

CLASS 4 SLIDES

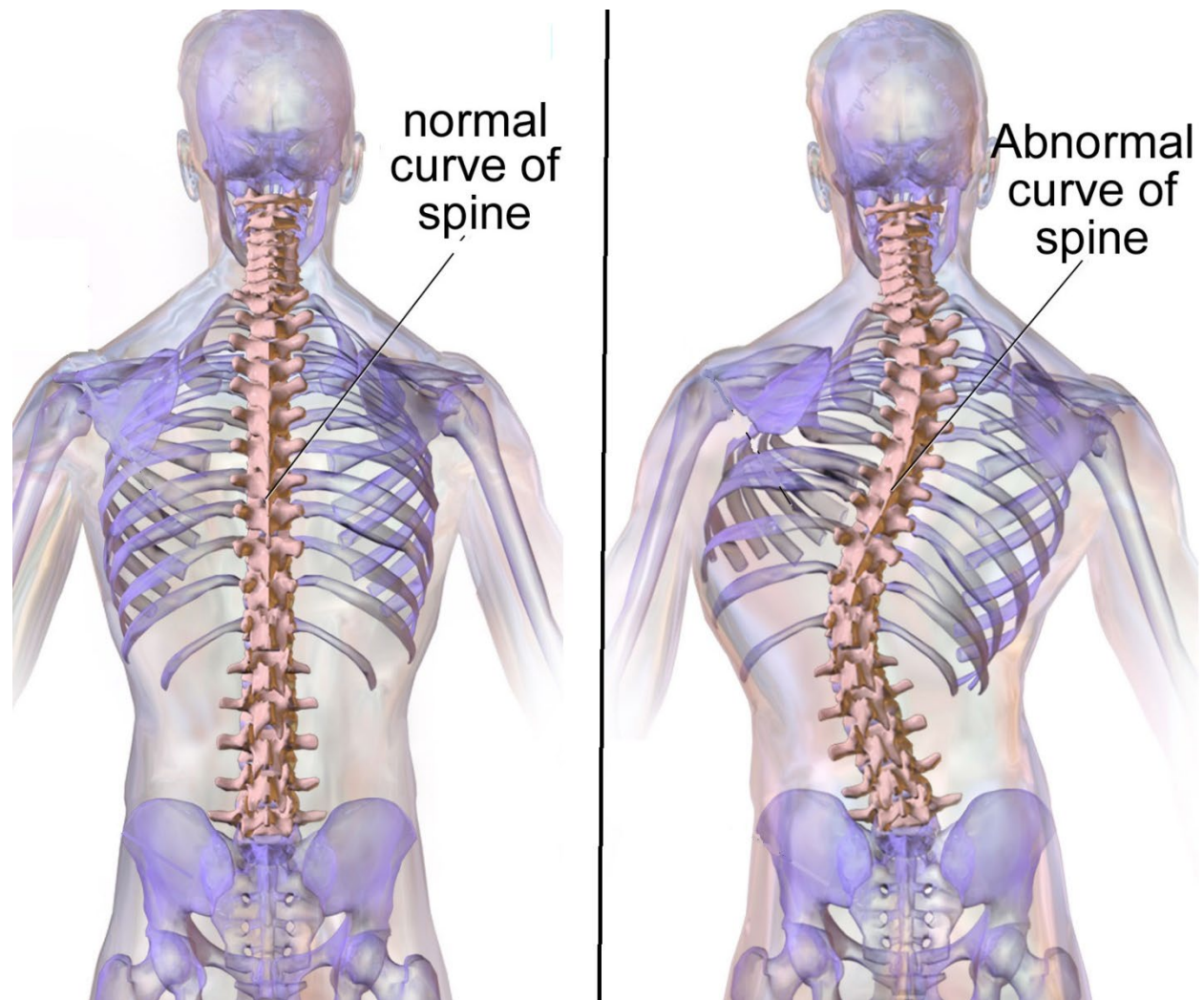
Unit 4. The DOJ/FTC Merger Review Process: The Spinal Implant Merger

