Comments of the Section of Antitrust Law
of the American Bar Association
On the Recently Announced Interim HSR Rules,
HSR Form Changes And
Proposed Rule Changes to the HSR Act

These views are being presented only on behalf of the Section of Antitrust Law and have not been approved by the House of Delegates or the Board of Governors of the American Bar Association ("ABA") and should not be construed as representing the position of the ABA.

These are the Comments of the Section of Antitrust Law (the "Section") of the American Bar Association concerning the new interim rules, form changes, and proposed rules changes under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the "HSR Act" or "the Act"). The Section supports several of the new rules and proposed changes, but recommends certain modifications to the rules announced. In particular, the Section objects to proposed rules that appear to have the sole objective of requiring additional unnecessary filings and substantial additional filing fees where there is no likelihood of additional antitrust significance.

I. INTRODUCTION

President Clinton signed legislation on December 21, 2000, which, among other things, amended the HSR Act. The amendments went into effect on February 1, 2001. The Section supported this legislation. 1/ On January 25, 2001, the Federal Trade Commission (the "FTC" or the "Commission") and the Department of Justice (the "DOJ") issued interim rules to conform the HSR implementing rules to these amendments. The interim rules became effective on February 1, 2001, the same date the amendments to the HSR Act became effective. The FTC and DOJ also announced proposed rules changes and requested comment by March 19, 2001. Finally, changes to the HSR Form were announced on that same date, changes which were first proposed in 1996, but not finalized until now.

These comments summarize these interim and proposed rule changes, as well as the announced changes to the HSR form, and recommend that the Commission make certain modifications to the announced rules.

1/ See Report of The Section of Antitrust Law on Proposed Hart-Scott-Rodino Antitrust Improvements Act Amendments, April 11, 2000, at http://www.abanet.org/ftp/pub/antitrust/hsr_antitrust_improvements_act.doc

II. SUMMARY OF HSR ACT AMENDMENTS

The amendments to the HSR Act were enacted principally to raise the size-of-transaction threshold test from its previous level of $15 million to $50 million. This increase represented the first increase in any of the size thresholds in the HSR Act since it was first enacted in 1976. In addition, the amendments eliminated the size-of-person threshold test for transactions valued in excess of $200 million. All such transactions are now reportable regardless of the size of the parties involved, unless an exemption applies.

These amendments were intended to reduce the number of transactions that would have to be reported under the HSR Act. When he introduced these amendments, Senator Hatch, the bill's co-sponsor, noted that since the filing thresholds had not been adjusted since the act was first enacted, the HSR Act had become a "costly regulatory and financial burden upon companies, . . , as well as a sizable drain on the resources of the agencies."2/ Consequently, he proposed raising the filing threshold in order to provide "significant regulatory and financial relief for businesses, while ensuring that transactions that truly deserve antitrust scrutiny will continue to be reviewed."

Since reduced filings would also have a commensurate negative impact on the total funds collected under the HSR filing fees, the new amendments also increased the HSR filing fees for many of the remaining reportable transactions. Specifically, the amendments introduced a multi-tiered system tying the filing fee level to the value of assets or voting securities that the acquiring person will hold as a result of a transaction. The new fees now range from $45,000 to $280,000.

The amendments also changed certain HSR waiting periods. If the normal HSR waiting period ends on a weekend day or a holiday, under the new law the waiting period is extended to the next regular business day. Also, the 20 day waiting period following substantial compliance with a Second Request has been extended to 30 days (except in the case of cash tender offers and bankruptcy matters).

To implement the changes to the HSR Act, on January 25, 2001, the FTC issued interim HSR regulations and a new HSR report notification form, both of which went into effect on February 1, 2001. In addition, the FTC published for comment other proposed changes to the HSR regulations. The comment period for these proposed changes expires

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2/ 106th Cong. Rec. S13,973 (1999) (statement of Senator Orrin Hatch).

on March 19, 2001.3/ This comment summarizes each of these changes and notes areas where the rules should be further changed or modified in order to make them consistent with the intended purpose of the amendments to the HSR Act to reduce the burden the HSR reporting system imposes on businesses.

