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Increased Merger Review Activity by US Department of Justice May Signal Increased Vigilance by Obama Administration

The start of the Obama administration in 2009 brought with it predictions of stepped-up antitrust enforcement activity by the Department of Justice's (DOJ) Antitrust Division, particularly in the area of mergers. To the surprise of many observers, those predictions proved largely overstated. While the US Federal Trade Commission (FTC) continued to be very aggressive in its antitrust enforcement, and the DOJ vigorously pursued cartels in the United States and around the world (as it has for the last two decades), civil non-merger challenges and merger enforcement have barely increased over the last two years. Instead, the DOJ's enforcement actions typically involved settlements—particularly in the vertical area—and consummated mergers.

However, a recent spate of actual and threatened court actions by the DOJ to block and undo mergers may signal a reversal of this trend and could be an indication that the DOJ is finally becoming more aggressive in merger review. This, combined with the joint DOJ-FTC promulgation of new horizontal merger guidelines in August 2010, puts the spotlight back on the antitrust aspects of mergers at a time when economic activity appears to be picking up steam. Businesses that are considering mergers, acquisitions or other combinations—particularly in concentrated markets—would do well to pay close attention to this emerging trend.

Below we discuss five actions brought by the DOJ, and the lessons that can be learned from each. While the enforcement trend may be a new development, the theories offered by the DOJ in these cases are very conventional:

- The mergers challenged were all horizontal and involved straightforward application of traditional antitrust principles;
- Assuming the government's proposed market definition was accepted, the challenged transactions generally would have resulted in large market shares for the post-merger firm;
- The government relied on evidence that the DOJ typically finds persuasive, including business documents analyzing the transaction; and
- The industries in which the mergers occurred—including agriculture, financial markets and high-tech industries—are ones that have historically received scrutiny from the government.

H&R Block/2SS Holdings

On May 23, 2011, the DOJ sued under Section 7 of the Clayton Act to enjoin the proposed merger of H&R Block and 2SS Holdings, makers of digital tax preparation applications. H&R Block and 2SS Holdings are the second and third largest providers of do-it-yourself tax preparation software and web application products in the United States. The DOJ's principal contention is that the acquisition is effectively a "3 to 2" merger, as the combined firm and its main competitor will control approximately 90 percent

of the market. The complaint relies heavily on documents collected from H&R Block during the merger review process, such as emails stating that a purpose of the acquisition is to "regain control of industry pricing" and that H&R Block and the remaining competitor "both obviously have great incentive to keep this channel profitable."

Although the high level of market concentration resulting from the proposed merger might have been enough, by itself, to trigger a challenge, similar to the FTC's 2007 action against Whole Foods, this case serves as a reminder that documents that explicitly or implicitly suggest anticompetitive motives for a merger can lead to heightened scrutiny by the enforcement agencies.

Verifone/Hypercom

On May 20, 2011, Hypercom Corp. abandoned its proposed agreement to divest its United States point-of-sale (POS) terminal business to Igenico S.A., one week after the DOJ filed suit to enjoin the acquisition of Hypercom by VeriFone Systems Inc. and to enjoin the divestiture (which the DOJ likened to a complex franchising agreement rather than a clean divestiture). The DOJ's suit to enjoin the VeriFone-Hypercom acquisition remains pending.

POS terminals are used by retailers to collect payment information from credit and debit cards. The DOJ's complaint expressed concerns that the merger of VeriFone and Hypercom would result in a duopoly in both segments of the POS market, and that the divestiture/franchise agreement would foster coordination between the merged entity and the one remaining competitor in one of the segments due to the "ongoing relationship" between the remaining competitors. This lawsuit signals the DOJ's increased scrutiny of "fix it first" remedies proposed by the merging parties. The suit is also notable because, in addition to seeking the usual remedy of an injunction against the merger under Section 7 of the Clayton Act, the DOJ also brought suit under Section 1 of the Sherman Act, alleging that the combined merger-divestiture deal amounted to a unitary agreement in restraint of trade.

NASDAQ OMX Group/NYSE Euronext

On May 16, 2011, NASDAQ OMX Group abandoned its unsolicited bid to acquire NYSE Euronext after being informed that the DOJ would file suit to block the deal. NYSE Euronext and NASDAQ OMX Group are best known as the owners of the two major stock exchanges in the United States and thus are the only two competitors for corporate stock listing services. The DOJ's press release announcing the termination of the merger pointed out that the companies are also the only providers of off-exchange trade reporting services and stock auction services that manage the unique order flows for equities at the beginning and end of each trading day.

The threatened action hinged largely on the merged entity's dominance in multiple markets related to equity trading. Significantly, it appears that the DOJ was not persuaded that global competition in equity trading, or that powerful companies that engage in equity trading, would be a sufficient restraint on the merged party. This stands in contrast to past mergers, including the 2006 merger of Whirlpool and Maytag, where foreign competition was considered a significant factor in approving the merger.

George's Acquisition of Tyson Foods Harrisonburg, Virginia Poultry Plant

On May 10, 2011, the DOJ filed a civil antitrust action challenging George's Inc.'s $3 million acquisition of Tyson Foods' Harrisonburg, Virginia, chicken processing plant. Tyson's, George's and a third firm, Pilgrim's Pride, are the only competitors in the chicken processing market in the Shenandoah Valley region of Virginia, with each competing for the purchase of chickens from local farmers. In its complaint, the DOJ alleged that the acquisition would reduce competition for the procurement of chicken

farmers' services and thereby reduce the farmers' ability to obtain competitive prices.

The $3 million acquisition was far below the $66 million threshold for reporting under the Hart-Scott-Rodino Act, yet the DOJ began an investigation into possible anticompetitive effects upon learning of the proposed acquisition through media reports. Despite the parties' knowledge of the investigation, and without responding to the DOJ's requests for information, the parties went ahead and closed the transaction. Thus, the DOJ's lawsuit seeks divestiture of the Harrisonburg facility. In general, the DOJ is paying more attention to agricultural mergers and acquisitions, and remains undeterred by the fact that an acquisition is not reportable under the HSR Act.

API Healthcare/Kronos

On April 29, 2011, API Healthcare and Kronos announced that they had abandoned their proposed merger after the DOJ expressed concerns that the acquisition would reduce competition in the healthcare workforce-management technology market. API Healthcare and Kronos make software products that track the time and attendance of health care professionals. The two companies have the largest and the second-largest market shares in this market. The DOJ balked at the transaction because it would have resulted in a single firm controlling approximately 70 percent of the market. The government remains focused on antitrust enforcement in the healthcare industry, and is likely to challenge mergers among the two largest competitors when the shares are this large.

Conclusion

These recent DOJ actions should not in any way discourage parties from continuing to explore strategic mergers. Most strategic mergers do not raise concerns and are allowed to proceed without a second request or government challenge. However, transactions that result in significant market shares and/or that take place in the context of highly concentrated markets are much more likely to result in an agency challenge or require a settlement. Strategic deals can still be consummated, even if they raise antitrust concerns, if the parties are able to provide the government an acceptable settlement. However, parties should be aware that the DOJ will not easily back down. A more active DOJ can add time, expense and uncertainty to transactions. While these new variable can be managed, it is wise to plan accordingly.

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