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Caught in the Act ... of Acquiring Some Shares: The Application of Merger Control Rules on the Acquisition of Non-Controlling Minority Shareholdings in Germany and the UK
by Martina Maier and Philipp Werner

Enterprises and corporate lawyers certainly know by now that they may have to go through merger control proceedings if they want to acquire “control” of another enterprise. It is also generally known that acquisitions of less-than-controlling interests may be reportable in the United States under the Hart-Scott-Rodino Act, where the notification thresholds are predicated on the dollar value of the acquisition (presently \$63.4 million), as opposed to a “change-in-control” test. But even experienced counsel are surprised that some other heavy-hitters amongst the world’s antitrust authorities may look into the acquisition even of non-controlling minority shareholdings. What is more, non-U.S. regulators such as the German Federal Cartel Office (FCO) and the UK Office of Fair Trading (OFT) may also require the divestment of such shareholdings under their respective merger control rules.

Under the German Act against Restraints of Competition (ARC), the acquisition of a shareholding of 25 percent may have to be reported to the FCO, subject only to turnover thresholds. The criterion is purely formal and the acquisition does not need to confer control to be reportable. Even below the threshold of 25 percent, the acquisition of a “competitively significant influence” is reportable. The “competitively significant influence” exists where the acquirer will be in a position to influence the target’s decision making process and market behaviour on a lasting basis and the minority shareholding can therefore be said to empower the acquirer to promote its own competitive interests. In the last few years, the FCO has aggressively applied the standard of “competitively significant influence” in a number of cases

and has no plans of scaling back the enforcement of this provision. This was the case when the FCO required A-TEC to divest all the shares it held in its rival Norddeutsche Affinerie. The FCO found that A-TEC had a “competitively significant influence” over Norddeutsche Affinerie, although its shareholding amounted to no more than 13.75 percent. The FCO states consistently that there can be no lower limit or safe harbor where a competitively significant influence could be excluded. It should be noted that Germany has a mandatory filing regime and that reportable transactions must not be implemented without the FCO’s prior approval.

Similarly, under the UK Enterprise Act 2002, if a company obtains the ability to exercise “material influence” over another company through the acquisition of a minority shareholding, this will lead to a situation that the OFT may review. “Material influence” requires less than the control standard that the EU and many other jurisdictions apply. For example, the OFT held that the acquisition by AP Møller-Maersk A/S of a 31 percent interest in DFDS A/S conferred “material influence” over DFDS A/S. The OFT’s view is that a shareholding of more than 25 percent confers “material influence” since it generally enables its holder to block special resolutions. While the UK is a voluntary filing regime, 25 percent is the threshold for when a filing is advisable. Even in the case of an acquisition of a stake below 25 percent, it is still possible for the UK regulators to find “material influence”, *e.g.* in BSkyB/ITV where the acquisition of a 17.9 percent shareholding was deemed sufficient to give “material influence.”

Currently, the OFT is investigating whether to require Ryanair to divest a minority shareholding that it had acquired in the build-up to a hostile bid for Aer Lingus. The European Commission had prohibited the acquisition of control of Aer Lingus by Ryanair under EU merger rules but had declined to order the divestment of the minority shareholding on the grounds that the acquisition of the minority shareholding was not reportable under EU merger control rules (because it did not confer control over Aer Lingus). If the OFT eventually requires Ryanair to divest its shareholding, this raises a number of interesting questions for buyers since it is common practice to acquire a minority shareholding before and while launching a bid. This acquisition of a non-controlling minority shareholding does not seem to be reportable as long as the overall acquisition (acquisition of all shares) has been notified. These questions become even more pressing in merger control regimes which - unlike the UK - have a mandatory filing regime.

Enterprises must be aware that the acquisition of a non-controlling minority stake may be reviewed under merger control rules not only in the U.S., but also in other jurisdictions such as

Germany and the UK. As the Ryanair case shows, this may even be the case if the minority shareholding was only the build up to an (unsuccessful) bid to acquire control. As the A-TEC case has shown, the thresholds for non-controlling minority shareholdings that may be reviewed by antitrust authorities may be fairly low. Considering the risk of a divestment order and a fine for gun-jumping in a merger control regime such as Germany's, enterprises are strongly advised to assess the full implications of the application of merger control regimes to the acquisition of minority shareholdings.

