Volume 1 | Issue 3 | September 2023

M&A, Activism and Corporate Governance

QUARTERLY REVIEW

Introduction

The *M&A, Activism and Corporate Governance Quarterly Review* is Mayer Brown's quarterly publication designed to keep you current on key legal developments involving mergers and acquisitions, shareholder activism and corporate governance matters.

For more information about Mayer Brown's M&A practice, visit our Mergers & Acquisitions webpage at Mergers & Acquisitions | Capabilities | Mayer Brown.

In This Issue

The Biden Administration Wants to Change the Rules of the Road for Antitrust M&A in the US: What Does It Mean for Dealmakers? 3

Antitrust Enforcement Spotlight on Private Equity Buyers 9

Key Takeaways: The European Union Foreign Subsidies Regulation 10

What Boards Need to Know Regarding the Forthcoming Artificial Intelligence-Related Legal Frameworks and What They Can Do to Prepare 16

The Biden Administration Wants to Change the Rules of the Road for Antitrust M&A in the US: What Does It Mean for Dealmakers?

By: William Stallings

The Biden Administration is proposing revisions to the procedural rules governing pre-merger filings as well as the substantive framework for analyzing antitrust implications of U.S. M&A deals. Once implemented—potentially as soon as summer 2024—the changes will act in tandem to add complexity, length and burden to U.S. antitrust reviews. Dealmakers should be aware of these changes and their impact on deal terms, timing, and ultimate success in closing U.S. deals.

The changes affect two core areas: (1) the up-front, mandatory Hart-Scott-Rodino ("HSR") pre-merger notification information requirements that initiate the antitrust review process and (2) the joint Merger Guidelines issued by the U.S. antitrust agencies—the Antitrust Division of the Department of Justice ("DOJ") and the Federal Trade Commission (the "FTC")—that provide the analytical framework that the agencies employ in conducting the reviews.

These changes do not occur in a vacuum; rather, they follow the Administration's efforts to reform the role of antitrust regulatory enforcement as a whole.

Biden Administration Focus on Antitrust Enforcement

Antitrust has increasingly been in the political spotlight. Less than six months after taking office, President Biden issued Executive Order 14036, titled "Executive Order on Promoting Competition in the American Economy" (July 9, 2021, the "EO"). It established a "whole-of-government effort" to addressing competition concerns, and directed federal agencies to commit to stronger and more vigorous enforcement of the federal antitrust laws. The EO expressed an expansive view of the importance of antitrust, opining that a perceived "excessive market concentration threatens basic economic liberties, democratic accountability, and the welfare of workers, farmers, small businesses, startups, and consumers."

Consistent with the EO, the FTC and the DOJ have recently taken a more aggressive course with respect to M&A. Officials made clear in speeches shortly after the EO that they considered past antitrust enforcement (including enforcement in prior Democratic administrations) to be "weak;" they signaled a strong preference for litigation to block deals instead of entering into settlements with divestitures; they did away with "early terminations" that previously allowed deals subject to HSR filing to clear prior to the 30-day statutory waiting period, and they issued more "second requests" in order to conduct in-depth investigations of transactions.

Judicial Resistance

The U.S. antitrust agencies cannot on their own force companies to abandon or change a merger. Instead, they have to negotiate an agreed-upon settlement with the parties or litigate in court to persuade an independent judge to take action. Keeping with the messaging in their speeches and statements, the agencies litigated. Both the DOJ & the FTC have in the past few years filed many court challenges to block deals, spanning industries such as airlines, agriculture, healthcare, pharma, tech, book publishing, and consumer products and services. At the same time, the number of negotiated settlements with divestitures (i.e., consent decrees—the traditional way that the government most often had resolved competition concerns) that the agencies entered into with merging parties dwindled to near-zero.

The courts, however, have more often than not disagreed with the government. While the DOJ prevailed in blocking two deals (a book publisher merger—the Penguin/Simon & Schuster transaction and an airline joint venture—the American/Jet Blue transaction), the government has lost every other M&A challenge that went to decision.[1] Moreover, courts have sent a strong message that traditional remedies continue to have value in antitrust cases, as judges have endorsed remedies offered by parties directly to the court (sometimes called "litigating the fix") and encouraged the government to settle merger cases by agreeing to divestitures.[2] That message is perhaps finally resonating, as the FTC has recently settled two litigated merger challenges with remedies that are similar to the types of remedies that prior administrations had used.[3]

The Proposed Changes to Antitrust Rules

Litigating in court is not the only tool at the Administration's disposal to affect antitrust enforcement. The Administration is now seeking to implement changes to antitrust rules and practices that would have a broad impact on all U.S. M&A.

