Expedited Antitrust Merger Clearances in Bankruptcy

April 2020

Bankruptcy can provide important advantages to companies considering M&A activity today. M&A purchases of bankrupt companies obviously often feature significantly depressed valuations and a small universe of potentially viable purchasers.

M&A activity that is part of the bankruptcy process will prioritize speed and efficiency, offering a number of potentially important benefits over the traditional merger process, including:

- expedited HSR timing and reduced burden for certain bankruptcies;
- an expedited merger review due to the exigencies of bankruptcy;
- failing firm, failing division and/or flailing firm defenses;
- expedited merger trials;
- a merger trial in bankruptcy court; and
- expedited merger clearances in multiple jurisdictions.

Expedited HSR Timing and Reduced Burden for Certain Bankruptcies

There are unique Hart-Scott-Rodino ("HSR")[1] considerations for reportable transactions involving bankruptcies under Section 363(b) of the Bankruptcy Code.[2] This is in contrast with Chapter 7, Chapter 11, and non-US bankruptcies, which are all treated normally under the HSR Act. In Section 363 bankruptcies, buyers are able to acquire assets free of any attached liens and most liabilities.

Parties to an acquisition under Section 363(b) enjoy expedited HSR timing. Rather than the typical 30-day HSR waiting period, acquisitions under Section 363(b) are subject to a 15-day HSR waiting period. Importantly, only the acquiring party bears the burden of responding to a Second Request, if the reviewing agency issues one. Furthermore, if the Department of Justice (DOJ) or Federal Trade Commission (FTC) issues a Second Request, the waiting period expires only 10 days after the acquiring party substantially complies with the Second Request, as compared to the usual 30 days. Any Second Request issued to the acquired person does not impact the waiting period timing.

The acquiring party and the trustee or DIP (on behalf of the acquired party) both submit HSR filings. Where there are multiple bidders, each bidder submits an HSR filing as a potential acquiring person and the trustee or DIP submits a separate filing for each potential acquiring person. The trustee or DIP is responsible for executing a Rule 803.5 affidavit and certification, stating a good faith intention to proceed with the sale upon approval from the bankruptcy court.

Expedited Merger Review Due to the Exigencies of Bankruptcy

Bankruptcy cases prioritize speed and efficiency in dispensing with a debtor's estate. Merger reviews involving companies in bankruptcy are thus usually much faster than merger reviews outside of bankruptcy. In 2019, significant merger investigations averaged nearly 10 months for the DOJ and more than 13 months for the FTC. Reviews involving companies in bankruptcy often take only a fraction of that time.

1 Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a(2020).

2 Section 363(b) of the Bankruptcy Code authorizes the bankruptcy trustee ("trustee") or debtor-in-possession ("DIP") to use, sell or lease bankruptcy estate property other than in the ordinary course of business after obtaining court approval. To obtain such approval, the trustee or DIP must first provide notice to stakeholders and an opportunity for a hearing.

In *SunGard/Comdisco* – one of the few litigated merger cases involving a target in bankruptcy – we were able to achieve an "accelerated review" of the proposed acquisition, taking only two months from the opening of the DOJ's investigation to filing the complaint in district court, as opposed to the typical five to six months. As discussed below, the DOJ's challenge based on its expedited review failed, and the parties were able to consummate the proposed transaction in time to prevent Comdisco from failing.

Failing Firm, Failing Division and/or Flailing Firm Defenses

Parties may be able to use the failing firm defense when a company is at risk of imminent failure and its assets would likely exit the market if the merger does not occur. This is in addition to all the other arguments the parties may raise in defense of their proposed transaction.