**Proposed DOL Regulation Would Impose Fiduciary Status On Valuation Firms:
Regulation Comment Period Closes January 20, 2011**

by Jonathan J. Boyles, Jeffrey Rothschild and Ashley J. McCarthy

The U.S. Department of Labor (DOL) recently issued a proposed regulation that would substantially expand the definition of 'fiduciary' under the Employee Retirement Income Security Act (ERISA). Under the new definition, valuation firms would, for the first time since ERISA's passage, be subject to its stringent fiduciary duties and their attendant liability. Many predict that an unintended consequence of this expanded definition could be a concerted exit from the valuation market by firms that have traditionally performed valuation services. Valuation firms will want to take action now to submit their comments on the proposed regulation before the comment period closes on January 20, 2011.

Background

Under the existing regulation, which the DOL published in 1975 shortly after the passage of ERISA itself, a firm or entity engaged to advise employers sponsoring benefit plans is only considered a fiduciary for ERISA purposes if it renders advice (1) on a regular basis, (2) pursuant to a mutual agreement and (3) if such advice serves as a primary basis for investment decisions. If a firm or entity does not satisfy all criteria, it is not considered a fiduciary for ERISA purposes and is shielded from the substantial liability that fiduciary status imposes under that law. One year after publishing this regulation, the DOL issued an advisory opinion confirming that a firm could provide a valuation of closely-held employer securities that an employee stock ownership plan (ESOP) could rely on in purchasing those securities without triggering fiduciary status. If the recently proposed regulation is adopted, it will effectively overturn this opinion and subject firms that provide such valuations to the liability exposure that attends fiduciary status under ERISA.

The Proposed Regulation and the Meaning of “Fiduciary Status” Under ERISA

Under the new regulation, a valuation firm would be considered a fiduciary if it provides (1) advice or an appraisal or fairness opinion concerning the value of securities or other property, (2) recommendations as to investing in, buying or selling securities or other property or (3) advice or recommendations as to the management of securities or other property to a plan, a plan fiduciary, or a plan participant or beneficiary. Essentially, the new regulation incorporates valuation firms into the definition of fiduciary by eliminating the requirement that advice be rendered “on a regular basis” before its provider qualifies as a fiduciary. Fiduciaries are subject to the “prudent man” rule of ERISA Section 404. The prudent man rule states that fiduciaries must act prudently and with undivided loyalty to the plan participants and their beneficiaries, subject always to the terms of the plan. The prudent person standard until trust law is a higher standard than the reasonable person standard required by many states’ corporate laws. Further, ERISA fiduciaries may be held personally liable for their breach of these duties, although similarly to Delaware corporate law, they may be exculpated from liability that results from a breach of their fiduciary duty to act prudently.

The Potential Implications of the Proposed Change

The potential implications of this change should not be underestimated. Because ERISA imposes stringent duties and potentially costly liability upon fiduciaries, persons who trigger fiduciary status typically purchase fiduciary liability insurance to protect themselves. Because valuation firms that provide fairness opinions to ESOPs have never been considered fiduciaries under ERISA, they have not had to invest in fiduciary liability insurance. If the proposed regulation passes, however, that will change. Because it will essentially require firms that provide fairness opinions to ESOPs to purchase fiduciary liability insurance and to contemplate litigation in the event they are accused of breaching a fiduciary duty, the proposed regulation could have the unintended consequence of driving experienced firms out of the ESOP valuation market. Such a concerted exit from the ESOP valuation market by firms that have long provided valuation services would likely dampen competitiveness in that market and diminish the quality of those services.

What You Can Do Now

Written comments on the proposed regulation must be submitted to the Employee Benefits Security Administration (EBSA) of DOL on or before January 20, 2011. Persons who want to

submit electronic comments may send an e-mail to e-ORI@dol.gov (enter into subject line: “Definition of Fiduciary Proposed Rule”) or use the Federal eRulemaking portal at <http://www.regulations.gov>. Persons who want to submit paper comments may send or deliver their comments to:

The Office of Regulations and Interpretations, Employee Benefits Security Administration

Attn: Definition of Fiduciary Proposed Rule Room N-5655, U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, D.C., 20210

All comments will be available to the public
at <http://www.regulations.gov> and <http://www.dol.gov/ebsa>.

The McDermott Difference

If you would like assistance in drafting and submitting your own comments, or if you have further questions about the proposed regulation and how it might affect your business, please contact [Jonathan J. Boyles](#), [Jeffrey Rothschild](#) or [Ashley J. McCarthy](#).

