How litigation may affect the mergers and acquisitions clearance process: US and EU compared

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Prudent business executives, M&A lawyers and competition law specialists should understand how antitrust-based litigation may affect the timing for clearing transactions and the finality of closed deals. When a merger or acquisition is reviewable in multiple and potentially unfamiliar jurisdictions, the parties should carefully consider at the outset the different ways litigation in the different jurisdictions might affect the timing, outcome and finality of the transaction. And they should seek to allocate risks accordingly. In this paper, we describe the pertinent highlights of the US and EU regimes relating to litigation, focusing on procedure and not on substantive competition law and economics.

United States

Standard clearance process – minimal risk of litigation

For three decades, the Hart-Scott-Rodino (HSR) amendments[1] have governed the initial aspects of US M&A antitrust review under section 7 of the Clayton Act.[2] If a transaction satisfies HSR thresholds and is not exempt (eg, for insufficient US nexus), the parties must notify the two federal antitrust authorities, the US Department of Justice Antitrust Division (DoJ) and the Federal Trade Commission (FTC), and may not consummate their transaction before completing the requisite HSR process. Consequently, when a reviewable deal is publicly announced, there is no need for the DoJ, FTC or opposing third parties to rush to court to prevent consummation.

A non-HSR-reportable transaction that nonetheless affects US commerce, however, is not immune from antitrust investigation and litigation. The Clayton, Sherman, and Federal Trade Commission Acts reach M&A transactions involving undue concentration in very small relevant markets, minor investments in a competitor, supplier or customer, or partnership and other arrangements not caught by the HSR law. The FTC or DoJ may investigate such a non-HSR transaction, discourage parties from closing before the investigation is complete and sue in federal district court to enjoin or rescind the transaction or to impose divestiture or other relief.

Indeed, transactions consummated pre-HSR law and those consummated after full compliance with then-applicable HSR notification and waiting period requirements can nonetheless be subject to a DoJ or FTC court suit at some time in the future.[3] But the agencies rarely bring such a challenge and would only do so if there had been a radical adverse change in competitive circumstances and the public need for a remedy outweighed the normal interest against disturbing lawfully accomplished transactions. On the other hand, the FTC or the DoJ will invoke the judiciary to rescind consummated transactions where the parties did not comply with applicable HSR requirements, such as failing to produce a required document that might have affected the outcome of the initial HSR review.[4]

For the vast majority of HSR-notified deals, typically neither federal agency identifies antitrust issues worth studying, or one agency investigates and quickly concludes there are no problems, and then the parties receive early termination or timely expiration of the 30-day[5] waiting period. In a small fraction of cases, the investigating agency sends the parties a 'second request' for additional information, thereby extending the waiting period until either 30 days[6] after 'substantial compliance' or an earlier agency decision to drop or settle the investigation.[7, 8]

Litigation to settle government antitrust investigations

If the investigating agency decides the deal is anti-competitive, the next step could involve litigation. The parties, of course, may drop their deal. They may not, however, initiate litigation at that point (or earlier) to have a federal district court declare their transaction legal, limit the agency's substantive analysis or determine that the agency lacks jurisdiction.

Alternatively, the parties may propose to fix a substantive antitrust problem in advance of closing, eg, by selling off certain assets or agreeing to license technology to third parties, thereby removing the agency's objections. Historically, the DoJ has been more willing than the FTC to rely upon a 'fix-it-first' solution that avoids the formality of a complaint, settlement stipulation and remedial order.

If the investigating agency has serious competitive concerns and a fix-it-first solution is not acceptable, some form of litigation will be initiated. When a negotiated resolution can be agreed with the FTC, that agency will issue an administrative complaint, agree with the parties on a consent agreement and proposed order, and publish the order and an accompanying analysis for 30 days' public comment. The DoJ has no comparable quasi-judicial intra-agency procedure for settlements, so it will file a complaint in federal district court along with (i) the parties' stipulation agreeing to comply with a proposed consent decree, (ii) the decree itself and (iii) DoJ's competitive impact analysis. Under the Tunney Act, the public has 60 days to submit comments to the DoJ. Thereafter the DoJ will file the comments and its formal response, after which the judge normally holds a brief hearing and signs the order.

