CLASS 7 SLIDES

Unit 6. The Atlanta Newspaper Merger

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The Atlanta Newspaper Merger

A Hypothetical

THE ATLANTA TIMES

The Atlanta Post

The set up[1]

Your firm represents The Atlanta Times, which together with The Atlanta Post are the two newspapers in Atlanta. The Post has approached the Times seeking to be acquired, and Katherine Hearst, the Times' publisher, is seeking advice as to whether the Times can acquire the Post.

- Hearst wants two things out of the meeting:
  1. What is the antitrust risk? Can the Times close the deal and operate the company without antitrust interference?
  2. Are there any ways to minimize the risk of antitrust interference?

[1] See the homework assignment for Class 7 for the full hypothetical.

The Kafee outline

1. Substantive risk
2. Inquiry risk
3. Remedies risk
4. Purchase agreement considerations

Substantive risk

- First question?
  - What are the identifiable customer groups that might be harmed as a result of the acquisition?
    - In a horizontal transaction, these will be overlapping customer groups
  - Readers
    - Print
    - Online
  - Advertisers
    - Print
    - Online
    - Each group may also divide between national/regional and local advertisers

Substantive risk

- Second question?
  - How could customers be harmed?
    - Readers
      - Print: Higher prices, lower quality, less content, fewer publishing days
      - Online: Higher prices, lower quality, less content
    - Advertisers
      - Print: Higher prices (how measured?), less reach?
      - Online: Higher prices, less reach?

Substantive risk

- Possible theories of anticompetitive harm
  - Print newspapers—Readers
    - Merger to monopoly in the sale of print newspapers serving Atlanta
    - Unilateral effect (uniquely close competitors) in the sale of newspapers in Atlanta (combined print and online)
    - Unilateral effects in the sale of news in Atlanta
  - Online newspapers—Readers
    - Merger to monopoly in the sale of online newspapers serving Atlanta with local content
    - Unilateral effects in the sale of online newspapers in Atlanta with and without local content
    - Unilateral effects in the sale of online news in Atlanta
    - Unilateral effects in the sale of news in Atlanta

Substantive risk

- Possible theories of anticompetitive harm
  - Print newspapers—Advertising
    - Merger to monopoly in the sale of advertising in print newspapers serving Atlanta
    - Unilateral effects in the sale of local print advertising in Atlanta
    - Unilateral effects in the sale of national/regional print advertising in Atlanta
    - Unilateral effects in the sale of print advertising in Atlanta
    - Unilateral effects in the sale of advertising in Atlanta
  - Online newspapers—Advertising
    - Merger to monopoly in the sale of advertising in online newspapers serving Atlanta
    - Unilateral effects in the sale of local online advertising in Atlanta
    - Unilateral effects in the sale of local advertising in Atlanta
    - Unilateral effects in the sale of national/regional online advertising in Atlanta
    - Unilateral effects in the sale of online advertising in Atlanta

Substantive risk

- Possible defenses
  - What is the essence of a merger antitrust defense?
    - A showing that for each allegedly problematic customer group, member of that group will be unharmed (or, even better, benefited) by the merger
  - Two ways to make out the defense—
    1. Show that there was no gross tendency of anticompetitive harm arising from the merger in the first instance
       - E.g., the merger creates no upward pricing pressure
    2. Show that any a gross tendency of anticompetitive harm arising from the merger is more than offset by the proconsumer benefits
       - E.g., the merger also creates downward-pricing pressure that outweighs the upward pricing pressure, and hence there is no consumer harm from higher prices

Substantive risk

- Possible defenses
  - Possible ways to make out these defenses
    1. *Incumbent competition*: Customers have enough realistic alternative incumbent suppliers to protect themselves
       - As part of this showing, must prove that incumbent firms will compete and not accommodate the merged firm with their own anticompetitive conduct (i.e., no coordinated effects)
    2. *Entry*: New firms will enter/expand/reposition to replace the competition otherwise lost from the merger
    3. *Power buyers*: The customers have sufficient bargaining power to protect themselves from any attempt by the merged firm to act anticompetitively
    4. *Efficiencies*: The merger creates sufficient procompetitive efficiencies to offset any likely consumer harms
    5. *Failing company defense*: The merger would be better for consumers than any other available alternative

Which of these defenses might apply in the merger here?
What questions do you need to ask to find out?