1. HSR Overhaul

On June 27, 2023, the FTC—which administers the HSR program—issued a proposed rulemaking that would dramatically overhaul the information that parties must provide upfront to the government before they can close certain transactions.

The proposed rule would apply to all "reportable" transactions—those that exceed the statutory threshold for "size of transaction" (currently, $111.4 million but increases on an annual basis) and other tests—regardless of whether the deals actually raise any competition concerns.

In essence, the revisions will convert the U.S. system from an objective "notice" filing protocol to more of a subjective framework that will require parties to provide up-front disclosures on multiple subjects and copious amounts of internal documents and data.

---

[1] E.g., Microsoft/Activision; Meta/Within; Booz Allen/EverWatch; UnitedHealth Group/Change HealthCare; U.S. Sugar/Imperial Sugar; Illumina/Grail (currently on appeal); Altria/Juul (ALJ decision); Jefferson Health/Einstein Healthcare.

[2] E.g., Assa Abloy/Spectrum (court on record pressing parties to settle; DOJ eventually agreed to a divestiture); United Health/Change & Microsoft/Activision (courts endorsing remedies offered by parties).

[3] E.g., ICE/Blacknight (divestiture); Amgen/Horizon (commitment not to engage in certain conduct)

The new requirements are far-reaching. (For a detailed discussion of all the requirements, see our Legal Update, "FTC's Proposed HSR Changes Will Complicate Merger Filings".) Several aspects are particularly important for U.S. dealmakers to appreciate, including that parties to all reportable deals will have to provide:

- Details about the structure of the transaction, its business rationale, and the entities involved in it, including significant information on minority and private equity investors and "entities or individuals that may have material influence on the management or operations" of the acquirer, such as certain creditors, board observers, and management service providers;
- Narrative descriptions of the parties' products and services, the markets in which they are offered, and up-front assessments of competitive overlaps and other interactions between the parties, such as supply agreements;
- A vastly expanded set of the "Item 4(c) and (d)" deal-related documents covering competition topics that must be submitted, including all draft documents (instead of just the final version) and documents prepared by or for the supervisory deal team leads, as well as ordinary-course strategic plans and reports, regardless of whether they were created in connection with the deal; and
- Disclosure of information that screens for labor market issues by classifying employees based on certain job categories and geographic market information ("commuting zones" in which both parties employ workers in such categories), as well as information on any past worker and workplace safety violations.

The changes will require significant additional work, with the FTC predicting that conformity to the proposed rules would result in approximately 12 to 222 additional hours per filing. Many practitioners believe that the time required to comply will be much greater. On a more positive note for dealmakers, the FTC Chair, Lina Khan, stated on September 22, 2023 that the antitrust enforcement agency drafters of these new HSR rules will be looking closely at the comments submitted to the draft form, including being open to evaluating the filing burden on companies whose transactions are the least "risky" from an anticompetition standpoint.

2. Merger Guidelines Revisions

While the HSR revisions govern the process of merger review, the proposed changes to the Merger Guidelines relate to the substantive analytical framework the agencies use to answer the question of whether a transaction "may substantially lessen competition or tend to create a monopoly" in violation of Section 7 of the Clayton Act.

The DOJ and the FTC have for decades issued Merger Guidelines, with the initial version dating back to 1968 and the most recent revision in 2010. The intent of the Guidelines is to provide transparency to stakeholders (e.g., merging parties, the courts and the public) as to the analytical factors the antitrust agencies consider when reviewing mergers. Indeed, lower courts have applied the Guidelines in deciding litigated antitrust challenges to mergers (which is important as the U.S. Supreme Court has not issued a decision related to an antitrust challenge to a merger in decades).

The agencies promulgated their proposed draft revisions to the Merger Guidelines on July 19, 2023, about three weeks after the proposed HSR rules. Like the proposed changes to the HSR rules, the draft Guidelines are in a public notice-and-comment period, after which the agencies will presumably issue the final version.

The draft Guidelines list thirteen different concepts (each a separate individual "guideline") that the government may rely upon to determine that a merger is problematic. This expands on the 2010 version; indeed, the 2010

Guidelines are 34 pages while the 2023 draft Guidelines and appendices come in at a whopping 51 pages. Further, 47 of those pages are devoted to ways in which a merger could cause harm, while only four cover potential "rebuttal evidence" (much of which the draft Guidelines discount).

