
CLASS 4 SLIDES

For September 12, 2019

Unit 3: The DOJ/FTC Merger Review Process

Merger Antitrust Law

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Premerger Notification

Failure to file

■ Violation

- Failing to file an HSR report and observe the waiting period requirements in a reportable transaction

■ Two scenarios

1. Failure to file at all

- Intentional failure to file
- Inadvertent failure to file
- Improper invocation of an exemption (usually the investment exception)

2. Make an insufficient filing

■ Prosecutorial discretion

- Vigorous enforcement for intentional failures to file
- “One-bite” rule for inadvertent failures to file
 - No enforcement action on first failure
 - Enforcement actions on subsequent failures
- Filing of an insufficient report requires a corrective filing
 - Restarts the waiting period
- Varies with culpability in invoking exemption

“Gun jumping”

■ Violation

- The FTC takes the position that a person has a beneficial interest in the voting securities or assets of the target company within the meaning of the HSR Act when the person can **exercise a material degree of management influence** on the current (preclosing) operations of the target
 - Especially decisions regarding how to compete in the marketplace
- Exercising this influence prior to the end of the waiting period is called “gun jumping”
 - Violates the HSR Act, regardless of effect on competition, because, for HSR Act purposes, the acquiring company has acquired the target without observing the waiting period—subjects the acquiring company to a civil penalty of \$42,530 per day (in 2019)
 - May also violate Section 1 of the Sherman Act if the influence creates an anticompetitive effect in the marketplace (e.g., the coordination of bids by merging competitors)
 - The acquiring person cannot violate the HSR Act after the waiting period has expired, but it can still violate the Sherman Act if the transaction has not closed

Initial Waiting Period Investigations

Preliminaries

- Parties must file their respective HSR forms with both the DOJ and the FTC
 - Separate forms are required for each reporting person
- FTC Premerger Notification Office review
 - Only for technical compliance on form—no review of substance
 - Allocated to DOJ or FTC for review through agency “clearance” process
 - Responsible agency assigns to litigating section for substantive review

“Clearance”

- DOJ and FTC decide which, if either, of the agencies will do the investigation (“clearance”)
 - “Liaison agreement” between DOJ and FTC prevents duplicative investigations
 - If neither DOJ nor FTC want to open a preliminary investigation—PNO grants early termination of the waiting period
 - If DOJ or FTC (but not both) want to open a preliminary investigation—Requesting agency gets clearance to open investigation
 - If both DOJ and FTC want to open a preliminary investigation—Agencies negotiate to allocate the investigation based on prior experience with the industry or the merging parties (and which agency got the last contested clearance)
 - Process can be fraught with strategic behavior by agencies
 - In extreme cases, “clearance battles” can last until the last day of the initial waiting period
 - Efforts to reform “clearance” process by allocating specific industries to specific agency have failed miserably
 - Neither agencies nor their respective congressional oversight committees want to relinquish jurisdiction over any type of merger

Initial contact by investigating staff

- Usually occurs 7-10 days after filing
- Three purposes
 1. Inform parties of the investigation and introduce the investigating staff
 2. Request that the parties provide certain information to the staff on a voluntary basis—
 - Most recent strategic, marketing and business plans
 - Internal and external market research reports for last 3 years
 - Product lists and product descriptions
 - (Perhaps) competitor lists and estimates of market shares
 - Customer lists of the firm's top 10-20 customers (including a contact name and telephone number)¹
 3. Invite the parties to make a presentation to the staff on the competitive merits of the transaction

¹ The agencies do not ask for customer lists in transactions involving consumer goods sold at retail.

