



# Acquiring US Business: Anticipating anti-trust filings and avoiding “gun-jumping” risks

by **Harry T. Robins** and **Michael J. Pedrick**

- A mid-sized UK company seeks to acquire the assets of a business as its first foothold in the US.
- A UK manufacturer and an established US trading partner believe they can more effectively bid on larger projects if they form a joint venture.
- A UK venture fund’s existing minority investment in a poorly-performing US company is at risk, with requests that it increase its investment and, with it, the fund’s level of ownership.
- A UK-based service provider is negotiating to buy a target, but wants to make sure the revenues are not just smoke and mirrors by examining the contracts and meeting with customers.
- A multinational corporation has signed a purchase agreement with a strategic target, and wishes to begin its integration efforts pre-closing.

In each of the first three examples above, it may be necessary for the parties to report the potential transaction to the US Federal Trade Commission and the US Department of Justice under the Hart-Scott-Rodino Antitrust Improvement Act (“HSR”) and await clearance. In each of the last two examples, the parties’ activities leading up to a transaction

could expose the parties to fines, penalties and delay in the approval of the underlying transaction if not undertaken mindful of antitrust authorities’ views of such behavior.

## HSR FILING: A GENERAL REVIEW

### Transactions which are Potentially Reportable

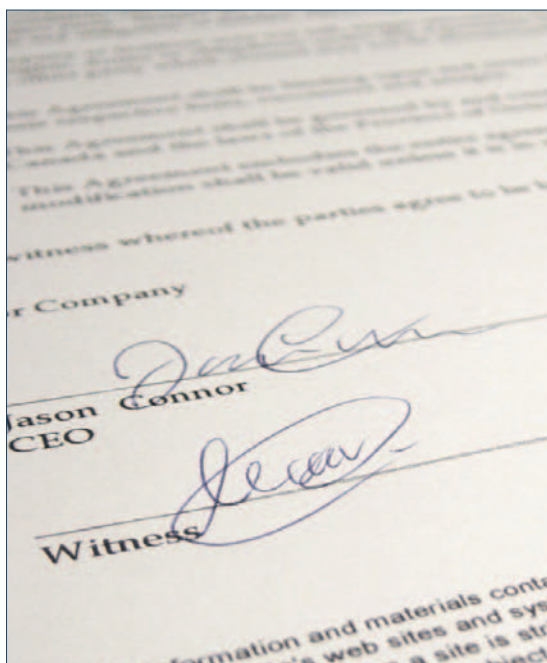
Most parties expect that a potential capital stock or asset acquisition in the US may require filing under HSR, but may be surprised that it is triggered in other transactions. Transactions that are **potentially** reportable include:

- Acquisition of assets;
- Acquisitions of voting securities of a corporation;
- Acquisitions of “control” of an existing partnership or limited liability company;
- Formations of corporate joint ventures;
- Formations of partnerships or limited liability companies where at least one participant acquires a “controlling” interest;
- Exclusive intellectual property licenses.

### Thresholds for Reporting

For parties considering such a transaction, the next determination will be whether the thresholds that trigger reporting are met. As a general rule, HSR requires both acquiring and acquired persons file notifications if all of the following post-adjustment jurisdictional thresholds are met:

- One person has sales or assets of at least \$106.2 million;
- The other person has sales or assets of at least \$10.7 million;
- As a result of the transaction, the acquiring person will hold an aggregate amount of stock and assets of the acquired person valued at more than \$53.1 million; or
- As a result of the transaction, the acquiring person will hold an aggregate amount of stock and assets of the acquired person valued at more than \$212.3 million, regardless of the sales or assets of the acquiring and acquired persons.





Conditions a. and b. are generally referred to as the "size-of-person" test, while conditions c. and d. are commonly described as the "size-of-transaction" test.

**Filing Fee**

The filing fee will range from \$45,000 to \$280,000, depending upon the size of the transaction. In the absence of agreement otherwise between the parties, the buyer is responsible for this fee.

**HSR waiting period**

A reportable transaction cannot be consummated until the expiration of the statutory waiting period, which is 30 days (fifteen days in the case of all-cash tender offers and bankruptcies), unless the reviewing agency grants early termination. Generally, the waiting period does not begin to run until all parties to the transaction required to file have submitted a notification form and the acquiring party has paid the filing fee. In certain securities transactions, such as tender offers, open market purchases, private purchases, or conversion of securities options or warrants, the waiting period begins to run when the acquiring party files.

If the reviewing agency is not interested in further investigation of the proposed transaction, it can grant

early termination of the initial waiting period or simply allow it to expire without taking any action. Before the initial waiting period expires, however, the reviewing agency may issue a Request for Additional Information ("Second Request"), which tolls the waiting period and prohibits consummation of the transaction until 30 days after both parties "substantially comply" with the request for information and documents.

If the parties learn that the reviewing agency merely needs more time to review or has narrowly focused concerns, the parties may decide to withdraw and refile their HSR filing to allow the agency more time, hoping to avoid a Second Request. The acquiring party does not need to pay an additional filing fee for an initial "pull and refile."

**Second Requests**

A Second Request is an extensive set of interrogatories and document requests that the reviewing agency issues to both parties to the transaction to obtain detailed information regarding the competitive issues presented by the transaction, such as product and geographic market definitions, market shares, concentration, market structure, customer reaction, prices, costs, and barriers to entry. The parties typically can negotiate with the agency to reduce the scope

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of the Second Request. It can take many months to comply with a typical Second Request; however, at any time after the agency issues a Second Request, the parties can continue to advocate for the agency to close its investigation or seek to resolve the agency's competitive concerns through remedial actions.

