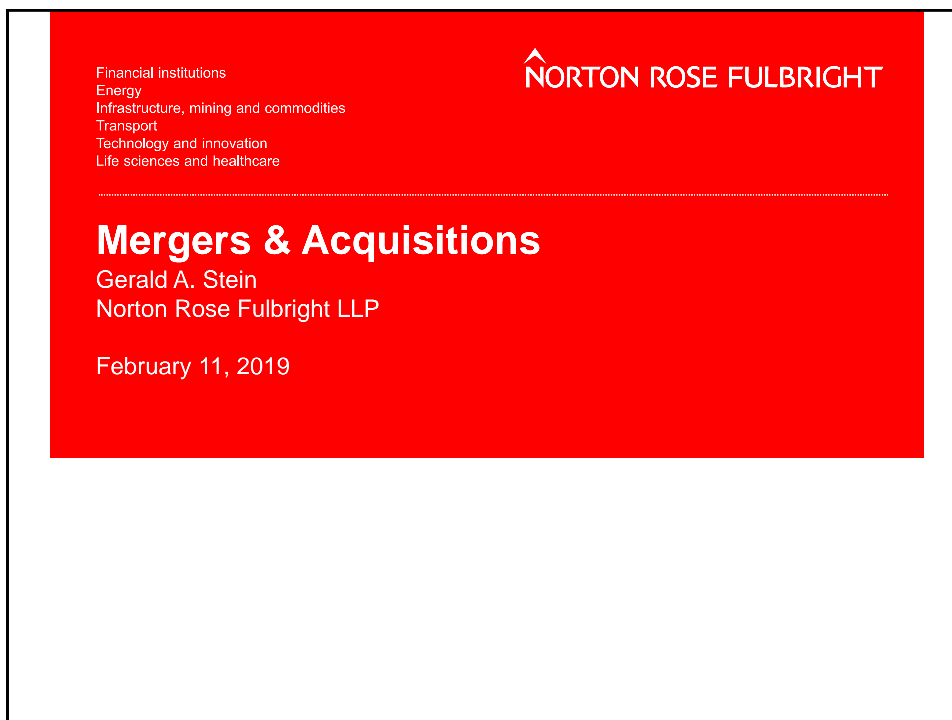
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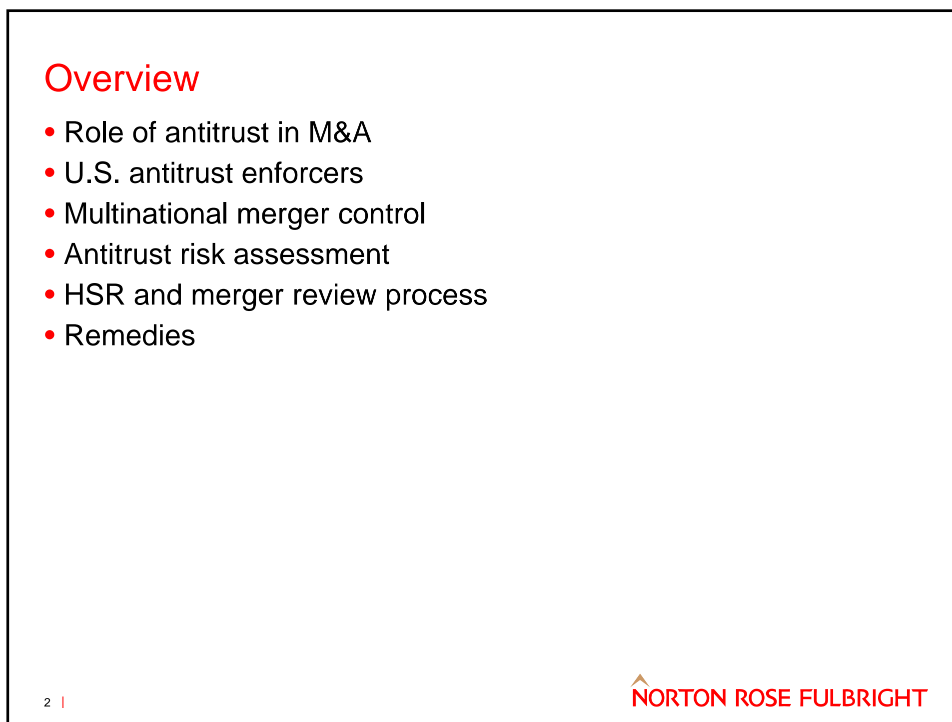
Mergers & Acquisitions
Gerald A. Stein
Norton Rose Fulbright LLP
February 11, 2019