III. THE INTERIM RULES

The interim rules announced by the FTC immediately put into place certain new rules intended to implement the changes encompassed by the amendments to the HSR Act. These new rules are now effective and permanent, subject to further additional modification by the Commission. Many of the changes are nonsubstantive, such as incorporating the new size of transaction threshold in the existing rules and examples accompanying the rules.4/ For example, the interim rules amend Rule 801.40 by eliminating the size-of-person test for the formation of joint ventures valued in excess of $200 million, tracking the elimination of the size of person test in the HSR Act amendments generally for transactions valued in excess of $200 million. The interim rules also have eliminated the minimum dollar exemption previously found in Rule 802.20, which exempted in certain circumstances acquisitions of more than 15% of the outstanding voting securities of an issuer which was valued at less than $15 million, since the HSR Act amendments eliminated the 15% size-of-transaction test and instituted a monetary size-of-transaction test alone.

Rule 803.9 has been added to set forth the new filing fee structure and provide examples on how the correct fee should be determined. Notably, the new rule requires only one filing fee for certain transactions where there are two acquiring persons (i.e., certain consolidations or stock for stock acquisitions).5/ The Section commends the agencies for eliminating double or triple filing fees.

3/ Although the interim rules were implemented without comment, the Commission nonetheless invited comment and reserved the right to further modify or change the interim rules consistent with experience and/or any comments received.

4/ Several examples to various rules have been modified to be consistent with the HSR Act amendments, including the examples in Rules 801.2, 801.4, 801.10, 801.11, 801.13, 801.14, 801.15, 801.20, 801.30, 801.31, 801.32, 801.40, 801.90, 802.1, 802.3, 802.4, 802.5, 802.6, 802.9, 802.21, 802.23, 802.31, 802.35, 802.41, 802.64, 803.5, 803.7, 803.10, and 803.20. In revising the example to Rule 802.6, the Commission left in a reference to the approval by the Civil Aeronautics Board, although that entity no longer exists. This example should be further revised to eliminate this reference.

5/ Several of the examples to Rule 803.9 provide discussions regarding the determination of the appropriate acquisition price when it has not yet been set by the parties. These examples, however, seem more appropriate to accompany other rules. Example 4 contains a detailed explanation of how a transaction can be determined by fair market value by the

The Section supports many of these changes in that they simply implement the HSR Act amendments and simplify and clarify many of these rules. However, several of the interim rules substantially change the reporting obligations of the parties and, in some cases, significantly increase the burden and the cost of HSR reporting on filing parties. Consequently, we recommend that the FTC change or modify the interim rules in accordance with the recommendations of this report in order to eliminate these additional burdens and costs.

a) Establishment of New Notification Thresholds (Rule 801.1(h))

The interim rules enact new filing thresholds. Formerly, the HSR Rules imposed three filing thresholds for acquisitions of voting securities: (a) 15%, (b) 25% and (c) 50%.6/ With respect to asset acquisitions, the only threshold applicable under the original HSR Rules was the $15 million size-of-transaction threshold.

Under these original percentage thresholds, if a filing party met the filing threshold within the first year after termination of the waiting period, it was permitted to acquire additional shares of voting securities up to but not exceeding the next highest filing threshold for an additional five year period without having to make additional HSR filings. For example, if the acquiring party filed to acquire 25% of the outstanding voting securities of an issuer, it could elect to file to meet the 25% filing threshold by "checking" the appropriate box on the HSR form. Then, following termination of the waiting period the acquiring party could acquire up to 25% of the issuer's outstanding voting securities without additional filings. If it acquired that stock within one year after termination of the waiting period, that same acquiring party could then purchase additional shares of voting stock from that same issuer for the next five years without making additional HSR filings, so long as its total holdings of voting stock in that issuer did not equal or exceed 50% of the outstanding voting securities of that issuer. The purpose of these thresholds was to eliminate filing

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board or its designee and would more appropriately fall under Rule 810.10. Example 5 is a complicated example of how exempt assets are excluded from determining the value of the transaction and should more appropriately accompany Rule 801.15. The Commission should amend these examples in accordance with these recommendations.

