



Jersey Competition Regulatory Authority ('JCRA')

Decision M820/11

PUBLIC VERSION

Proposed Acquisition

of

Virtustream C.I. Limited

by

Mr Julian Box

The Notified Transaction

1. On 21 November, the JCRA received an application (the “**Application**”) under Articles 20 and 21 of the *Competition (Jersey) Law 2005* (the “**Law**”), seeking the JCRA’s approval of the proposed acquisition by Mr Julian Box (“**Mr Box**”) of 100% of the issued share capital in Virtustream C.I. Limited (“**Target**”), a wholly owned subsidiary of Virtustream Inc. (“**Vendor**”).
2. The JCRA published a notice of its receipt of the Application in the Jersey Gazette and on its website on 24 November 2011, inviting comments on the proposed acquisition by 8 December 2011. No comments were received.

The Parties

(a) The Vendor

3. The Vendor is registered in the state of Delaware in the United States of America (“**USA**”) and is owned by institutional investors and senior members of its management. Columbia Capital Corporation, also registered in Delaware, is a venture capital fund, and owns [REDACTED]% of the shares in the Vendor. [REDACTED] owns 16.8%, while no other individual entity owns more than 10% of the share capital. The Vendor holds its interest in the Target through a company registered in Jersey, Virtustream Limited. As such, the actual transferor of the shares in the Target will be Virtustream Limited.
4. The Vendor and its subsidiaries (including the Target) (together, “**Vendor Group**”) provide IT services, such as the delivery of strategic IT infrastructure designs, incorporating servers, storage, networking, systems management and business continuity, using both traditional and virtual based technologies (“**Virtualization Services**”). According to the Application, virtualization is a broad term that refers to the creation of abstract and/or emulated computer platforms. In addition, the Vendor Group also supplies hardware and software.
5. The Vendor has no presence in Jersey, save as a consequence of its ownership of the Target. The Vendor does own other businesses operating in the information technology industry in the USA, United Kingdom and Ireland.

6. For the financial year ending 31 December 2010, the worldwide turnover of the Vendor Group was \$[REDACTED] (approximately £[REDACTED]) and its turnover in Jersey was £[REDACTED].

(b) Mr Box

7. Mr Box is a private individual who is currently employed by the Target and is a shareholder of the Vendor. He was the principal vendor when the Vendor acquired the Target (VirtualizeIT Limited, as it was then known) in 2009¹.

(c) The Target

8. The Target was incorporated by Mr Box, in his capacity as its founder, in Jersey in 2001. As part of a group re-organisation, it was acquired by the Vendor in 2009. The proposed acquisition involves Mr Box buying back the Target for a consideration of £[REDACTED]. On completion, it is proposed the Target will be renamed Calligo C.I. Limited.

9. Under the transitional arrangements described in paragraphs 25-30 below, the Target will assume the obligations that exist under contracts between clients and the Vendor, and will provide the services on behalf of the Vendor between completion and 31 December 2012, whereupon these arrangements will terminate.

10. For the financial year ending 31 December 2010, the Target's worldwide turnover was £[REDACTED] and its turnover in Jersey was £[REDACTED].

The Requirement for JCRA Approval

11. Under Article 20(1) of the Law, a person must not execute certain mergers or acquisitions except with, and in accordance with, the approval of the JCRA. According to Article 2(1)(b) of the Law, a merger or acquisition occurs for the purpose of the Law if a person who controls an undertaking acquires direct or indirect control of the whole or part of another undertaking.

12. The proposed acquisition involves Mr Box acquiring control of the Target as defined under Article 2(1)(b). The parties applied for JCRA approval of the proposed acquisition on the basis that the Vendor Group is likely to have a share of 40% or

¹ JCRA Decision M338/08, 7 January 2009

more in the supply of Virtualization Services within Jersey and therefore the acquisition falls within the conditions of Article 4 of the *Competition (Mergers and Acquisitions) (Jersey) Order 2010* (the “**Order**”).

13. On the basis of these facts, pursuant to the Order and Article 20(1) of the Law, the JCRA’s approval is required before the proposed acquisition is executed.

Assessment

14. Under Article 22(4) of the Law, the JCRA must determine if the proposed acquisition would substantially lessen competition in Jersey or any part thereof, pursuant to the procedures set forth in the JCRA’s *Guidelines for Mergers and Acquisitions*.²
15. The JCRA has concluded that the proposed acquisition will not substantially lessen competition in Jersey or any part thereof, for the reasons set out below.

Defining the affected relevant market(s)

(i) The Relevant Product Market(s)

16. ‘A relevant product market comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products’ characteristics, their prices and their intended use’³.
17. In the absence of any evidence of potential horizontal, vertical or conglomerate effects, the transaction will not give rise to a substantial lessening of competition in any potential product markets. Accordingly, the JCRA has not sought to analyse the product market(s) within which Virtualization Services are provided, but has accepted the parties’ contention that the relevant product market comprises Virtualization Services.

(ii) The Relevant Geographic Market

18. The relevant geographic market is, stated simply, the area in which competition takes place.

² JCRA (2010), *Mergers and Acquisitions*, at page 6.