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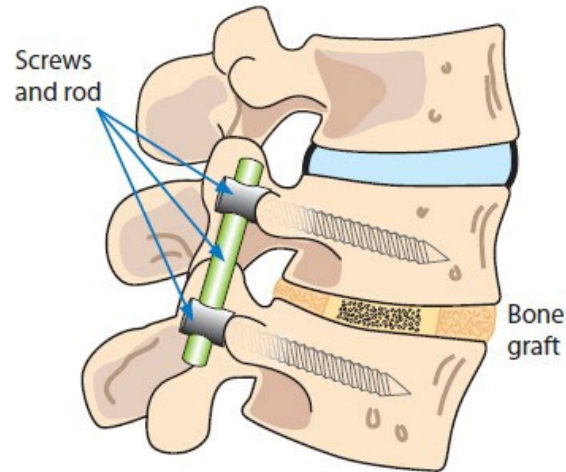
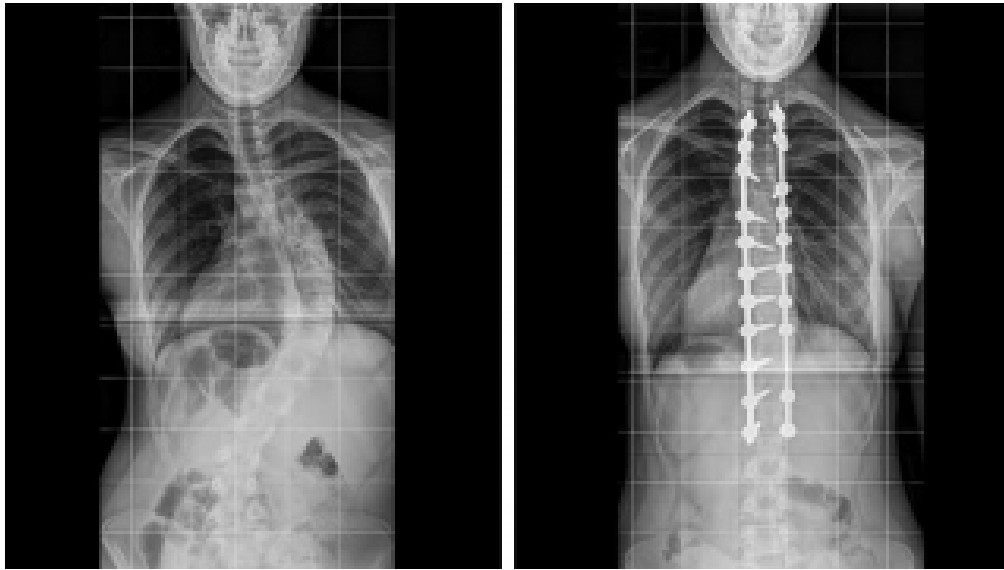
The setup

- Dr. Jack Smith, the CEO of your client Danek Group, has called you about a possible merger with Sofamor S.A. through stock swap valued at \$750 million
 - Danek and Sofamor overlap in the sale of spinal implants for the surgical treatment of scoliosis in the United States
 - Zimmer Corporation is the only other company that sells spinal implants in the United States
 - Danek and Zimmer manufacture their spinal implants in the United States
 - Sofamor manufactures its spinal implants in a suburb of Paris, France, and imports its products into the United States
 - Smith estimates the companies have the following U.S. market shares:
 - Danek: 40%
 - Zimmer: 40%
 - Sofamor: 20%
 - You have a meeting with Smith, along with his COO and general counsel, in your office this coming Thursday at 11:10 am to discuss—
 - the antitrust implications of the transaction and
 - the process you recommend for develop the defense of the transaction