The Administration has emphasized several areas that differentiate the proposed revisions from the current (2010) Guidelines, namely:

- *Concentration Levels:* The 2010 revisions to the Guidelines had increased the thresholds at which the government would consider a market "highly concentrated" as well as the changes in concentration levels that would raise concern. The draft Guidelines would restore both value to pre-2010 levels.
- *"Context" of Acquisitions:* The draft Guidelines emphasize the need to look at the broader "context" of a merger instead of simply examining the specific effects of the deal under review. Accordingly, the draft makes it clear that the agencies will consider patterns of serial acquisitions ("roll-ups") or acquisitions by a dominant firm of potential future competitors.
- *Platform Competition:* The draft Guidelines specifically focus on "platform" competition, where a firm operates in a two-sided market by facilitating transactions between two parties (e.g., Uber connecting drivers and riders). The draft calls-out whether mergers could allow such platforms to "entrench" themselves.
- *Labor Markets:* Consistent with the Administration's overall emphasis in applying antitrust laws in general to protect workers, the draft Guidelines make clear that they will examine whether a merger could result in "monopsony" power that would allow the combined firm to lower wages to workers. This emphases dovetails with the changes in the HSR form that would require up-front employee-related data. (The antitrust agencies, however, have never, to date, brought a merger case based on an impact to employees.)
- *Nomenclature:* Antitrust typically distinguishes between "horizontal" (firms competing against each other) and "vertical" (firms at different levels of the supply chain) theories of harm for mergers. The draft Guidelines reject such nomenclature, preferring to broadly ask "How does competition present itself in this market and might this merger risk lessening that competition substantially now or in the future?"
- *Legal Citations:* In an unprecedented move, the draft Guidelines cite to legal precedent. As mentioned, the Supreme Court has not heard a merger case in decades. Accordingly, most of the citations are to cases from the 1960s and 1970s, an era that predated modern economics. By citing cases, the draft Guidelines read more like a legal brief designed to advocate before a court, rather than a set of principles designed to provide merging parties and the public with meaningful insight into agency thinking.

The Impact on Dealmakers

Once adopted in their final forms, the new HSR filing rules and the Merger Guidelines will make the antitrust review process more challenging for U.S. deals, providing further evidence that the Administration is biased toward organic growth over strategic M&A. Despite the reoccurring headlines in the press, however, competition concerns should not necessarily be seen as a barrier to U.S. dealmaking, particularly for dealmakers who are already ahead of the new rules and are strategic-minded.

1. Deals are Still Getting Through

The most recent detailed data available from the government shows that the overwhelming majority of deals are still getting through, even ones that raise competition issues. The Agencies submit "Annual Competition Reports" to Congress with detailed data on HSR filings.[4] Fiscal year 2021 (October 1, 2020 through September 30, 2021) was a high-water mark for HSR-reportable transactions, with 3,413 transactions filed that year. Of those, the agencies opened initial investigations (referred to as seeking "clearance") into just 270 (7.9%) transactions. In other words, the agencies had *no* interest in over 92% of all deals. But, what about the 270 that at least triggered a competition review? Notwithstanding the Biden Administration's rhetoric about needing to stop problematic mergers, they issued second requests (i.e., conducted an in-depth review) in only 65 deals, and, ultimately, only 32 deals were stopped (less than 0.1% of all reportable transactions).[5] In short, U.S. antitrust review, even in the current climate, does not bar U.S. deals.

2. Possible Retrenchment?

Could the agencies be pulling back from their publicly stated aggressive enforcement position? As mentioned above, the agencies have faced tough sledding in court, where government losses have far outnumbered the wins. In addition, importantly, the courts have endorsed the traditionalist approach of favoring settlements that address competition concerns without necessarily blocking a deal outright. While it is too early to tell, the FTC's recent settlements of ICE/Black Knight and Amgen/Horizon through more traditionalist-style remedies could signal a less confrontational approach to antitrust review going forward.

There are other signs that the agencies may be tempering their views. For example, a FTC official recently discussed the draft Merger Guidelines and suggested that the final version will be amended to make clear that the agencies will consider merging parties' arguments that a transaction's increase in concentration will not necessarily harm competition.

Finally, the Merger Guidelines are just what their title states – guidelines, not law. Courts do not have to follow the agencies' pronouncements on how the agencies review mergers. Courts will follow the law and facts, and, as made evident by the agencies' recent losses, courts do not mechanically defer to the government's position.