ION Media: Developments in Intercreditor Disputes

by Dick M. Okada and Bryan V. Swatt

With the flood of debt-heavy capital structures created over the past decade, bankruptcy courts have been left to clean up the remnants of many failed transactions. Given the volume of debt provided, courts are likely to continue to be called upon to determine the relative rights of creditors that result from multi-tiered debt structures. Consequently, it is important to examine how recent decisions have handled intercreditor disputes as today’s markets continue to loosen and financial sponsors once again have the opportunity to use various forms of subordinated debt to finance acquisitions and refinance existing credit facilities.

One issue that senior and junior lenders should be particularly aware of is the difference between lien subordination and claim subordination. Lien subordination refers to the agreement between the lenders that one party’s priority with respect to any of its liens on common collateral will be junior to any liens of the other party. This ensures that the senior lender has priority in the event

of a bankruptcy and is generally accompanied by a standstill provision, allowing the senior lender the exclusive right to foreclose on the collateral for a period of time before the junior creditor may seek to exercise its remedies. The junior lender also typically agrees not to contest or otherwise challenge the validity, perfection or priority of any liens held or asserted by the senior lender's liens, and not to take any action or vote inconsistent with the priorities established under the Intercreditor Agreement in any bankruptcy case of the borrower. Claim subordination gives the senior lender priority in connection with any unsecured deficiency claims between the lenders.

This distinction played a integral role in the Bankruptcy Court's 2009 decision in *In re ION Media Networks, Inc.* ("ION"). The documentation for the credit facility, which included an intercreditor agreement between the holders of ION's first lien and second lien debt (the "Intercreditor Agreement"), was somewhat ambiguous with respect to the definition of "Collateral." The Pledge and Security Agreement (the "Security Agreement") provided for liens to be granted on all of ION's "Collateral," specifically stating that FCC licenses were to be included in the Collateral. However, the Security Agreement also included a carve out excluding from the Collateral "special property" in which any requirement of law prohibited the creation of a security interest. The limitations imposed by Federal communications law on the granting of liens against FCC licenses arguably meant that ION's FCC licenses were "special property" excluded from the Collateral.

In an attempt to block ION's proposed Chapter 11 plan, Cyrus, a distressed debt fund that had purchased a significant amount of ION's second lien debt at a steep discount, claimed that the lien subordination language of the Intercreditor Agreement did not apply to the FCC licenses or any value attributed to them because a security interest in the FCC licenses was prohibited under federal law and therefore they did not constitute "Collateral" subject to the terms of the Intercreditor Agreement. Cyrus argued that it could oppose the Chapter 11 plan under the theory that the FCC licenses were not "Collateral," thus, since the Intercreditor Agreement did not include claim subordination provisions, its claims should be treated on a *pari passu* basis with those of the senior lender with respect to any value attributable to such FCC licenses.

In rejecting Cyrus's arguments, the court relied upon, among other things, the language of the Intercreditor Agreement that stated "that the Second Priority Secured Parties' claims against [ION] in respect of the Collateral constitute second priority claims separate and apart from . . . the First Priority Secured Parties' claims against [ION] in respect of the Collateral." Despite the

fact that this subordination language only explicitly refers to “claims ... in respect of the Collateral,” the court’s broad application of this clause led it to an intriguing conclusion.

The court held that the Intercreditor Agreement prevented the second lien lender from challenging the validity of any lien “purportedly securing” the first lien lenders claims. Despite the fact that FCC licenses were arguably not Collateral based on federal law, they fell within the category of “purportedly securing” the obligations since they were expressly included in the Security Agreement. The court also addressed public policy concerns in upholding the negotiated terms of the Intercreditor Agreement, stating that “the parties fully intended to place the Second Lien Lenders in an indisputably subordinate position and to prevent interference with the stipulated senior rights of the First Lien Lenders.” Thus, it was clear that the court preferred to broadly interpret what it termed “bargained-for rights and restrictions” over allowing a second lien creditor to disrupt a bankruptcy plan with a “technical argument.”

Lenders should be cognizant of the fact that courts may favor applying the terms of a negotiated intercreditor agreement between sophisticated parties over allowing a second lien lender (especially one that has purchased its debt at a discount) to argue an ambiguity or technicality with respect to lien or claim subordination. In taking a commercial perspective, courts may prefer upholding bargained-for terms between creditors without regard to whether their intercreditor agreement specifically addresses lien subordination, claim subordination or some variation of the two.

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