Extension Of The HSR Waiting Period Increases Acquirer Risk

By **Thomas Donovan, Allen Bachman and Kenneth Knox** (October 15, 2021)

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Citing a shortage of resources to respond to what it called a "tidal wave of merger filings," the Federal Trade Commission has begun sending warning letters to the parties to many mergers and acquisitions stating that it has not completed its antitrust investigation of the transaction during the waiting period under the Hart-Scott-Rodino Antitrust Improvements Act.[1]

Further, the FTC has declared that it will continue its investigation after the expiration of the waiting period and that, if the parties close the transaction before the FTC completes its investigation, they do so at their own risk, since the FTC may pursue divestiture of the acquired business after closing.[2]

Earlier this year, the increased volume of filings had already led the FTC to suspend the practice of granting early termination of the statutory waiting period.[3] Until now, the FTC and the Antitrust Division of U.S. Department of Justice had generally completed their review within the statutory waiting period, and parties who made HSR filings had almost always known by the time that the waiting period would expire whether the transaction would face a federal antitrust challenge.

The latest announcement may create further delays for deals — including those seeking year-end closings — and may introduce additional risk, with some buyers facing the prospect of closing deals in the face of an ongoing FTC review.[4] Post-closing divestitures often result in sales at fire-sale prices.

This article will analyze the near-term impact of this new FTC practice on pending transactions and consider the possible longer-term impact on broader public policy considerations and how that might impact the M&A market under the Biden administration.

Background

The HSR merger review process generally requires the parties to transactions with a fair market value that exceeds annually adjusted thresholds to file premerger notifications with the FTC and the Antitrust Division and pay the associated filing fee.[5] The parties must then wait 30 days,[6] the initial waiting period, before closing.

Prior to the end of the initial waiting period, the FTC or the Antitrust Division may issue a request for further information, or second request.

After the parties substantially comply with the second request, the parties must wait an additional 30 days, known as the final waiting period, before closing the transaction.[7]

The purpose of the HSR notification and its statutory waiting requirements is to allow the antitrust enforcement agencies to challenge anti-competitive transactions before they are consummated and thus to avoid the competitive harm imposed by the consolidation, as well

as the problems of the so-called unscrambling the egg once the transaction has closed and the acquirer is free to control and intermingle or further transfer the assets of both the acquiring and the acquired companies.[8]

Before the FTC initiated the use of warning letters, M&A agreements typically contained a closing condition tied to expiration or termination — or similar wording — of the statutory HSR waiting period, but did not expressly address this new concept of a warning letter.[9]

Effects of New FTC Practice

In transactions in which the M&A agreements were executed before the FTC introduced the concept of a warning letter and in which the M&A agreements utilize the traditional waiting period language as a condition to closing, disputes may arise over whether that closing condition is satisfied if a warning letter has been issued when the waiting period expires.

Parties to such executed agreements should closely review the precise wording of those agreements and other evidence of the parties' intent to determine their respective rights and obligations in considering how to proceed.

Parties currently negotiating yet-to-be-signed M&A deals should carefully review with antitrust counsel their draft transaction agreements and how to address the parties' respective rights and obligations in the event a warning letter is received.

Agreeing upon such contract terms is complicated because:

- The warning letters typically contain no commitment regarding when the FTC will complete its investigation; and

- Some of the transactions in which warning letters have been issued appear to have little competitive effect in the market under traditional standards.

Buyers may seek to treat receipt of a warning letter as being equivalent to receipt of a second request, triggering an extended waiting period or otherwise providing that they have no obligation to close until circumstances indicate that an FTC challenge is unlikely.

Sellers, on the other hand, will likely resist such treatment based on the argument that not only has the FTC has not formally taken action and the waiting period has, in fact, expired, but also the FTC may never provide any assurance that a challenge is unlikely.