6/ Although the original HSR Act did not contain these filing thresholds, the original implementing Rules imposed these thresholds in order to reduce the burden upon filing parties. Under the HSR Act, since all previously held voting securities are included in determining the total amount held as a result of the acquisition, once the size of transaction threshold is passed, each additional acquisition of shares would have theoretically imposed additional filing requirements. The filing thresholds were established to relieve parties of this burden and only require additional HSR filings if and when the total holdings of the acquiring party exceeded certain levels that were likely to be of competitive significance.

requirements for any additional purchase of voting securities, which would be required under a literal reading of the HSR Act. Instead the rules established bright lines under which parties would have to make additional HSR filings, based on potential competitive significance of various levels of stock ownership.

The new thresholds established by the interim rules now include, in addition to two of the pre-existing percentage thresholds applicable to voting securities acquisitions, dollar amount thresholds that are based on the filing fee thresholds contained in the HSR Act amendments. Thus, the interim rules now establish five thresholds: (i) $50 million; (ii) $100 million; (iii) $500 million; (iv) 25% where the value of voting securities to be held is greater than $1 billion; and (v) 50%.7/ The dollar thresholds are applicable to both asset and voting securities acquisitions, while the percentage thresholds are applicable to voting securities acquisitions only.

Keying filing thresholds to the dollar value of voting securities purchased will result in parties losing certainty with respect to their filing obligations. Market fluctuations not controlled by the acquiring party could cause the value of its holdings to exceed the next highest threshold, resulting in an additional filing requirement if any additional shares are purchased. For example, if X files for the $50 million threshold, but the value of stock purchased later increases to more than $100 million, the next purchase of even a single share of voting securities would be reportable. The original filing thresholds eliminated this uncertainty by limiting the thresholds to percentages of total voting securities held, which is more within the control of the acquiring party. But by imposing dollar thresholds, the Commission creates uncertainty and imposes additional burden and additional costs, in addition to additional and higher filing fees.

Furthermore, keying the filing thresholds to the various fee levels contained in the HSR Act amendments creates the unintended effect that the filing thresholds act as additional revenue generators. In the example above, where market fluctuations result in X holding in excess of $100 million, acquisitions of even one additional share would be reportable and the filing party would be obligated to pay the higher filing fee, in addition to the filing fee previously paid (e.g., the higher filing fee of $125,000 in addition to the $45,000 filing fee previously paid). This may result in parties filing under the highest available threshold in the first instance, in order to achieve some certainty on their filing obligations, resulting in paying a higher filing fee than they otherwise would be required to pay.

7/ The new filing thresholds eliminate the 15% threshold, consistent with the HSR Act amendments that eliminated the previous 15% threshold in the statute.

The Section recognizes the concerns and interests the Commisison staff sought to address with these interim rules and commends the staff for their efforts as well as overall work product. The proposed interim solutions in this section, however, do not appear adequate to address all of the issues raised by these provisions and the Section suggests that Commission staff further refine this provision. The Section would welcome the opportunity to work with the FTC staff to develop a more comprehensive solution to address fully the above concerns.

b) Elimination of the 5-year timeframe for transactions filed before the effective date of the HSR Act amendments (Rule 802.21).

Under Rule 802.21, the acquiring party has a five-year period after termination of the waiting period to continue to acquire voting securities up to but not exceeding the next filing threshold without requiring any additional HSR filing. Due to the change in the filing thresholds enacted in the HSR Act amendments, the interim rules have established a transitional rule which will allow the prior thresholds to remain in effect for a short period of time with respect to acquiring parties who have filed to acquire voting securities during the past five years and are making additional acquisitions under the exemption provided by Rule 802.21. Under this transitional rule, such filers can continue to acquire voting securities up to what was the next reporting threshold at the time they originally made their HSR filing, until the end of the original 5-year period or until one year after the HSR Act amendments became effective (February 1, 2002), whichever comes first.

