a few things you should know …

Hart-Scott-Rodino and Foreign Merger Notification Requirements

Antitrust & Global Competition: This edition of *A Few Things You Should Know* concerns antitrust, Hart-Scott-Rodino filings, and foreign merger notifications. Antitrust authorities in the U.S. and competition authorities abroad often require certain transactions to be notified prior to consummation so that the deals can be reviewed for potential antitrust implications. Preparing for antitrust review, drafting deal documents to include the relevant antitrust clauses, and understanding the rules of the road with respect to pre-consummation conduct are all important issues to consider for potential transactions.

- ## HART-SCOTT-RODINO FILINGS

  All M&A deals need to be assessed for reportability under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (§ 7A of the Clayton Act) ("HSR"). M&A transactions (including proposed mergers or acquisitions of voting securities, non-corporate interests, or assets) are reportable (i.e., they must be reported to the Federal Trade Commission (the "FTC") and the Department of Justice (the "DOJ") prior to consummation) if they satisfy both (i) a "size of person" test and (ii) a "size of transaction" test, each of which are benchmarked to annually adjusted thresholds—currently, the size of person test requires one party to have total assets or annual net sales of $156.3 million and another party to the transaction to have total assets or annual net sales of $15.6 million, and the size of transaction test requires a deal value of at least $78.2 million. The size of person test is phased out for the largest deals (currently the cutoff is $312.6 million in deal value). If a transaction is reportable, the parties must wait a specified period, usually 30 days (15 days for a cash tender offer or bankruptcy sale) after making an HSR filing, before closing the transaction. Parties may request "early termination" of the waiting period, which the agencies may grant if they find that there are no substantive concerns with a reported transaction. An HSR filing also may be submitted before the definitive agreement is signed, but there must be at least a letter of intent defining the specific parties and the contours of the deal.

  The HSR filing itself calls for information about the parties (including their parent entities, subsidiaries, minority holdings, and associates), the transaction, revenues broken out by specific industry classification codes issued by the U.S. Census Bureau (North American Industry Classification System ("NAICS") codes), and any overlaps between the parties' NAICS codes. Additionally, the parties must submit any documents created by or for an officer or director that discuss competition, competitors, market shares, markets, sales growth, or expansion into product or geographic markets, as well as documents prepared by investment bankers, confidential information memoranda, and discussions of synergies or efficiencies. Antitrust counsel can assist the parties in identifying responsive documents, which can include emails between or among officers and directors, board presentation materials, and handwritten notes. HSR filings generally take one to two weeks to prepare, and they require significant input from each party. Each party prepares and submits its own HSR filing, and the filings are generally coordinated because the waiting period does not begin to run until both parties' HSR reports are on file. HSR filings are strictly confidential and are Freedom of Information Act–exempt. Note that the FTC publishes the names of the parties that receive early termination of the HSR waiting period.

- ## SUBSTANTIVE ANTITRUST RISK ASSESSMENT

  In reviewing an HSR filing, the FTC and the DOJ analyze the risk of potential competitive harm to consumers arising from the prospective transaction. The agencies examine the overlapping NAICS code revenues to determine

whether there are specific product and geographic markets in which the parties are direct competitors, and then assess the competitive implications of the transaction. The agencies consider input from customers, competitors, and potential new entrants and rely on econometric analysis to evaluate whether the transaction could result in an increase in consumer prices, a restriction in output, or a stifling effect on research, development, and innovation. In addition to an extended review period, if the agencies ultimately determine that such implications exist, the parties risk forced divestitures or litigation. Likewise, in situations in which a reported deal has not been publicly announced, the parties need to consider the likelihood that customers and competitors of the parties are likely to learn about it through the investigation. Strategic acquirors will generally face greater scrutiny and antitrust risk than financial investors that do not participate in overlapping product markets. It is important to assess substantive antitrust risk early in the deal process because the level of risk often influences the drafting of certain clauses in the acquisition agreement, as discussed below.

- HSR FILING FEES & TIMING

  The HSR filing requires payment of a filing fee that varies based on the value of the deal. The filing fees, which are adjusted periodically, currently range from $45,000 to $280,000, and the fee is per transaction (not per party). Under the statute, the acquiring party is responsible for paying the fee, but the parties often include language in the acquisition agreement to split the fee. The acquisition agreement should also provide for a window within which both sides must file their HSR report. Typically this window ranges from five to ten days after signing the acquisition agreement, although shorter windows are feasible if the HSR preparation process begins well in advance of the signing.

