CORPORATE
US ANTITRUST

Putting deals together

Buyers and sellers must consider several key points when negotiating antitrust provisions in strategic transaction agreements

When there is a merger that will likely draw antitrust scrutiny in the works between two competitors, what types of considerations need to be addressed in the merger agreement? There are many antitrust decisions to be made when crafting antitrust provisions for a strategic transaction. Companies need to consider which provisions are most important to them. A thoughtful antitrust risk assessment prior to signing can help a buyer or seller gain an advantage at the negotiating table by having a superior understanding the process and potential areas of risk. There are some key decision points that antitrust lawyers can advise on to help companies navigate in strategic transactions to best achieve their objectives.

How long do antitrust merger investigations take?

As antitrust merger review processes continue to take a long time, companies need to decide how much time they are willing to commit to obtaining antitrust merger clearance. Some companies may decide that a transaction is extremely valuable and favour a lengthy termination period to allow for a thorough government investigation and possible litigation. Others may not be willing to expend internal and external resources to defend a transaction if a lengthy, in-depth investigation or litigation becomes necessary. In particular, sellers may not want to leave their company in limbo for too long at the risk of losing key employees, customers and strategic focus.

So how much time do companies need to plan for if they want to go the distance? The Dechert Antitrust Merger Investigation Timing Tracker (DAMITT) has observed that significant antitrust merger investigations in the US – significant merger investigations include proposed Hart-Scott-Rodino-reportable transactions resulting in a closing statement, consent order, complaint challenging a transaction, or transaction abandonment for which the antitrust agency issues a press release – concluding in the first three quarters of 2017 have lasted 11.6 months on average from deal announcement to the completion

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Carrying out a proper antitrust risk assessment prior to signing off on a transaction can help the parties gain an advantage during negotiations. This will help them have a better understanding and overview of the process and of potential areas of associated risk. There are some key issues to take into account when undergoing this risk assessment: the duration of the antitrust investigation, any potential remedies such as divestitures, possible compensation in the event the deal falls through, as well as any possible ways to ensure buyers and sellers work as a team. A crucial additional point to consider is whether other government agencies need to give their seal of approval for the deal to go through.

of the investigation. This duration is up more than 50% from the 7.7 month average only three years ago. Antitrust merger litigation, when it ensues after the conclusion of the investigation, is taking longer, too. The most recent merger challenges – those litigated to a decision in 2016 – lasted nearly seven months from the beginning of the litigation to the time the judge decided the case.

While certain circumstances may lead to results above or below these averages, the DAMITT trends suggest that parties to the hypothetical average deal may have to plan on approximately 12 months for the agencies to investigate a transaction and another seven months if they want to preserve their right to litigate an adverse agency decision. If the current trends toward longer investigations and litigations continue, even more time may need to be allotted in merger agreements going forward.

Will divestitures be required?

Companies negotiate what commitments a buyer must make to obtain antitrust clearance in the event that the US antitrust agencies require a remedy. Some buyers may be unwilling to give up any portion of the acquired business or to accept any restrictions. In such cases, the merger agreement may not require the buyer to agree to any asset divestitures or behavioural remedies to obtain clearance. On the other hand, sellers typically focus on getting paid for the transaction and may not care how much the buyer has to give up to win approval. In these cases, sellers may seek a hell-or-high-water clause requiring the buyer to do whatever it takes to gain antitrust clearance, even if it means divesting the seller's entire business to a third party.

Many agreements land somewhere in the middle of these two positions. For example, a buyer may agree to divest assets only if the remedy will not have a 'material adverse effect' on the value of the acquired business. Some merger agreements leave open the question of what level of divestitures would be deemed material, creating uncertainty for later resolution. Others contain a more concrete definition of materiality, making the obligation clearer. For example, the merger agreement may explicitly state that the buyer must agree to divest the seller's manufacturing facility in Toledo, Ohio if necessary, but that the buyer shall not be required to divest the buyer's competing facility in Detroit, Michigan. Alternatively, a buyer may commit to divest only any assets generating up to a certain level of Ebitda or revenue. This type of cap would ensure that any divestitures will not be so large as to erode deal value beyond an agreed point. These types of specific commitments are carefully drafted based on the risk assessments of antitrust lawyers that identify, prior to signing, particular assets that may need to be divested to resolve potential competitive concerns.

Should the seller be compensated if the deal is blocked?

In the unfortunate event that a transaction is terminated after failing to gain antitrust approval, merger agreements sometimes require the buyer to pay the seller for its troubles. This payment – known as a reverse antitrust breakup fee – may compensate the seller for the resources it expended to obtain antitrust approval or for the damage to the seller's company while it was left in limbo. Reverse antitrust breakup fees are often viewed as seller-friendly. In some cases, however, a seller that is confident in obtaining antitrust clearance given the divestiture commitments may be willing to forego a reverse termination fee in exchange for a higher purchase price or some other favorable provision in the transaction agreement.

As shown in the chart below, reverse antitrust break fees are relatively uncommon, appearing in under 20% of strategic deals; the mean and median size of these fees are about five percent of total deal value. However, the size of the fee is individually negotiated and will vary. For example, after the $39 billion AT&T/T-Mobile transaction failed to obtain antitrust approval in 2011, AT&T paid T-Mobile $3 billion in cash and transferred about $1-$3 billion worth of wireless spectrum.

