

US MERGER CONTROL

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Antitrust planning typically is a central part of every transaction and public takeover bids are no exception. The substantive provisions of US antitrust law may affect the viability of a transaction, or its scope if divestitures or other remedies must be effected as conditions to completing the deal. The procedural provisions of US antitrust law may also affect the timing of a transaction and its visibility to the enforcement agencies and thus the likelihood of a government investigation and challenge.

This chapter focuses on how US antitrust rules impact on mergers and acquisitions, pointing out (where applicable) any differences which apply when the contemplated transaction is a public bid.

The merger control framework

The Clayton Act is the primary US statute governing the substantive competition issues raised by mergers and acquisitions. It prohibits acquisitions where “the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.” Joint ventures typically are also evaluated under the Clayton Act, although they may also be judged under the Sherman Act, which prohibits unreasonable restraints of trade, attempts to monopolize and monopolization.

The Hart-Scott-Rodino Antitrust Improvements Act (the HSR Act) is the statute governing the procedural aspects of the government’s review of mergers and acquisitions. It gives the two federal agencies which review the competitive implications of transactions, the Antitrust Division of the Department of Justice (DOJ) and the Federal Trade Commission (FTC), the opportunity to assess the antitrust issues posed by proposed transactions before those transactions are consummated. While the Antitrust Division and the FTC have parallel jurisdiction to review transactions, the agencies have developed a procedure, which allocates (or “clears”) transactions to one agency or the other.

The decision as to which agency will review a transaction cannot be influenced by the parties. It typically turns on which agency has developed some familiarity with the industry or companies involved or with the types of issues likely to be raised by the transaction.

Mergers and acquisitions also can be reviewed by the competition agencies of one or more of the 50 states, typically in conjunction with the review being conducted by the Antitrust Division or the FTC. Private parties, under certain circumstances, also can challenge a merger or acquisition through private litigation and have available to them the same remedies that are available to the government. Such challenges, however, are rare.

Jurisdictional thresholds

All mergers and acquisitions, regardless of size, are subject to the Clayton Act. However, transactions falling within the provisions of the HSR Act, which requires parties to file a notification and wait before completing the transaction, are far more likely as a practical matter to be scrutinized by the reviewing agencies.

Transactions and persons covered

In general, the HSR Act applies to any acquisition of voting securities and/or assets:

- If one party to the acquisition has annual net sales or total assets of US\$100 million or more and the other party has annual net sales or total assets of US\$10 million or more (the “size of person threshold”); and
- If, as a result of the transaction, the party making the acquisition (the acquiring person, see “HSR glossary”) holds voting securities and/or assets of the party whose voting securities or assets are being acquired (the acquired person) having a value of more than US\$50 million (the “size of transaction threshold”); or
- If, as a result of the transaction, the acquiring person holds voting securities and/or assets of the acquired person having a value of more than US\$200 million, regardless of whether the size of person threshold is met (see also box “Recent amendments and other proposed changes”).

Size of person threshold. For purposes of determining whether the size of person threshold is met, the Rules provide that:

- The annual net sales of a person is as stated on the last regularly prepared annual statement of income and expense of that person.
- The total assets of a person is as stated on the last regularly prepared balance sheet of that person.

Size of transaction threshold. For purposes of determining whether the size of transaction threshold is met, the Rules provide that the acquiring person must calculate the value of the voting securities and assets that will be held as a result of the acquisition. This calculation must include not only the value of those securities and assets that are currently being acquired, but also, in some circumstances, the present value of voting securities and assets previously acquired from the same person.

Transactions potentially caught. The HSR Act applies to acquisitions of assets and voting securities of all types, whether direct or indirect, including purchases, mergers, consolidations, exchange and tender offers (see box “Public bids or tender offers”), market transactions, conversions of non-voting securities into voting securities and the formation of corporate joint ventures.

Among the types of acquisitions that are easy to overlook for purposes of the HSR Act are:

- Secondary acquisitions. A secondary acquisition occurs when an acquiring person obtains control of an entity that holds voting securities of another entity, which it does not control. Secondary acquisitions are separately subject to the Act.
- Conversions. The conversion of non-voting securities into voting securities is an acquisition which is subject to the HSR Act, even though the acquisition of convertible securities itself is exempt.
- Exchanges. The acquisition of voting securities in an exchange transaction is an acquisition subject to the HSR Act.

