FTC and DOJ Announce Sweeping Changes to Hart-Scott-Rodino Reporting Requirements

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On July 19, the U.S. Federal Trade Commission and the Antitrust Division of the Department of Justice published the most comprehensive changes in decades to the Premerger Notification and Report Form ("HSR Form") required under the Hart-Scott-Rodino Antitrust Improvements Act of 1976. The Final Rule expands in some ways and limits in others the information that parties contemplating certain mergers, acquisitions, and joint ventures must include in their HSR filings. In addition, the new rule expands the universe of documents that parties must now submit with their HSR Forms. The Final Rule is scheduled to go into effect on August 18, 2011.

The Final Rule is the culmination of a process that was begun last year to streamline the HSR Form. The changes are also focused on gathering new types of information that the FTC and DOJ consider necessary for their initial review of transactions. While many of the changes will simplify the HSR filing process, certain entities, such as Private Equity Firms and Master Limited Partnerships (commonly found in the energy field), will face new challenges in preparing HSR filings. Moreover, all filers will have to submit new categories of documents, including certain documents created by third-party advisors. Ultimately, effective compliance with the revised rule will require greater coordination and consultation with antitrust counsel in the early stages of a transaction.

Key Changes:

- Acquiring persons must now disclose the identity of “Associates,” which are non-controlled entities that are under common investment or operational management, and include information regarding the revenues of Associates that overlap with the revenues of the target company. In addition, acquiring persons must disclose the minority holdings of the Associates that have revenues that overlap with the revenues of the target company. These changes most directly impact master limited partnerships and private equity firms in which a common general partner manages the operations of a number of separate entities within a given family.

- Additional documents must be submitted under new item 4(d) – including all confidential information memoranda, third-party advisor documents, and documents analyzing synergies/efficiencies.

- Parties no longer have to report revenues by North American Industry Classification System (NAICS) code for a base year (currently 2002). In addition, manufacturers that also sell their products through separate wholesale or retail establishments only have to report sales of those products under a 10-digit NAICS manufacturing code for the most recent financial year. Finally, revenues for products manufactured outside the United States and sold into the United States will also be reported under a 10-digit manufacturing code instead of a 6-digit wholesaling or retailing code.

Summary of Key Provisions

Acquiring Persons Must Provide Information on Associates

The HSR form has historically required acquiring parties to identify all entities that are "controlled" by the Ultimate Parent Entity and each issuer in which the UPE holds a non-controlling interest (5% or more of its voting securities). The new rule expands this requirement to include a new category of holdings, referred to as Associates. Associates are defined as follows:

> For purposes of Items 6 and 7 of the Form, an associate of an acquiring person shall be an entity that is not an affiliate of such person but: (A) has the right, directly or indirectly, to manage the operations or investment decisions of an acquiring entity (a ''managing entity''); or (B) has its operations or investment decisions, directly or indirectly, managed by the acquiring person; or (C) directly or indirectly controls, is controlled by, or is under common control with a managing entity; or (D) directly or indirectly manages, is managed by, or is under common operational or investment management with a managing entity.

The FTC explained that the purpose in requiring information on Associates is "to be able to analyze the holdings of entities that are under common investment or operational management with the person filing notification." Under the new rules, the acquiring person will have to report on its HSR Form the minority holdings of its Associates in the acquired entity and minority holdings of Associates that generate revenue-overlaps (Item 6(c) (ii)). The acquiring person will also have to report Associates whose revenue overlaps with the target company. (Item 7(a), (b) (ii), (d)).

This requirement will most directly impact HSR filings by private equity funds and master limited partnerships, but it is not limited to those entities. For example, if a private equity fund has multiple funds that are under common management, an acquisition by one of its portfolio companies would require the other managed funds and portfolio companies to provide information under 6(c)(ii) as Associates. Associates would have to provide information about their minority holdings (5% or more) in the target or in entities that either report revenues in the same 6-digit NAICS code as the target or, if revenue information is not available, that fall into the same industry as the target.

The FTC noted that the burden of providing such Associate information may be lessened by the fact that acquiring persons may rely on regularly prepared financials (not more than three months old) that list investments and the regularly prepared financials of Associates that list investments to respond to 6(c)(ii). Furthermore, the new rule also allows an acquiring person that cannot obtain more granular information about the minority holdings of its Associates to list all of their minority holdings. But the FTC warned that such an approach may delay review of the HSR filing and prompt follow-up requests from the staff.

