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FTC Finalizes Long-Awaited HSR Overhaul

- **Why It Matters and How It Will Affect Dealmakers**
- **Six Big Changes That Made the Cut (and Three Meaty Proposals Left On the Cutting-Room Floor)**
- **Early Terminations to be Restored**

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Our Practical and Strategic Guidance for Companies Expecting to Engage in M&A: the Big Picture

The long-awaited new HSR rules and Form have been released. They go into effect in approximately 90 days (mid-January), unless blocked by a federal judge. Companies engaging in M&A now face increased burdens compared to the previous rules.

It could have been worse. Several especially onerous requirements were eliminated from the original proposal made, after many (including Axinn) identified practical consequences and likely challenges to their legality. Nonetheless, the new rules represent a very substantial step change in the level of preparation, resources, and time required for a filing.

In addition to the amount of resources required, companies will need to invest in more sophisticated antitrust analysis as part of a filing. The new rules require a description of the overlaps between the parties, and also require identification of any supplier-customer relationships between the parties. These requirements are intended as a screen to *identify* deals that merit closer scrutiny, but they will require companies to go "on the record" about topics like market definition — and those statements could be used against the parties if the agency issues a "Second Request" or even seeks to challenge or impose remedies on the deal. For HSR frequent flyers, descriptions of products and overlaps will need to be developed with an eye to how they might affect future deals.

The Political Compromise that Allowed for a Bipartisan FTC Vote

There was an unusually long (15 months) period between the first proposal and the final rules. The updated HSR rules substantially increase the complexity, costs, and preparation time for HSR filings going forward. But many onerous proposals were axed.

The delay between the release of the FTC's proposed rulemaking and the final HSR changes seems to have been driven by a desire or need for the buy-in of two Republican commissioners. Rather than push through a dramatic change to the HSR process that could have been challenged in the courts and promptly reversed if the administration changed, the Democratic commissioners negotiated with the Republicans for a stripped-down version of the original proposal.

The Republican commissioners also bargained for the reinstatement of the FTC's discretionary "early termination" policy, whereby transactions clearly raising no competitive issues could be cleared before the expiration of the formal 30-day HSR waiting period.

The new HSR rules will not become effective immediately. The rulemaking is scheduled to take effect 90 days after it is published on the Federal Register (which has yet to occur), and if it is challenged in court, the new regime may be even further delayed. Those intervening 90 days will be critical for businesses to prepare themselves for the new filing requirements, minimize regulatory disruptions to deal timing, and hit the ground running in the new year.

A Breakdown of What's New (and What was Dropped from the Original Proposal)

<u>Six Big Changes that Survived</u>

1. **Narrative descriptions of horizontal overlaps and vertical supply relationships.** In a significant break from previous U.S. practice, the revised rules will require the parties affirmatively to identify and describe any products or services – including planned future products or services – where the merging parties *compete* with one another. The parties also will be required to identify and describe products that they *supply* to one another (or supply to one another's competitors).

   While the HSR Form and Instructions characterize the required descriptions as "brief," the parties' responses will require close consideration, as these will be the point of departure for the agencies' substantive analysis. Without appropriate nuance, the initial submission could potentially prejudice arguments that the parties may want to make as an investigation develops and be used against the parties as admissions in any later litigation. And for companies engaging in transactions regularly, how the products, overlaps, and relationships are described in one filing could have consequences for future filings.

2. **New requirement to identify top customers and suppliers.** One of the most onerous new obligations is that parties with horizontal overlaps will each be required to list their top 10 customers across several "customer categories" (this is troublingly vague as a requirement, and we hope it will be clarified through future agency guidance).

   Likewise, when parties identify vertical connections between their product or service offerings, they will each be required to list their top 10 customers or suppliers (depending on

where they are positioned in the supply chain). Such information was routinely requested by the agencies when conducting a preliminary investigation in the initial HSR waiting period. But by requiring such information in the filing itself, the new requirements may accelerate parties' considerations about customer or supplier outreach in connection with deal announcement, in anticipation of earlier and more-frequent agency calls to stakeholders.

