Anticipated acquisition by T&L Sugars Limited of certain assets of Tereos United Kingdom and Ireland Limited from Tereos SCA

Observations on the Issues Statement

Introduction

1 On 26 April 2024 the CMA published its Issues Statement (the **IS**) setting out the main issues that it will consider during the Phase 2 review of the Merger.[1]

2 The IS rightly notes that the **counterfactual** will be "*a central focus*" of this inquiry.[2] It is indeed a "*central*" matter because, as the CMA highlighted already in the Issues Letter (the **IL**), "[w]*here the CMA concludes that a merging firm would exit absent the merger and there would not have been an alternative, less anti-competitive purchaser for the firm or its assets, it will* ***not*** *find a substantial lessening of competition*" (emphasis added by us).[3]

3 The counterfactual of this Merger is **straightforward** – in short, if the Merger does not proceed, the most likely competitive situation (against which the competitive impact of the Merger must be compared) does not include [✂]. This is because:

(a) The Target's business model is uncompetitive and unsustainable for Tereos. The Target has **never been a profitable business** for Tereos and is not expected to become profitable. This is simply because Tereos can sell in different markets the same volume of sugar that it sells today to the Target at a better price and with a lower cost base (i.e. [✂]) – the existence of the Target and the consequent requirement for Tereos to supply sugar volumes to the Target to enable it to compete in the UK B2C market deprives Tereos today from the opportunity to sell those volumes under much better commercial conditions;

(b) Tereos has explored all options and done **everything it could think of to make this business profitable**, unfortunately to no avail – in particular it has materially reduced its UK B2C workforce ([✂]), sold an underutilised asset (e.g., its Stallingborough terminal) and explored every possible commercial partnership(s) to generate new sources of income (incl. considering offering to pack non-sugar products (e.g. pasta) to increase the utilisation rate of its packing facilities;[4]

(c) [✂] ([✂]);

(d) For all these reasons, without a sale to TLS, Tereos is not prepared to continue subsidising the Target to compete in the UK B2C market at a very significant ongoing opportunity cost to Tereos [✂]. [✂].

[1] Unless stated otherwise we use in this Response (the **IS Response**) the same acronyms and abbreviations used to date by the CMA.
[2] Paragraph 18 IS.
[3] Paragraph 17 IL. See also paragraph 3.23 of the CMA's Merger Assessment Guidelines (**MAG**), CMA129, 18 March 2021.
[4] However, there are many factors to take into consideration for packing non-sugar products, for example the explosive nature of the product, product feed systems being compatible, introduction of allergens to site and how cross contamination would impact the Target's sugar packing operation.

[✂][5], [✂]. [✂].

4 The CMA indicates at paragraph 18 of the IS that it will "*welcome any further evidence on [its] assessment*" of the exiting firm counterfactual. Tereos has already provided extensive evidence (including "*internal documents, financial analysis*" and other documents) to demonstrate why, for Tereos the [✂] alternative to a sale to TLS is [✂]. This IS Response (incl. its Annex which addresses the counterfactual section of the CMA Phase 1 Decision) explains why this body of evidence unequivocally satisfies the exiting firm counterfactual threshold ("*most likely competitive situation*") at Phase 2.

The Exiting Firm Counterfactual Legal Test at Phase 2

5 The exiting firm counterfactual consists of a two-limbed legal test:

(a) the Target is likely to have exited (through failure or otherwise) (**Limb 1**);

(b) there would not have been an alternative, less anti-competitive purchaser for the firm or its assets to the acquirer in question (**Limb 2**).[6]

6 Whilst the CMA accepted at Phase 1 that Limb 2 of the test was met[7] it did not accept that Limb 1 was satisfied, to the standard of evidence required at Phase 1, namely that the CMA accepts that there is compelling evidence that exit was "*inevitable*".[8] In other words, and as set out in paragraph 28 of the CMA's Phase 1 Decision, if exit is one of a number of plausible options, even if it were the most likely option, it would not meet the Phase 1 standard for an inevitable exit.[9] **Annex 1** below summarises the reasons why, in Tereos' view, the CMA made the wrong decision and should have accepted at Phase 1 that the exiting firm counterfactual was the relevant counterfactual.