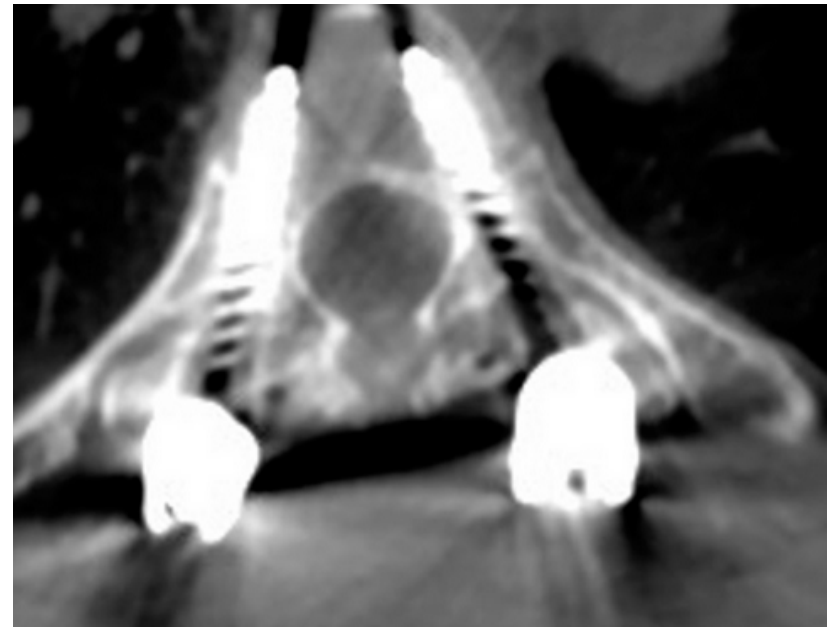
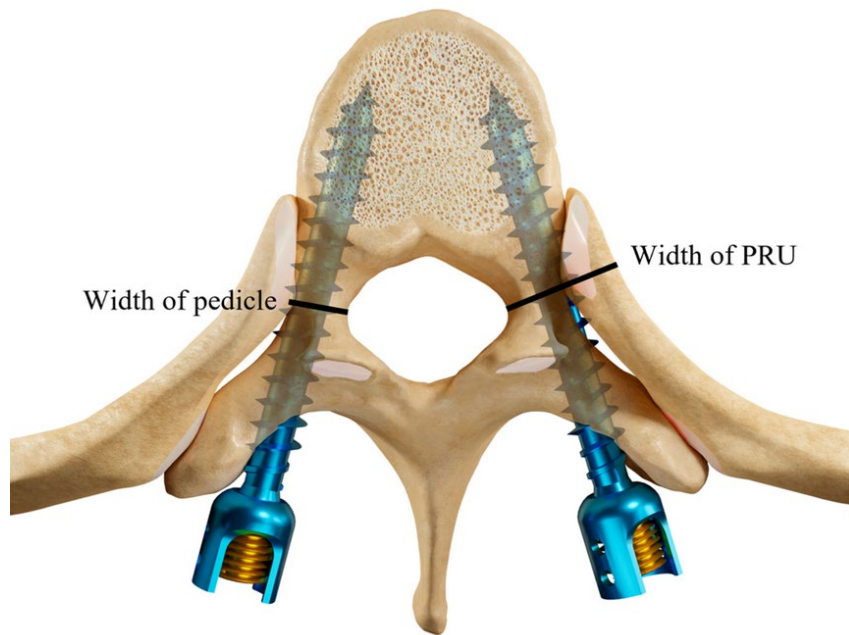
Adolescent idiopathic scoliosis



Corrected with spinal implants (rods and screws)



Pedicle screw placement



Spinal implant kits

- This is what Danek and Sofamor sell:



What Should You Do Before the Meeting?

Summary: Things to do before the meeting

1. Collect the information you know from the client
2. Do some initial research on the Internet and public documents
3. Prepare a preliminary information request and sent it to the client

1. What you would like to know at the start

- Who is the client
- Whether the client is a buyer or seller
- Who is the target/seller
- Whether the deal is a negotiated transaction or an auction
- The general range of the purchase price
 - In particular, whether it is > \$111.4 million
- The stage of the transaction

2. Initial research (for all involved companies)

- Examine websites
 - General knowledge
 - Horizontal overlaps
- Review the company 10-Ks
- Search the Internet for more information
 - Generally about companies
 - Generally about overlap markets
 - Search in particular for sites that mention both buyer and seller/target

3. Prepare a preliminary information request

- Basic model preliminary information request
 - Be sure to modify any request with the facts you know about the transaction, the products, or the market environment

**Attorney Work Product
Privileged and Confidential
Attorney-Client Communication**

ABLE & BAKER LLP

September 5, 2023

PRELIMINARY INFORMATION REQUEST

Below is a list of documents and other information that will help us in our initial U.S. antitrust assessment of the acquisition of Target by Danek and will make our meeting on Thursday more productive. Please note that we are asking only for information and materials that are readily available.

1. A list of any overlapping products that Danek and Target sell in the United States.
2. Any strategic or marketing plans for any overlapping product prepared in the last three years.
3. Any internal or external market research reports that mention both Danek and Target prepared in the last three years.
4. Any other documents that discuss Target or the competitive landscape in the United States where both Danek and Target are present.

