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FTC Will "Routinely" Require Prior Approval Provisions in Merger Orders

- The FTC issued a statement on its intended use of prior approval provisions for future transactions in merger orders. Companies may become subject to these orders either by consent or after an FTC administrative proceeding. The FTC has not said what standard it will use in determining whether or not to grant approval. The DOJ has not announced a similar policy.

- The FTC will require these provisions for any future transactions involving the same relevant market and for any re-sale of assets acquired by a divestiture purchaser as part of a merger remedy. In certain circumstances, the FTC might also require prior approval provisions for future transactions involving different relevant markets, and for future transactions of parties that abandon a transaction after an FTC challenge.

- Companies should consider the likelihood and consequences of becoming subject to FTC prior approval provisions when structuring transactions. We discuss some of these potential consequences and related considerations below.

On October 25, the Federal Trade Commission (FTC) issued a Statement of the Commission on Use of Prior Approval Provisions in Merger Orders announcing that it intends to include provisions in its orders in merger cases that would require parties to receive prior FTC approval for "*any* future transaction affecting each relevant market for which a violation was alleged." In some cases, the FTC will also include prior approval provisions for future transactions involving different relevant markets, and may seek to impose a prior approval requirement for parties' future transactions even if they abandon a proposed merger. The FTC will also require companies that purchase assets as part of a divestiture remedy to agree to prior approval requirements for future transactions involving those assets. Companies that propose to engage in transactions covered by these provisions could face an FTC approval process that is significantly more burdensome than the Hart-Scott-Rodino (HSR) Act merger review process. The two Republican Commissioners voted against issuing the policy. (In a break from standard practice, the FTC released the policy before the dissenting statement was available. Commissioner Phillips has previously argued that insisting on prior approval provisions would result in less willingness of parties to settle and more litigation, and "will chill procompetitive deals and hurt consumers.") The Antitrust Division of the Department of Justice (DOJ) has not announced a similar policy.

It bears keeping in mind that the clear majority of proposed transactions will not pose competitive concerns and, therefore, would not risk becoming subject to an FTC divestiture order. But for the small subset of transactions that do, it is important to understand what sorts of demands the parties might get from the FTC.

In What Circumstances Might the FTC Seek to Include Prior Approval Provisions in Merger Orders?

- **Deals involving the same markets.** The FTC will seek to include prior approval provisions "in all merger divestiture orders for every relevant market where harm is alleged to occur, for a minimum of ten years." This means that any of the parties' subsequent deals involving the same markets as those allegedly affected by the transaction which gives rise to the order could be subject to prior FTC approval.

- **Deals involving different markets.** The FTC might seek prior approval provisions for the parties' future deals involving markets *different* from those allegedly affected by the transaction in certain situations, including when: the transaction is “substantially similar to a transaction that was previously challenged” by the FTC; the transaction involves concentrated markets “or has seen significant consolidation in the previous ten years”; the transaction “significantly increases concentration”; when “one of the parties likely had market power”; when either party as a “history of acquisitiveness”; and when there is “evidence of anticompetitive market dynamics.”

- **Deals involving parties to abandoned transactions.** If the parties abandon their transaction after the issuance of an FTC complaint, the FTC might seek prior approval provisions. In determining whether to do so, the FTC will take into account the factors listed above. (This could give rise to a situation in which the FTC prevails in obtaining a preliminary injunction in federal court and, as is often the case when that happens, the parties abandon the transaction – but the parties nevertheless end up having to litigate an FTC administrative proceeding. This scenario unfolded at least once in the late 1980s and early 1990s.)

- **Deals involving companies that purchased assets as part of a divestiture remedy.** The FTC said that it will “require buyers of divested assets in Commission merger consent orders to agree to a prior approval for any future sale of the assets they acquire in divestiture orders, for a minimum of ten years.” According to the FTC: “This will ensure that the divested assets are not later sold to an unsuitable firm that would contravene the purpose of the Commission’s order.” (The FTC noted in its statement that while it had imposed prior approval requirements on divestiture purchasers “on occasion” in the past, it now “intends to require all buyers” to agree to such provisions.)

What Has Changed?

The new policy significantly expands the FTC’s use of prior approval provisions. From 1995 until recently, the FTC operated under a policy that limited the use of these provisions to narrow situations where it believed that parties to mergers the FTC found to be anticompetitive would “attempt the same or approximately the same merger” with “essentially the same relevant assets.”

Potential Consequences

Parties who become subject to prior approval orders potentially face increased burdens on their dealmaking activity, including increased delay and uncertainty. For example, companies could be in the position of having to wait an indeterminate amount of time for the FTC’s approval before they are allowed to close their transaction. Also, smaller deals that fall below the HSR thresholds and would therefore not be notified to the FTC or be subject to a waiting period could be tied up in a lengthy FTC review process. Moreover, the FTC has not articulated the standard it will use to determine whether to grant approval. Companies subject to prior approval provisions may have to prove to the FTC that a proposed transaction is not anticompetitive, is competitively neutral or is procompetitive. Under normal circumstances, the *FTC* has the burden of proving that a proposed transaction may substantially lessen competition.

The new policy has important implications for transaction planning. Among the relevant considerations are: What is the likelihood that the FTC will exercise jurisdiction over a proposed transaction? Should the parties conservatively structure a transaction to include up-front divestitures, with the goal of potentially avoiding an FTC order? Should companies seek to include terms in merger agreements addressing parties’ obligations to agree to a prior approval provision? Would the refusal by one party to accept an FTC prior approval provision risk triggering litigation between the parties? Depending on the parties’ willingness to agree to prior approval provisions, more transactions may become subject to lengthy litigation, and this could have additional implications for various terms in a merger agreement. As part of the due diligence process, companies will also want to understand the potential implications of agreeing to a transaction when the target or acquirer is already subject to prior approval provisions.

If the FTC insists on a prior approval provision, companies will have several strategic decisions to make. Points to consider include the likelihood that the FTC would litigate, and the costs and risks to the parties of settling and agreeing to the provision versus litigating with the FTC. If the FTC insists on prior approval provisions for the re-sale of divestiture assets, potential divestiture buyers, particularly private equity buyers, will have to consider the costs and risks that those provisions might have for their plans for the assets.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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