Clients&FriendsMemo

FTC/DOJ Announce Significant Changes to HSR Premerger Notification Form

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On July 7, 2011, the Federal Trade Commission ("**FTC**") and the Antitrust Division of the U.S. Department of Justice ("**DOJ**") announced significant changes to the Hart-Scott-Rodino ("**HSR**") Premerger Notification Rules and the Premerger Notification and Report Form ("**HSR Form**") that may substantially increase the burden placed on filing parties. The new HSR rules were published in the Federal Register on July 19, 2011, and will take effect on August 18, 2011. Any transactions notified to the agencies on or after that date must use the amended form.

The Hart-Scott-Rodino Antitrust Improvements Act of 1976 ("**HSR Act**") requires parties to transactions meeting certain thresholds to submit HSR Forms to both the FTC and DOJ, triggering a waiting period that must expire or be terminated before the parties may consummate the transaction. The changes are intended to streamline the HSR Form and capture additional information that the agencies believe will better inform and expedite their competitive review of a proposed transaction during the initial HSR waiting period. The revisions simplify the filing process by eliminating certain sections of the HSR Form; however, they also require new categories of information and documents.

The changes to the HSR Form, discussed in more detail below, could prove to be burdensome, time consuming, and expensive for certain filing parties – particularly private equity companies, hedge and other types of investment funds, master limited partnerships in the energy sector, and businesses with manufacturing operations outside the U.S. The changes with the most potential to increase a filing party's compliance burden include:

- Requiring the disclosure of information regarding an acquiring person's "associates," which are entities that are under common operational or investment management but are not controlled by that party for HSR purposes (*e.g.*, investment funds that have a common managing or general partner, "master limited partnerships" in the energy sector);
- Requiring manufacturing revenues from the most recent fiscal year, including for products manufactured outside the U.S. and sold inside the U.S. (either directly to a customer or through a U.S. entity), to be reported by 10-digit NAICS manufacturing codes; and

- Requiring the submission of additional categories of documents that may not meet the requirements of Item 4(c), including offering memoranda, bankers' books and other materials prepared by third parties, and documents describing synergies and efficiencies that may result from the proposed transaction.

New Disclosures Regarding Associates

The previous HSR rules limited reporting obligations to information about the ultimate parent entity ("**UPE**") of the acquiring and acquired persons and all entities controlled by each UPE.[1] Thus, for example, the previous HSR Form did not require information regarding a general partner ("**GP**") with a one percent interest in a partnership because the GP is not deemed to control the partnership for HSR purposes, even if the GP directs the partnership's activities and/or investments. Information also was not required for other partnerships with the same GP and other entities under common management with the acquiring partnership. The revised HSR Form changes this by requiring that the acquiring person provide information regarding its "associates," which are entities that are under common operational or investment management with the acquiring person.[2] These revisions particularly will be significant for businesses with complex partnership structures (*e.g.*, private equity companies, hedge and other investment funds, master limited partnerships in the energy sector, etc.).[3] The new requirements relating to associates do not affect the definition of "acquiring person" for the purposes of determining whether HSR notification is required.

Minority investments – Item 6(c) currently requires filing persons to report minority investments of at least 5% (but less than 50%) in other corporations. The revised Item 6(c) expands reporting by requiring an acquiring person to identify, to its knowledge and belief, information regarding the minority investments of each of its associates that derived (or may have derived) revenues in any of the same 6-digit NAICS codes as the acquired person in the transaction during the last year, even though the acquiring person may not have detailed NAICS code information about the business operations of such minority-held firms. In order to ease the compliance burden, the new rules allow filers to rely upon regularly prepared financial statements that list their associates' investments, provided that

[1] "Control" generally is defined as holding 50 percent or more of the outstanding voting securities or having the present contractual right to designate 50 percent or more of the board of directors of a corporation. Control of a noncorporate entity is determined by the right to 50 percent or more of the profits or assets upon dissolution.

[2] Common examples of associates include general partners of a limited partner, other partnerships with the same general partner, other investment funds whose investments are managed by a common entity or under a common investment agreement, investment managers of funds, and "master limited partnerships" in the energy sector.

[3] For example, separate investment funds that share GPs or managing partners with another fund will be considered associates of one another, as well as with the GPs/managing partners. If one fund is an acquiring person, it must submit information to the best of its knowledge regarding its GP, sister funds and their portfolio companies.

the financials are no more than three months old at the time of filing. Filers also may elect to list entities in the same general industry as the acquired person.

Overlaps among filing parties – Item 7 currently requires information regarding NAICS code overlaps among parties to the transaction. The new rules expand Item 7 to require an acquiring party to list entities controlled by its associates that derived revenues in the same 6-digit NAICS codes as the acquired person.