Initial merits presentation

- Critical to do completely, coherently, and quickly
 - Often a large “first mover” advantage in being the first to give the staff a systematic way to think about the transaction
 - Well-prepared business people are the best to present
 - Agencies not impressed with “testifying” lawyers—especially outside counsel
 - Need to anticipate and answer staff questions
 - Need to clear and compelling
 - Cannot win on an argument that the staff does not understand or finds ill-supported
 - Need to anticipate and be consistent with what the staff is likely to hear from customers
 - Staff is strongly biased to accepting customer view in the event of an inconsistency
 - Need to do quickly
 - By the time of the initial call from the investigating staff, one-third of the initial waiting period will be over

The best presentations anticipate all of the issues the staff will raise, provide answers that are supported by company documents and consistent with customer perceptions, and have all of the facts right. Ideally, the rest of the investigation needs to do no more than defend the analysis of the first presentation.

Initial merits presentation

- Ideal structure (when the facts fit)
 1. Provide an overview of the parties and the transaction
 - Identify other jurisdictions in which the transaction is reportable
 - Provide an overview of the industry (if the staff is not familiar with the industry)
 2. Explain the business model driving the transaction
 - Essential to give a compelling reason for doing the deal that is not anticompetitive
 - The deal is procompetitive—a win-win for the company and the customers
 - Identify the customers benefits implied by the business model
 3. Explain why market conditions would not allow the transaction to be anticompetitive in any event
 - “We could not raise price even if we wanted. Customers have alternatives to which they can turn to protect themselves in the event we try to raise price or otherwise harm them.”
 - Alternatives can be other current suppliers, firms in related lines of business that can expand their product lines, new entrants, or customer self supply (vertical integration)

Customer interviews by staff

- Occupies the bulk of the remaining time in the initial investigation
- Customer views are given great weight
 - *Theory*: The purpose of the antitrust laws is to protect customers from competitive harm, and sophisticated customers should have a good idea of whether they will be competitively harmed by the transaction under review
 - Staff will attempt to call all of the contracts on the customer lists provided by the merging companies in response to the initial voluntary request
 - Staff often will accept customer complaints uncritically but question customer support
 - Customer reactions may differ depending on the position of the contact person
 - The CEO may take a broader and more nuanced view of the transaction than a procurement manager

Competitor interviews by staff

- Competitor conclusions are given little weight
 - *Theory*: Anticompetitive transactions are likely to benefit competitors, so competitor complaints are more likely the result of concerns about procompetitive efficiencies than anticompetitive effect
 - But competitor interviews can be useful in understanding more about the industry
 - Complaining competitors are often willing to spend considerable time educating the staff
 - Customers usually just want the staff to go away unless they strongly oppose the deal

End of the initial waiting period

■ Three options for the agency

1. Close the investigation
2. Issue a second request

■ Most important factors—

- ❑ Incriminating company documents
- ❑ Significant customer complaints
- ❑ Four or less competitors postmerger for horizontal transactions (5→ 4 deals)
- ❑ Merging parties are uniquely close competitors to one another (“unilateral effects”)
- ❑ Merger eliminates a “maverick”
- ❑ Elimination of a probable and significant potential entrant into a highly concentrated market
- ❑ Obvious significant foreclosure possibilities (for vertical transactions)

NB: Any one of these factors can be sufficient to trigger a second request investigation

■ A second request must be authorized—

- ❑ By the assistant attorney general (typically delegated to a deputy assistant attorney general)
- ❑ By the Federal Trade Commission (typically delegated to the chairman or a commissioner)

