

MERGER ANTITRUST LAW

LAWJ/G-1469-05
Georgetown University Law Center
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Tuesdays and Thursdays, 3:30-5:30 pm
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CLASS 4 WRITTEN ASSIGNMENT—INSTRUCTOR’S ANSWER

Instructions

Submit by email by 3:30 pm on Thursday, September 12
Send to dale.collins@shearman.com
Subject line: Merger Antitrust Law: Assignment for Class 4

Assignment

Time: Early 2014
Calls for a memorandum

Alice Smith, the general counsel of Safeway, has read your initial memorandum and has come back to you asking for a brief memorandum describing the process the FTC would use to evaluate an acquisition of Safeway by Albertsons.¹ She would like you to describe how the process is likely to work, including the likely timing beginning with the filing of the HSR reports, to enable her to explain the process to the other executives so that they will not be blindsided as things unfold.

Smith also understands that the FTC has the power to issue a subpoena-like document for additional information in addition to what the company supplies in its HSR filing. In your description of the merger review process, Smith would like you to include a discussion of what this document is, what types of information and other materials the document is likely to request, the circumstances under which the FTC is likely to issue this type of request, how long it typically takes a company to comply with the request, and any effect that the issuance of the request might have on the waiting period.

Finally, Smith would like your views on the likelihood the FTC will issue a request in the review of the Albertsons’ acquisition.

NB: You should think about how you would like to organize your memorandum. The way I have listed the topics—which is somewhat typical of the stream of consciousness that is likely to come out of a general counsel—may be a good way for you to organize the memorandum, but perhaps there is a better way. Remember, you are writing for a very busy general counsel, so clarity in organization and style are important.

¹ Most retail acquisitions, including supermarket acquisitions, are reviewed by the FTC and not the DOJ.

If you have any questions, send me an e-mail. See you in class.

Dale

Instructor's answer follows

Note to students: In earlier discussions, the client told us that the code name for the transaction is Project Century and that the codenames for Albertsons and Safeway are Bertie and Alexandra, respectively. Be sure to use them and not the real names in the memorandum. As a general rule, you should always use the codenames that the client supplies. In any event, never include the real name of the counterparty in a confidential transaction in a memorandum or email. If the client did not give you one, make one up.

ABLE & BAKER LLP

To: Alice Smith, Esq.
General Counsel, Safeway Inc.

FROM: Dale Collins

Project Century
Description of FTC Merger Review Process

You have asked me to provide you with a description of the FTC's merger review process as it might apply should Project Century go forward.

The HSR filing

The FTC review of the transaction would begin with the filing by the merging parties of the prescribed premerger notification report form under the Hart-Scott-Rodino (HSR) Act, 15 U.S.C. § 18a, that I described in my prior memorandum to you. The HSR Act bars the closing of the transaction for an initial waiting period of 30 calendar days to permit the investigating agency to conduct a preliminary antitrust merger review.

The initial waiting period review

Clearance. In most transactions, the first step in a merger review is for the Antitrust Division and the FTC to determine through the "clearance" process which, if either, of the two agencies will review the transaction. In the case of supermarkets and other consumer retail businesses, the FTC has a long-standing history of being the reviewing agency, so we can be reasonably confident that the FTC will be cleared to review the Century transaction within two or three days after the filing of the premerger notification report forms.¹

Initial telephone call. Almost immediately after the FTC receives clearance, the FTC staff who had been assigned to review the transaction will call me as the contact person listed on the HSR form for our side. They will also call the outside counsel for Bertie. In those calls, they will introduce themselves and ask each party to provide them on a voluntary basis the following:

1. A copy of our most recent national strategic plan and, to the extent they exist, copies of the most regional strategic plans.
2. A copy of any internally or externally prepared market research reports.
3. A list of all of our stores nationwide and the annual revenues earned by each store in the last three years.
4. A list of any stores we opened or closed in the last three years.