7 At Phase 2, the CMA (now) must decide whether or not, absent the Merger, the most likely eventuality is that Tereos [✂].[10]

8 As regards the interpretation of Limb 1, the CMA also clarified that:

(a) Strategic failure (versus financial failure) in and of it itself can be sufficient to satisfy Limb 1:

(i) In *Chemring/Wallop* (a Phase 1 decision), the CMA analysed a similar business model whereby the Target had been sustained by means of the financial support it received from being a part of a profitable corporate group and therefore carefully considered whether it had "*compelling evidence that* [the Seller] *would have chosen to wind-up Wallop for <u>strategic</u> reasons*" (emphasis added by us);[11]

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[5] As of 10 May 2024, there is [✂] (see **Annex 017 S109N2**). [✂].
[6] MAG, paragraph 3.21.
[7] See paragraph 39 IL: "*The CMA currently considers that* [✂]". [✂] is therefore not further discussed in the IS Response.
[8] MAG, paragraph 3.23.
[9] In its Phase 1 Decision, the CMA recognised that "[t]*he evidence threshold to accept an exiting firm argument at phase 1 is high*", see paragraph 37.
[10] MAG, paragraph 3.23.
[11] Anticipated acquisition by Chemring Group plc of the air countermeasures and pyrotechnics business and certain assets of Wallop Defence Systems Limited (Phase 1 decision, 29 March 2016, ME/6523/15), paragraph 82.

(ii) Similarly in *Sector Treasury Services/Butlers* (a Phase 2 decision), the CMA noted that closing a business division may "*be rational in exceptional circumstances where there are compelling strategic reasons for closure*" – in that case, the CMA also highlighted the fact that the Target was a "*non-strategic and material-business*" as it accounted for a insignificant portion of the Seller's overall revenue.

In Tereos' case, [✂][12] and the CMA accepted in its Phase 1 Decision that Tereos' internal documents had evidenced that TUKI had failed to meet its strategic objective and that exit was commercially justified on the basis of such strategic failure.[13] More generally, it is clear that the Target's revenue accounts for a minuscule portion of the Tereos Group revenue (<0.5%) which demonstrates that the Target clearly is neither a strategic, nor a material business for Tereos.

(b) The presence of more promising strategic alternatives is relevant in justifying Limb 1 of the exiting firm counterfactual test. In *Aer Lingus/Cityjet*, Cityjet's strategic shift towards its wet leasing business, on the basis of the significant losses incurred by maintaining its LCY-DUB route and the diminishing need to rely on its LCY-DUB route as a "*shop window*" for its services, was part of the CMA's determination that it had met the Limb 1 threshold at Phase 1.[14]

In this case, absent the Merger, Tereos will [✂].

9 Indeed, the findings in the CMA Phase 1 Decision support this – see below (without limitation):

(a) Paragraph 29: "*Tereos' internal documents support Tereos' submissions that the Target had not been achieving its strategic objective, which* [✂]";

(b) Paragraph 30: "*this evidence provides illustrative context that TUKI was not meeting Tereos' strategic objective*";

(c) Paragraph 38: "*The CMA recognises that the Target has not been meeting Tereos' strategic aims and that, in this context, one commercially rational decision could be to decide to exit the UK B2C market*".

Exiting the UK B2C market is [✂] therefore the "*most likely*" option for the Target

10 Tereos has provided ample evidence demonstrating why [✂].

Evidence regarding the lack of profitability of the Target

11 Tereos has historically sold, and continues to sell, sugar to the Target at price [✂]. In this regard, Tereos has provided:

[12] See Annexes 193 and 194 S109N2.
[13] Phase 1 Decision, see paragraphs 29, 30 and 38.
[14] Completed agreement between Aer Lingus Limited and CityJet designated Activity Company (Phase 1 decision, 21 December 2018, ME/6782/18), paragraphs 60 and 61.

(a) A detailed explanation of its price-setting process and how Tereos assess the profitability of the Target considering the transfer price for the supply of sugar to the Target;

(i) The price-setting paper submitted on 26 April 2024;

(ii) Responses to Q3-5 of its Response to the CMA's Section 109 dated 12 April 2024;

(iii) The Final Merger Notice submitted on 18 January 2024 – in particular paragraphs 15.15 and 15.16.

