("Nokas") in the household alarm market and a non-controlling 49,99 % stake in Nokas.

The decision marks the first ever intervention against minority acquisitions in Norway, since the Norwegian Competition Act of 2004. It brings about several interesting learnings as regards how the NCA will approach jurisdictional issues (interrelated transactions), what competition concerns minority acquisitions may raise and introduces interesting new remedies.

2. The transactions

The transactions concerned Sector's acquisition of a part of Nokas' business named Small Systems Business pursuant to a purchase agreement dated 24 May 2018 ("**the Concentration**"), as well as the acquisition of 49,99 % of the shares in Nokas, pursuant to a share purchase agreement of 6 July 2018 ("**the Minority Acquisition**") (jointly referred to as "**the Transactions**"). The Concentration would confer 100% ownership of the overlapping small systems' business to Sector, but the Minority Acquisition would not grant Sector any control over Nokas.

Sector and Nokas are active competitors in the market for security systems to private homes and small businesses. Whereas Sector is one of the two largest players on the Norwegian alarm market, together with Verisure, Nokas is considered the third largest player on this market –significantly smaller than both Nokas and Verisure. Sector's acquisition of Nokas' Small Systems Business would marginally (< 2 %) increase the market share of Sector on the relevant product market.

3. A brief introduction to the Norwegian merger control rules

Norwegian merger control is governed by the Competition Act of 2004 (Chapter 4) and the Regulation on Notification of Concentrations of 11 December 2013. The primary enforcer is the

Norwegian Competition Authority and, as of 1 April 2017, the appellate body is the Competition Appeals Board composed of eight independent members.

The merger control rules apply to "concentrations", the same concept as found in the EU Merger Regulation (EUMR). A concentration is deemed to arise where two or more previously independent undertakings or parts of undertakings merge, or one or more persons already controlling at least one undertaking, or one or more undertakings, acquire direct or indirect control on a lasting basis of the whole or parts of one or more other undertakings (Competition Act, Section 17). A concentration must be notified to the NCA if least two of the undertakings concerned each have an annual turnover in Norway exceeding 100 million kroner and a combined turnover in Norway exceeding 1 billion kroner.

The NCA may choose to investigate transactions falling below the turnover thresholds, and require a notification if there are "reasonable grounds to assume that the competition will be affected" (Section 18 (3)). A notification order under these circumstances must be given within three months of the time of final agreement or acquisition of control, whichever is earlier. The NCA shall intervene against a concentration if it significantly impedes effective competition ('SIEC'), in particular as a result of the creation or strengthening of a dominant position and does not entail efficiencies that outweigh the losses resulting from restricted competition (Section 16).

Acquisitions of minority shareholdings that do not confer control are not subject to the mandatory merger filing requirement of the Competition Act. However, it follows from section 16a of the Competition Act that the NCA may intervene against acquisition of holdings in an undertaking even if the acquisition will not lead to control of that undertaking. According to then applicable Section 16a, the Norwegian Competition Authority (NCA) should prohibit an acquisition of holdings in an undertaking even if the acquisition will not lead to control of that undertaking "*if the acquisition will create or strengthen a significant restriction of competition contrary to the purpose of the Act*".***[1]*** An order by the NCA to submit a notification of an acquisition of a minority shareholding must be given within three months of the time of final agreement.

According to the preparatory works, this provision does not cover board or management representations as such, which are to be appraised in accordance with section 10 of the Competition Act (corresponding to article 101 of the Treaty on the Functioning of the European Union). The same presumably applies for contractual arrangements. The minority acquisition rule is a Norwegian peculiarity and is not part of the EUMR or most of the European Union Member States national merger control rules.

The Parties may notify the concentration voluntarily, even if the concentration is not subject to a filing or concerns a minority acquisition (Section 18 (6)).

4. The jurisdictional issues in the Sector case – expanding the scope?

From a jurisdictional point of view, there are two key takeaways from the Sector-case. The first concerns the issue of interrelated transactions, and the second concerns the legal threshold for intervention against minority acquisitions.

The Concentration was not subject to any merger filing requirement, since the turnover thresholds in Norway were not met, and the Minority Acquisition was not subject to any merger filing

requirement, since neither the stake nor the shareholder agreement gave Sector any (joint) control.

By an order of 24 August 2018, i.e. within the three months deadline from the signing of both the Concentration and the Minority Acquisition, the NCA ordered a filing in both transactions.

Interestingly, the NCA dealt with the Transaction together, although the Parties argued that they were separate transactions for merger control purposes, and therefore had to be dealt with consecutively on a *'first come, first serve basis'*. The NCA did not conclude as to whether two separate transactions existed for merger control purposes, but remarked that the two transactions were linked by condition upon each other, and that the interrelation between the agreements meant that the NCA "could not exclusively look at the transactions in isolation".