Sellers will prefer only some very limited and closely defined additional contractual waiting period after which buyer would be required to close the transaction unless a formal second request or a formal complaint challenging the transaction has been received. The appropriate terms, however, will depend considerably on the anticipated antitrust risks inherent in the transaction and other transaction-specific circumstances.

Publicly reported terms of transactions following the announcement of the warning letter procedure have included extension of the closing for a limited period; extension of the closing date for as long as the FTC or Antitrust Division continues actively to investigate the transaction; indefinite extension of the closing; and no extension at all.

Acquisition agreements also typically include covenants regarding the parties' respective obligations to pursue antitrust filings and the level of effort required by both parties in

seeking clearance. These provisions also will need to be reconsidered in light of this new FTC procedure.

Extended Investigations' Consistency With Other Biden Policies and Actions

When considering the antitrust risks of a particular deal, as well as possible impacts on the broader M&A market, it is important to consider the recent FTC procedural change in the context of other recent statements and actions from the Biden administration aimed at promoting competition and, possibly, more aggressively limiting M&A transactions.

President Joe Biden's executive order on promoting competition in the American economy declared:

> [O]ver the last several decades, as industries have consolidated, competition has weakened in too many markets, denying Americans the benefits of an open economy and widening racial, income, and wealth inequality.[10]

The order added that "Federal Government inaction has contributed to these problems, with workers, farmers, small businesses, and consumers paying the price."[11] One of the most important purposes of the federal antitrust laws, Biden said in the orther, is "resisting consolidation and promoting competition within industries through the independent oversight of mergers, acquisitions, and joint ventures."[12]

He called upon the FTC and the Antitrust Division "to enforce the antitrust laws fairly and vigorously" and to consider revising the merger guidelines.[13]

Recently appointed FTC Chair Lina Khan has similarly declared:

> [E]ven as the agency tackles the proliferation of unfair and deceptive practices, the current merger boom threatens to make these worse. Significant market consolidation deprives consumers, workers, and independent businesses of choice, further enabling dominant firms to engage in unfair practices.[14]

Kahn added that she was "deeply concerned that the current merger boom will further exacerbate deep asymmetries of power across our economy, further enabling abuses."[15] In the context of a letter to Sen. Elizabeth Warren, D-Mass., regarding a particular vertical merger in the defense industry, she declared:

> While structural remedies generally have a stronger record than behavioral remedies, studies show that divestitures, too, may prove inadequate on the face of an unlawful merger. In light of this, I believe the antitrust agencies should more frequently consider opposing problematic deals outright.[16]

Following the executive order, the FTC has withdrawn its support for the guidelines on vertical mergers that were jointly adopted with the Antitrust Division in 2020, and both agencies have announced a review of the existing guidelines for both horizontal and vertical mergers.[17]

In July 2021, the FTC also withdrew its 1995 policy statement limiting the use in merger consent orders of provisions requiring the consenting parties to give prior notice of future acquisitions in the affected market, even where the HSR would not require a filing, and requiring the acquirer to obtain prior FTC approval before making further acquisitions in the affected market, thereby shifting the burden of proof to the merging parties.[18]

Although the FTC has not articulated standards regarding when it will employ such prior-notice and prior-approval provisions in future consent orders, the FTC's action suggests broader use of such provisions in the future.

Conclusions

The new FTC policy introduces significant uncertainty and potential additional delays in an M&A market in which deals are being reached at a record pace. Many parties typically attempt to close transactions before the end of the calendar year. That objective is jeopardized both by the blanket denial to consider requests for early termination of the initial waiting period and, in some instances, by the FTC's introduction of the use of warning letters.

Parties should closely review existing M&A agreements in order to determine their respective rights and obligations if a warning letter is received and should pay particular attention to the drafting of pending M&A agreements to ensure that their respective rights and obligations in such a situation are clearly defined.

From a longer-term policy and market perspective, members of the antitrust bar are debating the purpose and the effect of the warning letters. One commonly held view is that the FTC is truly overwhelmed with the number of HSR filings and intends, when it is able to catch up, to go back and reconsider potentially problematic deals.