The filing and waiting period requirements

If the HSR Act applies, all acquiring and acquired persons must file a Notification and Report Form (the Form) with the FTC and the Antitrust Division of the DOJ. There is no deadline for filing.

The parties must then wait 30 days (15 days in the case of cash tender offers and bankruptcy matters) to consummate the transaction, unless early termination of the waiting period is granted (see below).

Either the FTC or the DOJ may request additional information (a Second Request) from any of the filing persons and extend the waiting period an additional 30 days (10 days in the case of cash tender offers and bankruptcy matters) measured from the date on which all parties have substantially complied with the Second Request.

Waiting period. The waiting period begins to run from the date on which all persons required to report have filed the Form, except in the case of tender offers, market transactions, and certain other specified transactions. In the case of tender offers, the waiting period begins to run from the date on which the acquiring person files its Form, thus preventing a tender offer target from delaying the commencement of the waiting period by failing to file. The end of any time period that would be a Saturday, Sunday or legal public holiday will be the next regular business day.

Early termination of the waiting period may be granted before the statutory 30-day period expires. The parties can, and routinely do, request early termination. Such requests are granted on approximately 70% of all transactions and typically are granted within two weeks of the start of the waiting period.

If early termination is requested and granted, the fact that the persons propose to engage in a transaction becomes a matter of public record. All other information contained in or submitted with the filing, however, remains confidential. The FTC also makes available by recorded telephone information system (+1 202-326-2222) and on its website (www.ftc.gov) a daily list of transactions in which early terminations were granted on the previous working day. If early termination is not granted, then there is no public record that a filing was even made. The filing itself is always confidential and not available under the Freedom of Information Act or otherwise.

Second Requests. The agencies may make one formal Second Request. A Second Request will be issued when the Antitrust Division or FTC concludes that the transaction may raise substantial antitrust issues warranting a more comprehensive investigation. In recent years, Second Requests have been issued on approximately 3% of all reported transactions; approximately 60% of Second Request investigations have resulted in some form of enforcement action.

Second Requests typically seek a large number of documents requiring broad searches of files, often in multiple locations. Written responses to what may be complex questions are also required. The issuance of a Second Request will almost always impact on the timing of a transaction.

Filing fees. In connection with each acquisition for which a filing is required, the FTC is required to collect from each acquiring person:

- A US\$45,000 filing fee for an acquisition valued at less than US\$100 million.
- A US\$125,000 filing fee for an acquisition valued at US\$100 million or more but less than US\$500 million.

- A US\$280,000 filing fee for an acquisition valued at US\$500 million or more.

These fees must be paid before or at the same time as the filing of the Form. Failure to do so will delay the start of the waiting period until the fees are paid.

Joint ventures, partnerships and LLCs

Joint ventures. The acquisition of voting securities in connection with the formation of a corporate joint venture is potentially reportable under the HSR Act and the Rules. Under the HSR Act and the Rules, any formation of a non-corporate business entity will not be considered a joint venture, regardless of whether the parties call it or regard it as a joint venture or whether the entity is what would generally be known as a joint venture. The formation of a corporate joint venture is covered by the HSR Act if:

- One participating person has annual net sales or total assets of US\$100 million or more, the venture will have total assets of US\$10 million or more, and at least one other participating person has US\$10 million of annual net sales or total assets; or
- If the venture will have total assets of US\$100 million or more and at least two participating persons have annual net sales or total assets of US\$10 million or more; or
- If the venture will have at least two participating persons and one of the participating persons will hold voting securities of the venture valued in excess of US\$200 million.

Partnerships. The formation of a partnership is not reportable as an acquisition of assets or voting securities according to the FTC's current interpretation of the HSR Act and the Rules, regardless of whether businesses will be combined in a partnership that will be controlled by one of the partners. An acquisition or transfer of less than all of the interests in a partnership is also not reportable.

Limited liability companies. The FTC will treat as reportable the formation of a US limited liability company (LLC) if:

- Two or more pre-existing, separately controlled businesses will be contributed; and
- At least one of the members will control the LLC (in other words, have an interest entitling it to 50% of the profits or 50% of the assets of the LLC upon dissolution).