In the authors' view, the reasoning from the NCA on this point is opaque and vague as it seems to indicate a legal obligation to view the two transactions in combination at the same time as the NCA does not take a position to the relevant legal test, namely whether they are in fact one or two concentrations. Under the EUMR Article 3, an asset transfer agreement between buyer A and seller B cannot be considered to form part of the same concentration as the establishment of a JV between A and B, since they concern different targets, control is not ultimately acquired by the same undertaking(s) and they concern separate combination of resources, cf. European Commission's Consolidated Jurisdictional notice, para 41 and Commission case IV/M.409:[2]

"The proposed operation consists of two transactions. In one transaction, RA will transfer its flexible automation systems business dedicated to the design and integration of body work and sheet metal work (automotive body-inwhite (BIW) activities) into a newly created 100% subsidiary, the so-called Newco; ABB will acquire a 50% participation in Newco through ABB France. In the other, ABB, through ABB Robotique, will purchase the assets of the robotics business which is organised in RA's ACMA robotics business division. 4. These two operations constitute two different concentrations because the nature of the control exercised by the undertakings concerned is different for the two operations. Furthermore, the two products concerned belong to separate markets which are not in the same sector, notwithstanding the fact that robots are one of the components of transfer line systems."

Clearly, an asset acquisition between buyer A and seller B and an acquisition by A of a minority stake in B's business, could for the same and other reasons not constitute one Concentration under EUMR (since a minority acquisition does not confer control, it would not even qualify as a concentration under the EUMR). In the authors' opinion, this should be the position also under the Norwegian Competition Act. The legal corollary to this is that the Business Purchase Agreement should be considered first and irrespective of the second and subsequent Share Purchase Agreement.

Turning now to the second point, the legal threshold for intervention against non-notifiable transactions, Sector advanced the argument before the NCA – and later the Competition Appeals Board – that there must be a qualified harm to competition to intervene, and that interventions should primarily concern local competition concerns. Sector also argued that the NCA must show present evidence to make probable the harm to competition. As concerned the minority acquisition, Sector argued that the NCA at least must assess whether the transaction was liable to hinder competition competition.

The NCA held that "reasonable grounds" indicated a low threshold to order filing in a non-

notifiable transaction, and that it was not necessary to show that competition concerns were more likely than not to arise. Turning to minority acquisitions, the NCA noted that they had a large discretion ("may order") to order a filing, and that a preliminary assessment on the facts in any event had been made in this case. In the NCA's view, the minority acquisition could in principle lead to both horizontal, vertical and coordinated effects (more to this later).

The Competition Appeals Board agreed with the NCA in that the threshold to order filing in a non-notifiable transaction was not particularly high, and that the NCA enjoyed a wide margin of discretion. The crux of the burden upon the NCA when ordering a filing, was to make an individual assessment and identify a case-specific risk to competition – nothing less, nothing more. The Competition Appeals Board did not agree that interventions should largely be limited to cases exhibiting local competition concerns. Given in particular the short period of time to intervene, i.e. three months from signing or acquisition of control, the NCA – according the Competition Appeals Board – could not be subject to a high burden of proof. The need to – occasionally – order a filing, could not be fulfilled by requests for information, since requests for information did not trigger any standstill obligation and therefore risked harming the competition before any potential intervention would be decided upon.

In the authors' opinion, the NCA and the Competition Appeals Board were right in holding that there is no strict requirement to qualify any competition harm in order to justify an order to file a transaction which does not meet the thresholds or concerns a minority acquisition, and that the NCA enjoys a significant margin of discretion. The corollary of this, however, is, firstly, that the NCA ought to provide guidance to the merger markets and private parties to clarify when minority acquisitions and transactions in the SMB market raises concerns. As we shall see, below, the Sector Alarm decision offers some, but arguably still not sufficient, guiding as regards the issue of competition concerns in non-notifiable transactions. Secondly, given the wide powers resting with the NCA, the limits to the NCA's jurisdiction is all the more important. A clearer view, from the NCA, on the issue of interrelated transactions would be helpful. Also, it would be helpful that the NCA clearly and unequivocally stated that there is no competence to intervene after three months (in the Interflora/Floriss merger case from 2015 the NCA opened a phase II investigation into an acquisition of joint control, even if the filing from one of the JV-parties was submitted *after* the three months period had expired).[3]

5. The substantive issues in the Sector case – theories of harm

5.1. Overview

The NCA concluded that both the Concentration and the Minority Acquisition raised non-coordinated and coordinated competition concerns, and that the existence of the other – related – transaction bolstered the risk in both cases. The findings in the review of the Concentration are relevant to the analysis of the Minority acquisition, and we shall therefore look at the Concentration first.