The rationale for the failing firm defense is that if the failing company would have otherwise exited the market, consumers are no worse off with the merger than they would have been if the reviewing agency had blocked the merger and the target failed on its own to survive. To support the defense, the agencies and many courts require that the parties demonstrate that the failing firm cannot (1) meet its financial obligations in the near future; (2) reorganize successfully in bankruptcy; and (3) find another buyer after good-faith efforts that would pose less anticompetitive risk. *See, e.g., DOJ & FTC, Horizontal Merger Guidelines § 11 (2010) ("Merger Guidelines").*

In evaluating the first element of this defense, courts usually consider the failing firm's finances at the time of the proposed acquisition, its cash flow over time, available working capital, and relationships with financial institutions.

Courts have not adopted a uniform standard regarding the inability to reorganize in bankruptcy. Some courts assess the possibility of reorganization collectively with the likelihood of business failure. Other courts require the parties show that the possibility of bankruptcy reorganization is dim or nonexistent. Declining revenue and increased capital expenditure leading to liquidation have been found to be sufficient to meet this standard, while declining assets with long-term contracts that could be carved off and sold in a bankruptcy proceeding have been found to be insufficient. Some courts even have questioned whether this element is necessary to establish the failing firm defense.

The third element, inability to find a better buyer, may be satisfied with a good-faith effort by the failing firm to obtain other offers that would pose less anticompetitive risk, which typically involves an organized effort to "shop" the business to multiple buyers. Here, it is typical to use an investment banker with industry experience, which can help defend against questions by the agencies about whether the search for buyers was extensive enough.

Merging parties may also be able to avail themselves of a failing division defense, which generally requires the parties show that (1) the failing division has a persistently negative cash flow on an operating basis; (2) the assets of the division would exit the market in the near future if the division is not sold; and (3) the seller made unsuccessful good-faith efforts to find another buyer to purchase the division that would pose less anticompetitive risk. *See, e.g., Merger Guidelines § 11.*

Lastly, parties may be able to avail themselves of a "flailing" firm or weakened firm defense, which the agencies or courts may take into account in evaluating the likely competitive effects of a proposed merger. For example, in *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109 (D.D.C. 2004), the district court found that while the target was not a failing firm "in the technical sense," it would be a "stronger competitive force in a post-merger market." Because there were no prospects for much needed investment or a different buyer, the target was "unlikely to be a strong competitor in the [relevant market] if the transactions [were] enjoined." The financially stable buyer promised to expand production, which further mitigated concerns about potential anticompetitive effects.

Expedited Merger Trials

Bankruptcy can create unique circumstances when litigating an acquisition against the government. White & Case is one of the few firms that has litigated a merger case involving a target in bankruptcy, and it did so successfully during the "tech wreck" downturn.

White & Case represented SunGard Data Systems in its successful defense of its acquisition of the computer disaster recovery assets of Comdisco. This litigation broke new ground at the intersection of US bankruptcy and merger law under Section 7 of the Clayton Act.

The SunGard/Comdisco antitrust case was tried in record time (and in parallel with the bankruptcy case). From the filing of the DOJ's complaint through discovery, a full-blown adversarial trial with expert witnesses before the US District Court for the District of Columbia (before US District Judge Ellen Huvelle), until the decision by the US Court of Appeals for the DC Circuit allowing the merger to proceed, only 19 business days elapsed. This also marked the first defeat of a government merger challenge in federal court in the District of Columbia in almost a decade.

The antitrust issues were challenging since many analysts and company business records of the parties could be interpreted to suggest the merger would combine two of three disaster recovery firms in the US, which could be viewed as resulting in a nominal post-merger market share of 66 percent or higher. The September 11 terror attacks occurred during the parties' HSR compliance, underscoring America's need for disaster recovery.

To stave off a competing bid from white knight Hewlett-Packard (which had no competitive overlaps with target Comdisco), White & Case pushed for an expedited merger litigation schedule that would resolve the DOJ's challenge in under a month. After only two weeks of discovery, White & Case provided the district court with hundreds of exhibits, a number of declarations, and the live testimony of three expert witnesses in a 10-hour evidentiary hearing and separate oral arguments. *See US v. SunGard Data Sys.*, 172 F. Supp. 2d 172, 179 (D.D.C. 2001) ("During this extraordinarily brief period of time, the parties have completed the entire litigation process involving complicated legal issues and a highly sophisticated and technical industry. Despite the extremely expedited nature of the process, both sides submitted thorough and well-crafted pleadings and have assisted the Court at every juncture.").

