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The HSR Act Makeover

Law360, New York (July 28, 2011) -- The Federal Trade Commission and the U.S. Department of Justice recently modified the premerger notification form and rules for transactions reportable under the Hart-Scott-Rodino Act (HSR Act), which requires preclosing approval for deals that meet certain size requirements. The new form and the amendments to the HSR rules will become effective on Aug. 18, 2011.

Almost every aspect of the form will be affected in some way. With the exceptions noted below, the changes should reduce the burden on most filing parties, particularly for acquisitive clients such as private equity firms and certain strategic buyers. The standard timing of 30 calendar days (15 for Tender Offers) for the initial waiting period, the filing thresholds and the fees associated with filing, remain unchanged.

The FTC and DOJ recognized that many items in the HSR form do not generate information useful to antitrust enforcement. As a result, many of these items have been modified or dropped completely. The agencies also added some new requirements that are intended to provide the FTC and DOJ with a more complete picture of the competitive implications of the notified transaction.

The most significant of these changes are summarized below:

Balance Sheets

Previously, filing persons[1] were required to submit the most recent regularly prepared balance sheet (even if unaudited) for all unconsolidated U.S. corporations. For a party with numerous corporate entities under its control, such as a private equity firm, collecting these balance sheets, which often are prepared monthly, could be a potential source of delay to the closing. This burden has been eliminated.

Documents

One of the most time-consuming tasks for filing parties is collecting the Item 4(c) documents (documents that analyze the target with respect to competition, sales growth or expansion in product and geographic areas). The new rules do not lessen this burden, but instead add new requirements intended to capture other information relevant to the competitive effects of the proposed transaction.

• 4(d)(i) requires that the parties submit any Confidential Information Memoranda (CIMs) or if there are no CIM, any similar document prepared for the buyer in connection with the sale that provides information pertaining to the business being sold, even if it does not contain "4(c)" content. For example, an investment banker presentation prepared for the buyer in connection with the sale transaction that provides financial information regarding the target if seen by an officer or director of the buyer may now be responsive in the absence of a CIM. Where there is no CIM or similar document, the rule requires the buyer to submit ordinary course materials of the seller that the buyer relied on that provide information similar to the information customarily found in a CIM. (This latter requirement could increase buyer's burdens, but the FTC has indicated that its expectation is NOT for the parties to submit the entire content of seller's data room when the seller did not create a CIM or equivalent selling document.)

• 4(d)(ii) requires that the parties provide studies created by third-party advisers (e.g., investment bankers and consultants) during an engagement or for the purpose of being engaged by the filing parties including "4(c)" content that relate to the sale of the target, even if not prepared specifically for the transaction to which the filing relates. One challenge with this new requirement may be that the parties would now need to submit even an unsolicited banker's book that may exaggerate the competitive effects of a proposed transaction and thus unnecessarily result in closer FTC or DOJ scrutiny of the proposed transaction.

The 4(d)(i) and 4(d)(ii) requirements are limited to documents created within the past year and seen by an officer, director or equivalent person of the buyer.

• Item 4(d)(iii) is an entirely new requirement. It asks for all studies (except those without stated assumptions) seen by an officer, director or equivalent person that evaluate or analyze efficiencies and/or synergies created for the transaction to which the filing relates. The addition of this requirement is intended to better enable the reviewing agency to test the strength of any efficiency defense in a competitively aggressive deal as well as identify any potentially anti-competitive revenue synergies, i.e., price increases to consumers.

Revenue

The HSR form requires filing parties to report revenue by NAICS codes. Under the old rules, in addition to identifying revenue information for the most recently concluded financial year, parties had to provide information for a base year (2002), even if the party did not own the entities or assets generating those revenues in 2002. This meant that parties would be forced to try and determine what revenues were from nine year ago for businesses they did not own at that time.

The new rules eliminate this burden.

There are also new requirements with respect to reporting of revenue. The new rules require that parties break out U.S. revenue for manufactured businesses by 10-digit NAICS codes for the most recently concluded financial year. The rules also ask the parties to report information by 10-digit codes for foreign manufactured goods sold in or into the United States.

Associates

The new rules have introduced a new concept — called "associates" — which is designed to provide the reviewing agencies with more complete information about companies and investments under the same investment management as the Acquiring Person that may compete with the target.
In general, the new requirements are designed to capture oil & gas companies as well as private equity firms, which frequently manage several investment funds organized in such a way that each fund is its own Ultimate Parent Entity for HSR filing purposes.

Before the new rules, a single fund could report as an Acquiring Person without identifying an investment held in a different fund under the same investment management that competes with target. Under the new rules, any investment under common investment management control that derives revenue in the same NAICS code(s) as the target would need to be identified:

• Item 6(c)(ii) requires that Acquiring Persons identify any minority holdings (i.e. greater than 5 percent, but less than 50 percent of an entity's voting securities or noncorporate interests) of associates, including the name of the entity and percent held which derives revenues under the same 6-digit NAICS code(s) as the target.

Example: Maximum Management GP has investment control of both Maximum Capital Fund II LP and Maximum Capital III LP. Maximum Capital Fund II LP, an associate of Maximum Capital III LP, holds 6 percent of Competitor A. Maximum Capital III LP intends to acquire Competitor B, which transaction is subject to the HSR Act. Competitor A and Competitor B both derive revenues under NAICS code 123456. Maximum Capital III will need to disclose information pertaining to its associate's holdings in Competitor B in its HSR Form.

• Items 7(b)(ii) and 7(d) require that the Acquiring Persons identify its associates which derive revenues under the same 6-digit NAICS code(s) as the target, as well as geographic information concerning its operations.

Example: Maximum Management GP has investment control of both Maximum Capital Fund II LP and Maximum Capital III LP. Maximum Capital Fund II LP, an associate of Maximum Capital III LP, controls Competitor A. Maximum Capital III LP intends to acquire Competitor B, which transaction is subject to the HSR Act. Competitor A and Competitor B both derive revenues under NAICS code 123456. Maximum Capital III will need to disclose information pertaining to Competitor B in its HSR Form.

Conclusion

For most acquisitive companies, life should be at least a little easier under the new rules. What remains the same is the need to get the HSR process started as early as possible to ensure that HSR preparation and approval does not impede a timely closing.

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[1] Under the HSR Rules, "person" here refers to the "Ultimate Parent" of the filing acquiring party and any entity it "Controls." We have not incorporated the detailed rules relating to "ultimate parent" and "control" in this article.