Highest EU Court Expands Presumption of Financial Investor Liability for EU Antitrust Infringements

2 February 2021

Goldman Sachs has lost its final appeal against a €37.3 million ($45.2 million) fine that it owed because one of its portfolio companies took part in a cartel. The ruling of the European Union's highest court confirms that financial investors can have parental liability for antitrust abuses by their portfolio companies. This is despite Goldman Sachs being unaware of the portfolio company's anticompetitive behaviour and the cartel actually pre-dating the fund's investment.

In 2014, the European Commission fined 11 high-voltage power cable manufacturers €301.6 million for sharing markets from 1999 to 2009. Prysmian, an Italian undersea-cable company that a Goldman fund owned until 2010, received the largest fine of €104.6 million ($127 million). The Goldman Sachs Group, Inc. was held jointly and severally liable for €37.3 million of that for its period of ownership from July 2005 to January 2009. During that time, Goldman Sachs was Prysmian's indirect parent company through GS Capital Partners V Funds, holding all of the company's voting rights (although its equity interest had gradually decreased) until 3 May 2007, the date on which Prysmian had an initial public offering on the Milan Stock Exchange. (Post-IPO the European Commission had relied on other factors to evidence Goldman's continued control.)

This recent decision of the Court of Justice of the European Union ('CJEU') is important for financial investors because it both restates the doctrine of parental liability and expands it. According to the parental liability doctrine, if a parent company (whether itself a trading entity or a mere investor) has "decisive influence" over a subsidiary, then it is jointly and severally liable with it for any penalty, on the basis that the entities together form a "single undertaking". There is a presumption of "decisive influence" for wholly owned (or near wholly owned) subsidiaries. That presumption also now applies where the parent company holds all (or nearly all) the voting rights as well as to the established position which applied to share capital.

The CJEU confirmed that *"[a] parent company which holds all the voting rights associated with its subsidiary's shares is able, like a parent company holding all or virtually all the capital of its subsidiary, to exercise decisive influence over the conduct of the subsidiary"*.

Given that Goldman Sachs solely and fully controlled the decisions regarding Prysmian, the investment bank was unable to rely on having only held a 33% interest in the relevant funds (the balance being owned by unaffiliated third-party investors), or on those funds never having owned the entirety of Prysmian's share capital. The CJEU emphasised that it is settled case law that the crucial factor is the degree of control rather than the share of ownership.

Financial investors are, therefore, liable in the same way any other corporate parent would be, despite the difference in relationship between a private equity firm and a portfolio company versus that between a subsidiary and its parent in a more "typical" corporate group. It is possible to avoid liability by successfully arguing that the holder is a "pure financial investor", but the threshold is set very high (for example, insurance companies or pension funds acquiring shareholdings solely for investment purposes).

Comparison with the United States. In the United States, limited liability for shareholders is a fundamental principle of U.S. corporate law. Distinct corporations, even parents and their subsidiaries, are presumed separate. Generally, U.S. courts must identify a basis for piercing the corporate veil before corporate parents or shareholders can be found liable. For example, the shareholder must have exercised "dominion or control" over the company such that it was acting as the shareholders' agent before a court will pierce the corporate veil. A year ago, a U.S. court confirmed this protection applied to a UK private equity firm when it was accused of participating in a price-fixing cartel through a wholly owned subsidiary. The court dismissed all claims against the private equity firm and its subsidiaries through which it owned a U.S. entity accused of price fixing. (*In Re: Packaged Seafood Products Antitrust Litigation*, 15-MD-2670 JLS (MDD) (S.D. Cal. Jan. 28, 2020).) The CJEU decision confirms that investors will not be able to rely on the same concept of the "corporate veil" in the context of EU competition infringements.

Another contrast between the EU and U.S. regimes is the method of apportioning liability between infringing companies. Although liability for fines is joint and several under both regimes, the European Commission may go a step further by dividing the total liability into specific amounts to be paid by each infringing party. In the United States, antitrust conspirators face joint and several liability for all damages caused by the conspiracy in which they participated—including the automatic treble damages provided by the federal statute—with no right to contribution from co-conspirators leaving each party individually liable for the full amount of the fine. (*Texas Industries, Inc. v. Radcliff Materials, Inc.*, 451 U.S. 630 (1981).)

Wider Significance? The European Union caps penalties for competition infringements at 10% of worldwide turnover. If the Commission concludes liability should be imputed to the financial investor, the 10% cap figure is likely to be far greater and the overall fine

higher. As an added detriment, a financial investor is also exposed to the risk of increased future fines for being a "recidivist", as the basic amount can be up to doubled for repeat infringements. For completeness, it is worth noting that some EU Member States have extended the same single-economic-unit doctrine when it comes to allowing follow-on damages claims for loss flowing from a cartel, including in one instance to private equity shareholders in a private investment company, while others have not.

The EU judgment may also have wider significance beyond competition law because the General Data Protection Regulation 2018 ("GDPR") utilises the same concept of an "undertaking" when it comes to administrative fines. European data protection authorities have confirmed in subsequent guidance that the concept of an undertaking is understood to mean an economic unit, which may be formed by the parent company and all involved subsidiaries. Currently, that concept is only used in the GDPR context to calculate the size of fines for data protection infringements and not in the attribution of liability to parent companies. It will be interesting to see whether this decision signals an expanded interpretation in future, either by courts or data protection supervisory authorities, giving investors additional reasons to be mindful of the GDPR compliance of portfolio companies. Infringements can carry severe penalties of up to the higher of 4% of an undertaking's worldwide annual turnover or €20 million ($23.2 million).

Practical Steps for Investors. The key takeaway is that financial investors will be held responsible both for conducting up-front due diligence on their prospective investments and subsequently for promoting compliance at the portfolio-company level. That is a hard message given the length of time between an initial investment decision and a case making its way through to eventual appeal when contrasted against private equity fund lives and investment cycles.

It is therefore important that investors in companies with European activities consider antitrust and data protection compliance during the due diligence process. To this end, any indication of non-compliance should be addressed using remediation plans and precisely worded indemnities. For existing investments, it is important that portfolio companies are made aware of competition and data protection rules and have systems in place for monitoring compliance. Moreover, open and honest lines of communication between the investor and the company are essential.

Strict liability for infringements under EU law means that these steps will not release investors from their responsibilities, but they should be effective to mitigate the risk of infringement.

The full decision is available here.

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