Overview
• Role of antitrust in M&A
• U.S. antitrust enforcers
• Multinational merger control
• Antitrust risk assessment
• HSR and merger review process
• Remedies
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Role of antitrust in M&A

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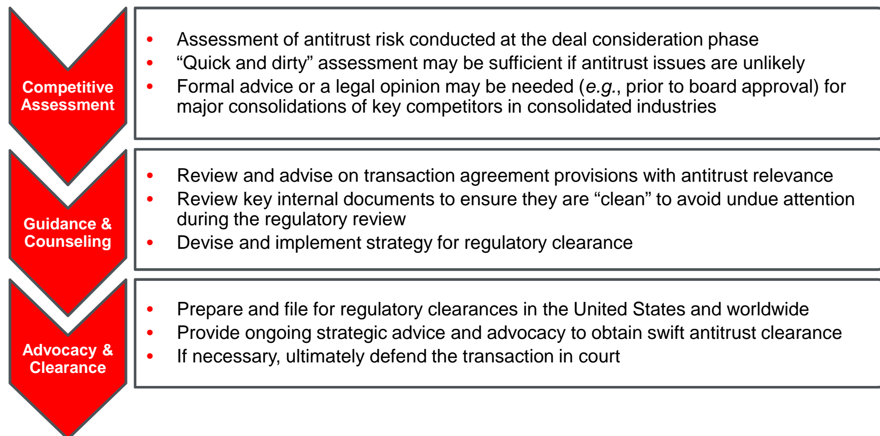
Antitrust Plays An Important Role In M&A

- Antitrust counsel provide guidance and counseling through all phases of a transaction, from deal consideration through antitrust clearance and closing



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U.S. antitrust enforcers

Enforcement Agencies – Department of Justice (“DOJ”)

- Led by Assistant Attorney General for Antitrust
  - Nominated by President, confirmed by Senate
  - Primary responsibility for enforcement decisions
- Responsible for civil and criminal enforcement
  - Shares responsibility with FTC for civil enforcement, including merger review
- Enforcement actions require filing in federal court

- Deputy Assistant Attorneys General

Enforcement Agencies – Federal Trade Commission ("FTC")

- Five commissioners
  - Staggered terms, no more than three commissioners from the same political party
  - Majority vote of a Commission required for any enforcement action
- Bureau of Competition responsible for antitrust enforcement
  - Director manages FTC investigatory teams
- Enforcement is administrative action with federal appellate court review
  - FTC must seek injunctive relief in district court pending administrative review

DOJ/FTC Share Merger Enforcement Responsibility

- When required, HSR filings are submitted to the FTC and DOJ
  - "Clearance" process then determines which agency will review a particular case
  - Agencies have established practices for some industries:
    - DOJ: beer, telecom, airline travel
    - FTC: chemicals, retail, energy
  - Some filings result in clearance fights, in a worst case the reviewing agency is not assigned until very late in the 30-day waiting period

- DOJ and FTC routinely investigate consummated transactions
  - If no HSR filing is required there is no statutory waiting period before a transaction can close, but the agencies can still open an investigation
  - Investigation may even occur after HSR clearance
  - Where a transaction has closed, DOJ/FTC may seek divestitures to resolve antitrust concerns ("unscrambling the eggs")

Risk Assessment

Clayton Act § 7

- Provides the U.S. antitrust standard for mergers

No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

- Simple summary: Prohibits transactions that—
  - may substantially lessen competition or create a monopoly
  - in any line of commerce (product market)
  - in any part of the country (geographic market)

“Tend To Substantially Lessen Competition”

- Transaction threatens to hurt an **identifiable set of customers** through:
  - Increased prices
  - Reduced product or service quality
  - Reduced rate of technological innovation or product improvement
  - (Maybe) reduced product diversity

Theories of Anticompetitive Harm—Major Theories

- Elimination of horizontal competition among current rivals
  - *Unilateral effects*: Merger of uniquely close competitors
  - *Coordinated effects*: Merger of significant competitors where customers have few realistic alternatives
  - Examples: *Ardagh/Saint-Gobain* (glass containers); *Office Depot/OfficeMax, Staples/Office Depot*
- Vertical harm—Major in EU/gaining traction in U.S.
  - Foreclosure of competitors (upstream or downstream)
  - Raising costs to rivals
  - Anticompetitive information access
  - Examples: *Google/ITA, St. Luke's/Saltzer* (private litigation, input foreclosure)

So How Do You Assess Substantive Antitrust Risk?