The formation of all other LLCs will be treated similar to the formation of a partnership, which, under the FTC's current position on partnership formations, will not be reportable.

Foreign acquisitions

The reporting requirements of the HSR Act apply to a wide range of foreign acquisitions, including acquisitions of foreign assets and voting securities of foreign issuers by US persons and acquisitions of assets and voting securities of US persons by foreign persons. The HSR Act may apply even if all entities involved in an acquisition are foreign persons.

Acquisitions of foreign assets by US persons. The HSR Act exempts an acquisition of assets located outside the US by a US person, unless, as a result of the acquisition, the acquiring person would hold assets of the acquired person to which sales were attributable in or into the US, aggregating US\$25 million or more during the acquired person's most recent fiscal year.

Acquisitions of voting securities of foreign issuers by US persons. The HSR Act exempts an acquisition of voting securities of a foreign issuer by a US person, unless the issuer (including all entities "controlled" by the issuer):

- Holds assets located in the US having an aggregate book value of US\$15 million or more; or
- Made aggregate sales in or into the US of US\$25 million or more during its most recent fiscal year.

Acquisitions by foreign persons. Acquisitions by foreign persons are exempt if either:

- The assets are located outside the US (regardless of the amount of sales in or into the US attributable to such assets).
- The acquisition is of assets located in the US valued at less than US\$15 million.
- The acquisition is of the voting securities of a foreign issuer and will not confer control (50% or more of the voting securities) of:
 - an issuer which holds assets located in the US having an aggregate book value of US\$15 million or more; or
 - a US issuer with annual net sales or total assets of US\$25 million or more.
- The acquired person is also a foreign person and both the aggregate annual sales in or into the US of both persons and the aggregate total assets located in the US of both persons are less than US\$110 million.

The FTC has proposed certain revisions to the current rules concerning exemptions for acquisitions of foreign assets and voting securities of foreign issuers.

The major changes to the existing rules consist of:

- Raising both the US\$15 million and US\$25 million thresholds that trigger filing obligations for foreign transactions to US\$50 million.
- Extending reportability to certain acquisitions of foreign assets by foreign persons.

The proposed rules are currently under review by the FTC and DOJ. It is anticipated that the FTC will issue the final rules during 2002. The final rules will become effective 30 days after publication.

Exemptions

The HSR Act exempts certain acquisitions, including:

- Acquisitions of certain goods and realty in the ordinary course of business.
- Acquisitions of voting securities “solely for the purpose of investment” if, as a result of the acquisition, the acquiring person will hold 10% or less of the voting securities of the acquired person (regardless of the value of the investment).
- Acquisitions of voting securities of an acquired person 50% of the voting securities of which are already held by the acquiring person.
- Acquisitions of non-voting securities (for example, bonds, mortgages and deeds of trust).
- Intra-corporate transactions.
- Stock dividends and splits.
- Certain acquisitions by securities underwriters, creditors, insurers and institutional investors.

Filing of additional materials

Significantly, unlike the ECMR, under the HSR Act, a filing person must submit with the Form “all studies, surveys, analyses and reports which were prepared by or for any officer(s) or director(s) for the purpose of evaluating or analysing the acquisition with respect to market shares, competition, competitors, markets, potential for sales growth or expansion into product or geographic markets. . .”.

The Antitrust Division and FTC strictly enforce this filing requirement and place great reliance on such materials when they screen transactions during the initial 30-day waiting period. Persons (including investment bankers) preparing these types of documents should be particularly sensitive to their potential antitrust impact.

Sanctions for non-compliance

Any person who fails to comply with the requirements of the HSR Act is liable for a civil penalty of US\$11,000 for each day of non-compliance. The FTC or the DOJ can also obtain injunctive relief delaying consummation of the acquisition until compliance has occurred. Over the last few years, the FTC has sought more aggressive remedies to deter parties from avoiding compliance with the premerger notification requirements. In addition to pursuing civil penalties and injunctive relief, the FTC recently required divestiture of assets and disgorgement of profits for violations of the HSR Act's notification requirements discovered after the consummation of a transaction. The Act also provides that any transaction or device employed for the purpose of avoiding the reporting requirements of the HSR Act will be disregarded and the failure to file will be treated as a violation of the HSR Act.

