e-Competitions
Antitrust Case Laws e-Bulletin

Concurrences
Antitrust Publications & Events

Preview

The US FTC resurrects the unilateral pre-approval in merger investigation settlements to halt future anticompetitive mergers

MERGERS, INVESTIGATIONS / INQUIRIES, SETTLEMENT, MERGER NOTIFICATION, ALL BUSINESS SECTORS, MERGER (NOTION), REFORM, UNITED STATES OF AMERICA, COMPETITION POLICY

US FTC, *Statement of the Commission on Use of Prior Approval Provisions in Merger Orders*, Statement, 25 October 2021

Michael A. Gleason | Jones Day (Washington)
Lin W. Kahn | Jones Day (San Francisco)
Bruce McDonald | Jones Day (Houston)
Jeremy P. Morrison | Jones Day (Washington)
Craig A. Waldman | Jones Day (Washington)

e-Competitions News Issue Preview

In Short

The Development: The Federal Trade Commission ("FTC") revived a long-abandoned policy requiring that Commission orders settling FTC merger investigations include a "prior approval" clause that grants the FTC the unilateral authority to approve (or deny) certain future transactions for a minimum of 10 years.

The Background: The FTC voted in July to restore the prior approval policy, and last week issued new guidance, in addition to its first merger settlement including a prior approval provision. In announcing the policy, the FTC stated its view that "too many deals that should have died in the boardroom get proposed because merging parties are willing to take the risk that they can 'get their deal done' with minimal divestitures." The FTC's dissenting commissioners, in a stinging and wide-ranging dissent, have called the effort a part of "the majority's desire to chill deal activity."

Looking Ahead: Although prior approval may affect a small absolute number of transactions, companies with a deal subject to a thorough FTC review need to consider the impact of prior approval on their M&A pipeline. Dealmakers also should pay close attention to how the FTC implements the policy, with a particular focus on the scope of prior approval clauses and whether the FTC exercises reasonable judgment in allowing deals without antitrust concerns to proceed. In the absence of restraint, expect more merger litigation with the FTC. It may cause some to reevaluate whether to pursue certain deals.

What Is the FTC's New "Prior Approval" Policy?

At the end of an FTC investigation into the competitive impact of a merger, the agency may (i) take no action (allowing the parties to close), (ii) challenge the transaction (through its administrative process and, if necessary, seek a federal court injunction against the parties' closing), or (iii) implement a settlement that permits the transaction to close subject to a divestiture or behavioral remedy. The merging parties may agree to a settlement with the FTC or contest the FTC's challenge in court, which may include "litigating the fix." In the latter context, parties sign a contingent divestiture agreement with a divestiture buyer and argue to the court that their prepackaged remedy solves the concerns that are the subject of the FTC's complaint.

Going forward, FTC merger settlements will include language that requires the buyer to notify the FTC of certain future transactions prior to closing those transactions, and that grants the FTC authority to reject a planned transaction at its sole determination.

- All divestiture orders will include prior approval provisions for every relevant market in which the FTC alleges harm, for a minimum of 10 years ("Prior Approval").
- The FTC likely will seek a potentially broader prior approval order for parties that abandon a transaction after the agency files a complaint.
- The FTC is less likely to seek prior approval where parties abandon their transaction before the FTC expends significant resources (i.e., prior to substantial compliance with a second request, the lengthy discovery request through which the FTC seeks information from the parties to inform its investigation).

- The FTC may seek prior approval orders that cover product and geographic markets beyond those affected by the proposed transaction, including related, adjacent, and/or complementary markets. As explained below, by going beyond the market at issue, prior approval could increase the burden and risks for companies subject to the requirement.
- All divestiture buyers will need to consent to prior approval for any future resale of the divested business, for a minimum of 10 years, a requirement not included in the FTC's previous policy.

Although not implied by the FTC's policy statement, one should expect there may be some room to negotiate the scope of the Prior Approval.

Why Is the FTC Changing Its Policy Now?

