Supreme Court considers mergers in the context of the Enterprise Act 2002

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Competition analysis: Matt Evans, partner, and Marguerite Lavedan, associate at Jones Day, consider the Supreme Court's decision in Société Cooperative De Production SeaFrance SA v Competition and Markets Authority and another, and discuss what lessons can be learned from the case.

Original news

Société Cooperative De Production SeaFrance SA v Competition and Markets Authority and another [2015] UKSC 75, [2015] All ER (D) 151 (Dec)

The Supreme Court allowed the Competition and Markets Authority's appeal against a decision that no merger situation had been created for the purpose of the Enterprise Act 2002 (EnA 2002) and that there was no jurisdiction to impose remedies. It held, among other things, that, if the assets of which an acquirer acquired control were to be regarded as constituting an enterprise: (i) they had to give him more than he might have acquired by going into the market and buying factors of production; and (ii) the extra had to be attributable to the fact that the assets had been previously employed in combination in the activities of the target enterprise. Ultimately, the question turned on 'economic continuity'.

What was the factual background to this case?

SeaFrance SA, a French company, operated a ferry service between Dover and Calais until, having run into financial difficulties, it ceased operations on 16 November 2011 following an order by a French court. It was formally liquidated on 9 January 2012, and most of its employees made redundant. Some employees remained to maintain the vessels in 'hot lay-up'. In July 2012, Groupe Eurotunnel SA (GET), the parent company of the group operating the Channel Tunnel, and Société Coopérative De Production SeaFrance SA (SCOP), a workers' co-operative incorporated by a number of former SeaFrance employees to secure the continuance of the ferry service, acquired substantially all of SeaFrance's assets. These included three of the four SeaFrance vessels, trademarks, IT systems, goodwill and customer lists. GET and SCOP resumed ferry services in August 2012 through GET's subsidiary company, MyFerryLink SAS. Almost all the employees operating the vessels had worked for SeaFrance. The reemployment of those employees had been incentivised by a statutory Plan de Sauvegarde de l'Emploi (known as the PSE3), by which SeaFrance's parent company SNCF would provide payments to employers for employing ex-SeaFrance employees. In November 2012, the French competition authority considered the transaction to be a merger but cleared it subject to commitments by GET.

In the UK, the acquisition was referred to the then Competition Commission, which concluded that there was a 'relevant merger situation' for the purpose of the merger control provisions of the Enterprise Act 2002, which could be expected to result in a substantial lessening of competition in the cross-Channel market. The Commission found that the 'enterprise' of SeaFrance had continued since its 'activities' continued, even though there had been a hiatus of over seven months in its operations. In its decision dated 6 June 2013, the Commission imposed restrictions on the operation of the service by GET and SCOP, including a ban on using the ex-SeaFrance vessels for ferry services from Dover for ten years.

On appeal to the Competition Appeal Tribunal (CAT), the CAT considered that the Commission had not properly formulated the applicable test for differentiating between the acquisition of an 'enterprise' and the acquisition of a 'bare asset' and remitted the question of jurisdiction back to the new regulator, the Competition and Markets Authority (CMA), on 4 December 2013 (Eurotunnel I).

The CMA applied the CAT's guidance and concluded that what had been acquired was indeed an 'enterprise' and therefore that a 'relevant merger situation' existed. In its decision of 27 June 2014 the CMA focused on several factors, emphasising the situation of the former SeaFrance employees. GET and SCOP challenged the CMA's decision on the grounds of irrationality, but on 9 January 2015, the CAT upheld the CMA's decision (Eurotunnel II).

SCOP appealed Eurotunnel II to the Court of Appeal. The Court of Appeal upheld its appeal by a two to one majority, holding that GET and SCOP had not acquired an 'enterprise', but only the means of constructing a new (but similar) one. In particular, this was because they had not acquired SeaFrance's crews—employees had not been transferred but rather

re-employed. The Court of Appeal concluded that it was irrational for the CMA to have reached it's decision. The CMA obtained permission to appeal that ruling to the Supreme Court.

What were the key issues before the Supreme Court?

There were two main issues before the Supreme Court—the legal test and the rationality finding.

The legal test centred round the issue of whether GET/SCOP had acquired assets amounting to an 'enterprise' rather than just 'bare assets'. The developments on the rationality of the CMA's decision related to the application by the CMA of the principle set out by the CAT in Eurotunnel I, which could only be discarded by a court of review if found to be irrational. This had been the opinion of the Court of Appeal, which had held that the CMA had been irrational in finding that what had been acquired by GET/SCOP was an 'enterprise' and not only the means to construct a similar but new enterprise.

What was the significance of the Court of Appeal's decision to quash the CAT's decision?

The Court of Appeal's decision was significant for this case but of limited wider significance. In particular, it did not quash the guidance provided by the CAT in Eurotunnel I—indeed, the appeal before the Court of Appeal was not an appeal against the correctness of the judgment in Eurotunnel I, but an appeal against the CMA's application of the guidance given in Eurotunnel I to the facts. In particular, SCOP had argued that the CMA's conclusion that relevant 'activities' had been acquired was irrational. The Court of Appeal had agreed, finding that what happened was not a transfer, but a true re-employment of employees.

