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Good News/Bad News: New Premerger Reporting Rules Streamline Form, but Create New Obligations, Particularly for Private Equity Funds and Hedge Funds

New rules issued by the Federal Trade Commission on July 7, 2011 will streamline some information required for the Hart-Scott-Rodino Act ("HSR Act") Notification and Report Form (the "Form"), but also will impose several new, potentially burdensome requirements on filing parties. Notably, the rules will now require acquiring persons to include information regarding "associates" that operate in the same industry code as the target company. This new requirement will have the most significant impact on private equity funds, hedge funds and master limited partnerships. In addition, the range of documents analyzing the transaction that must be included with the Form has been expanded. The new rules and a new Form will become effective in early August 2011, 30 days following publication in the Federal Register.

The most important changes include:

- **Documents now reach far beyond "4(c)" documents:** All parties must now provide new categories of documents with their HSR filings. These include unsolicited "pitch books" from bankers, documents created for earlier attempts to sell the target or assets, documents related to synergies and efficiencies, and ordinary business documents that served the purpose of a Confidential Information Memorandum.
- **Related "associate" entity information:** Buyers must now include information on holdings by "associates." This requirement will most directly affect private equity funds, hedge funds, master limited partnerships and other investment groups. In the past, information was typically only required for the particular fund making the acquisition. Now, investment groups must look to holdings—including minority holdings—by entities under common management.
- **Detail on manufactured products:** Revenue for products manufactured outside the United States must now be broken down by the more burdensome ten-digit manufactured product NAICS codes, rather than supplied in a more general distribution code.
- **Some good news:** The HSR Form has been modestly streamlined and certain requirements have been eliminated, such as the requirement for "base year" revenues and listing certain subsidiaries.

Detail on these and other changes follows.



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The Bad News

The rules have significantly expanded certain requirements of the Form. These changes fall into four primary categories:

- First, the scope of business documents that must be submitted with the parties' filings has been expanded beyond "4(c)" documents¹ to include several new categories of documents, such as:

- **Confidential Information Memoranda or similar documents:** Confidential Information Memoranda prepared within the year before filing regarding the sale of the target—even if prepared in contemplation of a different transaction. If no Confidential Information Memorandum was prepared for the transaction, then any documents given to the buyer that specifically served the purpose of a Confidential Information Memorandum must be provided, such as a pre-existing company presentation.
- **Documents from third-party advisors:** Documents prepared within the year before filing by third-party advisors (such as bankers and consultants) that contain competition-related content specifically relating to the sale of the entity or assets (even if prepared in contemplation of a different transaction) drafted during an engagement or for the purpose of seeking an engagement—for example, "pitch books," or "banker's books."
- **Documents regarding synergies or efficiencies:** Documents prepared by or for officers or directors (or individuals exercising similar functions) evaluating or analyzing synergies and/or efficiencies of the transaction. This new category of documents is essentially an extension of the 4(c) subject matter to include synergies and efficiencies.

- Second, the new rules introduce the concept of "associates" and require certain information related to associates. As discussed below, the term "associate" under the new rules is broad and includes entities under common investment or operational management with the acquiring person that are not "controlled," as defined in the HSR rules², by the acquiring person. The change is intended to help the agencies identify competitive overlaps that would not have been apparent under the old rules (for example, where interests in competing businesses are held or acquired through different limited partnerships within the same fund family).

- An acquiring person must now (i) identify any associates that derive revenue in the same industry code as the target and (ii) identify any associates with minority holdings in the same industry code as the target.
- The definition of "associate" is broad and includes any entity that:
 - Has the right, directly or indirectly, to manage the operations or investment decisions of an acquiring entity (such entities are now referred to as "managing entities")—for example, the general partner or investment manager of a private equity fund.
 - Has its operations or investment decisions, directly or indirectly, managed by the acquiring person.
 - Directly or indirectly controls, is controlled by, or is under common control with a managing entity—for example, where an individual controls a general partner of a private equity fund by virtue of having a 50% or greater economic interest in the general partner.
 - Directly or indirectly manages, is managed by, or is under common operational or investment management with a managing entity—for example, prior or successor funds, including their portfolio companies.
- Third, parties must now provide revenues by industry code from products manufactured outside the United States.
- Finally, the new rules create an HSR filing obligation for *unincorporated* entities engaged in commerce that are controlled by a government or government agency. Currently, the rules cover only corporations engaged in commerce that are controlled by a government or government agency.

The Good News

The new rules have modestly decreased parties' burdens in several ways:

- Parties will no longer need to report revenues for a base year (currently 2002); now, filing persons need only provide revenues for the most recent fiscal year.
- The scope of information regarding entities within the person filing notification and its holdings has been reduced:
 - Only US entities and foreign entities with sales in the United States will need to be listed as entities within the person filing, and the information required for each entity is more limited.

¹ 4(c) documents are studies, surveys, analyses and reports prepared by or for any officer or director (or in the case of unincorporated entities, individuals exercising similar functions) for the purpose of evaluating the transaction with respect to market share, competition, markets, potential for sales, or product and geographic market expansion.

² A corporation is "controlled" for HSR purposes by any entity that holds 50% or more of its voting securities or that has the contractual right presently to appoint 50% or more of its board of directors. Unincorporated entities like partnerships and LLCs are controlled by any entity that has the right to 50% or more of the profits of the unincorporated entity or 50% or more of its assets upon dissolution.

Client **Alert**

Antitrust/Competition

- The requirement to list all shareholders holding 5 percent or greater of a class of shares of the person filing notification has been changed. While the type of entities covered has expanded to include non-corporate entities, the information required has been reduced.
- The requirement to list information regarding minority holdings of corporations has been expanded to include non-corporate entities, but limited to holdings in entities that derive revenues in industry codes that overlap those of the target.

The expanded documentary requirements will affect all filers going forward and will require companies to revise and refresh their normal practices for collecting 4(c) documents. Private equity funds, hedge funds and master limited partnerships are most likely to be affected by the new obligations regarding associate holdings, though larger investment fund groups may be accustomed to tracking similar information for use in filings with the European Commission and other jurisdictions that require information related to entities under common management. With approximately one month before the new rules become effective, companies currently contemplating HSR filings should consider whether their transactions will be governed by the new rules and prepare accordingly.

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