Substantive risk

- Some questions
  - Three good starting questions:
    1. What is the business rationale for the deal? How is the deal going to make money for your shareholders?
    2. What are your plans for operating the combined company?
    3. What are the implications of the business model and your postmerger operating plans for your subscribers and advertising customers? If the customers knew the model and your plans, would they support the deal, oppose the deal, or be neutral?
  - Business rationale and postmerger operating plans
    - Hearst has already told you a bit about these:
      1. Save significant operating expenses by eliminating duplicative facilities and personnel
      2. Consider returning the Times to a daily publication schedule
      3. Consider expanding the newsroom by retaining some Post employees
      4. Consider reassigning some additional Post reporters (or hiring new reporters) to reinstitute coverage of the suburban areas
      5. Considering resuming distribution of print newspapers in the suburbs

Substantive risk

- Some questions
  - For subscription markets (for both print and online separately)
    - What do you think that readers would say about the deal? In favor, opposed, or neutral?
    - What, if anything, do you think readers would like to see from the deal?
      - More particularly, what would make readers support the deal?
    - Given their different ideological slants, do the two newspaper compete substantially with one another for readers?
    - When you reduced the publication schedule, how many of you readers switched their subscriptions to the Post?
      - For those who switched, why do you believe they switched?
    - When you set your subscription prices, do you take into account the subscription price of the Post?
    - What products or services are most important to consider in setting prices?
    - What prevents you from increasing your subscription price today?
    - Are you thinking about increasing the subscription price for the Times postmerger?

Substantive risk

- Some questions
  - For subscription markets (for both print and online separately)
    - Are alternative news sources sufficient to make a postmerger subscription price increase unprofitable for the combined firm?
      - That is, would the merged firm lose more profits from readers who abandon the paper (the *marginal customers*) than it would gain in profits from the increased margin on the readers who would be willing to pay the higher subscription price (the *inframarginal customers*)
    - How valuable would it be to readers to increase Atlanta proper news content (print and online)?
      - Can this be done profitably?
    - How valuable would it be to readers to increase news coverage to the broader metropolitan area and distribute newspapers there?
      - Can this be done profitably?

Substantive risk

- Some questions
  - For advertising markets (for both print and online separately)
    - What do you think that advertisers would say about the deal? In favor, opposed, or neutral?
    - Who are the major advertising firms that contract with the Times? With the Post? What would they say about the deal?
    - What, if anything, do you think advertisers would like to see from the deal?
      - More particularly, what would make advertisers support the deal?
    - To what extent do the readers of the two newspaper overlaps?
    - When you reduced the publication schedule, how many of you advertisers switched their advertising to the Post?
    - When you set your advertising prices, do you take into account the advertising prices of the Post?
    - What advertising platforms are most important to consider in setting prices?
    - What prevents you from increasing your advertising prices today?
    - Are you thinking about increasing the advertising prices for the Times postmerger?

Substantive risk

- Some questions
  - For advertising markets (for both print and online separately)
    - Are alternative advertising channels sufficient to make a postmerger subscription price increase unprofitable for the combined firm?
      - That is, would the merged firm lose more profits from readers who abandon the paper (the *marginal customers*) than it would gain in profits from the increased margin on the readers who would be willing to pay the higher subscription price (the *inframarginal customers*)

Substantive risk

- Some questions
  - The deal
    - How did you arrive at a purchase price in the neighborhood of $70 million?
  - Possible other buyers for the Post
    - Are you aware of any other potential buyers that might be interested in the Post?
    - Are you aware of anyone expressing interest in buying the Post over the last three years?
    - Are you aware of any efforts by the Post to shop itself?

Substantive risk

- What can the Times do to reduce its substantive risk?
  1. Needs to find ways to make the merger attractive to readers and advertisers
     a. What do readers want?
        - Lower prices
        - Daily publication
        - Higher quality content
        - Broader news coverage and distribution (for readers outside Atlanta proper)

     b. What do advertisers want?
        - Lower prices
        - Daily publication
        - Broader circulation

Substantive risk

- What can the Times do to reduce its substantive risk?
  2. Invoke the failing company defense: The allegedly failing firm—
     a. Must be unable to meet its financial obligations in the near future
        - To do: CHECK FACTS
     b. Would not be able to reorganize successfully under Chapter 11 of the Bankruptcy Act; *and*
        - To do: CHECK FACTS
     c. Has made unsuccessful good-faith efforts to elicit reasonable alternative offers that would keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger
        - To do: RUN AUCTION PROCESS

Downsides:

1. *Takes time and money (Seller may require Buyer to pay expenses)*
2. *Another less anticompetitive bidder may emerge with a lower bid price (but still above liquidation value)*

Inquiry risk

- Who has the incentive and ability to challenge the merger?
  1. The DOJ/FTC (the DOJ does newspaper mergers)
  2. The Georgia AG
  3. Readers
  4. Advertisers
- What at the incentives of each of them?
- How can the Times minimize inquiry risk from each of them?