The change is another step in the efforts of the current FTC to utilize more demanding standards, aggressive enforcement, and new tools to block or deter mergers, as detailed in this *July 2021 Commentary*. The FTC withdrew its prior policy of requiring prior approval clauses in 1995, citing the success of the Hart-Scott-Rodino Act ("HSR") premerger notification program at adequately protecting the public interest in merger enforcement. The current FTC claims Prior Approval is necessary to prevent "facially anticompetitive deals," preserve Commission resources and detect deals below HSR reporting thresholds.

In a strongly worded dissent, the dissenting commissioners held little back, calling parts of the Commission's prior approval policy "bonkers crazy." The dissent argued the new policy abrogates the HSR Act, discourages procompetitive transactions, will stifle economic growth, and will result in more, rather than less, strain on Commission resources. Given the level of opposition, the Commission's new prior approval policy may not have a long life if the Commission's political makeup changes.

Will the Prior Approval Policy Affect My Transaction?

Both the Department of Justice Antitrust Division ("DOJ") and the FTC review mergers, but only the FTC has adopted a prior approval policy (so far). The DOJ typically requires parties to agree to provide it with prior notice of future transactions valued below the HSR threshold if in the same market that is the subject of the settlement. But here, the burden remains with the DOJ to obtain a federal court injunction to block a transaction, unlike the FTC's prior approval requirement in which the merging parties have to convince the Commission to grant approval.

The FTC's Prior Approval policy could affect only a small number of transactions. The DOJ and the FTC receive premerger filings for approximately 2,100 transactions a year. Roughly 2% to 4% of those transactions result in a second request investigation (roughly half by the DOJ and half by the FTC), and not all of those investigations result in settlements. Therefore, Prior Approval is not likely to be a concern in the large majority of transactions filed with U.S. agencies.

What Are the Consequences of Prior Approval?

Although the absolute number of transactions affected is likely to be small, the policy might have outsized consequences for companies subject to Prior Approval, depending on how the FTC implements the policy. If merging parties are unwilling to accept an FTC settlement (or there is no settlement offered), the FTC typically must obtain a federal court injunction to block the deal by proving that the transaction will harm competition. Going forward, the FTC will claim that Prior Approval grants it the unilateral right to approve or deny a future transaction

subject to the order without resorting to federal court or its own administrative process. The FTC also likely will assert that merging parties have no legal recourse if it does not grant its approval.

The FTC also would not be bound by the timing rules of the HSR Act, which delays closing only for a certain period of time after the parties have complied with the FTC's second request. As a result, Prior Approval creates new uncertainty as to timing and closing of future deals subject to its terms.

The FTC may face fewer objections if it largely limits the scope of Prior Approval to the product and geographic markets at issue in the matter before it, and if it applies historic agency standards and merger law to its review of transactions subject to Prior Approval. If the FTC exercises restraint, there might be little difference in outcomes for transactions that would anyway be reportable under the HSR Act.

Alternatively, if the FTC broadly imposes Prior Approval requirements, subjects those transactions to a higher burden for clearance, and/or takes substantially longer in its reviews, more companies may litigate mergers with the FTC than agree to a Prior Approval settlement. There also could be disputes with the agency about whether the preapproval agreement actually applies to a new proposed merger, and some may challenge the FTC's authority to force prior approval settlements.

Should We Expect Expansive FTC Prior Approval Requirements?

The FTC warns that it may seek Prior Approval for future transactions involving product or geographic markets beyond the scope of the markets in which the FTC alleges harm from the initial transaction. The FTC says it will consider whether to seek that more expansive Prior Approval based on the following nonexhaustive list of factors: whether (i) the current transaction is substantially similar to a prior transaction the FTC challenged, (ii) the relevant market is already concentrated or has seen significant consolidation, (iii) the transaction significantly would have increased concentration, (iv) one of the parties had market power, (v) either party has a history of acquisitions in the same or related markets, or (vi) the transaction would have created anticompetitive market dynamics. Those stated considerations may not be much of a roadmap because they are similar to the factors that the FTC considers when deciding whether or not to challenge or seek a remedy in a merger, and therefore may apply to nearly all deals in which the FTC would seek a divestiture and order.