Perhaps the warning letters are an attempt to avoid appearing to have approved transactions that later appear to run afoul of the revised merger guidelines that both the FTC and the Antitrust Division have said they are working on. However, no timetable for the release of new merger guidelines has been published. The FTC's or the Antitrust Division's decision not to challenge a transaction at the close of the waiting period does not legally foreclose either agency from later challenging the transaction.[19]

Nevertheless, defendants in merger cases may be expected to attempt to utilize the FTC's silence at the end of the waiting period to undermine the credibility of the FTC's case or to argue that by investing in the acquired company the buyer has been harmed by the FTC's silence at the end of the waiting period. And if the FTC seeks a preliminary injunction requiring rescission of the transaction during the administrative proceeding challenging the transaction, the district court is required to give some consideration to private equities.[20]

However, no amount of private equities is sufficient to defeat divestiture where a compelling case has been made that a merger transaction is harmful to competition and the public interest.[21] Accordingly, any litigation advantage for the FTC arising from the warning letters is likely to be minimal.

Alternatively, the warning letters may be part of a comprehensive policy shift to aggressively dampen an overactive M&A market and confront what the new administration views as undesirable economic or political concentration.

Tim Wu, appointed by Biden to head the National Economic Council; Lina Khan, the new chair of the FTC; and Jonathan Kanter, nominated by the president to head the Antitrust Division, are all supporters of the New Brandeis school in antitrust.[22] The New Brandeis school, purportedly taking their inspiration from progressive lawyer and later, U.S. Supreme Court Justice Louis Brandeis, see rising market power as causally linked with economic inequality.

A democratic distribution of power, opportunity, and economic liberty are all seen to be jeopardized by monopolies and increased market power.[23] Preventing further concentrations of economic power by discouraging mergers in general thus promotes the economic liberty and democratic distribution of power that they see as the goals of the antitrust laws.

Further clarity regarding the FTC's strategy. and the Antitrust Division's response to it, may be forthcoming with the crystallization of leadership at the top of both agencies. Rohit Chopra has formed a part of the Democratic majority in the FTC since the advent of the Biden administration, but his appointment as director of the Consumer Final Protection Bureau was confirmed by the Senate on Sept. 30.[24]

Biden has nominated Alvaro Bedoya to fill the resulting vacancy in the FTC.[25] Meanwhile, Kanter's confirmation hearing as head of the Antitrust Division occurred Oct. 6.[26] With the leadership of both enforcement agencies becoming established, it is reasonable to expect the agencies to begin to clear up the uncertainty.

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[1] Hart-Scott-Rodino Antitrust Improvements Act (HSR), 15 U.S.C. §18a.

[2] Holly Vedova, Adjusting merger review to deal with the surge in merger filings, Federal Trade Commission (Aug. 3, 2021), www.ftc.gov/news-events/blogs/competition-matters/2021/08/adjusting-merger-review-deal-surge-merger-filings.

[3] Press Release, Fed. Trade Comm'n, DOJ Suspends Discretionary Practice of Early Termination (Feb. 4, 2021) www.ftc.gov/news-events/press-releases/2021/02/ftc-doj-temporarily-suspend-discretionary-practice-early.

[4] The Antitrust Division has not declared whether it is contemplating a similar procedural change.

[5] Exemptions are available for some transactions. 15 U.S.C. § 18a(c); 11 C.F.R. §§ 802.1–802.80.

[6] The Initial Waiting Period (and Final Waiting Period) is 15 days for certain transactions by persons in bankruptcy and for cash tender offers. 15 U.S.C. § 18a(b)(1)(B); 11 U.S.C. § 363(b)(2).

[7] U.S.C. § 18a (e)(2).

[8] William J. Baer, Reflections on 20 Years of Merger Enforcement Under the Hart-Scott-Rodino Act, Federal Trade Commission (Oct. 31, 1996), https://www.ftc.gov/public-statements/1996/10/reflections-20-years-merger-enforcement-under-hart-scott-rodino-act.