3. Prepare a preliminary information request

- Basic model preliminary information request

5. Any internal analyses or studies (including those performed by bankers and/or consultants at Danek's request) regarding the acquisition of Target, including any documents that address:
 - a. the rationale for the transaction
 - b. any synergies you expect from the transaction (including revenue synergies)
 - c. financial modeling of the transaction
 - d. likely present or future changes in the product line as a result of the transaction
 - e. likely changes in investment or direction of future R&D
 - f. likely changes in the facilities, distribution systems, or other operations of either company postmerger.

3. Prepare a preliminary information request

- Basic model preliminary information request

Separately, please think about how customers of either company are likely to react to the transaction. The antitrust agencies consider reactions—especially adverse reactions—highly probative of the competitive effect of a transaction. Indeed, the investigating agency will spend considerable time during the merger review calling customers to obtain their views of the transaction. We will discuss likely customer reactions in some detail at the Thursday meeting.

Finally, if you prepare any documents for us at any time, please mark them with the legend “PRIVILEGED & CONFIDENTIAL – PREPARED AT REQUEST OF COUNSEL” so that we can maintain the privilege on all documents that you prepare to help us with the antitrust analysis. If you have any questions about this information request, please do not hesitate to contact us.

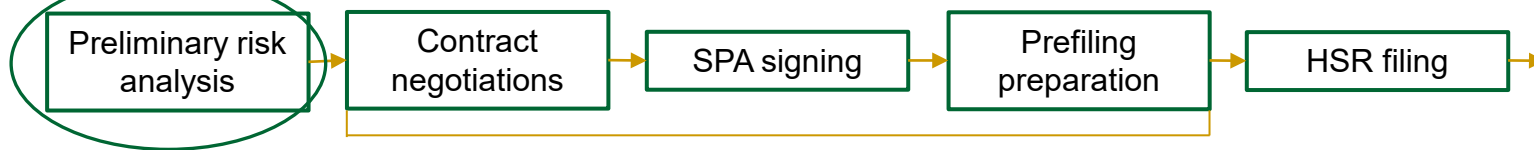
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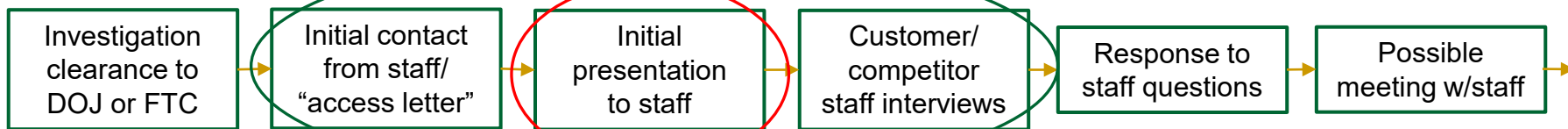
What Do You Want To Accomplish at the Meeting?