---

[4] Available at https://www.ftc.gov/policy/reports/annual-competition-reports.

[5] FTC & DOJ, "Annual Competition Report FY 2021" at Exh. A, Table 1 ("Data Profiling Hart-Scott-Rodino Premerger Notification Filings and Enforcement Interests"), available at https://www.ftc.gov/system/files/ftc_gov/pdf/p110014fy2021hsrannualreport.pdf.

3. Deal Terms

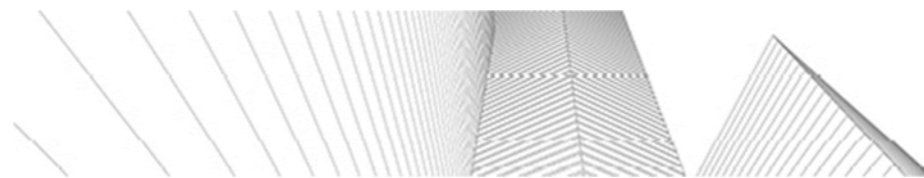
The Administration's antitrust enforcement efforts have led parties to anticipate longer merger review timelines, more frequent second requests and a higher likelihood that litigation against the government will be needed to get deals closed. The proposed HSR revisions will further complicate deal timelines for the merger review process.[6] As a result, the negotiation of deal terms addressing antitrust risk take on added importance. Such terms include:

- Longer outside dates;
- Reverse termination fees;
- Use of ticking fees and other creative tools to lessen sell-side risk;
- Negotiating remedies into the acquisition agreement; and
- Efforts covenant (although "hell or high water" provisions are rare).

For a detailed discussion on how these terms are used and scale with antitrust risk, see our Legal Update, "M&A Lawyers Adapt to New Era of Antitrust Enforcement: How Contractual Provisions Are Evolving".

The unequivocal result of the changes to the HSR requirements and to the Merger Guidelines will be increased burden, more risk and less certainty for parties looking to do U.S. M&A transactions. Even simple no-issues transactions will require a substantial investment in filing preparation and will add extra time and cost to the merger clearance process. It will be incumbent on deal teams to think through how the current regulatory environment impacts their transactions and take appropriate steps to address (and streamline data collection processes) and, where possible, minimize the risk. The increased antitrust risk, while important to assess, does not have to be determinative of whether deals move forward; as the data shows, the vast majority of transactions are still getting to the finish line even in this period of aggressive antitrust enforcement.

[6] The HSR statute provides that the initial waiting period is 30 days; the FTC cannot change that requirement. However, could the FTC "bounce" filings that they deem deficient for failure to meet the subjective requirements of the new rules, such as overlap descriptions and deal rationale? If so, the U.S. risks becoming more of an EU-like system where the parties engage in significant pre-filing "consultations" with the government, providing iterative drafts of the filing until the agency is satisfied and little predictability for when the 30-day clock would start.



Antitrust Enforcement Spotlight on Private Equity Buyers

By: Gail Levine and Camila Panama

Early in her tenure, Federal Trade Commission (the "FTC") Chair Lina Khan vowed to take a "muscular" approach to regulating U.S. private equity dealmaking. Recent events, such as the FTC's targeting of roll-ups, make clear, more than ever before, that U.S. private equity buyers should consider antitrust strategy when seeking to get deals done.

On September 21, 2023, in the current administration's first litigated case challenging serial acquisitions by a private equity firm, the FTC challenged Welsh, Carson, Anderson & Stowe's ("Welsh Carson") roll-up strategy of anesthesiology practices across Texas. The FTC brought suit against Welsh Carson and its partially owned portfolio company, U.S. Anesthesia Partners, Inc. ("USAP"), in Texas federal court, accusing them of using a roll-up scheme to systemically acquire "nearly every large anesthesia practice in Texas to create a single dominant provider with the power to demand higher prices." That same day, Chair Khan said in a statement that "the FTC will continue to scrutinize and challenge serial acquisitions, roll-ups, and other stealth consolidation schemes that unlawfully undermine fair competition and harm the American public." The FTC's complaint seeks "structural relief," presumably including divestitures to effectively unwind the acquisitions and to enjoin the defendants from engaging in similar conduct (potentially not limited to Texas and not just with respect to anesthesiology practices).