How Long Will Prior Approval Orders Last?

A minimum of 10 years, although the FTC will consider longer periods.

Has the FTC Invoked Its Prior Approval Policy in Any Deals Yet?

Yes. On the same day as it announced the policy, the FTC entered into a settlement with Davita, allowing its acquisition of the University of Utah's dialysis clinics to proceed subject to an FTC order with a Prior Approval obligation. DaVita, a "particularly acquisitive company" according to the FTC, must obtain FTC approval before acquiring any new ownership in a dialysis clinic for the next 10 years, anywhere in Utah, a geographic market broader than the City of Provo market alleged in the FTC's complaint. In a concurring statement, Republican Commissioner Wilson cautioned that her vote in favor of the prior approval provision "should not be construed as support for the liberal use of prior approval provisions foreshadowed" by the FTC's Democratic majority.

Will Prior Approval Apply if the Parties Abandon Their Transaction?

The FTC says it will be less likely to seek Prior Approval if the parties abandon their transaction during the FTC's investigation and before the parties have substantially complied with the agency's second request. Although that part of the policy is not likely to affect a large number of transactions, it creates a new risk for companies to consider when making an HSR filing for any deal. Indeed, as the dissenting commissioners stated: "God forbid we should do our job of analyzing deals notified pursuant to the HSR Act."

In contrast, the FTC says it may seek Prior Approval, again based on the six factors above, in cases where the parties abandon a transaction after the FTC initiates or threatens litigation. Parties that abandon a transaction are not likely to consent voluntarily to an FTC order with prior approval, but the FTC could initiate litigation in its administrative court to attempt to obtain an order with prior approval. For nine years in the 1980s and 1990s, the FTC litigated its attempt to impose a prior approval requirement on Coca-Cola after Coca-Cola abandoned its bid to acquire the Dr Pepper Company. The FTC abandoned that effort in 1995 when it withdrew its prior approval policy. In a June statement dissenting to the withdrawal of the 1995 prior approval policy (and in reference to the Coca-Cola case), Commissioner Wilson expressed concern about a "vindictive approach" against a party that would have the "temerity to exercise its legal rights and litigate."

What Does the FTC's New Policy Say About Buyers of Divested Businesses or Assets?

The FTC also will require the buyers of divested businesses or assets to agree to prior approval for any future sale of those assets, for a minimum of 10 years. According to the agency, "this will ensure that the divested assets are not later sold to an unsuitable firm that would contravene the purpose of the Commission's order." The FTC has in some past transactions required divestiture buyers to agree to prior approval terms; now the FTC intends to require all buyers to do so.

The 10-year obligation will present a new twist in parties' efforts to identify suitable divestiture buyers, as now a buyer may be required to hold divested assets for at least a decade if unable to obtain FTC approval for the resale of that business. It may also undercut the value of the divestiture sale or discourage buyers that see an opportunity to acquire the business, improve its operations or add value by combining it with another business, and then resell it to a third party at a higher value.

Three Key Takeaways

1. How the FTC implements Prior Approval will determine its real impact. If the FTC exercises restraint by limiting the scope of prior approval, applying historic agency guidance and merger law, and completing reviews expeditiously, then the outcome under Prior Approval may not differ meaningfully for transactions that would have been subject to HSR review anyhow. If the FTC adopts a more aggressive stance, more merger litigation is likely, and it may cause some to reevaluate whether to pursue certain deals.

2. Although Prior Approval may affect a small number of companies and transactions in absolute terms, it could have outsized consequences for the M&A strategies of companies subject to it. Companies evaluating a transaction that may result in an FTC settlement need to consider not just the antitrust risk of the deal at hand, but also the potential impact that a 10-year (or more) preapproval clause may have on the company's M&A pipeline and the sequencing of those deals.

3. Prior Approval might have its greatest effect on parties that have been making or are considering serial acquisitions, businesses in industries expecting further consolidation or subject to repeated M&A transactions, companies with significant market positions, and buyers acquiring targets that the FTC may see as critical future competitors.