Anticipated acquisition by Carpenter Co. of the engineered foams business of Recticel NV/SA

DECISION TO REFER

ME/6986/22

The CMA's decision to refer under section 33 of the Enterprise Act 2002 given on 18 July 2022. Full text of the decision published on 5 August 2022.

Please note that [✂] indicates figures or text which have been deleted at the request of the parties for reasons of commercial confidentiality.

Introduction

1. On 6 December 2021, Carpenter Co. (**Carpenter**) agreed to acquire the engineered foams business (**REF**) of Recticel NV/SA (**Recticel**) (the **Merger**). Carpenter and REF are together referred to as the **Parties**, and for statements relating to the future, the **Merged Entity.**

2. On 4 July 2022, the Competition and Markets Authority (**CMA**) decided under section 33(1) of the Enterprise Act 2002 (the **Act**) that it is or may be the case that the Merger consists of arrangements that are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation, and that this may be expected to result in a substantial lessening of competition (**SLC**) as a result of horizontal unilateral effects in relation to the (i) supply of unconverted polyether comfort foam (**comfort foam**) in the UK, (ii) supply of unconverted technical foam (**technical foam**) in the UK, and (iii) supply of converted comfort foam in the UK (together, the **SLCs**) (the **SLC Decision**).[1] Terms defined in the SLC Decision have the same meaning in this decision on reference unless otherwise specified.

3. On the date of the SLC Decision, the CMA gave notice pursuant to section 34ZA(1)(b) of the Act to the Parties of the SLC Decision. However, in order to allow

[1] See Carpenter/Recticel case page

the Parties the opportunity to offer undertakings to the CMA for the purposes of section 73(2) of the Act, the CMA did not refer the Merger for a phase 2 investigation pursuant to section 33(3)(b) on the date of the SLC Decision.

4. Pursuant to section 73A(1) of the Act, if a party wishes to offer undertakings for the purposes of section 73(2) of the Act, it must do so before the end of the five working day period specified in section 73A(1)(a) of the Act. The SLC Decision stated that the CMA would refer the Merger for a phase 2 investigation pursuant to section 33(1), and in accordance with section 34ZA(2) of the Act, if no undertakings for the purposes of section 73(2) of the Act were offered to the CMA by the end of this period (ie by 11 July 2022); if the Parties indicated before this deadline that they did not wish to offer such undertakings; or if the undertakings offered were not accepted.

5. On 11 July 2022, Carpenter offered the CMA the following undertakings (the **Proposed Undertakings**). Carpenter would divest (i) REF's plant, assets and business in Alfreton (Derbyshire) in the UK, that supplies both comfort and technical foam (**Alfreton 1**), and (ii) REF's plant, assets and business in Alfreton (Derbyshire) in the UK that supplies converted comfort foam (**Alfreton 2**) (together, the **Divestment Business**). The divestment would take place by way of a share and asset sale of Recticel Limited.[2] Carpenter offered three separate versions of the Proposed Undertakings:

   (a) a sale and purchase agreement of the Divestment Business with no upfront buyer (**Divestment Package Version 1**).

   (b) a sale and purchase agreement of the Divestment Business with a third-party upfront buyer (**Divestment Package Version 2**).

   (c) a sale and purchase agreement of the Divestment Business with Recticel (the seller of the REF business) as the upfront buyer (**Divestment Package Version 3**).

6. The Divestment Business would include (but not be limited to):

[2] Recticel Limited is a wholly owned subsidiary of Recticel NV/SA. Recticel Limited previously comprised of an insulation foams business and a technical converting facility in Corby in the UK (in addition to the Divestment Business), both of which have been carved out of Recticel Limited into entities within the Recticel group that do not form part of the Divestment Business.

(a) production facilities and businesses in Alfreton 1 and Alfreton 2 (including leasehold and freehold properties), machinery and inventory;

(b) key operational staff of Recticel Limited;

(c) customer and supply contracts and customer lists;

(d) trademarks and brand names as well as trade names; and

(e) other certain key intellectual properties and licenses.

7. The Parties also offered a number of transitional services and supply arrangements (the **TSAs**) with the Divestment Business, including (but not limited to):

(a) information technology support services (for a period of up to six months);

(b) certain HR functions and corporate services (for a period of up to six months);

(c) training or assistance relating to the production and formulation of any foam grades resulting from the research and development (**R&D**) project seeking to replace [✂] ([✂]) (for a period of no more than six months);

(d) supply of imported technical foam produced at REF facilities outside the UK to third parties (for a period of up to one year); and

(e) consulting services in relation to the negotiation and supply of chemicals (for a period of up to six months) along with the option to provide chemicals directly to the divestment purchaser if necessary.

Assessment of the Proposed Undertaking

8. The CMA concluded in the SLC Decision that it is or may be the case that the Merger may be expected to result in an SLC as a result of horizontal unilateral effects in relation to the (i) supply of comfort foam in the UK, (ii) supply of technical foam in the UK, and (iii) supply of converted comfort foam in the UK.

