MERGERS & ACQUISITIONS VIII: ANTITRUST MERGER CONTROL & CLEARANCE: DEAL POINTS

September 2022

I. Executive Summary

This is the eighth in our series of advisories on Mergers & Acquisitions ("M&A"). Its predecessors in the series, "Mergers & Acquisitions I: Overview and Transaction Types" ("M&A I"), "Mergers & Acquisitions II: Tax Structuring Considerations" ("M&A II"), "Mergers & Acquisitions III: Acquisition Consideration" ("M&A III"), "Mergers & Acquisitions IV: Preliminary Documentation" ("M&A IV"), "Mergers & Acquisitions V: Stock Purchase Transactions" ("M&A V"), "Mergers & Acquisitions VI: Asset Purchase Transactions" ("M&A VI") and "Mergers & Acquisitions VII: Mergers" ("M&A VII") are available at the preceding links, along with other M&A resources on our website at Kurtin PLLC Mergers & Acquisitions and on Lexology at the Kurtin PLLC Lexology Hub.

This advisory will focus on the antitrust (competition) issues that can arise in U.S. M&A transactions, for which certain U.S. government agencies exercise oversight, what must be done to obtain their approval for those transactions to close, and the direction of government policy on antitrust M&A review, which has shifted under the Biden administration from a decades-long relatively "hands-off," tolerant, laissez-faire policy to a markedly more interventionist, activist policy, which all dealmakers must be aware of and account for in planning and structuring their transactions.

In this and all future editions of this M&A series, familiarity with the preceding editions linked above will be assumed and previously defined terms will be used without further introduction. Following the discussion are "Deal Points" on important considerations in the purchase or sale of a business: what to do, and *what at all costs not to do*.

II. Merger Review and Clearance

Section 7 of the Clayton Act of 1914 (15 U.S.C. 12 *et seq*., §18), passed to give teeth to the Sherman Antitrust Act of 1890 (15 U.S.C. §1 *et seq*.), prohibits mergers and acquisitions of either stock or assets whose effect "may be substantially to lessen competition, or tend to create a monopoly." The Clayton Act provides for a private right of action for violations of either it or the Sherman Act, with the

possibility of treble damages, as well as criminal penalties. An amendment to the Clayton Act, the Hart-Scott-Rodino Antitrust Improvements Act of 1976 ("HSR") (§7A of the Clayton Act, 15 U.S.C. §18a) requires the parties to acquisitions of any voting securities or assets of the acquired party above certain thresholds to notify the U.S. Federal Trade Commission ("FTC") and Department of Justice ("DoJ"), and await the expiration of a mandatory waiting period (30 days generally, 15 days in the case of a cash tender offer) prior to the closing.

HSR reporting obligation thresholds are updated by the FTC yearly. Through the balance of 2022, HSR reporting obligations for most kinds of transactions arise when: (a) either the Acquiror or the Target is engaged in U.S. commerce or in any activity affecting U.S. commerce; *and either* (b) as a result of the transaction, the Acquiror would hold voting securities or assets of the Target in excess of $403.9 million *or* (c) as a result of the transaction, the Acquiror would hold voting securities or assets of the Target in excess of $101.0 million but not in excess of $403.9 million *and* (i) either the Acquiror or Target has total assets or annual net sales of at least $202.0 million *and* (ii) the other party has total assets or annual net sales of at least $20.2 million. New 2023 reporting thresholds will be set by the FTC early in the new year.

Filing fees for transactions that must be reported range from $45,000 (for transactions valued in excess of $101.0 million but less than $202.0 million), $125,000 (for transactions valued at $202.0 million but less than $1.01 billion), to $280,000 (for transactions valued at $1.01 billion or more). The maximum civil penalties for non-compliance with the notification and waiting period are $46,517 per day.

The qualification "voting securities" exempts bonds, notes, mortgages, and similar instruments and is limited to securities allowing the owner or holder to vote for directors, or analogous persons in the case of unincorporated entities. Also, rules and regulations assess the total assets and annual net sales thresholds with reference not only to the party to the transaction, but to the total assets or annual net sales of companies or individuals under an "ultimate parent entity" with "control" established by 50% or greater ownership of voting rights or rights to distribution. The present contractual right to appoint at least half of the board of directors or equivalent governing body also establishes "control" for HSR purposes – convertible securities not conferring a present right to vote do not count. "Assets" include exclusive licenses for purposes of triggering HSR filing obligations, although rules and regulations governing license territoriality, expiration, and reversionary rights to licensor may also come into play in assessing whether a given transaction is subject to HSR reporting. It is important to realize, contrary to

many M&A parties' assumptions that HSR reporting obligations are for the largest transactions only, that they can be triggered by relatively small transactions that cause the parties to pass the thresholds.

A joint venture ("JV") in which a corporation, limited liability company ("LLC"), partnership or limited partnership ("LP") is formed to embody the joint venture can activate HSR's reporting requirements, because HSR treats each JV participant as an Acquiror and the JV entity that is formed as a Target. The formation of a general partnership or an LP or transfer of less than all of the interests in a partnership ordinarily does not require a HSR filing, subject to the rule concerning acquisition of the voting securities for any issuer included in the partnership.