Thus, this transitional rule in effect will shorten the 5-year period available to any party who filed less than 4 years before the amendments took effect. For example, if ABC Company filed in 1999 to acquire 25% of the voting securities of an issuer, ABC now has only one more year to make additional acquisitions up to the next highest threshold without requiring additional filings and filing fees, not the remaining 3 years ABC would have under the original rule. In order to retain the benefits of the full 5-year period, the party must refile under the new thresholds (and incur the additional costs of preparing an HSR form and pay the additional filing fees) within the first year after the amendments take effect.

This limited transitional rule has the effect of potentially increasing the burden and costs to hundreds of previous filers. The Section recommends that the Commission provide that previous filers have the full 5-year period originally available at the time of their original filing to make additional acquisitions of voting securities up to the next highest threshold in effect at the time they filed.

c) Modification of the Commission's Previous Policy with respect to transactions involving assets in bankruptcy.

The Commission's revision of Rule 803.20(2) seems to change the agencies' past interpretations with respect to the start of the second waiting period8/ in the case of transactions covered by 11 U.S.C. § 363(b). In the past, the position of the FTC's Premerger Notification Office ("PNO") has been that the second waiting period starts with respect to transactions covered by the Bankruptcy Code when *both* the acquiring and acquired parties substantially complied with the second request. However, the Notice accompanying the interim rules states that this is not the case, but that instead only the acquiring party's substantial compliance is necessary to start the waiting period in such cases.

The Section recommends that the Commission's revision of Rule 803.20(c)(2) be amended to clearly reflect this change in policy.

IV. THE FORM CHANGES

The FTC has enacted several changes to the HSR form. These changes are now effective and permanent, although the Commission has stated that it reserves the right to further modify these changes. Some changes are made in order to conform the HSR form to the HSR Act amendments and the interim rules. Others enact certain changes first proposed by the agencies in 1996 but never implemented. The major changes are addressed below.9/

8/ The "second waiting period" refers to that period provided for in the HSR Act after parties have substantially complied with any Request for Additional Information and Documentary Materials (also known colloquially as a "second request")

9/ In addition to those discussed, the FTC also re-ordered some items in the form, now requires the party paying the filing fee by wire transfer to provide certain identifying information concerning the wire transfer, and has eliminated Item 8 (the vendor/vendee question) from the form. The Section applauds each of these steps in that they will simplify the HSR Form, but recommends that the Commission continue to find ways to further simplify the form consistent with the agencies' need for relevant information.

a) Description of the Method used to Determine the Filing Fee.

When the filing fee paid is different from what the acquisition price might appear to dictate it should be, the parties now will be required to provide a description of the method used to determine the proper fee amount. For example, if the acquisition price in the term sheet is above $100 million, it would appear to dictate that a filing fee of $125,000 would be paid. However, actual valuations of the deal might reveal a value less then $100 million, which would dictate that a $45,000 filing fee be paid. In such cases, if the acquiring party chooses to pay the lower filing fee, the new form will require the parties to provide a detailed description of the valuation method used to determine the filing fee to be paid. In addition, the form requires the parties in all transactions to identify the person who did the valuation.

Although the agencies might reasonably request this information in order to ensure that the proper filing fees are being paid, the proposed regulation does not adequately set forth the situations when such disclosure must be provided and how its requirements can be satisfied. For example, the notice states that the description of the valuation method must be provided when an acquisition price is undetermined and "may fall within a range that straddles two filing fee thresholds." It is unclear under what circumstances a party would meet this "straddle" requirement and thus have to provide the required description. In such situations, if the filer chooses to file under the lower fee threshold, it faces uncertainty whether the Commission may question its valuation and require the parties to refile at the higher threshold – thus delaying the transaction. This uncertainty may prompt filers to file for the higher threshold in the first instance (with the consequent higher filing fee) in order to remove this uncertainty.10/

The reason why parties should be required to identify the person who performed the valuation is also unclear. Although the Commission states that this will facilitate responding to any inquiry, this response can be obtained just as quickly through contacting the contact person identified in Item 1(g) of the form. If the agencies are looking for a responsible party to hold accountable for any errors in the valuation, then the agencies can look to the filing party itself and the officer who signed the certification; they do not need an additional person to be identified as accountable on the form itself.