- Recall that the purpose of merger antitrust law is to prevent the creation or facilitation of market power to the harm of customers in the market as a whole through—
  - Increased prices
  - Decreased product or service quality
  - Decreased rate of technological innovation or product improvement
  - [Maybe] decreased product variety[1]

Absent compelling evidence of significant customer harm from other sources, only price increases count

  - Economic theory not well-developed in predicting—
    - Consequences of transaction for nonprice market variables
    - Consequences of changes in nonprice market variables for consumer welfare
  - Implication: Need strong direct evidence to proceed on a theory other than a price increase

[1] Recognized as a dimension of anticompetitive effect in the 2010 DOJ/FTC Merger Guidelines.

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So How Do You Assess Substantive Antitrust Risk?

- Critical substantive questions
  - Are prices likely to increase postmerger?
  - Are the merging companies strong and uniquely close competitors with one another?
  - How many other effective competitors does each merging party have?
  - Do customers play the merging parties off of one another to get better prices or other deal terms?
  - How high are barriers to entry, expansion, and repositioning?
    - What are the gross margins for the overlapping products of each of the merging parties?[1]
  - Is the rate of innovation or product improvement likely to decrease postmerger?
  - Will the merged firm discontinue a product or product family?
    - If so, how will this affect current and future customers in the space?
    - If so, do the companies have a plan to support legacy products?[2]

[1] If high premerger gross margins did not precipitate entry, expansion, or repositioning, then a slightly higher margin due to a postmerger anticompetitive price increase is not likely to precipitate this type of market correction either.
[2] Concern about legacy product support is often a primary cause of customer complaints about a pending transaction.

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So How Do You Assess Substantive Antitrust Risk?

- Critical substantive questions (cont'd)
  - What is the business model behind the transaction?
    - What does the business model say about likely competitive effects?
    - How does the buyer expect to recoup any premium paid for the target?
    - Is there a procompetitive rationale for the merger?
      - That is, an explanation that makes customers as well as shareholders better off as a result of the transaction?
  - What are the operational plans for the combined company?
    - Fixed cost savings?
    - Marginal cost savings?
    - Product line integration and migration plans?
    - Changes in investment or direction of R&D activities?

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How Do You Assess Substantive Antitrust Risk?

- Economic and Factual consistency on the critical questions
  - Do the concomitant business documents support the economic theories?
- Important sources of evidence for the DOJ/FTC
  - Business documents
    - Strategic plans, marketing, emails, board/executive presentations
  - Business data (especially win-loss data)
    - Sales data
  - Interviews and depositions of company witnesses
  - Interviews and depositions of customers
  - Industry analyst and interviews
  - Competitor interviews

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Developing the Defense

- The best way to assess the substantive risk is to develop the defense
- Structure of the initial presentation of a complete defense
  1. The parties and the deal
     - Brief overview of the merging parties
     - Brief overview of the deal (including terms, timing, and conditions precedent)
  2. The deal rationale
     - Ideally, a rationale that both makes the deal in the profit-maximizing interest of the acquiring company's shareholders and interest of customers ("win-win")
     - Include any cost, cross-marketing, or product development deal synergies
  3. The market will not allow the deal to be anticompetitive
     - This is equivalent to saying that customers can protect themselves from harm if the merged firm sought to act anticompetitively

The best defense is a good offense

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The Procompetitive Argument

- *Key*: Reconcile the profit-maximizing interest of the acquiring firm's shareholders with the interest of customers

- Menu of customer benefits
  - Lower costs of production, distribution, or marketing make merged firm more competitive
    - Elimination of redundant facilities and personnel
    - Economies of scale or scope
  - Complementary product lines
    - Broader product offering desired by customers
    - Better integration between merging products further enhances customer value