3. **Expanded document production requirements.** In a major shift, parties now must search for and provide *ordinary-course business plans and reports* about overlapping products and services that were provided to the Board or CEO over the past year, expanding the pool of required documents beyond those that strictly relate to the deal (the bright-line standard under the current regime). As discussed in Commissioner Ferguson's statement regarding the new rules, the underlying purpose of seeking such documents is to obtain information on the parties' market shares. The revised rules also require collection and production of what used to be "Item 4" documents from the supervisory deal team lead, even where that person is not an officer or director. (As an aside, it appears that Item 4 is no more - in fact, there are no section numbers in the new Form at all.)

4. **More burdensome stakeholder reporting for private equity.** One of the major FTC criticisms of the current HSR Form has been the lack of a requirement to provide information on complex PE ownership structures and individuals who have management control. Under the FTC's revised rules, businesses will be required to list all officers and directors of (i) the entity that is party to the deal; (ii) all of that entity's direct and indirect subsidiaries; and (iii) all of that entity's direct and indirect parents. Significantly, limited partnerships will be newly required to identify minority partners holding at least a 5% stake; until now, partnerships have only been required to identify their general partners.

5. **New disclosures of foreign subsidies and defense contracts.** Implementing a Congressional mandate passed in 2022, the new rules will require parties to disclose economic subsidies received from certain foreign governments and entities, most notably including China. The definition of "subsidy" is quite broad, including tax credits and government purchases, which will require parties to expand their due diligence into subsidy issues ahead of an HSR filing. Parties will also be required to disclose a party's bids and awarded contracts in response to requests for proposals from the Department of Defense or other members of the U.S. intelligence community.

6. **Moderately easier financial reporting by NAICS codes.** One thing did get a little easier: under the current HSR rules, parties have been required to assign precise dollar figures to every industry in which they do business. In the new Form, parties need only provide that precise detail for industries in which the parties overlap, or which are linked in a common supply chain. For unrelated industries, parties need only disclose whether annual revenues exceed $10 million, $100 million, or $1 billion. Additionally, parties will no longer be required to subcategorize manufacturing revenues by 10-digit NAPCS product codes.

Three Onerous Proposals Cut from the Final Rule

1. **No labor and employment information.** The July 2023 draft heavily focused on new requirements to provide information about labor markets. Those proposals would have required businesses to categorize their worker headcount across "standard occupational

classifications" (as defined by the Bureau of Labor Statistics), and to further analyze those classifications by geographic commuting zones. The proposals also would have required businesses to identify any pending federal agency (i.e., Department of Labor's Wage and Hour Division, the National Labor Relations Board, or the Occupational Safety and Health Administration) investigations or workplace safety penalties or findings issued in the past five years. All of these proposals have been scratched from the final rule.

2. **No draft transaction-related documents.** The final rulemaking does not adopt the July 2023 proposal to require collection and production of iterative drafts of transaction documents. This development reduces the need for forensic collections, though in complex deals parties may continue to elect to conduct a forensic search to ensure that all required transaction-related documents are submitted with the HSR (and avoid potential hiccups in a later Second Request).

3. **No creditor or other interest holder information**. The FTC did not adopt proposed rules that would require acquiring persons to identify entities or individuals that (i) provide, or will provide, credit; (ii) hold non-voting securities, options or warrants; or (iii) have a management agreement with entities related to the transaction. In doing so, the FTC acknowledged that "the mechanisms of influence or managerial control are often bespoke and vary from entity to entity" and cautioned that it may revisit these proposals in the future.

Many may look to their calendars puzzled at why these long-awaited revisions did not wait a little longer. Election Day looms, and if these rules go into effect 90-plus days from now, Washington will be preparing to inaugurate a new president. Still, whatever comes of the election, it is unclear whether a Republican administration would abandon these revisions entirely. The Commission's unanimous vote to approve the final rulemaking suggests a hard-fought compromise to reach a bipartisan consensus. Against that backdrop, businesses should work with antitrust counsel to begin preparing for a new normal in HSR.

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We will be in touch with Axinn clients in the coming days with more granular guidance and with materials that clients can use to get organized and ready for the new requirements. Please contact any Axinn partner to discuss these changes or to schedule a presentation from our team.

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