(b) Extensive [✂]…

(i) …[✂]

	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂][15]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂][16]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

(ii) …the other markets where Tereos sells refined sugar (for each financial year)

	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂][17]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

[15] Not yet finalised.
[16] See also responses to Q3-5 of the section 109 dated 12 April 2024.
[17] ibid.

	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

(c) A plethora of documentary evidence confirming Tereos' assessment that the Target is [✂] – see below a few selected examples:

(i) **Annex 141 FMN** shows that TUKI business has [✂] (see slide 23);

(ii) **Annex 148 FMN** states that [✂] (see also **Annex 165 FMN**);

(iii) **Annex 156 FMN** shows that Tereos' board has a [✂];

(iv) **Annex 159a FMN** shows that during a meeting, [✂];

(v) **Annex 163 FMN** shows that the Target is (and was) [✂];

(vi) **Annex 167 FMN** states that the Target has [✂];

(vii) **Annex 117 FMN** clearly explains that [✂];

(viii) **Annex 120 S109N2** contains [✂]; and

(ix) all documents listed in paragraph 11.6 of the Merger Notice.

(d) Up-to-date tender information showing that the Target's market position continues to worsen in the UK – as summarised in the chart below[18]. Indeed, the limited ability of the Target to compete for Tier 1 customers can be observed in its results. Since 2019, the Target has not supplied branded sugar to [✂], [✂], [✂], [✂], [✂], [✂], [✂] or [✂]. The Target's biggest customer is [✂], which has a c. [✂]% share of the grocery market in the UK. On private-label contracts, the Target only supplied [✂] until 2019. Recently, it started supplying small amounts (only [✂] tonnes) to [✂]. Moreover, the Target continues to [✂]; for example, the contracted volume with its largest customer ([✂]) was reduced by [✂]%, and [✂] ([✂])[19]. Evidence presented to the CMA

[18] Note that the discrepancy between this table and one included in paragraph 11(b)(i) is due to the latter following financial years instead of the yearly sugar campaigns. As such, the FY23/24 volumes are pushed by a stronger first half (April 2023 to September 2023), which is related to the 22/23 campaign that is depicted in the table from this section. In addition, the table included in paragraph 11(b)(i) shows volumes of white sugar only.
[19] The CMA is referred to paragraph 4.67 of the IL response for more detail.

during the Phase 1 process, including customer emails, indicates that the Target has not been able to compete effectively in procurement processes on the basis of price and due to the lack of availability of sugar[20], in turn being driven by Tereos' strategic objective of selling sugar to the Target at a transfer price above export parity and, second, for the Target to return a positive EBIT.

UK B2C Customer	Campaign 22/23 contracted volume	Campaign 23/24 contracted volume	Variance
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]
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[✄]	[✄]	[✄]	[✄]
[✄]	[✄]	[✄]	[✄]

(e) A detailed explanation of the other drivers of the Target's profitability challenges during the teach in meeting of 19 April 2024. By way of reminder these are the following:

(i) The higher transport costs faced by Tereos because of, double handling, as it must first ship sugar in bulk from France to its packing plant in Normanton and then transport the final products from Normanton to its final customers;

(ii) The operation with substantial excess capacity and the loss of economies of scale of its packing plant after a steep decrease in the packed volumes since the acquisition from Napier Brown;

(iii) The absence of synergies with Tereos France:

[20] The CMA is referred to paragraph 4.68 of the IL response for more detail, and IRL Annexes 12 – 23.

(A) Normanton is Tereos' sole asset in the UK; and

(B) Normanton is Tereos' sole packing asset not located within (or in the vicinity) of a sugar production asset.

(iv) The rise of energy costs and the difficulties in passing on these to customers, which have an unusually high countervailing buyer power;

(v) The rise of the cost of raw materials (i.e., sugar beet).

Evidence regarding the improvement measures considered and implemented by Tereos to [✄] *its UK B2C business*

12 All improvement measures considered (and implemented by Tereos – where feasible) are described in the following three key documents:

(a) **Annex FMN 163** (dated October 2021) see in particular pp. 47-51 which discuss all measures considered (and then implemented when feasible) by Tereos to improve the Target's business;

(b) **Annex FMN 161** (dated February 2022) which lists the [✄]; and

(c) **Annex FMN 163** (dated November 2022) which concludes to the failure of the measures considered and implemented by Tereos (see in particular page 10) and initiates the sale process of the Target to a third party (incl. potentially TLS).