The Court of Appeal's judgment therefore did not invalidate the CAT's guidance in Eurotunnel I as to when the acquisition of assets amounts to an acquisition of an enterprise—although Sir Colin Rimer expressed doubts as to the Eurotunnel I judgment in an obiter dicta stating that in his view Parliament's intention was to focus only on cases where there is an acquisition of a going concern.

How did the Supreme Court approach this appeal?

As regards the legal test, the Supreme Court found that the merger control provisions of EnA 2002 are not limited to the acquisition of a business that is a 'going concern'. The possession of 'activities' is a descriptive characteristic of an enterprise under EnA 2002. An enterprise is subject to merger control if the capacity to perform those activities as part of the same business subsists (paras [32]–[35]).

In addition, the Supreme Court found that the relevant test to distinguish between 'bare assets' and assets amounting to an 'enterprise' is one of economic continuity:

'Put crudely, it depends on whether at the time of the acquisition one can still say that economically the whole is greater than the sum of its parts' (paras [40], [41]).

More specifically, the Supreme Court set out that a purchaser of assets will acquire an 'enterprise' where:

- those assets give the purchaser more than might have otherwise been acquired by going into the market and buying factors of production, and
- the extra is attributable to the fact that the assets were previously employed in combination in the 'activities' of the target enterprise

The period of time between cessation of trading and acquisition of control of the assets may be a relevant factor, but is not necessarily decisive (paras [36]–[41]). The Supreme Court noted that this was substantially the same principle which had been set out by the CAT in Eurotunnel I, and which the CMA had applied in this case.

The Supreme Court also held that the Court of Appeal's finding that the CMA's evaluation was irrational was unjustified. It noted that GET and SCOP acquired substantially all the assets of SeaFrance, including trademarks, goodwill, specialist vessels maintained in a serviceable condition, and substantially the same personnel. The CMA's conclusion that this demonstrated 'considerable continuity and momentum' and 'the members of an enterprise', which could be passed to GET and SCOP, was, in the court's view, unimpeachable. The order of the French court of 9 January 2012 to dismiss the employees did not disrupt that continuity and momentum because the order was made on terms that the PS3 preserved

the prospect of employment on the ships for the dismissed crew members (paras [41]–[43]). The majority of the Court of Appeal was wrong to narrow the question of economic continuity to the legal effect of the decision of the French court in January 2012 and whether this terminated the employment relationship between SeaFrance and its employees. That approach did not take into account the underlying economic substance of the re-employment of these ferry workers and acquisition of the assets.

Finally, the Supreme Court observed that appellate courts should exercise caution before overturning the economic judgments of expert tribunals such as the CMA and the CAT.

What are the practical implications of this decision?

The practical implications of this particular judgment are likely to be limited. The facts of this case were unusual, involving aspects of French employment and insolvency law, a transfer of employees to a third party and a seven-month period of inactivity. As the Supreme Court itself emphasised, the application of the elements of the legal test, such as economic continuity, are extremely fact dependent.

It is not news that the acquisition of a collection of assets and other factors can constitute an 'enterprise' for the purposes of EnA 2002, and the CMA often takes jurisdiction over such acquisitions—although the analysis of whether the assets acquired are an 'enterprise' does not usually lead to drawn out appeal processes, as we have seen in this case. In most cases, the CMA simply lists the collection of assets without further justification. When the CMA reviewed the acquisition by Sheffield City Taxis of certain assets and business of Mercury Taxis, its decision simply stated that the assets acquired, namely customer contracts, goodwill, information technology systems, intellectual property, business name, signs and licences, constituted an enterprise (see Completed acquisition by Sheffield City Taxis Limited of certain assets and business of Mercury Taxis (Sheffield) Limited), ME/6548-15, 13 October 2015, LNB News 25/06/2015 104). In cases where a period of inactivity preceeds the acquisition, this might change following the Supreme Court decision, as the 'economic continuity' test seems to invite the CMA not only to identify the combination of assets transferred, but also to explain how those assets contribute to the economic substance of the business. But in practice, such examples are likely to be few and far between.

Has the Supreme Court left any unresolved issues? What action should lawyers take in light of this decision?

The Supreme Court went beyond the strict question of rationality that was put before it to address the underlying question of the legal test, confirming the CAT's approach in Eurotunnel I. One might argue that the Supreme Court should have addressed in greater detail the economic continuity test and how 'the whole is greater than the sum of its parts'. But in the Supreme Court's own words, questions such as the meaning of economic continuity 'cannot be reduced to simple points of principle capable of analysis in purely legal or formal terms'.

UK lawyers have always known that the acquisition of assets could trigger a relevant merger situation under EnA 2002. This decision does not change that. It does however remind us that on the few occasions where there appears to be genuine doubt as to whether an asset acquisition triggers UK merger control, the purchaser's advisers may wish to consider the merits of a confidential discussion about jurisdiction with the CMA's mergers group before the deal completes—particularly given the deference the Supreme Court has shown to the CMA's own judgment.

Interviewed by Anne Bruce.

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