In addition, revised Item 7 now requires that acquiring persons provide revenue-overlap information for Associates and *entities controlled by Associates*. For example, Item 7(b)(ii) requires the acquiring person to list the names of any entities controlled by an Associate of the acquiring person that derived revenue in an overlapping-6-digit NAICS code. Similarly, Item 7(d) expands the required geographic information for entities that derive revenue in overlapping NAICS codes to entities controlled by Associates of the acquiring person.

New Documents Required Under Item 4(d)

Parties filing HSR Forms have always been required to submit 4(c) documents – those documents prepared by or for an officer or director that analyze the proposed transaction with respect to markets, market shares, competition, competitors, potential for sales growth, or expansion into product or geographic markets. But the new rules have added three new groups of documents that must now be submitted under new Item 4(d). These documents include offering memoranda, third-party advisor documents, and synergy and efficiency documents.

- **Offering Memoranda:** Item 4(d)(i) requires parties to submit any Confidential Information Memorandum ("CIM") prepared by or for any officers or directors of the Ultimate Parent Entity of the acquiring or acquired person within one year of a filing that specifically relates to the sale of the target. The FTC noted that even if the CIM was not given to the buyer, the seller is obligated to submit it under 4(d)(i) if it exists. In addition, the FTC explained that if no CIM exists, the parties must submit any documents given to the officers or directors of the buyer that served the function of the CIM within a year of the filing – creating a new potential ambiguity in the obligation of filing parties. The FTC further explained that ordinary course documents or financial data shared in the course of due diligence would not have to be submitted under 4(d)(i), unless such information was shared with the buyer specifically to serve the purpose of a CIM when no CIM was prepared.

- **Third-Party Advisor Documents**: Item 4(d)(ii) requires parties to submit all studies, surveys, analyses, and reports prepared by investment bankers, consultants, or third-party advisors for any officers or directions, within one year from the date of filing, for the purpose of evaluating or analyzing market shares, competition, competitors, markets, potential for sales growth, or expansion into product or geographic markets that specifically relate to the sale of the target. Unlike Item 4(c), this includes documents that were not necessarily prepared for the purpose of analyzing an HSR reportable transaction, such as materials developed by third-party advisors during an engagement or for the purpose of seeking an engagement (including "pitch books" or "bankers books"), even if they relate to the sale of assets to a specific company other than the ultimate purchaser. Furthermore, the FTC expects Item 4(d)(ii) to capture reports created by third parties analyzing strategic options available to a company and that have competition-related content.

- **Synergy and Efficiency Documents**: Item 4(d)(iii) requires parties to submit all studies, surveys, analyses, and reports evaluating or analyzing synergies and/or efficiencies prepared by or for any officers or directors for the purpose of evaluating or analyzing the acquisition. This does not include financial models without stated assumptions. While parties remain free to assert synergy arguments at any time, the FTC commented that "documents submitted with an HSR filing in response to Item 4(d)(iii) may carry greater weight with the Agencies than materials claiming synergies created and submitted at a later time during an investigation."

Revenue Reporting Under Item 5 (a) and Foreign Manufactured Products

Parties filing HSR forms still must report their revenues for operations conducted in the United States under the NAICS codes. The new HSR rules alter these reporting requirements, however, in three critical ways. First, the new rules eliminate the requirement to report revenues for a base year (currently 2002). Second, manufacturers that also sell their products through separate wholesale or retail establishments now only have to report sales of those products under a 10-digit NAICS manufacturing code for the most recent financial year. Third, if a party manufactures products outside the U.S. and sells those products into the U.S., those revenues must now only be reported under a 10-digit NAICS manufacturing product code rather than a 6-digit non-manufacturing code.

Conclusion

In the end, whether the Final Rule will lessen or increase a given company's overall burden in complying with the HSR Act will vary by industry, company, and transaction. Acquiring parties that have Associates that generate revenues in industries that overlap with a target will have to gather and report additional information. More generally, all parties will now have to search for and evaluate the potential impact of 4(d) documents. On the other hand, the elimination of any need to report revenues for a "base year" or in multiple codes for vertically integrated manufacturers should lessen reporting requirements for such firms.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors of this alert.

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