JONES DAY

COMMENTARY

JULY 2019

Transaction "Designed" to Evade Merger Control Leads to U.S. and EU Penalties

IN SHORT

The Situation: Antitrust authorities in the United States and European Union have assessed penalties and fines against Canon, and in the United States, Toshiba, for structuring a transaction to avoid premerger notification filings and the waiting period requirements.

The Result: If the European Commission's decision stands, Canon will pay more than $34 million in fines and penalties related to the transaction in the European Union, United States, and China. Toshiba will pay just $2.5 million in the United States.

Looking Ahead: Antitrust authorities around the world enforce their merger control statutes and waiting period requirements aggressively. Penalties for gun jumping (either failing to file or observe standstill obligations) are likely to grow as more jurisdictions enact premerger filing and standstill obligations, and transactions have an increasingly global dimension.

Background: The Transaction

In March 2016, Canon Inc. agreed to buy Toshiba Corporation's ("Toshiba") subsidiary, Toshiba Medical Systems Corporation ("TMSC"). According to the U.S. Department of Justice ("DOJ") complaint, Toshiba needed the sale proceeds by the end of its fiscal year, March 2016, to shore up its financial statement after financial irregularities became public. Because of this deadline, the parties found themselves without time to obtain merger control clearances before Toshiba's fiscal year ended.

To circumvent this problem, the parties executed Steps 1 through 3 in the following transaction structure in March 2016, prior to merger control filings:

- **Step 1**: Toshiba sold nonvoting equity and options in its subsidiary, TMSC, to Canon for $6.1 billion.
- **Step 2**: Toshiba and Canon formed a special purpose company, MS Holding Corporation.
- **Step 3**: Toshiba sold the voting equity in TMSC to MS Holding Corporation for $900.
- **Step 4**: Canon exercised options for TMSC voting equity.

The U.S. merger control rules provide that acquisitions of options and nonvoting securities do not require a filing under the Hart-Scott-Rodino ("HSR") Act. Arguably, the $6.1 billion that Canon paid in March 2016 for the nonvoting equity and options did not trigger an HSR filing.

> "Companies should select a transaction structure on the merits, independent of whether it leads to an HSR filing."

In April, Canon and the shell company, MS Holding Corporation, made an HSR filing related to Step 4, Canon's acquisition of the voting equity in TMSC. After receiving clearance, Canon exercised its options to acquire TMSC's voting equity for $1.

Investigations in Japan and China

In June 2016, the Japan Fair Trade Commission ("JFTC") cleared the transaction but warned the parties that their transaction structure "may be inconsistent" with Japan's premerger notification laws, without issuing a fine. The JFTC also warned the parties not to consummate future transactions in a similar structure without first submitting a premerger notification to the authority.

In January 2017, China's antitrust authority, then known as the Ministry of Commerce, or "MOFCOM," fined Canon CNY300,000 (approximately $43,000) for implementing the acquisition prior to obtaining clearance. Maximum gun jumping penalties in China are CNY500,000 (approximately $73,000), though there has been recent discussion about increasing the maximum fine. This was MOFCOM's first fine for gun jumping in a case that did not involve a company headquartered in China.

The U.S. Authorities Take Action

The HSR Act requires parties to file premerger notification for certain transactions with the DOJ and Federal Trade Commission ("FTC") and observe a waiting period prior to closing. Although many transaction structures may result in no HSR filing, parties may not structure their transaction for the specific purpose of avoiding the HSR Act.

Following an investigation, the government concluded that the parties deliberately structured the transaction to avoid HSR rules and that Canon had acquired beneficial ownership of TMSC in March 2016, long before it filed HSR and exercised the options to acquire the voting equity. The current maximum civil penalty for HSR violations is $42,530 for each day of noncompliance, which could have resulted in a maximum penalty of $6.36 million for each party. The parties settled with DOJ and will each pay $2.5 million. According to DOJ, the total penalty was less than the maximum because the parties were willing to settle and avoid litigation.

EU Follows Suit

Like in the United States, EU merger rules require that a buyer (i) notify the European Commission ("EC") of a transaction that meets jurisdictional thresholds prior to closing ("notification requirement") and (ii) not implement the transaction until it receives clearance from the EC ("standstill obligation").

The EC determined that Steps 1 and 2 (i.e., Toshiba's sale of nonvoting equity and options in TMSC to Canon for $6.1 billion and its sale of voting equity in TMSC to MS Holding Corporation for $900) formed a single notifiable merger. The EC also concluded that Canon violated EC notification and standstill requirements when it implemented Step 1.

Although the EC may impose fines of up to 10% of aggregated turnover of companies that intentionally or negligently breach the notification and/or standstill requirements, Canon's fine totaled €28 million (approximately $31.8 million). In determining the amount of the fine, the EC considered that Canon was aware of its obligations to notify the transaction and the standstill requirement, and that its breach of those obligations was, "at least, negligent." The lack of any competitive issues with the transaction and the EC's unconditional clearance mitigated the fine.

In a press release, Canon said it disagrees with the EC's analysis that it acquired control of TMSC before the EC cleared the transaction. Canon said it will appeal the decision to the General Court of the European Union in Luxembourg.

THREE KEY TAKEAWAYS

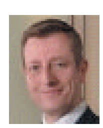
1. As noted in our Spring 2019 Global Merger Control Update, fines for gun jumping are on the rise globally, and this is the latest example. This case also demonstrates how an antitrust investigation in one jurisdiction can spread globally.

2. Cases involving a device for HSR avoidance in the United States are rare. A transaction structure designed to avoid an HSR filing, even temporarily, is likely to result in significant fines. Companies should select a transaction structure on the merits, independent of whether it leads to an HSR filing.

Michael H. Knight
Washington

Peter J. Love
Washington

Pamela L. Taylor
Chicago



Serge Clerckx
Brussels

3. While both buyers and sellers make HSR filings in the United States, in the European Union (and China), only the party acquiring control makes a filing. This explains why the European Union and China fined only Canon. As the buyer, Canon will pay substantial fines in the European Union (approximately $31.8 million) for agreeing to a transaction structure that accommodated Toshiba's need to receive the transaction proceeds early. Toshiba faces no fine in the European Union or China and a $2.5 million fine in the United States.

John W. Magruder, an associate in the Washington Office, assisted in the preparation of this Commentary.

YOU MIGHT BE INTERESTED IN: Go To All Recommendations >>

Jones Day Talks: Oversight of Foreign Direct Investment in the UK

EU's Highest Court Expands Cartel Damages Liability for Corporate Parents and Successors

EU Publishes Study on Impact of Loan Syndication on Competition

---

SUBSCRIBE SUBSCRIBE TO RSS

Jones Day is a global law firm with more than 2,500 lawyers on five continents. One Firm Worldwide®

North Point, 901 Lakeside Avenue, Cleveland, Ohio 44114-1190
www.jonesday.com