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The Procompetitive Argument

- Menu of customer benefits (cont'd)
  - Accelerated R&D and product improvement
    - Greater combined R&D assets (researchers, patents, know-how)
    - Complementarities in R&D assets
    - Greater sales base over which to spread R&D costs
  - Better service and product support
    - More sales representatives
    - More technical service support

The Not-Anticompetitive Argument

- *Key*: Customers will not get hurt even if the merged company attempts to act anticompetitively
  - *Usual argument*: Customers will have sufficient alternatives to the merged firm—from incumbent, repositioned, or new competitors or from vertical integration—to protect themselves from an anticompetitive effect
- Defense menu in horizontal transactions (in decreasing order of strength)
  - Parties do not compete with one another
  - Parties compete only tangentially
  - Parties compete but have significant other close and effective competitors
  - Parties do compete, have few existing competitors, but movement into market
    - is easy (no barriers to entry or repositioning), and
    - would occur quickly if merged company acted anticompetitively
  - Some other reason deal is not likely to harm customers

How Many Effective Competitors[1] Are Enough?

5 → 4
- Good case for clearance unless there is/are:
  - Significant customer opposition, or
  - Bad documents

4 → 3
- Close case but can clear with:
  - a strong procompetitive justification
  - significant customer support and little customer opposition, and
  - no bad documents

3 → 2
- Usually challenged, but can clear with:
  - a compelling procompetitive justification,
  - strong customer support and no material customer opposition, and
  - no bad documents

2 → 1
- Always challenged; no efficiency defense

[1] Critically, "effective" competitors are those that the customers regard as substitute suppliers that they to which they would readily switch without harm in the event that the merged firm acted anticompetitively postmerger. "Fringe" firms are usually disregarded.

Assessing the Defense—Exacerbating Factors

- "Hot" company documents
  - Suggest the merging companies are close competitors of one another in some overlapping product
  - Suggest that there are few realistic alternatives to merging firms
  - Suggest that business model behind transaction is anticompetitive (e.g., higher prices, reduced innovation)
- Customer complaints
  - Generally about price
  - The merging companies are close competitors of one another in some overlapping product
  - Customer "plays" the companies off one another to get better prices
  - Insufficient number of realistic alternatives to preserve price competition post-merger
  - *Customer conclusion*: Customer will pay higher prices as a result of the merger

Assessing the Defense – Other considerations

- High market shares
  - Not helpful
  - BUT not decisive if sufficient alternatives exist
- Effect on competitors
  - In U.S., irrelevant unless it hurts customers
  - BUT one of the best predictors of enforcement action in the EU
- Efficiencies
  - Heavily discounted by enforcement agencies
  - BUT important to provide a procompetitive deal motivation
- High visibility deals that threaten significant job loss
  - Explains some Obama administration enforcement decisions (e.g., NASDAQ/NYSE)

HSR Filings & Merger Review Process

Hart-Scott-Rodino ("HSR") Filing Requirement

- HSR Act of 1976 requires that the parties to transactions that meet certain size requirements must:
  1. Notify the DOJ/FTC by filing an HSR form
  2. Pay a filing fee (of between $45,000-$280,000), and
  3. Observe a 30-day waiting period before closing the transaction
- Rule of thumb: If as a result of the transaction the acquiring party will "hold" voting securities, assets, or "non-corporate interests" valued at $76.3 million or more, a filing may be required
  - Value of current holdings must be aggregated with value of interests to be acquired, net of any debt being paid off ("size of transaction")
  - Formation of new entities or joint ventures may require a filing
  - Apply "size of person" test for transactions smaller than about $300 million: one party must have assets/sales >~$152 million, the other must have assets/sales >~$15 million – otherwise no filing is required

Unless An Exemption Applies…

- HSR statute and regulations include a long list of exemptions that specify when no HSR filing is required
- Commonly applicable exemptions:
  - Exempt assets: non-U.S. assets, cash, real estate, certain inventory
  - Foreign voting securities if the company has <$76.3 million in U.S. sales/assets
  - Acquisitions of any voting securities if the company holds <$76.3 million in non-exempt assets ("look-through")
  - "Intra-person" acquisitions
  - Acquisitions for "investment-only"
- HSR regulations are extremely technical and assessing whether a filing is required and/or whether an exemption applies can be very complicated
  - FTC has an office dedicated to answering filing-related questions (the Premerger Notification Office, or "PNO")