By contrast, transfer of all of a partnership's interests is considered an asset acquisition and is reportable under HSR. The formation of an LLC may trigger HSR reporting obligations if two or more pre-existing, separately controlled businesses are contributed and at least one of the members controls the LLC, in that it has a 50% "membership interest" or a right to 50% of the LLC's assets on dissolution. Post-formation acquisitions of LLC interests are not reportable except in certain circumstances in which the acquisition is treated as a new LLC formation.

Exemptions from the HSR filing requirements exist, notably for transactions in the ordinary course of business, acquisitions of certain voting securities or non-U.S. assets of a non-U.S. entity, and in the case of an acquisition by an institutional investor of 15% or less of an issuer's voting securities that is made strictly for investment purposes (the purchaser has no intention of participating in the issuer's business decisions) – another type of transaction deemed to be in "the ordinary course of business." The FTC or DoJ may request from the parties additional documentation and extensions of the waiting period. It should be noted that other U.S. government agencies have concurrent jurisdiction with the FTC and DoJ to approve M&A transactions; for example, the Federal Communications Commission ("FCC") has concurrent jurisdiction to approve M&A transactions for certain parties in the broadcast, wireline and wireless communications and satellite industries; however, the FCC's review is conducted under a "public interest" standard separate from the HSR/Clayton Act-based review by the FTC and DoJ.

Once documentation requests have been fully complied with and during the mandatory waiting period (including as extended), the FTC or DoJ may move for a preliminary injunction to block the proposed acquisition. If no such action is taken and the mandatory waiting period has expired, the transaction is deemed to have passed HSR review and may proceed, subject to any other required regulatory review.

III. Merger Review Policy Update

Since the beginning of the Biden administration in 2021, we have been covering the shift from a decades-long relatively tolerant, hands-off merger review and clearance policy to a far more activist, interventionist posture under FTC Chair Lina Khan and DoJ Antitrust Chief Jonathan Kanter. Both Khan and Kanter are critics of Big Tech companies and consider companies like Meta/Facebook, Alphabet/Google, Apple, Amazon and Microsoft to be serial monopolistic enterprises that suppress competition and attempt to monopolize their industries, often to the detriment of competition, innovation and consumers. Since 2021, the FTC, often in concert with DoJ, has (all following cited articles available at Kurtin PLLC Mergers & Acquisitions):

- Issued a warning to M&A parties not to seek to avoid HSR filings by structuring deals to retire Target debt in place of paying cash consideration (see, "FTC Issues Warning on Use of Debt Retirement in M&A Transactions to Avoid HSR Filings," Sept. 17, 2021);

- Rescinded Vertical Merger Guidelines put in place by the prior administration only in 2020 and deemed too permissive (see, "FTC Sets Ambitious M&A Enforcement Agenda," Sept. 29, 2021);

- Reinstituted a restrictive "prior approval" Merger control review policy for requiring prior approval of transactions by companies that had previously engaged in anticompetitive conduct (see, "FTC Reinstitutes Restrictive "Prior Approval Merger Control Review Policy," Oct. 26, 2021); and

- Launched a joint public inquiry to detect and prevent anticompetitive mergers (see, "FTC and DoJ Launch Effort to Restrict Anticompetitive Mergers," Jan. 24, 2022).

Also, since the beginning of the Biden administration, the FTC has sued to block mergers in several cases, including four involving hospital/health care providers and Facebook parent Meta to block its acquisition of virtual reality company Within Limited. Most recently, in September, DoJ Antitrust Division Chief Kanter announced a review of the "efficiencies" rationale, in which many M&A parties for years have successfully urged that their deals be approved because the merged companies would be more efficient market players for both themselves and their customers, generating cost savings. Kanter described efficiency arguments as an area in which antitrust policy has diverged from the law.

IV. Deal Points

Deal Point: Don't fail to report a reportable transaction.

On Sept. 15, 2021, the FTC issued a report showing that 94 of 616 studied Big Tech sector M&A transactions between 2010 and 2019 that should have been reported under HSR were not (see, "FTC Sets Ambitious Enforcement Agenda," above, where the report itself can be accessed). 65% of the 616 transactions were between $1 million and $25 million, emphasizing that HSR reporting obligations do not arise only in the largest M&A transactions. 36% used assumption of debt as a structuring device to avoid HSR reporting thresholds, which cash payment would have triggered. Also, more than 79% used deferred or contingent compensation to founders and key employees to avoid paying HSR-triggering Acquisition Consideration. Bottom line: all of these techniques to avoid HSR reporting are on the FTC and DoJ radar screen, and parties should make sure that their transactions do not hit the thresholds even if the Acquisition Consideration were paid in cash. New sheriffs are in town. Don't fail to report a reportable transaction or rely on financial engineering not to do so.

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