Typically, the DoJ and FTC allow parties to consummate their transaction while the consent decree or order is subject to public comment and further review. Parties, however, must abide by the DoJ's provisional decree (and any associated agreement to hold assets separate for divestment) until the court formally approves it as a binding final judgment or the time for all appeals of the decision declining to approve the order expires. Similarly, parties must abide by an agreed FTC order (and associated hold separate and maintenance orders) as if finally entered, until the FTC either issues a final decision adopting the order or terminates the proceeding.

Parties may not consent to an order and then promptly turn around and challenge aspects of that order in court. In case of unanticipated changed circumstances, however, there is some precedent for a defendant years later to ask the DoJ and the court, or for a respondent to ask the FTC, to modify the agreed requirements.

New questions regarding litigation process under the amended Tunney Act

Since the passage of the Tunney Act in 1974,[9] judges have rarely questioned the adequacy of the DoJ's proposed settlements and even more rarely required the parties and the DoJ to negotiate additional or broader relief and then return to court with a revised consent decree. In 2004, the Tunney Act was amended to make clearer that

judges are not to simply 'rubber stamp' proposed consent decrees. Even with the amendments, the DoJ maintains that it has full discretion to identify in its complaint the relevant market or markets adversely affected by the subject transaction and that the court may not second guess the market definitions or require the DoJ to allege additional markets and other violations. The DoJ also contends the court may not disapprove the negotiated remedy unless there is evidence of corruption or the agreed remedies are clearly inadequate to remedy the alleged violations and outside the broad public interest reaches of reasonable alternatives.

In mid-2006, however, a court considering proposed decrees in the *SBC/AT&T* and *Verizon/MCI* mergers (which had closed months earlier) required the DoJ to submit for comment by friends of the court opposed to the decrees substantial underlying investigative evidence produced by the parties and third-party customers and competitors.[10] The court even indicated it may conduct an evidentiary hearing or invite expert testimony. Whether this development is an aberration or sets a precedent remains to be seen.

In the event a court does disapprove a consent decree (and is affirmed on appeal), the DoJ then faces the difficult question whether to litigate its complaint or seek to dismiss. In the interim, the parties may or may not have completed any required divestments. In theory, even if these were already consummated, the DoJ could still litigate on the merits and, if successful, seek additional divestments and other remedies.

Government-initiated litigation to enjoin transactions

Where the investigating agency has continuing competition concerns and a settlement is not possible, the agency will file suit in federal district court seeking a temporary restraining order and preliminary injunction to block the transaction. In court, the government has the burden of proof, and defendants have the right to discover evidence from the government and third parties. The DoJ and FTC injunction suits typically consume three months or more, and at least as many additional months on appeal (with a stay of the transaction likely until the appellate court rules). Although the standards for preliminary relief are skewed in the government's favour (in contrast to when a private party seeks preliminary relief against a merger), the government does sometimes lose at the district court level and stop there,[11] or seek relief in the appellate court and fail there as well.[12]

In a DoJ suit, the preliminary injunction matter and the trial on the merits of the complaint are often combined into one proceeding. An FTC district court injunction proceeding, however, is distinct from a trial on the merits – which would occur later (if needed) before an agency administrative law judge subject to appeal to the commissioners en banc.[13] If the FTC does not go to court in the first instance to stop the merger, it may opt to litigate its complaint administratively even though the deal has been consummated.[14] In that event, if a violation is later found, the FTC may order divestiture – or conceivably rescission, if the seller is a named respondent in the complaint – and other relief, subject to appeal (but not a de novo trial) in a federal appeals court.

Third-party litigation for injunctions, divestitures and damages

State attorneys general, and rival bidders, customers, suppliers and even competitors who satisfy antitrust standing requirements, may bring their own federal court (or conceivably even state court) litigation to challenge M&A transactions and may obtain divestments and other structural and behavioural relief. State attorneys general usually coordinate with the DoJ or FTC on litigation and consent decree strategy, but they may go their separate way, ie, filing suit even though the federal authorities do not, or insisting on broader relief than the DoJ or FTC require.