The first two requests are common to all merger investigations. Those documents typically are prepared in the regular course of business and have sections that discuss the competitive environment of the company. In most merger reviews, the FTC staff also will ask that each party

¹ Normally, the clearance process takes seven to ten days.

provide a list of their top 10 or 20 customers in each product line or geographic area of interest to them along with a contact name and telephone number. The FTC staff usually will spend most of the initial waiting period calling those contact persons and soliciting their views on whether the merging parties compete for the customer's business, what other realistic alternative suppliers the customer has in addition to the merging parties, and how the customer expects to be affected, if at all, by the transaction. The FTC staff will be particularly interested in whether the customer expects that the prices it pays will increase as a result of the transaction. In retail deals, however, the FTC does not find retail customers to be reliable sources of information about competitive effects. Instead, they will ask for data on the location and revenues of our stores and Bertie's stores. They will plot these stores by state using a geocoding program and focus their preliminary review on the stores that are sufficiently close to one another to be alternative suppliers to some identifiable group of customers. Most likely, the FTC will have concerns with respect to areas where the transaction would reduce the number of alternative suppliers (by company, not by individual store) from four to three or even five to four.

Initial presentation. In the initial telephone call, the FTC staff also will offer the merging parties the opportunity to make a presentation in person as to their views on the competitive analysis of the transaction. We should definitely take them up on this offer and make a presentation to the staff as soon as possible after the initial telephone call.

I suggest that the presentation have three parts: (1) an overview of the parties and the deal; (2) the deal rationale; and (3) the competitive analysis. I also suggest that one or more senior business executives from each party present the overview, that Bertie present the business rationale, and that an economist present the competitive analysis. Alexandra's business people and lawyers can work jointly with Bertie to prepare the presentation under the common interest privilege. The competitive analysis should be presented by an economist.² In a supermarket transaction, the economic analysis will have two parts: (1) identifying geographic areas where both companies currently have stores that compete with one another and the transaction will reduce customer choice to four or fewer companies; and (2) performing an econometric analysis using store opening and closings to show that prices do not materially increase when a store closing reduces customer choice from five-to-four company alternatives (or even four-to-three) or materially decreases when a store opening increases customer choice from four-to-five company alternatives (or even three-to-four). The idea here is to try to convince the FTC that divestitures are not required in areas where the number of company alternatives to customers are at least three or four postmerger (depending on what the data shows). We should provide the

² My suggestion is that we retain our own economist. We could jointly retain an economist with Bertie, but Jupiter would control the economist and therefore the economic analysis. If we want to explore our own ideas of possible economic arguments and, equally if not more importantly, do quality control on Bertie's economic analysis, we will need to retain our own economist. Both merging parties frequently retain their own economists.

[*Note to students:* In most deals, I would not bring an economist to the first meeting with the investigating agency even if we have retained one, since the presence of an economist suggests that there are real antitrust concerns to be explored. Retail deals, and especially supermarket deals, can be an exception. There is lots of transaction data from the tracking services and the agency economists will be doing their own econometric analysis (we can talk more about this in class). In this situation, it is a good idea to get ahead of the game, do your own econometric analysis first, and then present it to the investigating agency at the first meeting.]

FTC staff with all of the data and econometric specifications to replicate our analysis. They will not accept our analysis until they can replicate it.

Once we have finished our internal analysis, we may want to prepare some divestiture proposals for stores in clearly problematic areas to give the FTC during the initial waiting period, if not the first meeting. We can be confident that the FTC will uncover all local markets in which the number of alternatives available to customers will be reduced to three or less as a result of the transaction and the FTC will insist on the divestiture of all of the stores of one or the other merging party as a condition of not going into court to block the deal in its entirety. Proposing divestitures that inevitably will be required early in the investigation both gains us goodwill with the agency and narrows the investigation to the areas where we have meaningful arguments that no divestitures should be required.

The staff will spend the remainder of the 30-day waiting period collecting data, replicating our analyses, and beginning their own geographic overlap and econometric price analyses. The FTC staff will have questions and data requests and we should do what we can to supply them with answers as soon as possible. If we do not provide them voluntarily with the information and data they want, the staff will use compulsory process to obtain it.