10/ For example, it is unclear whether a person filing for a cash tender offer for a minimum condition (i.e., 66 2/3%) should be able to file based upon a valuation for the minimum condition being satisfied (allowing the waiting period to start) or, to avoid the risk of crossing a higher threshold, file based on the assumption that 100% (or nearly so) of the shares will be tendered.

The Section recognizes that the agencies have a legitimate interest in obtaining the information necessary to assess the accuracy and adequacy of each filing. Although the approach adopted by the interim rules is minimally intrusive, this approach still could raise significant questions as to compliance. The Section recommends that the agencies modify the applicable rules and instructions to the form to delineate clearly the situations when such a disclosure will be required and detail how parties will meet those requirements.

b) Transactions Subject to Foreign Antitrust Reporting Requirements.

The new form requests the parties to indicate voluntarily whether the transaction is subject to any foreign antitrust reporting requirements and to list voluntarily the names of any foreign antitrust or competition authority that will be notified of the proposed transaction. The original 1996 proposal would have *required* parties to indicate whether the transaction is subject to foreign reporting requirements and to identify each such authority. Most comments submitted at that time strenuously objected to the mandatory nature of the proposed change.

Although listing of the foreign authorities to be notified is now voluntary, and only requires the parties to provide it based on their knowledge and belief at the time of filing, the burden associated with responding to this item may outweigh the probative value to the agencies. In the first instance, this requirement is unnecessary in the vast majority of filings, since most filings are given little if any substantive review by the U.S. agencies. Thus, parties may feel obligated to undertake this exercise when it is most likely not even needed by the agencies. Furthermore, many countries now have merger-reporting regimes, and determining foreign reportability requirements for transactions is difficult, time-consuming, and not always precise. In addition, the analysis of foreign reporting requirements is often not completed before HSR filings are made.

Although this requirement is voluntary and not burdensome on its face, this change still raises several potential concerns. First, the voluntary nature of this item should be clearly disclosed on the form so infrequent filers will know without reference to the instructions that responding to this item is voluntary. Furthermore, even though responding to this item is voluntary, this item raises the risk that parties may inadvertently err in their reporting; there is no explanation of the obligations that a party must undertake to ensure that even their voluntary answer is accurate. Finally, it is important, given the uncertainty regarding foreign filing requirements, that any such requirement remain voluntary. The Section would have grave concerns if in the future any consideration were given to making this a mandatory disclosure.

V. THE PROPOSED RULE CHANGES

In addition to the interim rules and the form changes, the FTC also announced additional proposed HSR rules changes and has sought public comment for these changes until March 19, 2001. The proposed changes include revisions of examples to Rules 801.4, 801.14, 801.90, 802.8 and 802.52. The Commission also has proposed to amend Rule 801.15 to reflect the new size-of-transaction thresholds. The Section supports each of these changes.

The most dramatic change, however, is the proposed restructuring and revision of Rules 802.50 and 802.51, the rules exempting certain acquisitions of foreign assets and voting securities of a foreign issuer. The restructuring is such that Rule 802.50 now applies to acquisitions of foreign assets and Rule 802.51 applies to acquisitions of voting securities of foreign issuers. The Section supports this change in that it will more clearly define what rules apply to acquisitions of foreign assets and foreign voting securities. However, the substantive revisions to these rules raise substantial questions and potentially reduce the scope of the previous exemptions (hence increasing filings) quite significantly.

Under the proposed Rule 802.50, the acquisition of foreign assets will be exempt unless the foreign assets generated sales in or into the United States exceeding $50 million during the combined period of (ii) the person's most recent fiscal year, and (ii) the subsequent period since the end of that fiscal year. This proposed change will substantially narrow the exemption previously available and increase the number of deals that are reportable. For example, if A acquires certain foreign assets in July, A will have to determine the level of sales, if any, those assets generated in or into the United States in both the most recent fiscal year, as well as during the period since that fiscal year ended and the time of the acquisition. If those assets generated sales of $40 million during the most recent fiscal year, and sales of $20 million during the period following that fiscal year, under the proposed rule, this transaction would now be reportable since the total sales in both the fiscal year and since the end of the fiscal year exceed $50 million (total of $60 million).

