Client Advisory

Katten
Katten Muchin Rosenman LLP

M&A/Antitrust

July 11, 2011

Significant Changes Announced to the Hart Scott Rodino Premerger Notification Program

On July 7, 2011, the Federal Trade Commission, with the concurrence of the U.S. Department of Justice, jointly announced significant changes to the Hart Scott Rodino (HSR) Premerger Notification Program. The changes, which are included in amendments to the HSR Premerger Notification Rules, the Premerger Notification and Report Form, and its Instructions (collectively, the Amendments), will likely go into effect by mid-August 2011. They will have a significant effect on private equity firms, hedge fund managers and other investment firms that manage investments in multiple funds or other investment vehicles. Other changes will affect all HSR filers by requiring them to include additional information in their HSR Premerger Notification and Report Forms (the Notification Form). The full text of the FTC's announcement, the Amendments and the FTC's explanation of the changes being made can be found **here**.

OVERVIEW

While many changes to the HSR program are included in the Amendments, three are quite important and are the subject of this Advisory. The first reflects a concern by the FTC that the current HSR Rules do not require an Acquiring Person to disclose competitive holdings of related entities that are not treated as part of the Acquiring Person itself under the HSR Rules. For example, under the current Rules, a private equity fund acquiring a widget maker need not disclose in its HSR filing that one of its sister funds, with which it shares a common manager, owns a competing widget manufacturer. The Amendments remedy this concern by creating the concept of an "Associate" and requiring the disclosure of the competitive holdings of an Acquiring Person's Associates.

The second significant change involves documents that must be submitted with the HSR filing. Until now, both the Acquired and Acquiring Person were required to submit "4(c)" documents in response to Item 4(c) of the Notification Form. Such documents generally contain information concerning the market in which the parties compete and the competitive implications of the transaction. The FTC has concluded that there is "competition-related content" in other materials that are not being produced in response to Item 4(c). Accordingly, it has added Item 4(d) to the Notification Form to capture this additional content.

The third significant change involves the reporting of sales of goods manufactured by the parties overseas, but sold in or into the United States. Previously, the parties did not need to report the manufacturing NAICS codes for the sale of these goods.[1] Under

[1] NAICS codes are designations given to narrowly defined categories of economic activity under the North American Industry Classification System.

For further information in connection with HSR matters generally or the changes to the HSR Rules discussed in this memorandum, please contact your Katten Muchin Rosenman LLP attorney, or any of the following members of Katten's **Mergers and Acquisitions** and **Antitrust** practices:

James J. Calder
212.940.6460 / james.calder@kattenlaw.com

Laura Keidan Martin
312.902.5487 / laura.martin@kattenlaw.com

Jeffrey R. Patt
312.902.5604 / jeffrey.patt@kattenlaw.com

the new Amendments, they will. For firms with significant foreign manufacturing operations, this will represent a significant change to their HSR filings.

As explained in greater detail below, the Amendments impose substantial new reporting obligations on investment firms with large portfolios held in multiple investment funds. Satisfying these obligations will require significantly more time and effort than is required by the current HSR regime. Accordingly, investment firms with significant portfolios may wish to consider creating HSR "shelf filings" now and establish other disclosure controls so that they are not delayed in executing time-sensitive acquisitions after the Amendments go into effect. They may also wish to negotiate longer deadlines in their acquisition agreements for making HSR filings.

1. Capturing Information of Competitive Holdings by Associates

To ensure that it learns when an Acquiring Person is linked to another firm that owns a business or assets that compete with the target being acquired, the FTC created the concept of "Associate" and required that Acquiring Persons disclose certain information about their Associates in Items 6 and 7 of the Notification Form.

A. Associates

The FTC created the concept of "Associate" by adding a new Section 801.1(d)(2) to the HSR Coverage Rules. The definition is exceptionally broad, but it only applies to Acquiring Persons, not Acquired Persons. Under a simplified description of the definition, a person or entity who manages the operations or investment decisions of an acquiring entity is a "managing entity." The managing entity, anyone who controls or is controlled by the managing entity (essentially its parents or subsidiaries, direct or indirect), and any entity whose operations or investments are "managed" by the managing entity are "Associates" of the Acquiring Person. In addition, to the extent the Acquiring Person itself manages the operations or investment decisions of another entity, that entity is also an "Associate." Thus, if an investment fund shares a common investment manager with other funds, the manager and all of the funds served by the manager are Associates. If an investment fund has separate investment managers for its funds, but the managers are commonly owned, the managers, and all the funds they manage, are also Associates. The same analysis applies to general partners of limited partnerships.