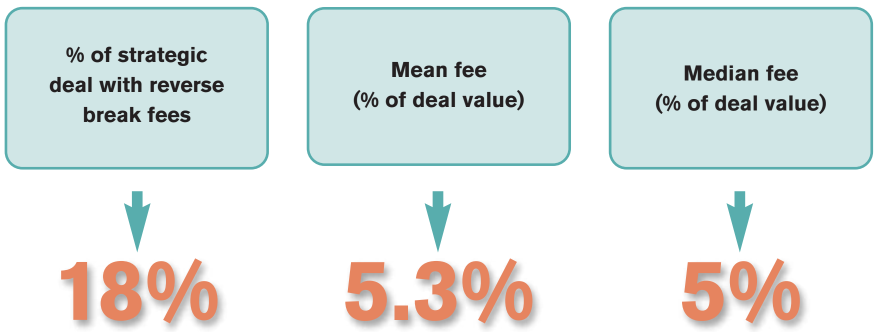
Will the buyer and seller work as a team?

The merger agreement will need to define the extent to which the buyer and seller will work together as a team. Merging companies often make both individual and joint written advocacy submissions. They may make presentations to the government individually or jointly. The FTC or DoJ may interview or depose executives. Ensuring consistency in themes and arguments may be challenging in this setting. Also, knowing what the other side is saying and doing may be important to monitor deal progress.

Each company may insist on a right to review and comment on any written work product before submission. Another approach is to insist on review and approval before any submission. For meetings or conference calls, each company may insist on a right to be present. These cooperation rights may be important to assess how the other company is approaching the regulatory review. Another consideration is the ability to use these rights to influence your partner's actions as well as the government. It may be important to have a seat at the table.

Efficiency in regulatory decision-making and strategy is another consideration. Who decides what arguments to make? Who decides when to submit a white paper? What about going over the head of government staff to management level positions? The merger agreement may reflect a consensus approach – both sides decide. There may be uncertainty on how exactly disagreements are resolved. That could inject delay and even animosity into the process.

Another approach is to spell out clearly that the buyer controls regulatory strategy. While the seller may feel left out to some extent, this approach may provide more clarity and certainty. A seller can lessen the impact by insisting on strong access and



Source: Shearman & Sterling's public deal antitrust reverse termination fee database (January 2012 – June 2017) participation rights even though the buyer has ultimate control on strategy.

What can the buyer do to ensure the seller's business remains intact?

During the lengthy investigation process, the seller may have to decide whether to enter into major supplier or customer contracts. The seller may also want to make substantial investments, such as an investment in a new plant or expansion into Asia. While the seller may face significant decisions, the buyer wants assurance that it will get the same business it contracted to buy.

Reverse antitrust break fees are actually relatively uncommon, appearing in under 20% of strategic deals

In a few instances in the US, buyers have endured antitrust investigations and enforcement actions for exercising too much control over the seller's business during the pre-closing review period. Exercising too much control can be viewed as gun jumping' – *ie* exercising control over the seller's business in the period before regulatory clearance. It is acceptable for a buyer to negotiate for approval rights over extraordinary or once-in-a-long-time actions. A problem may arise, however, if the merger agreement gives the buyer excessive approval rights over customary business decisions of the seller. For example, the merger agreement may require the seller to get the buyer's approval before entering into customary customer contracts.

For the merger agreement, the seller may insist that it retains authority over many of its core decisions. The buyer has a right to ensure that the seller does not transform itself into something very different from what was negotiated. But it could go too far if it insists on weighing in on more customary commercial decisions.

What is needed to get to closing?

What exactly must occur before the parties can close? There is more complexity here than might be expected. For transactions that are reportable in the United States, antitrust clearance under the Hart-Scott-Rodino Act must be a condition to closing. It is required; otherwise the companies would face significant penalties.

The same dynamic may arise with foreign competition filings. Some jurisdictions have well-established antitrust reporting laws and approval must be obtained before closing. An obvious example is the European Commission Merger Regulation. For deals that are subject to mandatory reporting to the European Commission, approval must be obtained before closing. Less certainty may arise with new competition regions in less developed countries. The laws may be written so that it is unclear whether mandatory filing applies. There may be a question of whether there are any penalties for failure to file. The companies will need to decide which countries have laws mandating reporting and approval before closing.

Another consideration is whether approval is needed from other government agencies. For example, in the US, approval from the Federal Communications Commission may be required for some telecommunications transactions. Departments of insurance at the state level may need to sign off. As with foreign competition agencies, there may be situations of uncertainty in terms of whether pre-closing approvals are required for a particular transaction.

Merger agreements are sometimes written so that the pendency or a lawsuit or an investigation may prevent closing. In the United States, State Attorneys' General (AG) offices often investigate mergers. However, state laws do not require parties to a merger to obtain state AG approval. Thus, the companies should consider whether they want to require closing despite the pendency of an investigation by a state AG. The same issue may arise with the pendency of a private antitrust lawsuit attacking the merger. How the merger agreement addresses these scenarios may have a significant impact on whether and when the deal closes.

What's in store?

Buyers and sellers have a full menu of options available to them to fit their interests – subject to negotiations that often require certain tradeoffs. Companies must decide which provisions are most important given various possible outcomes in negotiations. Leveraging guidance from antitrust counsel early in the process can provide companies with a significant advantage in maximising the value of these negotiations.

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