The HSR merger review process

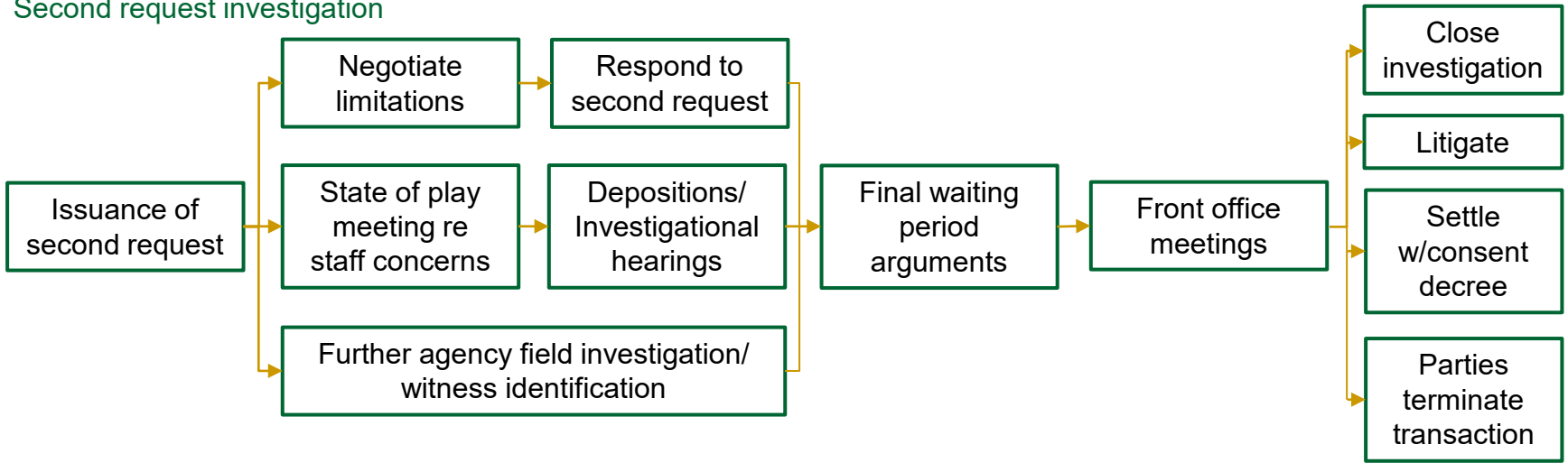
Profiling/filing



Initial investigation



Second request investigation



What do you want to accomplish at the meeting?

1. Find out if the transaction is HSR reportable
2. Find how the business rationale for the deal
3. Develop a working defense strategy
4. Test the defense strategy against customers, company documents, and the target
5. Provide strategy advice
6. Review next steps

1. Find out if the transaction is HSR reportable

- Prima facie reportability threshold in 2023: \$111.4 million
- Does an exemption apply?
 - Danek (domestic) stock swapped for Sofamor (foreign) stock →
 - *Foreign stock exemption*: Issuer does not have assets in the U.S. or sales in or into the U.S. over \$111.4 million
 - Here, with a purchase price of \$750 million and a 20% market share in the United States → Most likely outside the foreign stock exemption
 - Confirm with client
- If reportable, explain the HSR merger review process

2. Teach the client the operational § 7 test

- Important to start with the operational test for Section 7 illegality
 1. Unless the client understands the test, they will not be persuaded by your advice
 - The client will not be persuaded unless they can replicate your analysis and reproduce your conclusion
 2. If the client understands the test, they are more likely to give complete and meaningful answers your factual questions
 3. If the client knows the test, they can continue to think after they leave the meeting about what other facts may be relevant and follow up with you to sharpen the risk analysis
 4. The client needs to know the operational test as they move forward with the transaction

Start prepping the client with the first meeting so that they can understand the antitrust implications of—

- *What they write in their documents*
- *What they say to the press and to customers*
- *What they say in meetings with the investigating agency*

2. Teach the client the operational test

- Start with Clayton Act § 7
 - Governing merger antitrust statute
 - Other statutes may apply, but they will not be more restrictive than Section 7
 - Section 7 prohibits transactions that “may substantially lessen competition”
- But what does this mean *operationally*?
 - A transaction “may substantially lessen competition” when it is likely to harm an identifiable group of customers by—
 1. Increasing prices
 2. Reducing market output
 3. Reducing product or service quality
 4. Reducing the rate of technological innovation or product improvement
 5. [Maybe] reducing product variety

Clients can grasp the operational test immediately

2. Teach the client the operational test

- Tell the client how the investigating agency is going to find the facts about the likely competitive effect
 - HSR reportability and merger review process
 - Time to ask questions to find out if the deal is likely to be reportable
 - The investigating agency will—
 1. Entertain a presentation from the parties on the deal
 2. Interview—and perhaps later depose under oath—you and other relevant employees in both companies
 3. Obtain massive amounts of the documents and data from both companies
 4. Interview customers and competitors (and maybe obtain documents and data from them)
 5. Analyze win-loss records of the companies in bidding for projects
 6. Use economists to assist in analyzing the likely competitive effects of the transaction

2. Teach the client the operational test

- Bottom line
 - The agency's conclusion on the likely effect on customers will determine the outcome of the investigation
 - NB: It is the *agency's conclusion*, not necessarily the truth, that counts
 - The best defense is a good offense
 - Can we argue that the deal is a “win-win” for the merging parties *and* the customers?
 - Companies do not do deals out of the goodness of their heart—*they do deals to make money*
 - Do we have a story consistent with the business model for the transaction, the documents and other company evidence, and the likely customer responses in staff interviews that the deal will be good for customers?

