Legal Backgrounder

Washington Legal Foundation
Advocate for Freedom and Justice®
2009 Massachusetts Avenue, NW
Washington, DC 20036
202.588.0302 wlf.org

Vol. 37 No. 2 January 14, 2022

The FTC's Prior Approval Policy Likely Will Eliminate Incentives to Cooperate with Antitrust Investigations

by Gerald A. Stein and Michael A. Primrose

In another blow to the cooperative spirit between private businesses and federal regulators, the Federal Trade Commission (the "Commission") issued its "Statement of the Commission on Use of Prior Approval Provisions in Merger Orders," (the "Policy") on October 25, 2021, announcing that it now intends to "routinely require[e] merging parties subject to a Commission order to obtain prior approval before closing *any* future transaction affecting each relevant market for which a violation was alleged . . . for a minimum of ten years."[1] Companies willing to enter into a consent decree with the Commission will now be required to subject future transactions to Commission review and approval without any of the statutorily prescribed rules governing merger review under the Hart-Scott-Rodino ("HSR") Act; meaning the Commission can now review—and block—such transactions without complying with any statutory timeframe or substantive standards.

The Policy intentionally encumbers merging parties with increased risk and uncertainty.[2] Parties that consider entering consent decrees to avoid the delay and expense of long investigations and litigation must now also anticipate that future deals in the same or similar markets could be blocked for at least ten years at the Commission's whim. Moreover, the Commission stated that it may also choose to apply the Policy even when parties abandon a proposed transaction in response to the Commission's commencement of litigation.[3] Thus, the Commission gives itself virtually unfettered discretion to block certain *future* mergers when parties chose to avoid costly investigations that are based only on mere *allegations* by the Commission that a past merger had the *probability* to lessen competition. In other words, the Commission would effectively block present and future mergers without any judicial determination that any of these mergers *actually* violated the Clayton Act.

The full effect of the Commission's Policy derives from a combination of (1) the Policy circumventing the HSR-prescribed guidelines for merger review; and (2) deference by courts to this circumvented procedure because the parties "agreed to" the procedure in the consent order. Many parties to transactions that already have been significantly delayed by a burdensome antitrust review with high attendant legal bills will have very little choice but to accept onerous terms as the only way forward.

The HSR Review Process. A brief review of the HSR process highlights the new Policy's drastic effects.[4] Under the statutorily prescribed HSR procedure, parties to a transaction that meets certain thresholds must file

---

[1] Statement of the Commission on Use of Prior Approval Provisions in Merger Orders (Oct. 25, 2021), https://www.ftc.gov/system/files/documents/public_statements/1597894/p859900priorapprovalstatement.pdf.
[2] *See id* ("Acquisitive firms in particular are too willing to roll the dice on an anticompetitive deal because there are few downsides (from their perspective) to their long-term strategy that contemplates other acquisitions down the road. Parties pursuing facially anticompetitive deals should now know that they are at risk of being subject to a prior approval provision.").
[3] *Id* ("The fact that parties may abandon a merger after litigation commences does not guarantee that the Commission will not subsequently pursue an order incorporating a prior approval provision.").
[4] *See generally* 16 C.F.R. § 801-03.

Gerald A. Stein is a partner with Norton Rose Fulbright US LLP in the firm's New York, NY and Washington, DC offices. **Michael A. Primrose** is a partner with Benesch Friedlander Coplan & Aronoff LLP in the firm's Cleveland, OH office.
The authors gratefully acknowledge the assistance of Timothy Chung, a law clerk in Norton Rose Fulbright's NY office.

an HSR notice.[5] This filing triggers a 30-day waiting period,[6] during which the Commission must decide whether to (1) allow the waiting period to expire, in which case the parties may proceed to close the transaction;[7] or (2) issue a second request (seeking additional information about the transaction), in which case the parties must respond to voluminous document and information requests while the statutory waiting period is further extended until 30 days after all parties have substantially complied with the second request.[8]

After the Commission issues a second request, the merging parties may request a conference to discuss the competitive issues raised by the proposed transaction and which information and documents may be obtained relating to those issues.[9] Moreover, the merging parties may avail themselves of a review process to determine whether the second request "is unreasonably cumulative, unduly burdensome, or duplicative;" or whether the second request "has been substantially complied with by the petitioning person."[10]

Importantly, if the Commission wants to block a proposed transaction that it believes may violate the antitrust laws, it must seek an injunction in federal district court. The Commission is otherwise powerless to enjoin a merger only on its say-so.