5.2. The analysis of the effects of the Concentration

The NCA held that the Concentration would likely lead to a loss of competition and price increase (non-coordinated effects) post-concentration. In particular the NCA noted that:[4]

- Sector had relatively high market shares (34 % in terms of contracts and 29 % in terms of turnover), whereas Nokas had less than 2 %. In reality, the NCA held that the market shares would be higher as the Parties' estimated shares wrongly included alarms to large businesses.
- The Norwegian alarm market was a highly concentrated market (HHI of 4 444), although the NCA ignored the notifying Party's objection that the change in HHI following the transaction was only 150 (within the European Commission's "safe harbour" in the guidelines for horizontal mergers) and exhibited high margins.
- Nokas showed sign to be a sort of "maverick" with an increasing number of customers (the NCA and Sector disagreed on the data and the significance of Nokas' customer acquisition). The NCA relied among others on Nokas' internal documents in making this finding.
- The market players in the house alarm market were differentiated, which meant that closeness of competition was key to the competitive analysis. An analysis by the NCA of the content of the alarm offerings of Sector and Nokas showed that they were close substitutes and had an overlapping marketing focus, although their sales organisations had differences.
- Customer switching was used as basis for calculating diversion ratios which, in the NCA's view, supported the analysis.
- The NCA rejected Sector's point that 90 % of the customers acquired by Sector came from Verisure, and noted that the second most important "recruitment channel" was Nokas, i.e. indicating closeness of competition.
- Sector's closest competitor, Verisure, could, in the NCA's view, not sufficiently constrain any post-transaction price increase, since they would have an incentive themselves to increase price in a differentiated market, cf. the Commission's decision in Hutchison 3G Austria/Organe Austria (367).
- The barriers to entry in the alarm market were significant and market entry or expansion would not be sufficiently likely, timely, and sufficient to prevent or compensate loss of competition (costs by establishing new customer relations, national marketing, access to alarm dispatch centre and economies of scale).

The NCA also pointed towards coordinated effects post-consummation:[5]

- The market (highly concentrated, cf. above) was prone to coordination among the competitors
- The NCA held that the main competitor had large similarities in terms of costs and vertical integration and incentives to coordinate, whereas the target, Nokas, had different characteristics and less incentive to coordinate.
- The NCA pointed to the fact that prices were relatively transparent and that direct-sales (door-to-door etc.) meant that existing supplier relations would also be transparent which made coordination possible and stable.
- On the point of product differentiation (coordination is easier the less differentiated the products are), the NCA's argument is succinct and not entirely coherent; the NCA states that the market is differentiated (hence the importance of closeness of competition), and that the products are "somewhat differentiated, but relatively alike" (463). In the authors' view, this comes close to having it both ways. Further clarifications on this point would have been helpful.
- The NCA rejected the notifying Party's argument that any potential price coordination would only intensify competition on quality, and noted that the end-consumer in this case would be left with a worse-off combined quality/price offering.
- In addition to price coordination, the NCA noted that the two main competitors, Sector and Verisure had an incentive to avoid chasing one another's customers given the subsidisation of new customers and the low variable costs to serve existing customers. It should be noted in this regard that the NCA 17 June 2019 issued a statement of objections to Sector and Verisure

notifying a potential fine of NOK 425 million (Sector) and NOK 784 million (Verisure) for unlawful coordination in the house alarm market. Sector has already accepted this fine.
- The potential to punish any deviations from the coordination through targeted price reductions and/or target customer acquisition.
- The loss of Nokas' as a 'maverick', particularly prone to compete aggressively and hinder coordination, increased the likelihood of sustaining coordination.

Lastly, the NCA held that the minority acquisition (see below) increased the transparency and helped carburise a highly concentrated market, thereby decreasing the likelihood that Nokas will discipline Sector in the future.

5.3. Minority acquisition

The NCA starts out by referring to the Ministry's preparatory works and the note that the merger control rules are there to hinder potential competitive harm whether caused by the establishment of a new entity or a reduction of the incentives to compete due to acquisition of minority shares. In doing so, the NCA starts its analysis of the minority acquisition on the same facts that it analysed the Concentration, namely that the market is highly concentrated and that the Parties are close competitors in the home alarm market.

On substance, the NCA held that the minority acquisition increased Sector's market power and enabled Sector to unilaterally increase price or reduce quality of the offerings. These non-coordinated effects were found to arise on two levels. *First*, Sector would be incentivised to compete less aggressively. This would happen since parts of the lost sales in the event of a price increase would be caught by Nokas (internalised), Sector would have access to more information and would meet limited competition (close competitors and few other competitors, cf. above).[6] *Second*, Sector would be able to influence Nokas to compete less aggressively in the market. The NCA noted that this was particularly sensitive to competition, since Nokas' was a sort of 'maverick'. The shareholding (four times the number of shares as the second largest shareholder, a trust with 10,79 % of the shares), the composition of shareholders and the board representation, in the NCA's view, enabled Sector to exercise influence. This finding was made possible by the fact that there were few other competitors, barriers to entry and no buyer power. In reality, the NCA in its analysis describes a 3:2 merger (Sector, Nokas Small Systems Business and Verisure), where the acquirer now also acquires a minority stake in the potential fourth competitor (Nokas).