3. Convince the parties to “pull and refile” their HSR forms to restart the initial waiting period

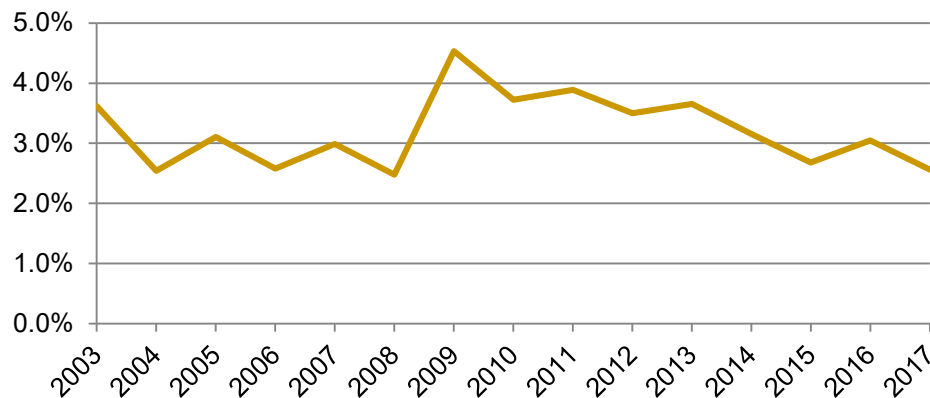
- Typically used when the initial investigation to date indicates no problem but requires a short additional time to complete customer interviews
- The agency usually grants early termination in the middle of the second initial waiting period

Second Request Investigations

The second request

- HSR Act authorizes investigating agency to issue one request for additional information and documentary material (a “second request”) during the initial waiting period to each reporting party
- Issuance of a second request extends waiting period until—
 - All parties comply with their respective second requests, and
 - Observe a final waiting period (usually 30 days) following compliance
 - 10 days for all cash tender offers

Percentage of Eligible Transactions Receiving Second Requests



Source: Fed. Trade Comm'n & U.S. Dept. of Justice, Hart-Scott-Rodino Annual Report Fiscal Year 2017, at App. A.

Second request investigations

- **Second request**
 - **Blunderbuss request**
 - If you can only ask once, ask for everything
 - DOJ and FTC each have “model” second requests, but typically customized with additional specifications
 - **Typically takes 6-16 weeks to comply**
 - Often covers 60-120 custodians
 - Agencies are making meaningful efforts to reduce this number—target 30-35
 - Interrogatories, including:
 - Detailed sales data (CRM database)
 - Bid and win/loss data
 - Requirements for entry into the marketplace
 - Rationale for deal
 - Document requests, including:
 - Business, strategic and marketing plans
 - Pricing documents
 - Product and R&D plans
 - Documents addressing competition or competitors
 - Customer files and customer call reports
 - Covers e-mail and other electronic documents
 - Non-English language documents must be translated into English

Second request investigations

- Depositions of business representatives of parties
 - Often 3-5 employees for each party
 - Often senior person knowledgeable about U.S. sales and competition for U.S. customers
 - Can include sales representatives for key accounts
 - R&D directors (if R&D is important to defense)
 - In Washington
 - Can be compelled
 - Civil Investigative Demand (CID) by the DOJ
 - Subpoena by the FTC
 - Transcribed and under oath
 - Typically each lasts 6-8 hours
- Documents and testimony from customers and competitors
 - Testimony will be memorialized in a sworn affidavit
- Expert economic analysis
 - By experts retained by the parties
 - By agency experts
 - Or, in investigations where litigation is foreseeable, by outside experts retained by agency

Final waiting period

■ Timing

- Begins when all parties have submitted proper second request responses
- Ends 30 calendar days later
 - 10 days in a cash tender offer
- Parties often voluntarily “extend” the final period¹
 - Provides additional time for agency to complete investigation
 - Usually better than being sued!
 - May be necessary to complete meetings
 - May be necessary if a consent decree is being negotiated

■ “Timing agreements”

- Agencies like to negotiate “extensions” early in a second request investigations so that they know how much time they have before the deal can close
- Typically will accept 60 days beyond the normal expiration of the waiting period
 - 30 days for the staff (making a total of 60 for the staff after second request compliance)
 - 30 days for the front office
- Technically a contract, but real effect is more of an estoppel

¹ Surprisingly, many members of the bar believe that you can voluntarily extend the waiting period. The FTC’s position, however, is that the waiting period is set by statute and cannot be extended by agreement, although the parties can commit by contract not to close the transaction before a certain time. This has significant implications for “gun-jumping” violations, which cannot occur after the waiting period has ended.