Non-governmental parties with standing may litigate and even obtain divestitures or injunctions against mergers that government enforcers decline to prevent.[15] Treble damages are also a possibility. However, given litigation's expense and the high hurdles for obtaining equitable or monetary relief when government enforcers have permitted transactions to go forward despite objections, private suits are rare and usually limited to the deep-pocket rival bidder seeking tactical advantages before a target's shareholders have voted upon a transaction.

Third parties' best option remains that of influencing the government enforcer's prosecutorial and remedial decisions. Although private parties are rarely allowed to intervene as parties (with discovery and appeal rights) in DoJ/FTC suits and Tunney Act proceedings, their participation as commenters and friends of the court in DoJ Tunney Act or FTC proceedings can sometimes make a difference. If the 2004 Tunney Act amendments (as discussed above) ultimately lead to evidentiary hearings and expert testimony, third parties will have increased opportunity to influence the outcome of DoJ litigation and settlements.

European Union

Under the European Union's Council Regulation (EEC) 139/2004 (ECMR), mergers and acquisitions having 'a Community dimension' must be notified to and approved by the European Commission. This concept of Community dimension applies to large transactions that affect trade between EU member states and are between parties exceeding a series of revenue thresholds. Under the ECMR's 'one-stop shop' principle, the Commission has exclusive power to decide on mergers that have the requisite Community dimension. Individual member states may not exercise jurisdiction. The Commission, however, may refer a case to competition authorities in one or more member states, if these are better placed to examine the issues.

Once a transaction is notified, the Commission has 25 working days (plus 10 more, if the parties submit commitments) to either (i) decide the transaction falls outside the ECMR, (ii) approve the transaction with or without conditions or (iii) open a second phase investigation.[16]

The second phase extends the waiting period 90 working days, subject to limited further extension.[17] A second phase investigation concludes with a Commission decision either (i) prohibiting the transaction, (ii) clearing it unconditionally, or (iii) clearing it subject to conditions and the parties' commitments to the Commission. In contrast to the US system of court injunctions and decrees (and leaving aside FTC administratively developed consents and orders), a Commission decision prohibiting the transaction or making it subject to conditions requires no court involvement for it to take effect.

Commission rulings subject to judicial review

Commission acts that are intended to have legal force and are taken during a merger investigation are reviewable by the Community courts, namely the European Court of First Instance (CFI) and, above it, the European Court of Justice (ECJ). Reviewable Commission acts include decisions approving, making conditional, or rejecting a transaction, referring cases to member state competition authorities, and requesting information from the parties or ordering an inspection at a company's premises. Even Commission acts that were not formal decisions but nonetheless were intended to have legal force may be reviewed by the Community courts.[18]

Legal standing to challenge rulings

Generally, parties to a transaction prohibited or cleared subject to conditions by the Commission may institute a court challenge. Parties to a merger approved by the Commission without conditions have, however, been denied standing to question a non-'operative'

part of the Commission's decision.[19]

Third parties also have standing to challenge a Commission decision if they are "directly and individually concerned" by it. In the past, the CFI has granted standing to competitors and customers of the merged entities and to bodies representing the merging parties' employees, while minority shareholders of the merging companies have been denied this right.

The courts' powers of review

Actions challenging Commission decisions in merger cases must be brought in the first instance to the CFI within two months from the time the decision was notified to the parties (or was published, in the case of third-party challengers).

The CFI has jurisdiction to provide a definitive interpretation of the ECMR and any other applicable EU legislation. It can therefore decide whether the Commission correctly applied the Community dimension jurisdictional thresholds as well as the substantive test for infringement. Additionally, the CFI may rule on procedural points, such as the Commission's failure to grant parties access to the file or sufficient time and information to provide their views on a statement of objections preceding a formal decision.

In theory, the CFI is not supposed to rehear the merits de novo or substitute its findings for those of the Commission. Nonetheless, on occasion, the CFI has conducted its own in-depth economic analysis and factual interpretation in considering Commission rulings disallowing transactions[20] and recently used its own economic analysis to overturn the Commission decision clearing the Sony/BMG joint venture.[21]

CFI judgments can be appealed to the ECJ on points of law only, within two months of the notification of judgment. To date, only three judgments of the CFI in merger control cases have been appealed to the ECJ.