³ *European Commission Notice on the definition of the relevant product market for the purposes of Community competition law*, O.J. C 372 at 2 (9 December 1997)

19. In the Application, the parties state that the geographic scope of the relevant market is the Channel Islands, as the Target only provides Virtualization Services in Jersey and Guernsey.
20. For the purpose of this Decision, the JCRA need not make a definitive determination of the extent of the relevant geographic market, given the absence of any substantive effects on competition arising from the proposed acquisition. The JCRA has therefore proceeded on the basis that the relevant geographic market is the Channel Islands.

Effects on competition

21. As noted in paragraph 12 above, the obligation to apply for the JCRA's approval of the proposed acquisition arises by virtue of the share held by the Vendor Group in the supply of Virtualization Services within Jersey.
22. However, Mr Box is not engaged in the provision of Virtualization Services, except in his capacity as an employee of the Target. In addition, there is no other horizontal or vertical overlap between the parties' activities, because Mr Box does not have any investments in entities that are active in relevant markets or connected to customers, suppliers or competitors of the Target or the Vendor. The Vendor does not have any presence in Jersey, other than through its ownership of the Target.
23. As such, the JCRA has concluded that there is no basis for concluding that the proposed acquisition would substantially lessen competition in any relevant markets in Jersey.

Ancillary Restraints

24. Under European Union competition law, so-called 'ancillary restraints' – agreements that do not form an integral part of the asset or share transfer but are considered to be 'directly related and necessary to the implementation of the concentration' – are subject to analysis as part of the review of the relevant merger.⁴

⁴ See *Commission Notice on restrictions directly related and necessary to concentrations*, O.J. C 56/03 paragraphs 1 and 10 (5 March 2005). Article 60 of the Law requires that, so far as possible, matters arising under competition law in Jersey are treated in a manner that is consistent with the treatment of corresponding questions arising under competition law in the European Union.

25. The Application notes that, in addition to the Share Purchase Agreement (“SPA”),⁵ it is contemplated that a Services Agreement will be entered into between the Target and the Vendor, which records the terms on which the Target will continue to provide support services, including out of hours and helpdesk support, to fourteen clients of the Vendor based in the Channel Islands.
26. Clause 7.1 of the SPA and clause 8 of the Services Agreement contain a number of restrictions on the activities of Mr Box and the Target, including non-compete and non-solicitation covenants applying for a period of one year. Applicable European Commission (“EC”) guidance states that non-competition and non-solicitation clauses for periods of up to two years are justified when the proposed acquisition includes the transfer of goodwill, and for periods of up to three years when the proposed acquisition includes the transfer of both goodwill and know-how.⁶ However, the guidance stipulates that such clauses will only be regarded as “necessary to implementation of the concentration” where they restrict the activities of the vendor, not the purchaser:
- “In general terms, the need for the purchaser to benefit from certain protection is more compelling than the corresponding need for the vendor. It is the purchaser who needs to be assured that she/he will be able to acquire the full value of the acquired business. Thus, as a general rule, restrictions which benefit the vendor are either not directly related and necessary to the implementation of the concentration at all, or their scope and/or duration need to be more limited than that of clauses which benefit the purchaser”⁷.
27. Given that the non-compete and non-solicitation covenants in the SPA and Services Agreement restrain the activities of the purchaser, not the vendor, the JCRA has decided that they are not necessary to the implementation of the proposed acquisition, and so are not covered by the JCRA’s approval of the proposed acquisition under Article 22(1) of the Law.

⁵ Subject to JCRA approval, it is proposed that Mr Box will acquire the entire issued share capital on 31 December 2011.

⁶Footnote 4 at paragraph 20.

⁷ Footnote 4 at paragraph 17.

28. In circumstances where non-compete covenants are not directly related to a concentration, and so are not otherwise justifiable, they could be construed as market sharing provisions, which may constitute restrictions of competition by object. However, it should be noted that the covenants in this case appear to relate mainly to the parties' activities outside the Channel Islands. In the JCRA's view, the question of whether Article 8 of the Law proscribes the parties from giving effect to these provisions should be considered outside the terms of this Decision.
29. Under the Services Agreement, the Target will also supply transitional services to existing clients of the Vendor, and will be paid a fixed monthly fee until December 2012 by the Vendor to cover the cost of the support services being provided. The client contracts will be assigned to the Target, to the extent permitted by their respective terms,⁸ and all such client contracts will be serviced by the Target.
30. Applicable EC guidance states that purchase and supply obligations aimed at guaranteeing the product previously supplied can be justified for a transitional period of up to five years.⁹ The JCRA has concluded that, following this EC guidance, the supply obligations in the Services Agreement are ancillary to the proposed acquisition and justified for the period up to 31 December 2012.

Conclusion

31. The JCRA concludes that the proposed acquisition will not substantially lessen competition in Jersey or any part of Jersey. Given this conclusion, the JCRA hereby approves the proposed acquisition under Article 22(1) of the Law.

19 December 2011

By Order of the JCRA Board

⁸ All the contracts are on 12 month terms and will renew at various points during 2012. Where clients renew their support contract during 2012, delivery of the support work will be sub-contracted to the Target for the balance of the contract term.

⁹ See *Commission Notice on restrictions directly related and necessary to concentrations*, O.J. C 56/03 (5 March 2005), paragraph 33.