Best story: The transaction will enable the combined company to make money by reducing costs and by making better products faster to the benefit of our shareholders and our customers

3. Develop a working defense strategy

1. Learn more about the business and the market environment
2. Learn about the deal rationale
 - ❑ *Query:* How will Danek make money from the transaction?
 - ❑ *Query:* What are the implications of the business model for customers?
3. What will the company documents say about competition between the two companies?
 - ❑ If the government conducts a full investigation, it will see all your documents eventually. Are there any documents that might suggest—or the government might read to suggest—that customers will be harmed in any way by the transaction?
 - ❑ We need to know about any bad documents now so that we can deal with them now. Waiting to deal with them later can be disastrous.
4. Identify—
 1. All horizontal overlaps
 2. Any dominant market positions
 3. Any significant vertical relationships

3. Develop a working defense strategy

5. Learn what the client thinks are the benefits of the deal to customers (if any)
 - *Query*: Who are the customers?
 - *Alternative query*: Who is likely to be affected positively or negatively by the deal?
6. Do we have a sales pitch that we can give the customers that the deal will be good for them?
 - Will they accept it?

With this background, work with client in the meeting to develop a working defense strategy

*Critical that the client be involved from the beginning in developing the defense strategy—
You want the client to “own” the strategy and make it theirs*

Why?



4. Test the defense strategy

1. Learn how the customers are likely to react
 - *Query:* Will the defense strategy resonate with our customers?
 - *Query:* Will the defense strategy resonate with the target's customers?
 - *Query:* If a customer wanted to attack the deal as anticompetitive, what would the customer say?
2. Learn what the medical societies are likely to say about the deal
3. Learn whether the company's documents will support or contradict the defense strategy
4. Identify any spinal surgeons we can retain as industry experts to support the deal in the investigation?
 - *Query:* Will the experts support the factual predicates of the defense strategy?
5. Learn what the client thinks the target will support the defense strategy
 - *Query:* Who will support, oppose, seek to modify?

As best we can at this point, reconcile the defense strategy with customers, documents, industry experts, and the target

5. Provide any strategic advice

1. Emphasize the need for a compelling sales pitch for the deal to customers of *both* companies
 - ❑ Offer to help the relevant business people develop this pitch and advise on when and how to roll it out
 - ❑ Note that it is the customers of the target company that are typically the most difficult to persuade
 - Will eventually need to work with the target company as to how best to persuade its customers
2. Emphasize the need for care in drafting documents
 - ❑ “Bad” documents alone can kill a deal
 - Avoid creating documents that suggest—implicitly as well as explicitly—that the deal could harm customers
 - Some documents are “bad” because they were carelessly phrased or factually incorrect, not because they speak the truth—These can also kill a deal
 - ❑ If there is one, include the procompetitive business rationale for the deal in as many documents as possible

Provide any strategic advice

3. Consider whether the deal can be structured to make it non-HSR reportable to minimize inquiry risk

5. Review next steps

1. Determine if we have client representatives who will be compelling witnesses (*witness evaluation*)—*not to be discussed at the meeting*
 - a. The strength of the client witnesses will be a major factor in the success of the defense
2. Ask the client—
 - a. Who are likely to be the best business witnesses for the target, and
 - b. How good are they likely to be
3. Follow-up with requests for documents and information that will support the defense strategy
 - a. Also, for documents and information that will contradict the defense strategy
4. Prepare a customer “roll-out” strategy
5. Begin to prepare for a joint defense meeting with the target
6. Prepare for merger agreement negotiations
 - a. We will defer this until Class 8

6. Final thoughts for the meeting

1. Caution the client that this advice is only preliminary and depends on what the client has told you in the meeting
2. Note that more work should be done with the company
 - Would like to send the client an additional *information request* for easily obtainable documents and data relevant to the defense strategy
 - When confidentiality considerations permit, would like to set up a *meeting with knowledgeable employees* to develop the facts and the arguments further
3. Tell the client that all documents created at the request of counsel should have the following prominent legend:
 - Whenever possible, make this legend *machine readable*

PRIVILEGED AND CONFIDENTIAL
Prepared at the request of counsel

Do NOT forget this!!!