Most often, however, the parties seek to avoid a protracted closing delay. Therefore, companies often have a strong incentive to cooperate with the Commission during its investigation to expedite the process and to reduce burden and legal expenses. After all, complying with a comprehensive investigation followed by litigation is a significant expense that few companies can sustain, and each day of delay threatens to decrease the target company's assets and the ability or willingness of the merging parties to close the subject transaction.

Indeed, in typical transactions a mutual trust and willingness of the merging parties to cooperate with the Commission largely prevails, with parties generally viewing antitrust regulation as part and parcel of the deal-closing process. The more readily a party cooperates with an investigation, the quicker it is able to close the deal—whether that manifests through the Commission staff allowing the waiting period to expire or closing its investigation, or with mutually agreed upon conditions attached to a consent order. Thus, for transactions that are susceptible to remedies, it is commonplace for parties to enter a consent order purely for economic reasons notwithstanding their belief that the Commission's theories or allegations that the transaction *may* substantially lessen competition lack merit.

The Prior Approval Process. The Policy's broad and severe impact will likely erode the willingness of merging parties to cooperate with the Commission or enter consent orders (which would expedite the conclusion of the Commission's review). A consent order with a prior approval provision would add material uncertainty to a transaction and can be expected to act as a poison pill to otherwise meritorious transactions by depriving future deals of the protections and assurances provided under the HSR Act and the Commission's own rules, and slamming shut the door on legal challenges to this process. Contrary to the HSR process, the prior approval process sets few demands on the Commission, and instead requires only that parties seeking prior approval "fully describe the terms of the transaction" and "set forth why the transaction . . . merits Commission approval."[11] Applications are placed on the pubic record for 30 days, but the Commission, in its own discretion, can "shorten, eliminate, extend, or reopen a comment period."[12] There is no prescribed period during which the Commission must conduct its investigation or issue its decision, nor statutory guidance on how the Commission must weigh the strength of the parties' applications.

The Policy thus exploits the parties' eagerness to resolve the Commission's concerns so that they may end the cost and burden of a lengthy investigation and proceed to closing—even if they strongly disagree with

[5] 16 C.F.R. § 803.1, *et seq*.

[6] 16 C.F.R. § 803.10. The parties may, at their option, "pull and refile" at the end of the initial waiting period and thereby extend the initial waiting period by an additional 30-days. § 803.12.

[7] 16 C.F.R. § 803.11.

[8] 16 C.F.R. § 803.20(c).

[9] *See* FTC's Model Request for Additional Information and Documentary Material (Revised Apr. 2019).

[10] *See* Clayton Act Section 7A(e)(1)(B); *see also* FTC's Model Request for Additional Information and Documentary Material (Revised Apr. 2019).

[11] The entire prior approval process is set forth in 16 C.F.R. § 2.41(f).

[12] 16 C.F.R. § 2.41(f)(2).

© 2022 Washington Legal Foundation

the Commission's position and believe it lacks merit. Other than the few parties with the considerable resources to challenge the Commission, this policy will effectively coerce parties to accept the onerous terms and costs of prior approval to get their deal done. As such, the reality is that—based only on the FTC's unproven *theories or allegations* that the *first* transaction could be illegal—parties must now routinely agree that the Commission may block *future* transactions. Though the Commission frames the Policy as a return to prior practice pre-1995, the usage of prior approval even then involved only a "minute universe of cases."[13] But the current Policy likely expands this universe into something far, far larger today.