Preparation of the filing

The Notification and Report Form requires the parties to provide certain basic information about the transaction and their businesses. Preparation of the filing can take from several days to several weeks depending upon whether the parties have filed notifications in the past and the manner in which they maintain their financial systems.

The content of the filing is far less substantive than Form CO under the ECMR and, for example, does not require the parties to define markets or provide information about affected markets.

The typical investigatory process

Contact with the Antitrust Division or the FTC about the substance of a transaction before its announcement is rare. Unlike in the EU, there is virtually no expectation that contact will occur and little likelihood that the agencies will provide guidance before a transaction is ripe for notification.

Once a transaction has been notified and cleared to either the Antitrust Division or the FTC for review, the agency staff may contact counsel identified on the Notification and Report Form to seek the voluntary submission of additional information during the initial 30-day waiting period. Parties typically cooperate with these preliminary inquiries, although they are not required to do so. Common requests are for the identification of the parties' largest customers or

suppliers and for recent strategic plans not encompassed within the documents required to be filed with the Notification and the Report Form itself.

The parties may submit additional documents which they believe will assist the agency in its evaluation or address specific questions raised by the staff. They may also make written submissions outlining their views of the competitive implications of the proposed transaction, with the objective of avoiding the issuance of a Second Request or narrowing the scope of any such request. In addition, the parties may also meet with the staff to present their views. Such discussions may include counsel, business people, economists or other consultants if the parties believe this will be constructive.

The agency staff will contact customers and suppliers, either those identified by the parties or those they identify themselves. At the preliminary stages these contacts will be informal and third party cooperation will be voluntary. The agencies place great reliance on the views solicited in this process. The staff will also listen to the views of competitors that may be affected by the proposed transaction, but typically gives less weight to these views than that accorded by the European Commission. The staff evaluating a transaction will include lawyers, economists, and supporting investigators.

The staff will make a determination whether the transaction warrants a Second Request. If a Second Request is issued, it commonly is communicated on the final day of the initial waiting period. The parties typically meet with the staff in an effort to develop an approach to compliance with the Second Request (which will provide the staff with the material needed to assess the transaction, while reducing the burden on the parties in retrieving the requested documents and other information). This often is an ongoing process.

The staff may also interview or take sworn testimony from the parties' representatives about the underlying facts relating to the competitive consequences of the transaction. The staff will also continue to speak with third parties, either through voluntary interviews or, less frequently, through sworn testimony; the agencies may also issue formal requests for documents to third parties. Parties objecting to the transaction may be proactive in providing information and suggesting areas for the staff to pursue.

Enforcement guidelines

The Antitrust Division and FTC have issued Merger Guidelines, most recently amended in April 1997, and Guidelines for Collaboration Among Competitors, issued in April 2000, which generally set out the approach they follow in evaluating proposed transactions. The fundamental concerns of US merger policy are:

- "Coordinated interaction" among competitors as markets become more concentrated.

- "Unilateral effects" through market dominance.

The guidelines focus on the question of whether a transaction will create or enhance "market power," which the guidelines define as the ability to profitably maintain prices above competitive levels for a significant period of time. This is a lower threshold than "dominance" under the ECMR. While the guidelines use certain indices derived from market shares to measure market concentration as a starting point, merger analysis invariably is a fact-intensive exercise, driven by the peculiar characteristics of competition in specific markets.

Challenged transactions

The Antitrust Division and the FTC do not have the power to block transactions by themselves. If they decide to challenge a transaction, and cannot reach a negotiated remedy with the parties that will satisfy the government's concerns, the agencies must:

- Commence an action in federal court to halt the transaction.
- Sustain their burden of proof to demonstrate that the proposed transaction will violate the Clayton Act.

The federal courts generally apply the same methodologies used by the Antitrust Division and FTC, although there commonly is some variance between the agencies' enforcement policies and appellate court precedent.

Although the 2001 Annual Report is not yet publicly available, unofficially there were 2,232 Hart-Scott-Rodino Act filings made in financial year 2001. According to the 2000 Annual Report, the Antitrust Division initiated investigations of approximately 3% of all filings and challenged approximately 35% of all transactions investigated. Of those transactions challenged, approximately 56% were either restructured or abandoned prior to a complaint being filed and approximately 42% resulted in the commencement of court proceedings.

