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Big trouble for Biglari under the HSR Act

And why cannabis operators should take note

By Lisl Dunlop and Sam Sherman

Last December, investment fund operator Biglari Holdings Inc. agreed to pay a $1.4 million civil penalty to settle charges that it violated federal pre-merger filing requirements under the Hart-Scott-Rodino (HSR) Act. Biglari acquired shares that increased the value of voting securities it held in the Cracker Barrel restaurant chain from $155.1 million to $159.4 million, triggering an obligation to make an HSR filing. This was not Biglari's first penalty for failure to file an HSR form: It was previously fined $850,000 for HSR violations related to 2011 purchases of Cracker Barrel stock.

Nor was Biglari alone. On the same day, Clarence L. Werner, founder of the Omaha, Nebraska-based truckload carrier Werner Enterprises, Inc., agreed to pay a $486,900 penalty for failing to file an HSR form for open market acquisitions of Werner stock over a twelve-year period. In September 2021, Capital One CEO Richard Fairbank agreed to pay $637,950 for failing to report acquisitions of his company's stock in a multi-million dollar compensation package (he failed to report similar stock acquisitions in 1999 and 2004). And in December 2018, James Dolan, Executive Chairman and CEO of The Madison Square Garden Company, agreed to pay a $609,810 failure-to-file penalty related to the vesting of restricted stock units (RSUs) in the company.

Thriving industries like cannabis should take note of the penalties levied on Biglari and others. With annual cannabis sales reaching over $1B in multiple states and 306 cannabis-related mergers and acquisitions in 2021 alone, many cannabis companies' valuations are on the rise. Take three multistate operators who had an IPO in 2018: Trulieve increased its market capitalization from $950 million in 2018 to $5 billion in 2021; over the same period, Green Thumb Industries increased from $1.3 billion to $4.6 billion; and Curaleaf increased from $2.1 billion to $6.2 billion. While the HSR Act is more commonly known to apply to mergers and acquisitions between entities, it can also apply to an individual's acquisition of voting securities. Executives of rapidly growing companies may not realize that a filing obligation could be triggered by an acquisition of company stock following an increase in the underlying value of stock they already hold — and may have held for some time.

Under the HSR Act, an individual may be required to make an HSR filing with the federal antitrust agencies (the Federal Trade Commission and the Department of Justice) and observe a mandatory waiting period before acquiring voting securities. The HSR Act applies to all acquisitions of voting securities, including acquisitions by way of new issues, open market purchases, grants of restricted stock, settlement of RSUs, exercises of share options, or any other share-vesting event.

HSR obligations are triggered when a person meeting certain size requirements will hold voting securities valued at or above an HSR threshold after an acquisition of voting securities. The minimum threshold is currently $101 million, with several higher thresholds that may require filings if they are crossed. It is not uncommon for an executive's acquisition of stock in the public market or as part of their compensation to trigger HSR obligations. Importantly, HSR obligations can be triggered when an acquisition is made that results in the person holding shares valued over a threshold when aggregated with existing holdings. So, if the value of the shares already held exceeds $101 million — whether through an acquisition or because the underlying value of the shares has increased — the acquisition of even a single additional share could trigger a filing obligation.

If an HSR obligation is triggered, both the person acquiring the shares and the company will need to file HSR forms. One party (usually the acquiring person) will need to pay an HSR filing fee ranging from $45,000 to $280,000. The person acquiring the shares must observe a 30-day waiting period before the acquisition can take place.

If HSR filings should have been made in connection with previous acquisitions, the executives and the company will need to submit corrective filings to the FTC and DOJ explaining the failure to file. They also will need to consider whether additional filings are required for any upcoming share acquisitions. Once HSR filings are made, the filing covers any further acquisitions up to the next threshold for 5 years. For example, if an executive files HSR for an acquisition that will result in them holding over $101 million in shares, they do not need to make further filings for 5 years with respect to further acquisitions, so long as they will not exceed the next threshold of $202 million.

Penalties for HSR violations are currently over US$46,000 per day, assessed from the date of the acquisition of shares. The FTC and DOJ generally will not impose penalties for a first offense; however, they will likely impose penalties for any further omissions, even if inadvertent. And the agencies have assessed penalties for even brief periods of non-compliance by repeat offenders. For example, hedge fund founder Ahmet H. Okumus crossed a filing threshold when he purchased shares of internet services company Web.com Group Inc. on June 27th, 2016, and by July 14th he sold enough shares to bring him under the threshold again. Okumus agreed to pay a $180,000 civil penalty the following year.

There are several takeaways for cannabis companies and their executives from the recent experience of Biglari and others. First and foremost, assessing HSR requirements is complicated. There are myriad exemptions and highly technical nuances that can trap the unwary. Second, cannabis is a fast-growing industry, and increases in underlying value over the last several years may have left executives of large cannabis operations holding shares that may put them in jeopardy of triggering HSR obligations with future share acquisitions. Before executing any share acquisitions, companies should check the value of shares already held by their executives and consider whether further analysis is required. Third, delay can be costly, given the hefty daily penalties for each day of non-compliance.

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