Additionally, though the Commission purports to argue the Policy is crafted with the intent to consolidate and preserve resources,[14] the Policy instead opens the door to the possibility that the Commission will expend rather than conserve more resources because transacting parties with resources will likely opt to litigate rather than enter a consent order. Accordingly, those parties may now recognize the adversarial posture of Commission investigation given the higher price exacted through consent orders and act accordingly. Absent incentive to cooperate, parties may be loath to take a proactive, expeditious and informative approach to dealing with Commission requests, and instead take an adversarial approach to the entire process. In effect, the Commission may face lengthier and more adversarial investigations, leaving them with fewer resources to dedicate elsewhere as intended.

Since its October 25 announcement, the Commission already has made good on its promise to impose prior approval terms in consent orders. First, *In the Matter of DaVita Inc.*, a transaction involving outpatient dialysis services, the Commission required the parties to divest certain assets, agree to certain prohibitions, and obtain prior approval for certain future acquisitions within the State of Utah for a period of ten years.[15] Second, *In the Matter of Golub Corporation*, a supermarket transaction allegedly having anticompetitive effects in 11 markets in New York and Vermont, the consent order requires the divestiture of certain stores, and prior approval before acquiring supermarket assets in certain markets in New York and Vermont for a period of ten years.[16] Third, and most recently, *In the Matter of ANI/Novitium*, involving generic drug marketers, the Commission required the divestiture of development rights and assets of certain generic drugs as well as Commission approval prior to the acquisition of three generic drug products or their "Therapeutic Equivalent or Biosimilar" for ten years.[17]

Courts Defer to Prior Approval Clauses. While courts may set aside Commission rulings on the basis they are arbitrary or capricious under the Administrative Procedure Act (the "APA"),[18] parties seeking to invalidate prior approval clauses in consent orders will have a very difficult time doing so through litigation. The most recent challenge came in *Dr. Pepper/Seven-Up Companies, Inc. v. F.T.C.*,[19] which illustrates the great deference given to the Commission by the judiciary in this regard. After enduring a 14-month litigation against the Commission, Harold Honickman, an entrepreneur and owner of various bottling companies, entered into a consent order (the "Consent Order") that required him to obtain prior approval before acquiring any bottling operation in the

---

[13] Dissenting Statement of Commissioner Mary L. Azcuenaga on Decision to Abandon Prior Approval Requirements in Merger Orders, 60 Fed. Reg. 39746, 39747 (Aug. 3, 1995). In her statement, Commissioner Azcuenaga claimed that in the five years prior, the Commission issued only 58 orders with prior approval provisions, amounting to fewer than 12 per year. Based on figures in Commission annual reports, this suggests a prior approval usage rate of 51% or less in the years leading up to 1995, when the Commission ceased its practice of requiring prior approval requirement in consent orders.

[14] *See* Statement of the Commission on Use of Prior Approval Provisions in Merger Orders (Oct. 25, 2021), https://www.ftc.gov/system/files/documents/public_statements/1597894/p859900priorapprovalstatement.pdf ("Conducting merger review after a petition for prior approval would allow the Commission to husband its scarce resources without the brinksmanship we encounter during HSR reviews.").

[15] Decision and Order, Da Vita Inc. and Total Renal Care, Inc., FTC Matter 2110013 (Oct. 25, 2021) (consent order), https://www.ftc.gov/system/files/documents/cases/davita_order_9_24_final.pdf. Notably, the prior approval provision applies to transactions in the entire State despite the Commission's designating only the area encompassing the City of Provo as the relevant market in its enforcement action.

[16] Decision and Order, The Golub Corporation, Top Markets Corporation, and Project P New Holdings, Inc., FTC Docket No. C-4753 (Nov. 9, 2021) (consent order), https://www.ftc.gov/system/files/documents/cases/2110002pricechoppertopsorder.pdf.

[17] Decision and Order, Ani Pharmaceuticals Inc., Novitium Pharma LLC, and Esjay, Inc., FTC Docket No. C-4754 (Nov. 10, 2021) (consent order), https://www.ftc.gov/system/files/documents/cases/2110101c4754aninovitiumdecisionandorder.pdf.