Interestingly, the NCA rejected Sector's argument that it is unclear whether changed incentives could justify intervention at all, since the incentives as competitor are more important than incentives as minority shareholder. Reference was made to the CMAs findings in the Ryanair/Air Lingus case. The NCA distinguished the Ryanair/Air Lingus from the Sector/Nokas case by emphasising that whilst Ryanair's minority acquisition was a "*first step in Ryanair's bid for the entirety of Aer Lingus*", Sector had not expressed any intention to acquire further shares. The incentives for Sector to dampen competition given its minority stake, would therefore be different than Ryanair's incentives.

In addition to non-coordinated effects, the NCA held that the minority acquisition would also lead to coordinated effects. *First*, the minority acquisition gave Sector an incentive to influence Nokas (not to compete aggressively against Sector). *Second*, the acquisition would give Sector privileged insight into the activities and strategies of Nokas. *Third*, the incentives for Sector to break out of a coordinated effort would decrease, since it would also need to calculate the costs and loss Nokas' if

the prices (and margins) were lowered. To be fair to the notifying party, the incentive is only a half-way incentive (49 % of the shares) and goes both ways since a break out of Sector and Nokas from the coordination would also mean that two players gain customers/turnover instead of one pre-transaction.

5.4. Concluding remarks

Against this background, the NCA did not approve the Concentration and the Minority Acquisition, and the notifying party offered remedies.

6. Remedies – a novel design

The notifying party offered substantial and multiple remedies to cater for NCA's competition concerns.

First, the notifying party committed to simply not executing the Concentration. This remedy applies to Sector and any related party (as defined in the Norwegian Limited Companies Act, Section 1-5). Second, the notifying party offered, and the NCA accepted, that it should reduce the ownership stake in Nokas from 49,99 % to 25 %. The reduction of the ownership stake should take place through redemption or amortization of shares. At the same time, Sector would be given a subscription right to the number of redeemed shares. Third, it was suggested, and accepted, that neither Sector nor any related party should acquire any further shares or exercise any subscription rights entailing an increase of the shareholding beyond 25 %. The subscription rights should be placed on a separate shareholders account monitored by an independent trustee appointed by the NCA. Fourth, the notifying party suggests to make changes in the articles of association and the shareholders' agreement limiting Sector's influence on the general assembly meetings, so that in effect Sector could not vote for more than 25 % of the shares. The remedies should apply for five years with an option for the NCA to prolong the remedies. To the authors' knowledge, it is the first time in Norway (and the other Nordic countries) that such remedies have been put in place.

An important commercial aspect of the "remedy package" was that the remedies should not affect Nokas' acquisition of 100% of the shares in Avarn Security Holding AS, a subsidiary of Sector with business in Sweden and Finland.

7. Implications for minority shareholder acquisitions and risk of intervention

The Sector/Nokas case shows that the NCA will prioritize and look into also non-notifiable concentrations and minority acquisitions, if there are national or local competition concerns. It also adds to a number of cases in which the NCA has evidenced an expansive view on jurisdiction, and underlines the message from the legislator that the threshold for ordering a filing is low and largely at the NCA's discretion. The case also falls into a general trend whereby the NCA is particularly interested in high-profile consumer deals, although by no means excluding interventions in other markets or sectors.

Note that a filing order could well happen to a foreign-to-foreign transaction. The Norwegian Competition Act applies to any agreement and transaction liable to affect competition in Norway.

Transactions involving only national or local markets outside Norway are likely deemed to fall outside the scope of the act, although no formal guidance has so far been issued, and the parties do face the risk that a customer or a competitor could approach the NCA and argue that the transaction could affect competition in Norway or in the EEA as a whole.

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[1] As of 1 July 2019, the substantive test for minority acquisitions is SIEC, i.e. the same test as with other notifiable concentrations.

[2] The decision is available here: http://ec.europa.eu/competition/mergers/cases/decisions/m409_en.pdf

[3] See press notice from the NCA of 4 December 2015: https://konkurransetilsynet.no/tillater-interflora-floriss/

[4] See the decision pp.23-55.

[5] See the decision pp. 55-74.

[6] This echoes concerns raised in the by the European Commission in its 2014 white paper "*Towards more effective EU merger control*" and in the Norwegian preparatory works Ot.prp. nr.6 (2003-2004) side 78 og Prop 75 L (2012-2013) side 121.

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