Merger Review Outcomes

The final arguments

- Formal meetings at the end of the investigation

| | DOJ | FTC |
|---|--|--|
| 1 | Investigating staff | Investigating staff |
| 2 | Section Chief & staff | Assistant Director & staff |
| 3 | Deputy Assistant Attorneys General (legal and economics) | Directors meeting (Bureau of Competition/ Bureau of Economics) |
| 4 | Assistant Attorney General | Five FTC Commissioners (meet individually) |

- Numerous informal meetings can occur up the chain at the end of the investigation
- *Critical question:* How much of its analysis will the investigating staff disclose to the parties?

Possible outcomes in DOJ/FTC reviews

Close investigation

- Waiting period terminates at the end of the investigation with the agency taking no enforcement action, or
- Agency grants early termination prior to normal expiration

Litigate

- DOJ: Seeks preliminary and permanent injunctive relief in federal district court
- FTC: Seeks preliminary injunctive relief in federal district court
Seeks permanent injunctive relief in administrative trial

Settle w/consent decree

- Typical resolution for problematic mergers
- DOJ: Consent decree entered by federal district court
- FTC: Consent order entered by FTC in administrative proceeding

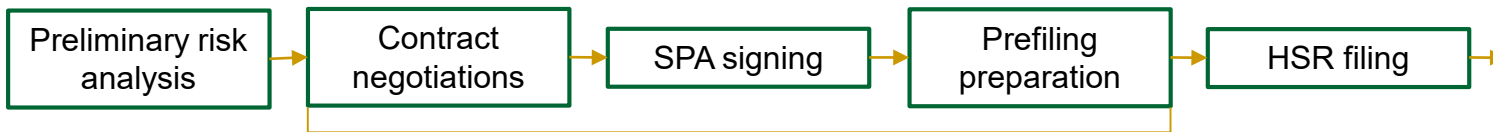
Parties terminate transaction

- Parties will not settle at the agency's ask and will not litigate, or
- Agency concludes that no settlement will resolve the agency's concerns and the parties will not litigate
 - Examples: AT&T/T-Mobile, NASDAQ/NYSE Euronext