The disclosure requirements relating to associates likely will increase significantly the burden for GPs and investment managers or directors of investment funds, who will need to track and report holdings of each of the (potentially many) "associate" investment funds they manage, the holdings of which may change frequently. The burden is further increased given that Items 6(b) and 6(c) no longer are limited to corporations and now will require information about minority investments in or by unincorporated entities.

Increased Revenue Reporting Obligations

Item 5 of the previous HSR Form required a filing party to submit historical (i.e., "base year") and current revenues classified by NAICS code for any products or services sold through U.S. establishments. The revised HSR Form eliminates the base year requirement, as well as the requirement that parties identify the years in which manufactured products have been added or deleted since the base year. This change will lessen the burden for some filing parties (particularly those with U.S. manufacturing operations). However, manufacturing companies now must provide more detailed information regarding their current operations.

Filers previously were required to report revenues from foreign manufacturing facilities only if products were sold through their U.S. establishments (*e.g.*, warehouses) and only by 6-digit wholesale NAICS codes. The revised HSR Form requires parties to report, by the more granular 10-digit NAICS manufacturing codes, revenues for the last fiscal year for all products manufactured in the U.S. and for products manufactured outside the U.S. that were sold into the U.S. Direct shipments to U.S. customers no longer may be excluded from Item 5. These changes will increase the burden on businesses with foreign manufacturing operations that now must report U.S. revenues by codes that those operations may not maintain in the ordinary course of business.

Production of Additional Documents

Item 4(c) always has been one of the most critical and potentially time-consuming requirements of the HSR Form. Item 4(c) requires the production of documents created by or for officers or directors of the filing party for the purpose of evaluating or analyzing the transaction with respect to "market shares, competition, competitors, markets, potential for sales growth, and the potential for

expansion into new products or geographic markets" (the so-called "4(c) content"). Ordinary course business documents generally (with limited exceptions) are not responsive to Item 4(c). The requirements for Item 4(c) remain unchanged, but the revised HSR Form requires the production of a new category of "4(d) documents."

Item 4(d) calls for three additional types of documents that would not necessarily be captured by Item 4(c):

(1) *Offering memoranda* – Item 4(d)(i) requires confidential information memoranda ("CIMs") that were prepared for officers or directors (or, with respect to unincorporated entities, those serving similar functions) within one year of the HSR filing date and that relate specifically to the sale of the acquired entity or assets but not necessarily to the specific transaction at issue. Item 4(d)(i) requires the inclusion of such CIMs regardless of whether they contain 4(c) content or whether they were shared with the buyer. If no CIM exists, the parties must submit any documents actually given to officers or directors of the buyer meant to serve the function of a CIM (*e.g.*, a preexisting presentation containing a company or industry overview). Ordinary course documents and/or financial data shared in the course of due diligence are not responsive, except to the extent that such materials are shared with the buyer specifically to serve the purpose of a CIM in the absence of a CIM. The agencies' stated intent is to "capture materials that provide an in-depth overview or analysis" of the target.

(2) *Third-party advisor documents* – Item 4(d)(ii) requires documents prepared for officers or directors (or, with respect to unincorporated entities, those serving similar functions) within one year of the HSR filing date by investment bankers, consultants, or other third-party advisors, during an engagement or for the purpose of seeking an engagement. Unlike Item 4(d)(i), however, Item 4(d)(ii) only requires the inclusion of such third-party advisor documents to the extent those documents contain 4(c) content specifically relating to the sale of the acquired entity or assets, but not necessarily relating to the transaction at issue. Common examples include "bankers' books" or "pitch books" or other documents that address competitive issues developed by third-party advisors during an engagement or for the purpose of an engagement.

(3) *Synergy and efficiency documents* – Item 4(d)(iii) requires documents evaluating or analyzing synergies and/or efficiencies prepared for the purpose of evaluating or analyzing the transaction in question, regardless of whether those documents contain 4(c) content. Financial models without stated assumptions may be excluded. The agencies have indicated that documents submitted with an HSR filing may carry greater weight than materials claiming synergies created and submitted later on in an investigation.

The collection, review, and production of 4(c) documents often is a gating item that requires a substantial amount of time and resources. The addition of Item 4(d) will require parties to expand their document search and will increase the time and expense required for compliance.

Conclusion

Companies with internal processes in place to meet current HSR obligations may need to modify those processes and/or create new ones, including: (1) the collection and review of certain categories of documents; (2) the methods used to maintain and compile the required annual financial information; and (3) for acquiring persons, the methods used to collect information from "associates." Given the expanded scope of data and document collection, as well as the fact that some of the additional information required will be transaction-specific (making it more difficult for companies to have a filing "on the shelf" that is ready to be updated for a time-sensitive transaction), parties to reportable transactions should take into account the likelihood that preparing the HSR filing will be more time consuming and expensive. For example, standard contract provisions requiring the parties to file notification under the HSR Act within a short period of time may need to be revisited, particularly for parties who are filing the revised HSR Form for the first time.

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