HSR Item 4(c) and 4(d) documents

Item 4(c)

- Documents that were prepared for both:
  - By or for officers or directors, ultimate parent entities
  - For the purpose of evaluating or analyzing the transaction
    - Markets/market shares
    - Competition/competitors
    - Sales growth/expansion into product or geographic markets

Item 4(d)

- Confidential information memoranda
- Bankers' books
- Third-party consultants' materials
- Synergies documents

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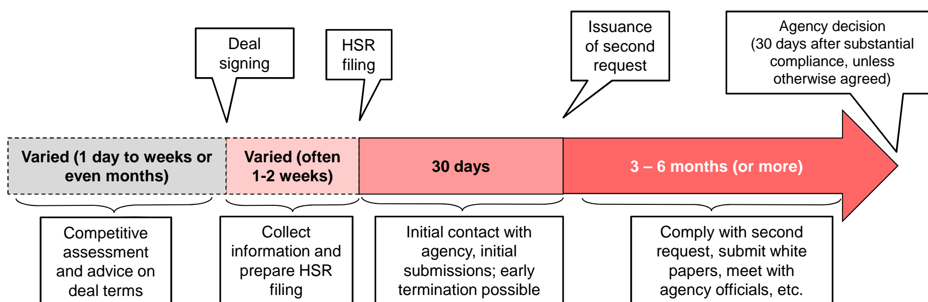
Typical U.S. Merger Review (HSR) Timeline



- Timeline tends to be longer for complicated or unique transactions
  - Parties may "pull and re-file," resulting in a new 30-day waiting period
- If a Second Request is issued, the DOJ/FTC staff that is investigating will frequently seek a timing agreement to allow additional time

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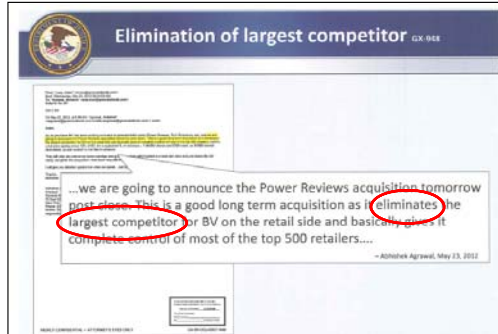
Advocacy During 30-Day Waiting Period

- If the DOJ/FTC staff identify questions or concerns about the transaction, they will contact antitrust counsel
  - Staff may issue voluntary requests for information, e.g., customer names and contact details, additional sales/share data, or additional internal documents ("ordinary course" documents)
- Staff will make recommendation on whether to issue a Second Request
- Company documents are often a key factor in triggering (or avoiding) a Second Request

DOJ Opening Statement In *Bazaarvoice/PowerReviews* (2013)



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Second Requests Are Costly And Burdensome

- Broad requests for "all documents" (broadly defined) …and all data

6. Submit all documents discussing the company's or any other person's plans relating to any relevant product [service], including, but not limited to, business plans; short-term and long-range strategies and objectives; budgets and financial projections; expansion or retrenchment plans; research and development efforts; plans to reduce costs, improve products [services], introduce new products [services], or otherwise become more competitive (*e.g.*, plans to close, consolidate or rationalize any facility identified in response to specification 4, or to discontinue the manufacture or sale of any product or product line [provision of any relevant service]); and presentations to management committees, executive committees, and boards of directors. For regularly prepared budgets and financial projections, the company need only submit one copy of final year-end documents and cumulative year-to-date documents for the current year.

7. Submit all documents relating to competition in the manufacture or sale of each relevant product [provision of each relevant service], including, but not limited to, market studies, forecasts and surveys, and all other documents relating to:

(a) the sales, market share or competitive position of the company or any of its competitors;

(b) the relative strength or weakness of companies producing or selling each relevant product [providing each relevant service];

(c) supply and demand conditions;

(d) allegations by any person that any company that manufactures or sells any relevant product [provides any relevant service] is not behaving in a competitive manner, including, but not limited to, customer and competitor complaints, threatened, pending, or completed lawsuits; and federal and state investigations; and

(e) any actual or potential effect on the supply, demand, cost, or price of any relevant product [service] as a result of competition from any other possible substitute product [service].