The second request investigation

At the end of the 30-day initial waiting period, the FTC will either close the investigation or issue a Request for Additional Information and Documentary Material (more commonly known as a “second request”), which will extend the HSR Act waiting period until 30 calendar days after both merging parties have complied with their respective second requests. In this case, the FTC almost certainly will issue a second request. The initial waiting period will not give the FTC staff the time to complete its geographic overlap and econometric price analysis, which means that the FTC staff will not be prepared to make a final recommendation to senior management and the Commissioners as to the divestitures that should be demanded to negate the competitive problems in the transaction. The way the FTC staff will get the time is to issue a second request and extend the waiting period.

The second request. The HSR Act provides that the investigating agency can issue one and only one second request to each merging party by the end of the initial waiting period. There is no limit, however, on the types or amounts of documents or information a second request can require. Since the staff can only issue one second request to each party and the amount of time it takes the parties to comply with their second requests will determine the amount of time the staff has to conduct the investigation, the FTC institutionally has an incentive to make second requests time-consuming and voluminous.

The second request will include document requests, narrative interrogatories, and data interrogatories. The document request, which is likely to cover 30 or 50 or more custodians, will require the production of all paper or electronic documents (including emails) that relate to such topics as business, strategic and marketing plans (including plans to open or close stores), pricing, and competition. The narrative interrogatories will ask us to describe the reasons for the deal, the synergies the parties expect (Bertie will do this), and the requirements for opening and supplying new stores. The data interrogatories, which will be critical to the FTC economic analysis, will require a variety of statistics on our individual stores (e.g., store number, address,

size by SKUs³ or square footage, the extent to which the store sells products other than the typical supermarket SKUs offered, date of opening (and, if closed, date of closing), revenues, cost of goods sold, profit margin). The request will probably cover the last ten years and the FTC will want data on an annual or perhaps even monthly basis for those variables that can change over time. The FTC will make the same document requests and interrogatory demands of Bertie. The FTC also will issue civil investigative demands (CIDs, essentially precomplaint subpoenas) to other supermarkets for the data for their stores in the areas that the FTC will investigate.

These second requests are voluminous and compliance typically requires several months. Given the size of the parties in this transaction and the large number of local geographic markets in which they both operate, you should expect that the FTC will issue a second request in this investigation. The issuance of a second request extends the waiting period for the time it takes the parties to comply plus an additional 30 calendar days. You should expect that the FTC will request, and the parties will find it in their interest to give, a commitment not to close the transaction for an additional 30 to 60 days after the waiting period has expired in order to enable the FTC to complete its investigation and to give the parties the opportunity to present the best possible defense of the transaction. On a fast track, it usually takes the parties two to three months to comply with their respective second requests and the final waiting period is an additional 30 calendar days. If the parties voluntarily commit not to close the deal for another 60 days, the time from the filing of the HSR forms to the time when the parties can close in the absence of an injunction—and hence the time the FTC will conclude its investigation—will be about seven months.⁴

There are four possible outcomes of the investigation:

1. The FTC could close the investigation without taking enforcement action. This is unlikely, given that almost surely there will be local markets that the FTC will find problematic.
2. The FTC and the merging parties negotiate a consent order requiring, for local market for which the FTC has competitive concerns, the divestiture of all of the stores of one or the other merging parties. Across the local markets, the stores to be divested can be from different parties but within a given local market it will be all of the stores of one party or the other (i.e., no mixing and matching).
3. The FTC and the parties cannot agree on a mutually acceptable consent decree and the FTC initiates litigation in federal district court for a preliminary injunction and at the same time files an administrative complaint to adjudicate the merits before an FTC administrative law judge.
4. The FTC and the parties cannot agree on a mutually acceptable consent decree and the parties, rather than fight the FTC in court, terminate the purchase agreement.

In supermarket transactions, a consent decree is almost always the outcome of the merger review. The real question is how many stores in what areas will need to be divested.

³ [Note to students: These are “stock keeping units,” that is, individual product designations.]

⁴ Initial waiting period (1 month) + second request compliance (say 3 months) + final waiting period (1 month) + voluntary commitment not to close (say 2 months) = 7 months.

If you have any questions or would like to discuss the FTC process further, please let me know.