Expedited procedure possibility

The average time for a court challenge before the CFI gives its judgment is about 20 months – too long in most merger cases to be of any practical benefit to a party whose transaction was blocked by the Commission. In 2001 a special procedure was created whereby a challenger may apply for priority review, based on the particular urgency and circumstances of the case. Under this expedited procedure, the CFI is able to reach judgment in less than a year.

Interim relief very rare

Applicants challenging a Commission decision may file an action for interim relief with the CFI. Actions for interim measures may only be requested after or at the same time as the main action is brought before the court. Applications for interim measures are dependent on the viability of the main action. An applicant for interim measures needs to (i) establish the existence of a prima facie case for infringement; (ii) substantiate the risk of serious and irreparable harm to individuals or to the public which implies the urgent need for interim measures; and (iii) show that the granting of the interim measures will not prejudice the final decision in the main action.

Although somewhat similar to the criteria that the DoJ and FTC must satisfy in a US court to temporarily enjoin a merger, this EU test has proven extremely hard to meet in merger cases. To date, applications to suspend a Commission decision approving a merger (thereby stopping the parties from executing their transaction) have never succeeded. The economic harm to the parties in delaying their transaction has proven too significant to warrant granting interim relief on the balance of convenience. There is precedent, however, for the court suspending in the interim a condition the Commission imposed in clearing a transaction.[22]

Referral back to the commission

Under article 10(5) of the ECMR, if the CFI annuls a Commission decision in whole or in part, the merger must be reexamined by the Commission in the light of current conditions. The parties would need to submit promptly a new or supplemental notification to address changes in market conditions and critical issues identified in the court's ruling.

In today's business world, where markets are in constant change and time is of the essence, the commercial rationale for a transaction (or for opposition to a transaction) may have changed during the pendency of a lengthy appeal and article 10(5) remand proceeding. Deals that the Commission has prohibited might no longer make business sense. And, the passage of time may make a complete review of already consummated transactions and possible new conditions unsatisfactory even to the challenger.

Conclusions

The EU's slow-paced court review and remand procedure is less than satisfactory and seems ripe for reform. It contrasts unfavourably with aspects of the generally faster-moving US preliminary injunction and Tunney Act consent decree review processes. Both EU and US systems have the potential for the unnerving possibility of consummated transactions being reversed through subsequent government decisions, although examples are quite rare.

Neither system offers particularly attractive litigation opportunities for third parties if the enforcement authorities have approved the transaction. In the US, full-blown private suits to enjoin government-cleared transactions are theoretically available but exceedingly rare. And it remains to be seen whether third party challenges to DoJ consent decrees will have real substantive impact under the 2004 Tunney Act amendments. In Europe, third-party challengers recently did manage to convince the CFI to overturn one EC clearance, but the ultimate outcome in that lone example remains uncertain.

Notes

1 15 USC §18A.

2 15 USC §18 (prohibiting acquisitions whose "effect ... may be substantially to lessen competition, or tend to create a monopoly").

3 See, eg, *US v EI du Pont deNemours & Co*, 353 US 586 (1957) (DoJ may challenge, under §7 of the Clayton Act, a 27 per sent stock ownership acquired 30 years earlier), 366 US 316 (1961) (complete divestiture ordered); *Chicago Bridge & Iron Co*, Dkt No. 9300 (FTC, 6 January 2005), appeal docketed, *Chicago Bridge Co v FTC*, No. 05-60192 (5th Cir) (FTC issued administrative complaint eight months after merger closed and over 4 years later ordered divestitures); *Evanston Northwestern Healthcare Corp*, Dkt No. 9315 (FTC complaint filed February 2004, four years after merger closed; ALJ's initial decision ordered divestiture, see: http://www.ftc.gov/opa/2005/10/evanston.htm).

4 Eg, *US v The Hearst Trust*, 2001–2 Trade Cas. (CCH) ¶73,451 (DDC 2001); *FTC v The Hearst Trust*, Case No. 1:01CV00734 (DDC, settlement order filed 14 December 2001).