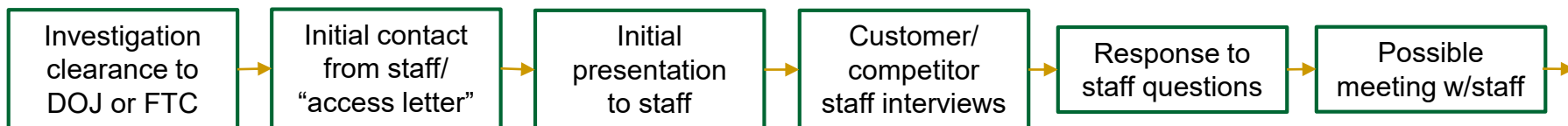
The HSR Review Process: A Summary

The HSR review process

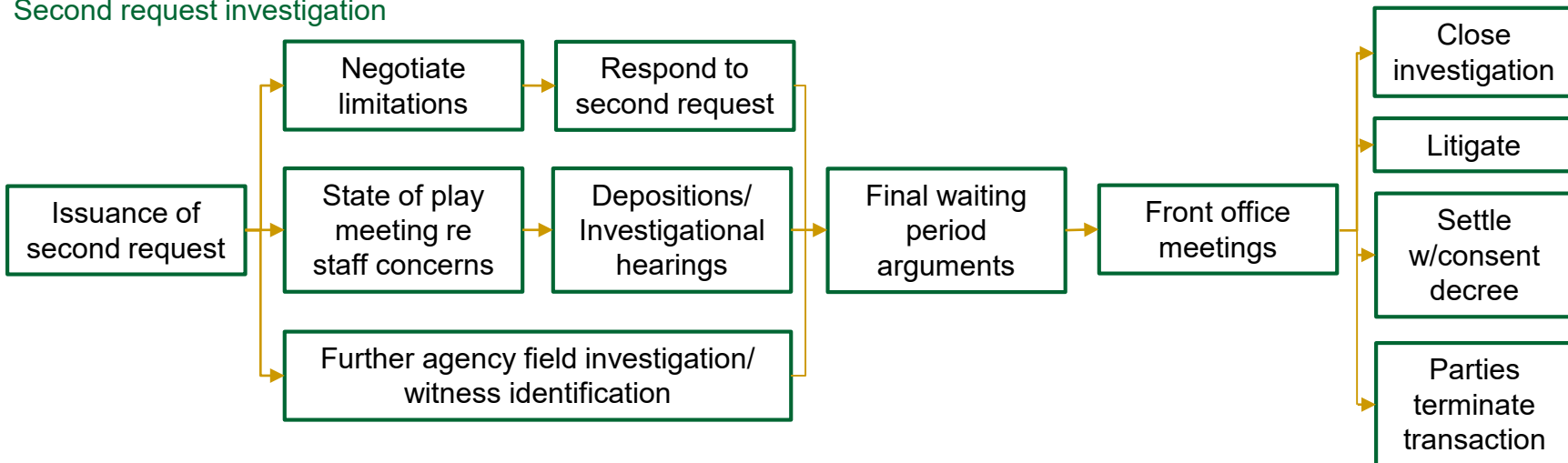
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Initial investigation

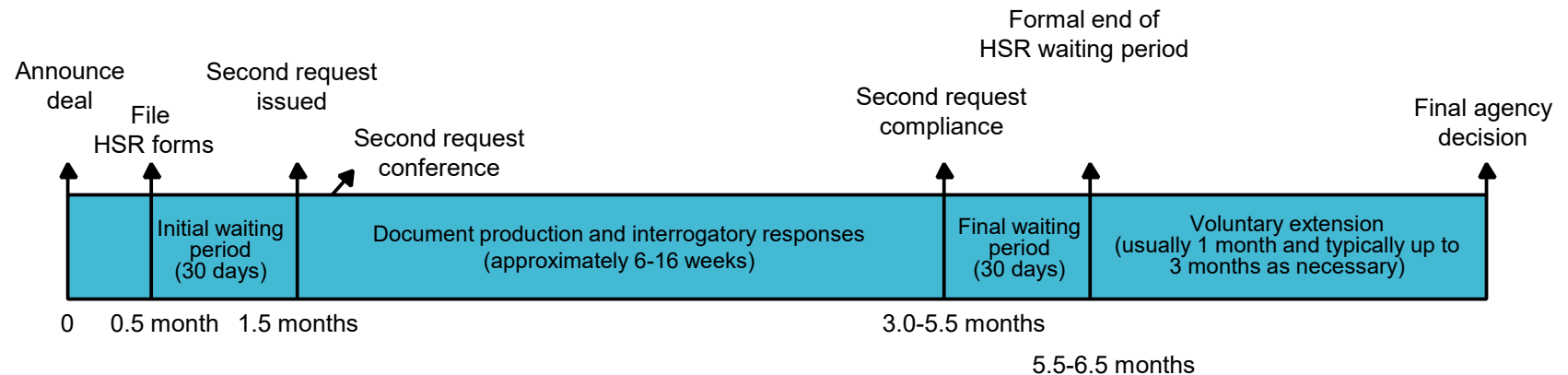


Second request investigation



The HSR Act review process

■ Typical domestic transaction



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|------------------|--|--|--|
| Customer rollout | <ul style="list-style-type: none"> – First telephone call (voluntary request) – First presentation – Follow-up meetings – First DOJ/FTC customer interviews – First DOJ/FTC competitor interviews – Filings in other jurisdictions | <ul style="list-style-type: none"> – Second request conference – Collect and review documents – Prepare interrogatory responses – Depositions of employees – Additional meetings – Follow-up DOJ/FTC customer interviews and affidavits – Follow-up DOJ/FTC competitor interviews | <ul style="list-style-type: none"> – Final meetings with staff – Meetings with senior staff – Negotiate consent decree (if necessary) |
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