D. The term "documents" means all written, recorded, and graphic materials and all electronic data of every kind in the possession, custody, or control of the company. The term "documents" includes electronic correspondence, drafts of documents, metadata, embedded, hidden and other bibliographic or historical data describing or relating to documents created, revised, or distributed on computer systems, and all duplicates of documents (whether or not identical) in the files of or in the files maintained on behalf of all directors, officers, managers, or other supervisory employees, duplicates of documents in all other files that are not identical duplicates of the originals, and duplicates of documents the originals of which are not in the possession, custody, or control of the company. The term "documents" includes spreadsheets, as well as underlying cell formulae and other codes. The term "documents" also includes electronic mail messages and other documents and data stored in, or accessible through, computer or other information retrieval systems, such as personal computers, portable computers, workstations, minicomputers, personal data assistants, archival voice storage systems, group and collaborative tools, electronic messaging devices, portable or removable storage media, mainframes, servers, backup disks and tapes, archive disks and tapes, and other forms of online or offline storage, whether on or off company premises. Unless otherwise specified, the term "documents" excludes bills of lading, invoices in non-electronic form, purchase orders, customs declarations, and other similar documents of a purely transactional nature and also excludes architectural plans and engineering blueprints.

11. Submit a useable copy of each database or data set identified in response to specification 10, any accompanying data dictionary, and any software product or platform required to access the database or data set. For each database or data set identified in response to specification 10 that contains cost or margin information, submit one copy of each regularly produced (no more frequently than in four week periods) report generated using that database since January 1, **[Yr-3]**, and any documentation that defines, describes or explains the calculation in any terms, measures, or aggregations appearing on the materials provided.

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Documents, Data, Information, And Testimony

- Massive request for information, much like a subpoena, sent to both parties
  - Companies must certify "substantial compliance"
  - Response typically takes 3-4 months, although can be faster or slower
- Document requests
  - Burdensome and costly review process – often involves 30-40 custodians, 2-3 years of data, possibly millions of documents, although subject to negotiation
  - Attorneys interview custodians, review documents for responsiveness and privilege
- Written Interrogatories
  - Counsel works closely with the parties to draft responses
  - Data: Often work with economists and business people to respond
- Deposition testimony
  - Depositions of key business personnel, relying heavily on internal documents

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Advocacy During Second Request Compliance

- Antitrust counsel work closely with the parties and the DOJ/FTC to answer any questions and address any concerns
- Advocacy takes multiple forms:
  - Customer outreach
    - Communicating merits of transaction and addressing any customer concerns
    - Obtaining customer support for transaction, possibly including letters or even sworn declarations
  - Legal advocacy
    - Formal and informal interaction with agency
    - Preparation for depositions of key personnel
    - White papers and presentations
  - Economists
    - Parties may hire economic consultants to engage with DOJ/FTC economists
    - White papers and presentations

Company documents used extensively throughout

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Timing Agreements

- Merger investigations commonly involve timing agreements that provide an agreed-upon framework for the timing of certain steps in the investigation.
- Timing agreements are typically negotiated shortly after the issuance of Second Requests
  - Provides certainty during and after the Second Request period
  - Parties will agree not to close the proposed transaction until (usually) 60 to 90 days following certified compliance (rather than 30 days under HSR)
  - Parties will agree to provide notice before certifying compliance and notice before consummating the proposed transaction.

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FTC Model timing agreements

FTC's Review Period: 60-90 days after the parties substantially comply with the Second Request before the parties may close the transaction

30-Day Notification Requirement: parties agree to provide 30 days "pre-notification" before both certifying substantial compliance and before closing.

Custodians: final custodian list within five days of execution of the timing agreement.

Mandatory TRO Stipulation and Prohibition on Declaratory Judgment Actions: parties stipulate to a temporary restraining order and agree that they will not seek a declaratory judgment on the merits of the transaction.