5 15 days for all-cash tender offers and sales by a bankruptcy trustee.

6 10 days for all-cash tender offers and sales by a bankruptcy trustee.

7 Very rarely, the parties or the agency may go to federal district court for a decision as to whether or when substantial compliance occurred. Eg, *FTC v McCormick & Co*, 1988–1 Trade Cas (CCH) ¶ 67,976, at p57,985 (DDC 1988).

8 The investigating agency may also issue civil investigative demands (CIDs) requesting documents and testimony from third parties or even the deal parties. CID recipients may (but very rarely) file suit in federal district court to modify or set aside such CIDs, potentially delaying the agency's substantive clearance review – although the HSR's waiting period is not formally extended thereby. Antitrust Civil Process Act, 15 USC §§1311–1314.

9 Antitrust Procedures & Penalties Act of 1974, 15 USC §16(b)-(h).
10 See *US v SBC Communications Inc et al*, No. 1:05CV02102 (EGS), and *US v Verizon Communications Inc et al*, No. 1:05CV02103 (EGS) (DDC), United States' Submission in Response to the Court's Minute Order of 25 July 2006 (filed 9 August 2006).
11 Eg, *US v Oracle Corp*, 331 F Supp 2d 1098 (ND Cal 2004).
12 Eg, *US v Baker Hughes Inc*, 908 F 2d 981 (DC Cir 1990) (affirming denial of preliminary injunction); *FTC v Arch Coal Inc*, 329 F Supp 2d 109 (DDC 2004) (preliminary injunction denied), stay pending appeal denied, No. 04-5291 (DC Cir, 20 August 2004).
13 If the FTC wins a preliminary injunction that is sustained on appeal, the parties generally abandon their transaction knowing that the alternative – a full-blown FTC administrative litigation and appeal – would likely consume several years. Conversely, if the FTC tries but fails to win an injunction from the courts, the agency has the authority to ask its Bureau of Competition staff to litigate the complaint (including remedies) before an administrative law judge, subject to appeal to the commissioners en banc, and a further appeal to the court of appeals by the merger parties if they lose at the agency. In practice, current FTC policy tends to disfavour taking a 'second bite' after a loss in court. See Commission Statement justifying dismissal of administrative litigation, *In the Matter of Arch Coal et al*, Docket No. 9316, File No. 031-0191 (13 June 2005).
14 Eg, *Chicago Bridge & Iron Co*, supra footnote 3.
15 *California v American Stores Co*, 495 US 271, 281 (1990).
16 A transaction is not compatible with the common market if it significantly impedes effective competition in the common market, or a substantial part of it, in particular as a result of the creation or strengthening of a dominant position.
17 The 90 days can be further extended by up to 35 working days if the parties or the Commission so request and the parties submit remedies. The submission of commitments by the parties after the 55th day of a second phase investigation extends the deadline by 15 working days. If the parties and the Commission agree, the 90 working days waiting period can be extended by an additional 20 working days if a request is made by the parties or the Commission within 15 working days of the initiation of a second phase investigation.
18 In *Dan Air* (Case T-3/93), the CFI held that a statement made by a spokesman for the EC's director general for competition that a proposed merger between Air France and Dan Air lacked a Community dimension and fell outside the Commission's exclusive jurisdiction was an act with legal force subject to the court's review.
19 In *Coca-Cola v Commission* (Case T-125/97 and T-127/97), the CFI denied Coca-Cola standing to challenge a statement in the *Coca-Cola/ Amalgamated Beverages* decision that Coca-Cola held a dominant position in the UK market for cola-flavoured carbonated soft drinks.
20 See, eg, *Airtours plc v Commission* (Case T-310/01), *Schneider Electric SA v Commission* (Case T-77/02) and *Tetra Laval BV v Commission* (Cases T-5/02 and T-80/02).
21 *Impala v Commission* (Case T-464/04).
22 *Société Commerciale des Potasses et de l'Azote and Entreprise Minière et Chimique v Commission* (Case T-88/94 R) (the CFI suspended a condition that would have caused irreparable private harm whereas delaying the condition would have caused little adverse public harm).

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