13 By way of reminder of the measures implemented or considered by Tereos to improve the Target's business included the following:

(a) **Reduction in the Target's workforce** (as shown in the chart below) – [✄].

[✄]

(b) **No replacement of TUKI B2C MD** – when TUKI's General Manager ([✄]) resigned, Tereos did not replace him but asked its Business Planning & Margin Optimisation head based in Paris to run the TUKI business (from Paris);

(c) **Reduction of the shift numbers of TUKI's packing line** (from 3 to 1);

(d) **Sale of a underutilised asset** (TUKI's Stallingborough terminal);

(e) **Transfer TUKI's packing operation** of 5 and 25 kg bags to its French facilities and ultimately halt non-profitable products (incl. 25 kg bags);

(f) **Leverage TSF assets in France and outsource part of the production**. This option has been considered by Tereos but ultimately abandoned for the following reasons:

(i) [✄].

[✄]	[✄]	[✄]	[✄]	[✄]	[✄]

[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

(ii) [✂].

(iii) [✂].

(g) [✂];

(h) **Purchase sugar from local producers or traders.** This option has been considered by Tereos but ultimately abandoned for the following reasons:

(i) Pursuing this alternative would have departed from Tereos' core business model and was inconsistent with the rationale for which the Target was acquired from Napier Brown. As a cooperative, Tereos' mission is to get the most value from the sugar that its farmers produce, not to sell sugar procured from third parties.

(ii) Notwithstanding the previous issue, Tereos' management still explored two options:

(A) <u>Local producers</u> [✂].

(B) <u>Sugar trader</u>: [✂].

(i) **Co-pack sugar for third party competitors**. [✂]. [✂]. [✂]. [✂]. [✂]. [✂].

(j) **Other improvement measures have also been considered** as showed in **Annex FMN 150.**

14 However, as repeatedly explained to the CMA, while some of these measures may have improved the cost base of the Target, none of these measures has succeeded in materially shifting, for Tereos, the dynamic of the Target's fundamentally uncompetitive and unsustainable business model or outcomes. Tereos is not prepared to continue to lose money by extensively subsidising the Target's business model, [✂] if the Merger does not proceed.

Evidence of Tereos' [✂]

15 Tereos' Board took a unanimous decision on 13 February 2024 that [✂]. This decision is not related to the [✂].

16 This decision has been [✂] and therefore constitutes genuine and compelling evidence of [✂]. This decision confirms the decision that was implicitly taken soon after December 2020, [✂].

17 The [✂] was based on:

(a) [✄]; and

(b) [✄].

18 Further evidence of Tereos' [✄].

Sensitivity exercise for the Oxera counterfactual net present value evaluation

19 During the site-visit session with Tereos, there was one question regarding the sensitivity exercise for the Oxera counterfactual net present value evaluation. More precisely, the question was about how the business [✄].

20 Regarding the increase of profitability through higher volumes, [✄]. [✄].

21 This sensitivity testing is included in the attached addendum to the Excel Annex to the Oxera note (**Annex 2**). Tab 'Indifference analysis' includes the underlying calculations for the graph that was presented during the meeting at the CMA on 19 April.

Conclusion

22 In conclusion, it is submitted that there is ample, compelling evidence (as summarised above) to support the proposition that both limbs of the exiting firm counterfactual are satisfied in this case. [✄].

* * *

Annex 1

Response to the counterfactual section in the CMA's Phase 1 Decision

1 Although the CMA recognised that a decision to exit could be one commercially rational decision on the basis that the Target has not been meeting Tereos' strategic aim on the basis of its being consistently unprofitable and declining volumes,[21] the CMA concluded that it had not seen compelling evidence that the exit of the Target was inevitable absent the Merger i.e., the CMA concluded that Limb 1 of the exiting firm framework was not satisfied.[22] The CMA therefore proceeded to assess the Merger under the prevailing conditions of competition i.e., on the basis that the Target would have continued to compete in the supply of packed sugar to B2C customers in the UK.