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DOJ Model Timing Agreement

DOJ Review Period: parties give DOJ 60 days from the time the parties substantially comply with the Second Request before the parties may close the transaction

10-Day Notification Requirement: requires that the parties give DOJ 10 days' notice prior to closing.

Custodians: DOJ will seek documents from no more than 20 custodians, and DOJ reserves the right to add up to five additional custodians

TROs and Prohibition on Declaratory Judgment Actions: parties agree to refrain from consummating the deal if DOJ is going to challenge it and to refrain from closing for at least seven days following entry of judgment by the court.

Why would I agree to give the agencies more time?

- Parties are not required to enter into a timing agreement.
- However, in practicality, if parties do not agree to the timing agreement, the agency will proceed as if it must be in court to block the deal within 30 days of compliance.
- Therefore, it will prepare for litigation and will not consider settlement options or engage with the parties on the issues in the same way it would if the agency had more time under a timing agreement.

Possible Outcomes: Clearance, Remedy, Or Challenge

- Agency conducts investigation while parties comply with Second Request
- Substantial compliance with the Second Request puts the ball in the agency's court – 30 days to close investigation or take action
  - DOJ/FTC may seek additional time – by implementing or extending any existing timing agreement

Outcome	Description	Impact on Closing
Unconditional clearance	▪ DOJ or FTC terminate the HSR waiting period or allow the HSR waiting period to expire ▪ Could occur in the first 30 days, while the parties are responding to a Second Request, or after compliance with the Second Request	▪ Parties are free to close
Remedy	▪ Parties negotiate a settlement with the agency that provides antitrust clearance, subject to conditions (such as divestitures of assets/businesses) ▪ May require appointment of a trustee	▪ Varies, but closing may be allowed immediately subject to the remedy – *e.g.*, divestiture to be completed within 120 days ▪ Conduct remedy typically immediate
Court challenge	▪ Procedure varies by agency ▪ DOJ files a complaint in federal district court, likely with a motion for preliminary injunction ▪ FTC files an administrative complaint, but may seek a preliminary injunction in federal district court	▪ Closing delayed until court challenge resolved or any injunction is lifted ▪ If no injunction is issued, parties are free to close at risk

Remedies

Predicting Remedies—Horizontal

- Almost always require the sale of a complete “business”
  - Agency: Essential to the effectiveness/viability of the solution
  - *Exceptions*:
    - Divestiture buyer has necessary infrastructure and limited divestiture assets will enable rapid and effective entry into divestiture business
    - Divestiture assets are commonly traded (e.g., grocery stores)
  - Will permit “trade up” solutions
    - Buyer may sell its own business in order to purchase a larger business
  - *Everything* associated with the divested business must go
    - Agency will negotiate exclusions
    - But must be convinced that the exclusions will not undermine the effectiveness or viability of the solution

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Predicting Remedies—Vertical

- To remedy foreclosure concerns
  - Non-discriminatory access undertakings (e.g., FRAND commitment in *Bosch/SPX*, content licensing in *Comcast/NBCU*)
  - Undertakings to maintain open systems to enable interoperability (e.g., EU undertakings in *Intel/McAfee*)
- To remedy anticompetitive information access
  - Information firewalls (e.g., restrictions on access in *Google/ITA* and *Comcast/NCBU*)

> “Conduct relief also may be required to remedy the anticompetitive effects of a vertical merger. Such conduct relief may include a requirement to erect firewalls to protect confidential information or a requirement not to favor certain entities.”
> – *Negotiating Merger Remedies*, FTC, January 2012

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Negotiating Remedies

- Where remedies are likely, antitrust counsel can assist in early planning
  - Identification of divestiture package and likely buyers
  - Remedy must completely eliminate competitive concerns and agency must approve, but there is scope for negotiation
- "Fix it first" vs. consent decree/order
  - "Fix it first" – Parties unilaterally eliminate any competitive concerns, in advance
  - "Buyer up front" – Consent decree requiring identification of a divestiture buyer (and possibly completion of the divestiture) before closing the main transaction
  - Consent decree/order – Consent decree allowing main transaction to close, but subject to requirement that divestiture occur within a set timeframe (*e.g.*, 120 days)
- A divestiture is a separate transaction and can take significant time/resources
  - Related reporting/monitoring can last many months (or even years)

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