Final thoughts for the meeting

4. Note that at some point in the process we will need to bring the target company onboard
 - The target's evidence and customer outreach program will be equally if not more critical to the outcome of any merger review
 - Note that we should be able to work with the target company under the "common interest" privilege
 - We need to think about whether we want this "joint defense meeting" to occur before or after the signing of the merger agreement
5. In addition, we will want to work with the target company to develop a "customer rollout" strategy to maximize customer support and minimize customer opposition to the deal
 - Need finalize and implement the customer rollout before the filing of the HSR forms
6. The target, unless incompetently advised, is likely to recognize the antitrust risk in the transaction
 - Should expect that the target will attempt to negotiate some provisions in the purchase agreement to—
 - Decrease the risk of a deal failure, *and*
 - Compensate the target for risk that cannot be eliminated

What Do During between the First Meeting and the HSR Filing

Immediate postmerger projects

1. Send information requests to the client to obtain additional documents and information that support (or contradict) the defense strategy
2. Work with the client to develop the customer rollout strategy
 - Identify the relevant customers and contact names
 - Develop the “sales pitch” for the deal
3. Make sure that you have all of the documents that the agency is likely to request in the initial waiting period
 - Any “4(c)” and “4(d)” documents
 - Strategic and marketing plans for the company and, if any, separately for any overlapping products
 - Internal and external market research reports prepared over the last three years
 - Any documents on synergies resulting from the deal
4. Continue to work closely with the client to refine the defense strategy

Presigning projects

- For auctions where the client is the seller (not relevant here)
 - Require antitrust presentations by each strategic buyer on—
 - Their antitrust analysis of the transaction
 - Their strategy for defending the transaction as the buyer
 - Their estimated chances of success (i.e., the deal closes)
 - Aside on privilege
 - Attorney-client privilege
 - Work product doctrine
 - Common interest privilege
- For transactions where the client is the buyer
 - Only if necessary or desirable, make antitrust presentation to the seller presigning
- Assist in the negotiation of the merger agreement
 - Covered in Class 8

Postsigning postannouncement projects

- Internal client meeting with employees knowledgeable about the products of interest but were not “in the loop” until now
 - Modify defense strategy accordingly
- Joint defense meeting with Target to—
 - Convene an in-person “all hands” joint defense strategy meeting
 - Usually 4 hours to two days
 - With follow-up with additional subgroup meetings and conference calls as necessary
 - i. Should include—
 - Client GC, senior client representative on the antitrust business team, client representatives knowledgeable in the areas of antitrust interest, economists
 - Counterparty GG and counterparty representatives knowledgeable in the areas of antitrust interest, counterparty economists
 - Present the defense strategy and get the Target’s reaction
 - What do the Target’s documents say?
 - What are the likely reactions of the Target’s customers?
 - Does the Target see benefits or harms to customers that we have not addressed?
 - Modify the defense strategy accordingly

Critical to obtain Target buy-in of the defense strategy

Postsigning postannouncement projects

- Joint defense meeting with Target re joint customer rollout strategy
 - Develop and finalize the “sales pitch” for the deal to be delivered to customers
 - Identify the companies and contacts to be given to the agency after the first meeting
 - Identify who will call each customer contact to make the sales pitch
 - Implement the customer rollout strategy/companies to respond to any concerns
- Interview and retain support industry experts
- Finalize the defense presentation to the agency for the first meeting
- Finalize HSR reports
 - Can usually accomplish all postsigning postannouncement projects 10 business days after deal announcement
 - BE SURE you have collected all “4(c)” and “4(d)” documents
 - Failing to include all responsive documents is likely to result in an ineffective filing

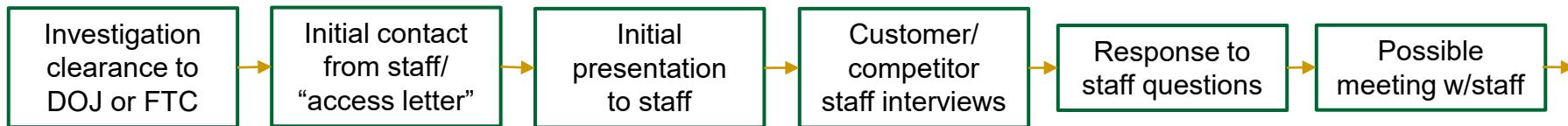
Now You Are Ready To File and Begin the Defense of the Transaction

The HSR merger review process

Prefiling/filing



Initial investigation



Second request investigation