- ANTITRUST CLEARANCE COVENANTS

  The acquisition agreement should clearly set out the respective obligations of the parties to cooperate with each other and with the antitrust authorities in addressing and resolving antitrust questions during the HSR and applicable foreign merger control clearance processes. The specific language for antitrust clearance covenants will be influenced by the nature and extent of the substantive antitrust risks, and, for acquirors, may range from the less onerous “reasonable best efforts” for a deal with less competitive risk, to the harder line of “hell or high water” if litigation, divestitures, or consent decrees are among the governmental requirements that could reasonably be expected. Antitrust clearance covenants typically also address provision of documents and information to the agencies if a “second request” is issued (which tolls the HSR waiting period until substantial compliance with the additional request is met), along with taking cooperative steps to quickly resolve any antitrust questions by participating in meetings or providing information to the agencies that would enable the regulators to close their inquiry expeditiously. Parties also often negotiate reverse break-up fees to incentivize compliance with an extended antitrust clearance process or mitigate significant antitrust clearance risk.

- CONDUCT OF BUSINESS COVENANTS

  During the pendency of the HSR waiting period, under law, the parties may not prematurely integrate their businesses and must continue to operate as independent entities. Therefore, the acquiring party has an interest in protecting its investment in the target by ensuring that the target does not undertake any actions that could reduce the value of the business or impose restrictions or limitations on the operation of the business following closing. The antitrust enforcement agencies have challenged provisions in acquisition agreements that restricted a target’s pre-closing activities to such a degree that the acquiror effectively exercised control over the target. Acquisition agreements typically address this problem by providing express permission for the target to continue to conduct its activities “in the ordinary course of business, consistent with past practices” (or words of similar effect) or, alternatively, banning new contracts that would adversely and materially affect the target.

- DUE DILIGENCE AND INFORMATION SHARING

  The parties are prohibited by law from sharing competitively sensitive information that would afford the other party an unfair advantage if the deal is not consummated (e.g., pricing information, costs, details on pending research or pipeline projects, etc.). In structuring due diligence, data rooms, and integration teams, it is important to restrict access to this type of sensitive information and maintain "arm's-length" discussions. As a rule of thumb, it is generally acceptable to share historical data or aggregated data, but sharing of customer-specific information is generally not acceptable. As practical guidance, each party should consider whether the information in question is something it would be comfortable sharing with a competitor in the absence of a deal; if not, then the information is likely competitively sensitive and should be restricted.

- INTEGRATION WITHOUT GUN-JUMPING

  To promote the maintenance of the parties as independent entities during the pendency of the HSR waiting period, U.S. antitrust laws restrict the parties from prematurely integrating any operational functions prior to consummation of the deal ("gun-jumping"). For example, the acquiring party is not allowed to exercise any control over operational decisions (including pricing, production, sales, etc.). Consequently, integration efforts should be structured to use "clean teams" (i.e., groups comprised of individuals not otherwise actively involved in the transaction) where possible, and joint communications should be reviewed by antitrust counsel. Additionally, integration should focus on processes, ensuring system compatibility and establishing roadmaps, as opposed to actually merging operations or transferring decision-making control over the acquired entity. Historical or "dummy" data should be used to test the compatibility of systems instead of current customer, account, financial, sales, or pricing data. Antitrust counsel should be engaged to monitor integration team meetings and joint calls to customers and suppliers to ensure that such communications do not cross the gun-jumping line.

- FOREIGN MERGER NOTIFICATION ANALYSIS

  In parallel to the HSR protocol in the U.S., there are numerous other competition (i.e., antitrust) regimes around the world that may require notification of a proposed transaction. Some of these regimes have a pre-merger suspensory process like the U.S., whereas others have a post-merger notification or a voluntary notification approach. Additionally, some foreign filings are particularly detailed, extensive, and time-consuming. Antitrust counsel should be consulted early in the process for any transactions with foreign companies, subsidiaries, assets, or sales to determine what foreign filings may be required, as some competition filings can take months to process and complete. Whether a transaction is reportable in a foreign jurisdiction depends on the particular requirements of the country in question. Some jurisdictions rely on turnover data; others look to share of local supply or local assets. Nearly all foreign jurisdictions require some degree of local effects before a filing is required. Once the preliminary determinations on which foreign filings may be necessary are made, antitrust counsel can help prepare the filings in conjunction with local counsel in the foreign jurisdiction.

Prepared by Barry J. Reingold (e-mail: BReingold@perkinscoie.com; telephone: 202.654.6226) and K. Shiek Pal (e-mail: KPal@perkinscoie.com; telephone: 202.654.1719), July 2016

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