[18] *See* 5 U.S.C. § 706.

[19] 991 F.2d 859 (D.C. Cir. 1993).

New York Metropolitan area.[20] Honickman subsequently sought consent for an acquisition that he argued would enable economies of scale and lower prices.[21] But after eight months, the Commission summarily rejected his application.[22]

In its decision, the Commission noted that an acquisition resulting in lower costs is not "necessarily procompetitive or lawful if it results in an increased likelihood of higher prices."[23] Though the Consent Order contained no guidelines or requirements regarding Honickman's evidentiary burden, the Commission claimed that he failed to prove that "the proposed acquisition is not likely to lessen competition substantially or tend to create a monopoly," nor that the acquisition would "not otherwise conflict with the remedial purposes of the [Consent Order.]"[24] The Commission concluded that even if it "were to assume that the transaction would have the procompetitive benefits that the Application claims . . . the Application does not demonstrate that those purported benefits outweigh the anticompetitive effects alleged in the complaint[.]"[25]

Honickman appealed the Commission's denial to the U.S. District Court for the District of Columbia, arguing, *inter alia*, that the Commission improperly flipped the burden of demonstrating a violation of Section 7 of the Clayton Act and that he was entitled to a formal on-the-record hearing for his application.[26]

The court disagreed, holding that the application did not constitute a formal administrative proceeding.[27] As such, when reviewing petitions for prior approval, the Commission did not bear the burden of proof in establishing a violation of law as it would in a formal administrative litigation.[28] For similar reasons, the court also held that Honickman was not entitled to an on-the-record hearing, given that Commission Rule 2.41(f), which governs prior approval proceedings, only entitled Honickman to a thirty-day public notice-and-comment period.[29] Further, Honickman was properly given opportunity to appear in person to the Commission and receive notice of the denial under 5 U.S.C. § 555(b) and (e).[30]

On appeal, the D.C. Circuit affirmed, holding that a prior approval proceeding was not a formal adjudicative procedure, and that the Commission's procedures were not infirm.[31] While the burden of proof that Honickman had to meet may not have been prohibitively high,[32] Circuit Judge Edward concluded that Honickman was simply entitled to what he had bargained for, writing:

> [P]rior approval proceedings are used by the Commission to determine whether and how to exercise regulatory discretion that has been created pursuant to a consent agreement. In such circumstances, the burden of proof is on the party seeking 'prior approval.' *Any party desiring to avoid this burden may simply decline to execute a consent agreement with the Commission (or seek to execute an agreement with more favorable terms).*[33]

Though Honickman was eventually permitted to make acquisitions in the New York area after further

---

[20] *Harold Honickman, et al.*, 114 F.T.C. 427, 431 (1991).
[21] *Id* at 435.
[22] *Dr. Pepper/Seven-Up Companies, Inc. v. F.T.C.*, 798 F. Supp. 762, 764 (D.D.C. 1992), aff'd in part, rev'd in part and remanded, 991 F.2d 859 (D.C. Cir. 1993).
[23] Letter from Secretary Donald S. Clark to Peter E. Greene, Esq. (Aug. 7, 1992).
[24] *Id*.
[25] *Id*.
[26] *Dr. Pepper/Seven-Up Companies*, 798 F. Supp. at 768-69.
[27] *Id* at 771.
[28] *Id* at 771-72.
[29] *Id* at 772.
[30] *Id* at 773-74.
[31] *Dr. Pepper/Seven-Up Companies, Inc. v. F.T.C.*, 991 F.2d 859, 863 (D.C. Cir. 1993).
[32] For further discussion on the requisite burden of proof applicants must meet, *see* Philip D. Bartz, *Through the Looking Glass: Prior Approval Clauses In FTC Antitrust Consent Orders*, 8 ANTITRUST 36, 37-38 (1994) (suggesting that "the burden is not unduly heavy," and that the Commission likely cannot dismiss evidence simply by asserting that it does not meet the burden of proof, as in civil trials, but rather must conform their decisions to existing administrative law, absent rational explanation to rebut the evidence.).
[33] *Dr. Pepper/Seven-Up Companies*, 991 F.2d at 863 (emphasis added).