According to the 2000 Annual Report, the FTC issued Second Requests in less than 1% of all filings made. Of the transactions for which Second Requests were issued, approximately 72% were challenged, approximately 40% were resolved by consent decree, approximately 20% were restructured or abandoned, and approximately 12% were challenged in court.

The vast majority of transactions pass through the merger review process unchanged. In contested transactions, the parties invariably engage in extensive discussions with the staff and senior agency officials in an effort to find a negotiated remedy that will meet the agency's concerns and still preserve the fundamental economic benefits of the transaction for the parties.

The agencies have a clear preference for structural as opposed to regulatory remedies. They will almost always insist that purchasers of divested operations be identified and approved

before a transaction will be cleared. Recently, the Antitrust Division and the FTC have tightened up their requirements for proposed divestitures to better ensure that the competitive conditions existing before the transaction will continue after any divestitures are completed.

US merger review is an apolitical process. The Antitrust Division and FTC have often stated that they do not and will not take non-competition-related factors into consideration in evaluating a proposed transaction.

Cooperation with other antitrust authorities

The Antitrust Division and FTC actively liaise with merger control authorities in other jurisdictions. The cooperation is especially well-established with Canada and the European Commission. Parties should take this into consideration when dealing with the agencies and, in particular, should be aware that faster timetables in some jurisdictions may force the parties to address remedies earlier than in those situations where only US merger approval is required.

HSR glossary

Person: includes the ultimate parent entity and all entities that the person, directly or indirectly, controls (see definitions below). In the case of corporations, the term encompasses the entire corporate structure, including parent companies, subsidiaries, divisions and all related companies or partnerships under common control with any of the foregoing. In the case of partnerships, the term also includes all partners that control the partnership (see below).

Control: means holding, directly or indirectly, 50% or more of the voting securities of an entity; having the contractual power to designate 50% or more of the directors of a corporation (or the members of a comparable governing body of another type of business entity); or in the case of an entity that has no outstanding voting securities (for example partnerships and limited liability companies), having the right to 50% or more of the profits of the entity, or having the right in the event of dissolution to 50% or more of the assets of the entity.

Entities: means natural persons and virtually every kind of formal and informal organization.

Ultimate parent entity: means an entity that is not controlled by any other entity.

Hold/holding: means beneficial ownership, direct or indirect.

Beneficial ownership: this term is not defined in the HSR Act. However, the indicia of “beneficial ownership” include the following:

- The right to any increase in value or dividends.

- The risk of loss of value.
- The right to vote the stock or to determine who may vote the stock.
- Investment discretion (including the power to dispose of the stock).

The FTC has not adopted the expansive definition of beneficial ownership which is used by the Securities and Exchange Commission for purposes of reporting ownership of more than 5% of a class of equity security under Section 13(d) of the Securities Exchange Act of 1934 (the “investment power test”).

Public bids or tender offers

The US antitrust enforcement agencies are careful to remain neutral in hostile and contested bids and will not permit themselves to be used by a party to gain a procedural advantage. They can and do, where needed, work within tight deadlines dictated by the securities laws. At the same time they will not compromise antitrust principles because they arise in the context of a tender offer battle.

The Hart-Scott-Rodino Act, except in very limited areas, has no provisions uniquely applicable to public bids or tender offers. Parties with substantive antitrust issues must be prepared to move quickly and decisively to address open issues with the FTC or Antitrust Division and perhaps agree to broader remedies that would otherwise result at the end of a more leisurely investigation.

In a tender offer the duration of the pre-merger waiting period turns on whether the offer is a cash tender offer (where cash is the sole consideration) or non-cash tender offer, not on whether the tender offer is friendly or hostile. For cash tender offers the initial waiting period is 15 calendar days from the date of receipt of the acquiring person’s filing; for non-cash offers the waiting period is 30 days.

The HSR Act requires the target to make its filing no later than the fifteenth or, in the case of a cash tender offer, the tenth, calendar day after the date of receipt by the FTC and the DOJ of the acquiring person’s filing. A tender offer target cannot use the HSR Act to stall a transaction; the failure of the acquired person to file does not affect the running of the waiting period.

If there is a Second Request, the parties must wait an additional 30 days in a non-cash tender offer after substantial compliance by the acquiring party before shares can be acquired. In all cash tender offers the additional waiting period is shortened to ten days.