In effect, the concept of Associate will, in many if not most situations, bring all the funds in a fund family into the HSR process. As a practical matter, each fund making an acquisition will need to look at its structure and relationships with general partners and investment managers to determine who its Associates are. This will be a fact-intensive exercise for each acquiring firm that will have to be done at the beginning of the HSR preparation process, or earlier, before information for the filing is collected.

B. Item 6 of the Notification Form

The Associate concept is put into effect in new additions to Items 6 and 7 of the Notification Form, where specific information pertaining to Associates is required. The Amendments create a new Item 6(c)(ii) to the Notification Form, which need only be completed by the Acquiring Person. This new section requires the Acquiring Person to report certain minority holdings for each of its Associates, where those holdings represent a competitive overlap with the business or assets being acquired in the transaction. In essence, the Acquiring Person now has to report the same information about its Associates' minority holdings that it has to report for itself. Specifically, the Acquiring Person must report whether any of its Associates hold an ownership interest between 5% and 50% in the acquired entity itself. In addition, it must report for each Associate any ownership interests between 5% and 50% in other firms that derive revenue from the same six-digit Industry NAICS code as the acquired entity (a "NAICS Code Overlap"). This will enable the FTC staff to identify where an acquisition will create a competitive overlap with the Acquiring Person's Associates as well as the Acquiring Person itself.[2]

[2] Existing Item 6(c) to the HSR Notification Form has now been redesignated Item 6(c)(i). Previously, it required the Acquiring Person to list all entities in which it held minority interests of 5% to 50%. That Item has now been modified only to require disclosure of minority holdings that have NAICS Code Overlaps with the acquired entity or assets.

The FTC recognizes that the Acquiring Person may not have access to detailed information concerning sales made by firms in which its Associates have minority interests as small as 5%. Indeed, it is possible that for Associates who are separated by two or three degrees from the Acquiring Person, it may not know their minority holdings at all. Accordingly the Amendments provide that, in completing Item 6(c)(ii), the Acquiring Entity may: a) base its answer on knowledge or belief; b) list firms that are in the same industry as opposed to those with revenues in the same NAICS codes if that information is unavailable; or c) simply list all entities in which its affiliates own 5% to 50% of the equity irrespective of NAICS Code Overlaps.

C. Item 7 of the Notification Form

The Amendments also extend Item 7 of the Notification Form to the Acquiring Person's Associates. Currently, parties making HSR filings must disclose NAICS Code Overlaps between the Acquiring Person and the Acquired Entity or assets. In addition, the parties must disclose certain information about the entities involved in the overlap. Under the Amendments, the Acquiring Person must now provide Item 7 information for its Associates as well. Specifically, it must identify: 1) the six-digit NAICS Codes in which the Acquiring Person or any of its Associates have a NAICS Code Overlap with the Acquired Entity or assets; 2) the names of each Acquiring Person or Associates, and if different, the entities they control that derive revenues from the overlapping codes; and 3) certain geographic information concerning the markets in which those entities sell their products or services.

The combined effect of the changes described above is to provide the FTC and DOJ with a far broader view of the competitive implications of an acquisition. Whereas before the Amendments, the antitrust enforcement agencies did not see the competitive holdings of sister funds or other Associates, now they will. This may result in an increased number of preliminary investigations of acquisitions by private equity firms and fund managers who own large portfolios of business assets through multiple ownership vehicles. It may also draw some Associates into investigations arising from transactions in which they have no vested stake. It will certainly result in increased time and effort required to prepare HSR filings. For firms that make many acquisitions and operate multiple funds, it may be advisable to maintain a filing that has up-to-date information concerning the firm's "Associates." It may also be advisable to negotiate longer deadlines for HSR filings in acquisition agreements.

2. Expanding the Categories of Competitively Significant Documents That Must Be Included with the HSR Filing

The new Amendments also expand the category of documents concerning competition that must be submitted with the HSR Notification Form. Currently, documents addressing competition, competitors, markets, market shares, sales growth, or product or geographic expansion that were prepared by or for officers or directors of the parties in connection with the transaction, need be produced. These are the traditional "4(c)" documents that must be produced in response to Item 4(c) of the Notification Form. The Amendments add a new Item 4(d) to the Notification Form that expands the categories of documents containing "competitive information" that must now be produced. While many practitioners previously produced as 4(c) material some of the materials now covered by 4(d), the Amendments add other materials that were traditionally not covered by Item 4(c).