9. Section 73(2) of the Act states that the CMA may, instead of making a reference and for the purpose of remedying, mitigating or preventing the SLC concerned or any adverse effect which may be expected to result from it, accept undertakings in lieu of a reference (**UILs**) to take such action as it considers appropriate. When considering whether to accept UILs in phase 1 of its investigation, the CMA has an obligation under the Act to have regard to the need to achieve as comprehensive a

solution as is reasonable and practicable to the SLC and any resulting adverse effects (section 73(3) of the Act).[3]

10. Accordingly, in order to accept UILs, the CMA must be confident that all of the potential competition concerns that have been identified in its investigation would be resolved by means of the UILs without the need for further investigation. UILs are therefore appropriate only where the remedies proposed to address any competition concerns raised by the merger are clear-cut and capable of ready implementation.[4] This clear-cut requirement has two separate dimensions:

    (a) in relation to the substantive competition assessment, the clear-cut requirement means that 'there must not be material doubts about the overall effectiveness of the remedy'; and

    (b) in practical terms, the requirement for remedies to be capable of ready implementation means that 'UILs of such complexity that their implementation is not feasible within the constraints of the Phase 1 timetable are unlikely to be accepted'.[5]

11. The CMA's starting point in deciding whether to accept UILs offered is to seek an outcome that restores competition to the level that would have prevailed absent the merger, thereby comprehensively remedying the SLC (rather than accepting a remedy that simply mitigates the competition concerns).[6]

12. The CMA generally prefers structural remedies, such as divestiture, over behavioural remedies.[7] In identifying a divestiture package, the CMA will take, as its starting point, divestiture of all or part of the acquired business, because restoration of the pre-merger situation in a market or markets subject to SLC will generally represent a straightforward remedy.[8] The CMA may consider a divestiture drawn from the acquiring business if this is not subject to greater risk in addressing the SLC.[9] The CMA will generally prefer the divestiture of an existing business, which can compete effectively on a stand-alone basis, independently of the merger parties, to the divestiture of part of a business or a collection of

[3] Mergers remedies (CMA87), December 2018 (**Remedies Guidance**), paragraph 3.30.
[4] Remedies Guidance, paragraph 3.27.
[5] Remedies Guidance, paragraphs 3.28.
[6] Remedies Guidance, paragraphs 3.27 to 3.28 and 3.30 to 3.31.
[7] Remedies Guidance, paragraphs 3.46.
[8] Remedies Guidance, paragraphs 5.6.
[9] Remedies Guidance, paragraphs 5.6.

assets.[10] This is because divestiture of a complete business is less likely to be subject to purchaser and composition risk and can generally be achieved with greater speed.[11]

13. In the present case, the CMA has material doubts that the Proposed Undertakings under each of the Divestment Package Versions 1, 2 and 3 would effectively remedy the competition concerns identified in the SLC Decision. The CMA considers that the Proposed Undertakings do not offer a clear-cut solution to the competition concerns identified in the SLC Decision for the following reasons:

(a) The Divestment Business is currently reliant on the wider Recticel group business for a number of functions, including R&D. Carpenter has offered to provide to the divestment purchaser on completion information relating to certain R&D projects which it considers to be relevant to the UK. However, the CMA is concerned that it is not clear that all relevant R&D projects have been included in the package, particularly given that details of at least one project, which the CMA considers to be highly relevant to the SLC in [✂] foam identified in the SLC Decision, were not provided to the CMA until very late in the process on 14 July 2022. The CMA notes that information provided to it on 14 July 2022 contradicted previous information provided by the Parties and it remains unclear that all relevant R&D projects have been identified. It is also not clear that information on the relevant R&D projects alone would be sufficient to allow a divestment purchaser to compete effectively. The CMA considers that a divestment purchaser may also need access to relevant personnel involved in the R&D projects, as well as potentially equipment and facilities in order to continue the planned innovation. The CMA is therefore concerned that the Proposed Undertakings would not effectively remedy the competition concerns identified in the SLC Decision, as any divestment purchaser may not have access to the necessary R&D to compete effectively going forward.

(b) The CMA is also concerned that Carpenter intends to retain rights to the information relating to the relevant R&D projects, rather than divesting such information for a divestment purchaser's sole use. The CMA is therefore concerned that the Proposed Undertakings would not effectively restore competition to the pre-merger conditions, on the basis that the divestment

[10] Remedies Guidance, paragraphs 5.12.
[11] Remedies Guidance, paragraphs 5.12.

purchaser and the Merged Entity would have the same information on key R&D projects and would therefore no longer be competing to innovate.

(c) The Proposed Undertakings consists of part of the target business, with a number of other group functions, such as chemicals purchasing, not forming part of the Divestment Business. While these functions can be replicated to some extent in the short-term through TSAs, additional risks relating to composition and implementation arise from the configuration of the Proposed Undertakings.

14. For completeness, we also note that these risks cannot be fully addressed through the purchaser approval process, in particular because of the asymmetry of information between the Parties and any divestment purchaser in relation to the identification of assets that are important for the effectiveness of the remedy package. The fact that a divestment purchaser may be willing to purchase a given package of assets does not, in itself, provide sufficient comfort that the asset perimeter is appropriate to restore the competition lost as a result of a merger, given that the incentives of the merger parties and the purchaser during the implementation period may not be aligned with those of the CMA.

15. The CMA therefore considers there is a significant risk that the Proposed Undertakings would not effectively restore competition to the level that would have prevailed absent the Merger. The CMA considers the Proposed Undertakings are not clear-cut and would not fully address the competition concerns identified in the SLC Decision. The CMA does not consider that these issues could be addressed through further modifications of the Proposed Undertakings in the phase 1 process.

Decision

16. For the reasons set out above, after examination of the Proposed Undertakings, the CMA does not believe that it would achieve as comprehensive a solution as is reasonable and practicable to the SLCs identified in the SLC Decision and the adverse effects resulting from the SLCs.

17. Accordingly, the CMA has decided not to exercise its discretion under section 73(2) of the Act to accept undertakings in lieu of reference.

18. Therefore, pursuant to sections 33(1) and 34ZA(2) of the Act, the CMA has decided to refer the Merger to its chair for the constitution of a group under Schedule 4 to the Enterprise and Regulatory Reform Act 2013 to conduct a phase 2 investigation.

Sorcha O' Carroll
Competition and Markets Authority
18 July 2022