Recent amendments and other proposed changes

1st February, 2001 was the effective date of the first significant changes to the Hart-Scott-Rodino Antitrust Improvements Act in the 26 years since the pre-merger filing and waiting requirements were enacted. The amendments raise the size of transaction threshold for reportable transactions to US\$50 million. This change should cut in half the number of transactions subject to the Act. Other changes, however, will mean that some larger transactions (which previously fell outside the Act) will now be caught.

The most significant amendments to the HSR Act are:

- The threshold for HSR Act notification has been raised from US\$15 million to US\$50 million regardless of the percentage of voting securities or assets being acquired (in other words, the 15% size of transaction threshold was eliminated).
- The size of the person requirement (the requirement that one side of the transaction has sales or assets of US\$10 million or more and the other side has sales or assets of US\$100 million or more) has been eliminated for transactions valued in excess of US\$200 million. As a result, transactions that were not previously reportable under the HSR Act (because, by way of example, one side of the transaction was a newly formed entity and did not have sales or assets in excess of US\$10 million) will now be caught.
- The US\$45,000 filing fee remains for transactions valued at less than US\$100 million; for deals valued at US\$100 million or more but less than US\$500 million, the filing fee has been increased to US\$125,000; for transactions valued at US\$500 million or more, the filing fee is now US\$280,000.
- The length of the waiting period following substantial compliance with a Second Request will be 30 days instead of 20 days. The 10 day period for cash tenders and bankruptcy transactions is not changed. The end of any time period that would be a Saturday, Sunday or legal public holiday is now the next regular business day.
- The FTC and the DOJ adopted official review procedures to expedite the resolution of disputes regarding Second Requests when the filing parties believe that the requested information is unduly burdensome and not reasonably necessary for the federal antitrust enforcement agencies to decide whether to challenge a transaction.

In addition, the FTC issued new rules that relate to the recent amendments to the HSR Act. The new rules also went into effect on February 1, 2001. The most significant of these rules are the new notification thresholds and a transitional rule to address filings made under the former notification thresholds. The notification thresholds specify the levels of ownership of assets/voting securities that cannot be attained or exceeded without making a filing under the

Act. The former notification thresholds were \$15 million, 15% of the voting securities, 25% of the voting securities, and 50% of the voting securities. The new notification thresholds are as follows:

- Assets/voting securities valued above US\$50 million but less than US\$100 million
- Assets/voting securities valued at US\$100 million but less than US\$500 million
- Assets/voting securities valued at US\$500 million or more
- 25% of the voting securities of any issuer if valued at above US\$1 billion
- 50% of the voting securities of any issuer if valued at more than US\$50 million

Similar to the former rules, the notification thresholds are primarily intended to cover situations in which the same acquiring person subsequently acquires additional voting securities of the same issuer for which it has previously filed. Acquisitions of voting securities of the same issuer between these levels not meeting or exceeding the next threshold for a period of five years after expiration or early termination of the HSR waiting period for the transaction that initially crossed the prior threshold are exempt from filing under the HSR Act. If, however, the acquiring person would meet or exceed the next filing threshold as a result of a subsequent acquisition of voting securities, a subsequent filing is required and the applicable waiting periods need to be observed.

The FTC also issued a transitional rule in order to address filings made under the former notification thresholds. Acquiring persons who filed under the former notification thresholds and who have met or crossed the threshold for which they have filed within a year of the waiting period's expiration, but whose five-year period for making additional acquisitions has not expired as of February 1, 2001, will have until February 1, 2002 or the end of the original five-year period for making additional acquisitions, whichever comes first, to acquire up to what was the next reporting threshold at the time they filed, and they may do so without making another filing under the HSR Act, even though they might cross one of the "new" notification thresholds. Any acquiring person filing on or after February 1, 2001 must observe the new notification thresholds.

The FTC has also proposed certain additional revisions to the existing rules affecting foreign acquisitions. These changes are expected to be made during 2002. The most significant proposal concerns the exemptions for acquisitions of foreign assets and voting securities of foreign issuers. The major changes would:

- Raise both the former US\$15 million and US\$25 million thresholds that trigger filing obligations for foreign transactions to US\$50 million.

- Extend the obligation to report to certain acquisitions of foreign assets by foreign persons.