The extraordinary circumstances showed that the US District Court for the District of Columbia could accommodate the merging parties quickly for a resolution.

A Merger Trial in Bankruptcy Court

Virtually all federal district courts send cases invoking bankruptcy jurisdiction to federal bankruptcy courts. Depending on the parties' objectives and the transaction's characteristics, litigating antitrust issues in a bankruptcy court may be preferable. For example, if parties are motivated to close a transaction as quickly as possible, a bankruptcy court might provide a more timely resolution of antitrust issues compared to a district court proceeding.

Bankruptcy courts may hear and determine core matters (concerning administration of the bankruptcy estate) and non-core matters (otherwise related to the bankruptcy case). Courts are split on whether bankruptcy courts may properly decide merger challenges. Some bankruptcy courts have affirmed their authority to decide antitrust issues and select the acquirer, after considering the relevant antitrust implications. For example, in In re *Financial News Network*, two competing bidders, the Dow Jones/Group W partnership and CNBC, vied to acquire Financial News Network ("FNN") out of a Section 363 bankruptcy. Because the Dow Jones/Group W partnership's bid did not comply with the bankruptcy court's rules, the bankruptcy court accepted CNBC's bid, even though CNBC was FNN's only competitor in the cable television business news industry. The FTC and certain state attorneys general opposed the bankruptcy court's jurisdiction over issues of antitrust law. On appeal, the Second Circuit Court of Appeals affirmed the bankruptcy court's jurisdiction over the antitrust issues, noting that the FTC and state attorneys general could seek withdrawal of the entire proceeding or antitrust issues to the district court. Ultimately, the FTC terminated its antitrust investigation and never challenged the merger in court.

Expedited Merger Clearances in Multiple Jurisdictions

Merging parties may be able to leverage expedited merger clearance in the United States to expedite merger clearances in other jurisdictions. This strategy may be particularly effective where counsel is able to engage on issues common to the US and foreign jurisdictions.

It is important to coordinate messaging and engagement on crises-related considerations such as those discussed above (e.g., risk of business failure by the target company, the need for expedited deal timing, etc.) and to actively manage strong and consistent advocacy on key substantive issues and themes (e.g., business rationale, efficiencies, etc.) across jurisdictions.

Judicial approval (or approval of US regulators) of a purchaser in the United States may also help expedite approvals from foreign competition authorities.

Key contacts

George Paul
Partner, Washington, DC
T +1 202 626 3656
T +1 202 626 3600
E gpaul@whitecase.com

Rebecca Farrington
Partner, Washington, DC
T +1 202 626 3599
E rfarrington@whitecase.com

Noah Brumfield
Partner, Silicon Valley, Washington, DC
T +1 650 213 0395
T +1 202 626 3698
E nbrumfield@whitecase.com

JD Donaldson
Partner, Washington, DC
T +1 202 637 6253
E jdonaldson@whitecase.com

Anna Kertesz
Partner, Washington, DC
T +1 202 729 2320
E akertesz@whitecase.com

J. Mark Gidley
Partner, Washington, DC
T +1 202 626 3609
E mgidley@whitecase.com

whitecase.com

In this publication, White & Case means the international legal practice comprising White & Case LLP, a New York State registered limited liability partnership, White & Case LLP, a limited liability partnership incorporated under English law, and all other affiliated partnerships, companies and entities.

This publication is prepared for the general information of our clients and other interested persons. It is not, and does not attempt to be, comprehensive in nature. Due to the general nature of its content, it should not be regarded as legal advice.

© 2020 White & Case LLP

NY/0420/AC/M/157308_02