litigation in 1993,[34] he would remain subject to the Consent Order until the Commission reversed its policy regarding the use of prior approval conditions in 1995.[35] On March 31, 1998—nearly ten years after the original Commission complaint—the Commission granted Honickman his request to put aside the Consent Order, on the basis that the deletion of the prior approval condition would eliminate Honickman's obligations.[36]

Practical Effects: Inside the Boardroom. Fear of being on the receiving end of a deleterious consent order with prior approval provisions will have a powerful chilling effect in the boardroom. Consider, for example, that a typical merger or acquisition comes with a laundry list of concerns and expenditures. Sellers, in particular, face myriad uncertainties and sources of pre-closing losses in a transaction that are exacerbated when closings are materially delayed. News of a deal may trigger unfavorable reactions—particularly for publicly-traded companies—stemming from competitors and shareholders alike. Sellers must also contend with the onset of employee retention issues. Key employees, fearful of redundancy and low perceived value to the buying party, may feel compelled to seek new opportunities, which may in turn trigger further departures across the firm. Customers uncertain of a seller's ability to deliver future goods and services may seek out other firms with which to do business. Certainty of closure is a significant consideration for sellers and can be a significant competitive factor for a potential buyer. One of the Policy's effects will likely be that acquisitive buyers subject to a consent decree will be at a competitive disadvantage.

Mindful of this, sellers in a transaction at risk of antitrust investigation often negotiate risk-shifting provisions into the Purchase Sale Agreement to transfer some of the burden to the buyer, usually in the form of an "efforts" clause (*e.g.*, a hell or high water or reasonable best efforts), a reverse break-up fee (where the buyer would pay the seller if the deal terminates for lack of antitrust approval), or a remedies clause where the purchaser agrees to certain divestitures to secure antitrust approval. Risk-shifting mechanisms provide some level of confidence and commitment to closing the deal and are entered into with the expectation that the transaction will be subject to a recognized regulatory process and timeline.

In today's post-Policy world, the flexibility of a buyer to accept a consent order evaporates with the certainty of being subjugated to prior approval. A company that has made the requisite divestitures to close a deal now faces the prospect of the Commission blocking future acquisitions, hanging over them for years like a business-ending sword of Damocles. This is especially true for acquisitive companies who will be far less eager to enter into a consent order knowing that it likely will affect future deal flow. It will also affect whether a prospective seller will enter into a deal that is subject to prior approval and if so it likely will seek an increased purchase price, demand increased reverse break-up fees, and/or demand more stringent efforts clauses. While shifting policies are part and parcel of changes in administration, they need not come with the heavy cost of throwing business planning into chaos and a loss of accountability.

Regrettably, the Policy creates conditions for a possible lose-lose scenario—perhaps an intended consequence of the Commission's animosity toward all mergers. Prior consent orders that excessively punish parties for willfully submitting to a consent order diminishes incentive to cooperate and expedite review. Absent this, Commission investigations will take longer and further tie up precious resources on all sides. In lieu of trust and cooperation, the Commission has opted instead to foster an adversarial climate between businesses and antitrust regulators, and in the process created yet another impediment to good government regulation.

[34] *Dr. Pepper/Seven-Up Companies, Inc. v. F.T.C.*, 151 F.R.D. 483, 490 (D.D.C. 1993) (holding that Honickman could acquire a soft drink license from the New York Bottling Company because it was not subject to the Consent Order as a defunct, non-bottling operation).

[35] Notice and Request for Comment Regarding Statement of Policy Concerning Prior Approval and Prior Notice Provisions in Merger Cases, 60 Fed. Reg. 39745 (Aug. 3, 1995).

[36] Order Setting Aside Order, Harold Honickman, et al., FTC Docket No. 9233 (Mar. 31, 1998), https://www.ftc.gov/sites/default/files/documents/cases/1998/04/honicmod.ord_.htm.

© 2022 Washington Legal Foundation