Item 4(d) is significant in several respects. First, unlike Item 4(c) it is not limited to documents prepared in connection with the "acquisition." Instead, in two of its subsections, Item 4(d) covers documents "that specifically relate to the sale of the acquired entity(s) or assets" whether or not prepared in connection with the actual acquisition being notified. Second, two of the new subsections require the parties to search for and produce documents prepared "up to one year before the date of [the HSR] filing." Third, in at least one situation, Item 4(d) requires the production of gratuitously prepared materials by third parties that the filing parties did not seek or request. The specifics follow.

A. Confidential Information Memoranda

New Item 4(d)(i) of the Notification Form requires both filing parties to include "Confidential Information Memoranda" (CIMs) or, in the absence of such a document, "any documents(s) given to any officer(s) or director(s) of the buyer meant to serve the function of a Confidential Information Memorandum." These materials are often provided as 4(c) documents when they relate to the actual transaction being notified. Item 4(d)(i), however, jettisons the 4(c) limitation and requires that CIMs be provided even if they were created for another transaction or possible transaction, provided they "relate to the sale of the acquired entity(s) or assets."

B. Documents Prepared by Third Party Advisors

New Item 4(d)(ii) explicitly requires that documents prepared by "investment bankers, consultants or other third party advisors ("third party advisors")" that contain 4(c) material be submitted with the HSR notification. These materials were also historically filed as 4(c) documents when they related to the actual transaction being notified. Item 4(d)(ii), however, expands the obligation in two material respects. First, it is not limited to the transaction. Like Item 4(d)(i), it covers any materials related to the sale of the acquired entity(s) or assets. Second, the obligation to provide documents under Item 4(d)(ii) is not limited to documents created by third party advisors actually retained by the parties. In explaining its rational for adding 4(d)(ii) to the Notification Form, the FTC explicitly stated that it wanted to capture competition-related information in "'pitch books,' which are 'developed by investment banking firms for the purpose of seeking an engagement.' These materials are sometimes also known informally as 'bankers' books.'" Thus, unsolicited materials by third party advisors seeking business from the parties are now potentially subject to filing with the HSR, even if the advisor is never retained.

C. Documents Concerning Synergies and Efficiencies

Finally, the Amendments add a new Item 4(d)(iii) to the Notification Form. This addition requires that materials "evaluating or analyzing synergies and/or efficiencies prepared by or for any officer(s) or director(s) . . . for the purpose of evaluating or analyzing the acquisition" be included in the HSR filing. These materials were not required by Item 4(c).

3. Inclusion of Revenue Data for Products Manufactured Abroad

Item 5 of the Notification Form currently requires the filing parties to list U.S. sales broken down by NAICS code for the last fiscal year and a base year, which is 2002. The Amendments eliminate the need to report sales for the base year. However, they expand reporting obligations by requiring that revenues generated by the manufacture of goods outside of the United States be reported in Item 5 where those goods are sold into the United States at the wholesale or retail level or are sold directly to U.S. consumers. Currently, sales of foreign manufactured products need not be reported by their 10-digit NAICS manufacturing codes. To the extent they are sold in the United States, those sales are reported under wholesaling or retailing codes. Under the Amendments, such sales will now be reported under the appropriate 10-digit manufacturing codes. Since such sales may be made at internal transfer prices (from the filing party's foreign factory to its U.S distributor) rather than at its wholesale or retail prices in the United States, the change in reporting will almost certainly change the amounts reported in Item 5 and will likely require filing parties to examine different accounting records to obtain the required information.

CONCLUSION

In sum, the Amendments represent a significant change and potentially increased burden on parties—especially Acquiring Persons—making HSR filings. Parties who are active in the M&A markets would be well advised to consider preparing an HSR "shelf filing" well before their next acquisition, in order to avoid the significant work and delay that the Amendments may create for those making their first filings under the new reporting regime.

Katten

Katten Muchin Rosenman LLP

www.kattenlaw.com

CHARLOTTE CHICAGO IRVING LONDON LOS ANGELES NEW YORK WASHINGTON, DC

Published as a source of information only. The material contained herein is not to be construed as legal advice or opinion.

©2011 Katten Muchin Rosenman LLP. All rights reserved.

Circular 230 Disclosure: Pursuant to regulations governing practice before the Internal Revenue Service, any tax advice contained herein is not intended or written to be used and cannot be used by a taxpayer for the purpose of avoiding tax penalties that may be imposed on the taxpayer. Katten Muchin Rosenman LLP is an Illinois limited liability partnership including professional corporations that has elected to be governed by the Illinois Uniform Partnership Act (1997). London affiliate: Katten Muchin Rosenman UK LLP.