[9] For instance, the 2011 American Bar Association Model Stock Purchase Agreement suggests the following wording as an HSR closing condition:

Any waiting period under the HSR Act applicable to consummation of the Contemplated Transactions will have expired or been terminated, and no action will have been instituted by the U.S. Department of Justice or Federal Trade Commission challenging or seeking to enjoin consummation of the Contemplated Transactions, which action shall not have been withdrawn or terminated.

[10] Exec. Order No. 14036, 86 Fed. Reg. 36,987 (July 9, 2021), https://www.federalregister.gov/documents/2021/07/14/2021-15069/promoting-competition-in-the-american-economy.

[11] Id.

[12] Id. at 36,989.

[13] Id. at 36,991.

[14] Press Release, Fed. Trade Comm'n, FTC Testifies Before House Energy and Commerce Subcommittee on Legislation to Modify the Commission's Authority and Address Challenges Facing the Agency (July 28, 2021). https://www.ftc.gov/system/files/documents/public_statements/1592966/oral_remarks_of_chair_lina_khan_on_hearing_re_transforming_the_ftc_legislation_to_modernize_consumer.pdf.

[15] Id.

[16] Letter from FTC Chair Khan to Senator Elizabeth Warren, NEW: FTC Chair Khan Shares Warren's Concerns About Giant Defense Industry Mergers, Elizabeth Warren (Aug. 12, 2021), https://www.warren.senate.gov/oversight/letters/new-ftc-chair-khan-shares-warrens-concerns-about-giant-defense-industry-mergers.

[17] Press Release, Fed. Trade Comm'n, FTC Withdraws Vertical Merger Guidelines and Commentary (Sept. 15, 2021) www.ftc.gov/news-events/press-releases/2021/09/federal-trade-commission-withdraws-vertical-merger-guidelines; Press Release, Fed. Trade Comm'n, Statement of FTC Chair Lina Khan and Antitrust Division Acting Assistant Attorney General Richard A. Powers on Competition Executive Order's Call to Consider Revisions to Merger Guidelines (July 9, 2021), https://www.ftc.gov/news-events/press-releases/2021/07/statement_ftc-chair-lina-m-khan-antitrust-divison-acting.

[18] Press Release, Fed. Trade Comm'n, FTC Rescinds 1995 Policy Statement That Limited the Agency's Ability To Deter Problematic Mergers (July 21, 2021), https://www.ftc.gov/news-events/press-releases/2021/07/statement-ftc-chair-lina-m-khan-antitrust-division-acting.

[19] In the Matter of Seven & iHoldings Co., Ltd., Docket No. C-4748 (FTC, July 20, 2021); Chicago Bridge & Iron Co. N.V. v. FTC, 534 F.3d 410, 420–21 (5th Cir. 2008).

[20] FTC v. Elders Grain, Inc., 868 F.2d 901–03 (7th Cir. 1989).

[21] Id.

[22] Jacob M. Schlesinger, The Return of the Trustbusters, Wall St. Journal (Aug. 27, 2021), www.wsj.com/articles/the-return-of-the-trustbusters-11630076102.

[23] Lina Khan, The New Brandeis Movement: America's Antimonopoly Debate, 9, J. of Eur. Law & Prac. (March 2018), https://academic.oup.com/jeclap/article/9/3/131/4915966.

[24] Aaron Gregg, Senate confirms Rohit Chopra to lead Consumer Financial Protection Bureau, Wash. Post (Sept. 30, 2021), https://www.washingtonpost.com/business/2021/09/30/rohit-chopra-cfpb/.

[25] Press release, The White House, President Biden Announces Ten Key Nominations (Aug. 10, 2021), https://www.whitehouse.gov/briefing-room/statements-releases/2021/08/10/president-biden-announces-ten-key-nominations/.

[26] https://www.judiciary.senate.gov/meetings/09/29/2021/nominations.