Remedies risk

- Is the deal “fixable” through a consent decree?
  - The DOJ
    - The DOJ wants divestiture relief in horizontal transactions
    - Is there something here to divest that would negate the DOJ’s concerns about the deal?
  - The Georgia AG
    - Likely to be much more willing to accept behavioral relief

Purchase agreement considerations

- What should both parties want?
  - Closing conditions
    - Expiration or termination of HSR waiting period (if applicable)
    - No injunction or legal restraint making the closing unlawful
  - Covenants
    - File HSR reports (if one is required)
    - Information sharing
    - Cooperation in defending transaction
      - But Buyer will want the contractual right to take the lead
    - Efforts to defend investigation (probably “reasonable best efforts”)
    - Respond to government requests
    - Right to attend each other’s meetings
      - But Buyer probably will want a carve-out for settlement discussions
  - Termination
    - By mutual agreement
    - Drop-dead date of 12 months
      - Could be disputed if one party wants a considerably shorter termination date

Purchase agreement considerations

- No threatened or pending litigation closing condition
  - Buyer: Wants
  - Seller: Will not want (if you can close, you must close)
- Covenant to comply with any second request or CID
  - Buyer: ??
  - Seller: Probably will want
- Litigation covenant
  - Buyer: ??
  - Seller: May want
- Extension of drop-dead date to litigate
  - Buyer: Yes, Buyer wants a litigation covenant. No, otherwise
  - Seller: May want

Purchase agreement considerations

- Hell or high water covenant
  - Buyer: No way
  - Seller: Will want
- Antitrust reverse termination fee
  - Buyer: No
  - Seller: Yes (as an alternative to a HOHW covenant)

How are these disputed provisions likely to be resolved?

Grand strategy

1. In general
    1. Keep the deal non-HSR reportable by keeping the purchase price below $94 million
    2. Keep strict confidentiality during negotiations to minimize
    3. Hold the line on all prices
    4. Increase reader and advertiser benefits to the maximum extent possible consistent with financial constraints
        - Include this in the public announcement of the deal

This strategy is fine as far as it goes and maximizes the probability that the deal will close without a DOJ investigation. But it does not protect the Times from a postclosing DOJ investigation and possible litigation to force the Times to divest the Post at a deeply discounted "firesale" price.

Grand strategy

2. Need more to protect the Times postlitigation
   a. Alternative 1: Seek DOJ "clearance"
      - Notify the DOJ in advance and precipitate a non-HSR review
      - Only sign a purchase agreement that delays the closing until after the DOJ review and permits a termination if the review results in a challenge
      - Proceed with the acquisition if and only if the DOJ "clears" the transaction
        - NB: If the DOJ does not challenge the deal after an investigation, the Georgia AG is unlikely to do so
        - More likely, the Georgia AG would join in the DOJ's investigation
   b. Alternative 2: Invoke the failing firm defense
      - Confirm that the first two requirements of the defense are satisfied
      - Tell the Post that that the Times will only acquire the company if it is the winner of a full auction process
      - If the Times is the winner of the bid and no other less anticompetitive bidder has bid above liquidation value, sign a purchase agreement subject to the condition that the DOJ agrees that the failing company defense applies
      - Precipitate a DOJ non-HSR review on the failing company defense

Grand strategy

2. Need more to protect the Times postlitigation
   c. Alternative 3: Obtain support of Georgia AG
      - Keep the deal confidential to avoid a non-HSR DOJ investigation
      - Develop a business plan to deliver substantial benefits to Atlanta subscribers, potential suburban subscribers, and (not as importantly) advertisers postmerger
      - Consult with the Georgia AG about the deal and the expected benefits to subscribers and advertisers
      - Obtain the strong support of the Georgia AG for the deal
      - If necessary, enter into a consent decree with the Georgia AG to make the investments necessary to deliver the planned benefits to subscribers and advertisers
      - Only sign a purchase agreement that—
        - Conditions the closing on the Georgia AG's support of the deal and the AG's commitment to intervene in any antitrust litigation challenging the deal
        - Contains a mutual litigation provision covenant and an extension of the drop-dead date to permit a litigation
      - Once the closing conditions are satisfied, close without informing the DOJ