Previously, acquisitions by foreign firms of foreign assets were completely exempt while such acquisitions are not exempt under the proposed rules. However, the Commission sets forth no explanation as to why such transactions are likely to raise competitive issues in the United States in order to justify removing the exemption for such transactions.

Furthermore, requiring parties to combine the sales in the most recent fiscal year with the sales in the current year will result in more deals falling outside of this exemption, especially deals consummated late in the subsequent year, thus making a number of transactions reportable that

would have previously been exempt. For example, if the foreign assets operate on a calendar year and they are purchased in December 2001, then the parties must determine its sales in or into the United States for the full year 2000 and for the 11 months of year 2001. In most cases, adding the sales of these two periods will most likely result in the $50 million sales level being exceeded and require an HSR filing. The avowed purpose of this proposed change is to pick up filings involving firms with large run-ups in sales in the current year. But this change will pick up, for example, transactions involving assets with sales into the United States of $49 million in the most recent fiscal year and sales of $2 million in the current year – hardly the type of large run-up in sales the FTC indicates it is trying to pick up.

The Section recommends that the Commission not implement this change or, if it does, that the change be revised such that the sales numbers not be aggregated, but that the larger of the sales in the current year or most recently ended year be used to determine if the exemption applies.

In addition, the proposed rule eliminates the current three-part size test for transactions valued at more than $200 million.11/ Therefore, if a transaction is valued at more than $200 million and the foreign assets being acquired generated sales during the relevant time period of more than $50 million, then the transaction is reportable, even if the previous three-part test is met. Although the current three-part size rule is complex, eliminating it completely will greatly narrow the reach of this exemption. The Section recommends that the three part size tests be retained as in the current rule. 12/

The Commission also proposes amending Rule 802.51 to only govern acquisitions of voting securities of foreign issuers. Significantly, the proposal would change the test for determining the value of the assets the

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11/ The three-part size test refers to current Rule 802.51 which governs acquisitions by foreign persons and provides that in order to determine if the exemption applies, filing parties must examine (i) in the case of an acquisition of voting securities, the value or holdings or sales of the issuer in the United States, (ii) in the case of an asset acquisition, the value of those assets in the United States, and (iii) if the acquired person is also a foreign person, the aggregate sales and total assets in or into the United States of both the acquiring and acquired persons.

12/ Eliminating the size test for acquisitions valued at less than $200 million also results in double-reportability of many combined formation/acquisition transactions. In the past, an acquisition by a newly-formed entity was often exempted from reporting under Rule 801.11(e) – the so-called "flow-through rule" – which allows a Newco, without a regularly prepared balance sheet, to exclude cash being used for the purchase from its "size", and hence to fall below the size-of-person test. The new rules will likely require filings for both the formation of Newco and its related acquisition.

foreign issuer holds in the United States from the current "book value" to fair market value. This proposed change will increase the burden on filing parties since it means that parties will have to split out U.S. assets and assign a fair market value to the U.S. assets. The current rule's reliance on book value is simple and not burdensome and provided parties with some certainty that the agencies will not later dispute the fair market valuation.

The proposal also incorporates the same change proposed for Rule 802.51 to require aggregating sales in the most recent fiscal year and those in current year. Again, for the same reasons stated above with respect to Rule 802.50, the Section recommends that this proposal be rejected or at least modified to provide that one looks at sales in either the most recent fiscal year or the current year, whichever is higher.

V. CONCLUSION

The FTC staff did a commendable job conforming the rules to take into account the recent HSR Act amendments under very tight time constraints. However, a further refinement of these changes, as outlined above, is necessary in order to avoid increasing the burden and substantial costs that the HSR Act and its requirements place on filing parties.