The issuance of a Second Request tolls the waiting period until the parties have substantially complied with the request. The waiting period after the parties have complied with the Second Request is 30 days (when the transaction is not a cash tender offer in which case the waiting period is 10 days). The parties can extend the reviewing agency additional time on a voluntary basis.

#### **Information and Analyses required in the HSR Notification**

In addition to descriptive information (a description of the transaction that identifies the parties and the value of the deal; SEC and financial documents; revenues broken down by North American Industrial Classification System Codes; shareholder information; subsidiary information; and information regarding whether the parties compete in the same geographic market), Item 4(c) of the notification form requires the parties to submit certain documents that analyze the competitive aspects of the proposed transaction. This can include all studies, surveys, analyses and reports that were prepared by or for any officers or directors (or in the case of unincorporated entities, individuals exercising similar functions) for the purpose of evaluating or analyzing the proposed acquisition or merger, with respect to market shares, competition, competitors, markets, potential for sales growth or expansion into product or geographic markets. Consequently, the Item 4(c) requirement is quite broad. Failure to comply with the Item 4(c) requirement can result in the agencies restarting the HSR waiting period, seeking civil fines and possibly seeking other remedies.

In preparing any document that may meet the specifications of Item 4(c), authors should keep in mind that the document may be reviewed by the antitrust agencies. Documents containing erroneous, speculative, exaggerated, or ambiguous statements or data can delay and even prevent government clearance of a transaction. Executives and consultants (including investment bankers and management consultants), therefore, should: write accurately and succinctly; omit exaggeration and speculation; avoid unnecessary or unsubstantiated references to market definition, market shares, or market power; avoid inartful expressions (e.g., "dominate the market" or "destroy"

a competitor); and involve counsel, whenever possible, in the review of drafts of such documents before they are circulated to anyone else.

#### **Penalties for Failure to File**

Any person or entity that fails to comply with the requirements of HSR can be fined up to \$11,000 per day for each day that the person or entity remains in violation. In addition to monetary penalties, the agencies can also seek equitable relief, including rescission of the transaction or disgorgement of profits made from the illegal acquisition. There have been numerous HSR enforcement actions, all of which to date have been settled by consent decree and payment of penalties. On occasion, parties will inadvertently fail to file an HSR notification form and observe the waiting period; in such cases, the FTC exercises discretion as to whether or not to seek penalties.

#### **GUN-JUMPING AND RELATED ISSUES**

An additional risk in pursuing an acquisition in the US is that the investigations preceding an agreement, and the cooperation and integration efforts that generally follow the parties' executing an agreement to purchase, may be viewed by antitrust authorities in the US as "gun-jumping" and inappropriate exchanges of information. Gun-jumping occurs where one party exercises undue control over the commercial activities of another party prior to obtaining regulatory approval. Exchanges of information among competitors can create antitrust exposure where they dampen competition among the merging firms before closing. Both types of violations can cause at least two adverse consequences:

- They can be prosecuted as violations of law, with attendant fines and penalties.
- They can seriously delay investigation and approval of the underlying transaction.

While the activities and the attendant risk clearly overlap, it is helpful to examine three stages of a transaction: due diligence, the terms of the contract and integration efforts.

#### **Due Diligence**

Firms considering an acquisition or joint venture need to exchange information to explore whether the transaction makes sense. At the same time, if they are competitors, exchanges of information about pricing, customers, costs, etc., can, under certain circumstances, affect competition between them. Accordingly, the parties should exchange confidential



PRACTICAL ADVICE

and competitively sensitive information only to the extent it is reasonably necessary for due diligence.

In particular, discussions between the parties as to current or projected pricing, identification of customers, costs (particularly as to specific products or services), marketing and competitive strategies, future bids and ongoing R&D are areas that may be viewed as anti-competitive exchanges of information between two competitors. Certain safeguards can be used to limit the potential exposure, including confidentiality agreements limiting the use of the information, limiting access to the information and, in the cases of particularly sensitive data, using third parties such as accountants and bankers to review and “sanitize” summary reports, aggregating data or making it anonymous (such as deleting customer names).

**Contract Terms**

A buyer needs to ensure that the assets to be acquired do not lose value after signing the definitive agreement. Thus, a buyer will often want to exert some control over the seller’s business prior to closing, particularly if it expects that a lengthy antitrust or other regulatory review might delay the closing. This desire competes with the antitrust agencies’ demand that the parties remain independent (and, if competitors, that they compete vigorously) until closing. This tension, and the need for careful examination of appropriate levels of control and cooperation, is particularly true in regulated industries such as utilities, where the time necessary to complete regulatory review may far exceed the antitrust review.

As a general guideline, parties may agree not to take certain actions that would cause a material adverse change in the value of the assets to be acquired,

and a buyer may require the seller to continue to act in the ordinary course of business consistent with past practices. A buyer should not prohibit the target from offering certain discounts or setting prices aggressively without the buyer’s approval or otherwise exercise control over competitively sensitive issues such as prices, promotions, output, territories, execution of customer contracts, etc., except after careful review by antitrust counsel.

**Integration Efforts**

There is a further tension between the parties’ desire “to hit the ground running” after the deal is closed and the antitrust agencies’ insistence (1) that the parties remain independent pending the closing and (2) that competition not be adversely affected before closing or if the deal does not close. In general, parties may *plan* – but not implement – the integration of their business. The two principles to keep in mind are:

- Throughout the course of negotiations and integration discussions, the companies must continue to operate independently.
- The parties must not exchange commercially sensitive information likely to dampen competition.

As with due diligence, limiting the people allowed to see certain types of information can facilitate necessary planning activities while minimizing antitrust risk.

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