2 Tereos highlights three key issues in the CMA's assessment in the Phase 1 Decision:

Misplaced reliance on the November 2022 Board Presentation and Board Minutes

3 In its Phase 1 Decision, the CMA accepted that Tereos' internal documents support Tereos' submissions that the Target had not been achieving its strategic objective, [✂].[23] The CMA also noted that "[the] *accumulated loss figures submitted by Tereos are consistent with the figures and statements the CMA has seen in a number of internal documents that suggest that selling through TUKI had not been profitable in this context*."[24] Notwithstanding that the CMA considered that "*deciding to exit could be one commercially rational option on the basis of its being consistently unprofitable* [✂]", the CMA considered that it was "*not possible to infer that exit is inevitable from Tereos' documents*" and that "[s]*everal documents indicate that Tereos' outlook was becoming more positive for the Target by the time it decided to initiate the sales process in November 2022*".[25]

4 Tereos submits that the CMA both excessively and erroneously relied on the November 2022 Board Presentation and Board Minutes (FMN Annexes 161 and 162) to support the propositions that there are still several options open [✂], and that there had been a degree of improvement in the Target's business. During this board meeting, the Tereos board decided to start the process of selling TUKI [✂]. The contents of both the Board Minutes (FMN Annex 162) and the Board Presentation (FMN Annex 161) largely support this decision:

(a) Tereos' board minutes of November 2022 (Annex 162) – see e.g.:

(i) [✂];

(ii) [✂]; and

(iii) [✂].

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[21] Anticipated acquisition by T&L Sugars Limited of the UK packing and distribution site and business-to-consumer activities of Tereos United Kingdom and Ireland Limited from Tereos SCA (Phase 1 Decision, 8 March 2024, ME 7074/23), paragraphs 29, 30 and 38.
[22] ibid, paragraph 38.
[23] ibid, paragraphs 29, 30 and 38.
[24] ibid, paragraph 30. These internal documents were produced prior to the Meger and the decision to sell the Target.
[25] ibid, paragraph 30.

(b) Tereos' board presentation of November 2022 (FMN Annex 161) – see e.g.:

(i) See page 3: 2022 [✂]; and

(ii) On page 18, the presentation explores the possibility of [✂].

5 The CMA clearly placed too much weight on a handful of isolated, out-of-context and overly optimistic statements included in the November 2022 Board Presentation and Board Minutes that go against the overall tenor of the totality of the documents themselves. [✂], Tereos submits that the CMA's reliance on these documents to support the propositions set out in paragraph 4 above was misplaced.

A large number of documents establishing the Target's lack of profitability were ignored

6 In reaching its conclusion that Limb 1 of the exiting firm framework was not satisfied, the CMA ignored numerous internal documents submitted to the CMA which clearly establish the lack of profitability of the Target over time, including the following:

(a) FMN Annexes 131-136 showing [✂];

(b) FMN Annex 165 containing [✂]; and

(c) FMN Annex 142 which refers to [✂] (see page 22);

(d) Annex 156 contains the minutes of another [✂];

(e) Annex 160 contains the minutes of the [✂].

Insufficient weight placed on the Oxera counterfactual net present value report detailing the current and projected profitability of the Target, [✂]

7 In its Phase 1 Decision, the CMA did "*not consider the Oxera Analysis to provide compelling evidence that the Limb 1 test is met*" on the basis that the CMA did "*not consider that it would be appropriate to substitute its own assessment from that of senior stakeholders responsible for the business*" as "[t]*he test the CMA must apply is not whether the CMA in the position of executives of the company might have chosen to exit the market, but rather whether a strategic exit was inevitable absent the merger*".[26]

8 Tereos submits that the further evidence on the exiting firm counterfactual prepared by Oxera provides cogent and compelling empirical evidence to support Tereos' submission that [✂].

9 As this analysis is backwards-looking, Oxera did an exercise to calculate [✂]:

(a) [✂];

(b) [✂].

[26] ibid, paragraph 34.

10 Both of these scenarios – [✂] – are highly unlikely, [✂].

11 Notwithstanding that the Oxera counterfactual net present value report was not produced prior to the Merger and the decision to sell the Target, [✂]. [✂].