One of the most interesting facts about this challenge is that Welsh Carson formed USAP back in 2012, with the roll-up acquisitions in question occurring between 2012 and 2020, the vast majority of which took place prior to 2017 and likely all of which were of a deal value below the threshold requiring a Hart-Scott-Rodino ("HSR") filing. USAP has been operating in its "rolled-up" form for years, so why is the FTC now asserting that the acquisitions were illegal "whether considered individually or as a series?"

It doesn't help that private equity buyers are on the administration's stated agenda. In June 2022, Chair Khan issued a statement calling out private equity firms and their serial acquisitions in the healthcare industry, highlighting the following sectors: anesthesiology, emergency medicine, hospice care, air ambulances, and opioid treatment centers. The takeaway here is that even non-reportable transactions that closed years ago may get attention from today's U.S. antitrust agencies, particularly those involved in a roll-up strategy in any of the named healthcare sectors.

Key Takeaways: The European Union Foreign Subsidies Regulation

By: Dr. Andrea Pomana and Nikolay Mizulin[1]

A new regime tackling foreign subsidies has begun to take effect in the European Union (the "EU"): the Foreign Subsidies Regulation (the "FSR").

The FSR introduces a new set of rules for M&A transactions that have a nexus to the EU.[2] It will have a significant impact on businesses active in the EU, particularly with respect to increased compliance obligations and potential delays in obtaining the required regulatory approvals in M&A transactions.

In the M&A context, as of October 12, 2023, the new regime will introduce mandatory obligations on contracting parties who meet certain thresholds under the regime to notify the European Commission (the "Commission") before closing their transaction. The filing obligation will rest, in an acquisition scenario with the acquirer and the target; in an outright merger scenario with both merging entities; and in a joint venture ("JV") constellation with all JV parents exercising "control" (within the meaning of EU antitrust law) over the JV company and the JV company itself. It has already been the case since June 12, 2023 that the Commission can "call in" and review any M&A transactions *ex officio* if it finds sufficient evidence that a foreign subsidy distorts the EU market.

The Q&A below provides more detail of the FSR, with a focus on implications on M&A transactions.

What is the New FSR About?

The FSR introduces a new regulatory layer that parties to M&A transactions need to comply with in the EU—in addition to the already existing merger control and foreign direct investment rules.

The FSR aims to combat the effects of potentially distortive subsidies granted by non-EU (i.e., "foreign") countries to companies operating in the EU. Through this new regime, the Commission seeks to ensure that subsidized companies do not enjoy what it views as an unfair advantage when participating in M&A transactions. Transacting companies implicated by the FSR may need to repay the subsidy or offer other remedies to obtain clearance before closing their deal.

The EU already has in place rules that screen subsidies granted within the EU (i.e., the EU State Aid regime), as well as rules combatting injurious subsidies granted to foreign imports (i.e., the anti-subsidy trade defense regime). However, prior to the FSR, no rules existed to effectively deal with distortions in the EU market caused by foreign subsidies in the context of M&A transactions.

Who is Subject to the FSR?

All international companies, irrespective of their country of origin or primary location, will be subject to the FSR if they (i) receive a foreign financial contribution ("FFC") from non-EU government entities (see further

---

[1]The authors co-lead the FSR practice within Mayer Brown.
[2] The FSR also applies to public procurement procedures that are not further discussed in this paper.

discussion on what constitutes a subsidy below) and (ii) engage in M&A deals that impact the EU (see the relevant thresholds below).

What is a Subsidy?

A foreign subsidy exists where a non-EU country provides, directly or indirectly, a financial contribution that confers a benefit on an undertaking engaging in an economic activity in the EU and that is limited, in law or in fact, to one or more undertakings or industries.

The most common types of subsidies are cash grants, interest-free loans, unlimited guarantees, capital injections, preferential tax treatment, purchases from the government or sales to the government.

The FSR will ensure that acquisitions of an EU target are not supported by a foreign government providing, for example, a preferential loan or an unlimited guarantee to the acquirer, thus enabling it to outbid potential competitors.

When Will the FSR Apply?

The FSR entered into force on January 12, 2023, but has applied partially as of July 12, 2023 and will be in full effect beginning October 12, 2023.

As of July 2023, the Commission has had the power to examine any foreign subsidy in any sector of the EU economy in its sole discretion (so called *ex officio* investigation power), regardless whether the thresholds mentioned below are met or not.

As of October 12, 2023, the Commission must be notified of all M&A transactions that meet the relevant thresholds. All M&A transactions signed after July 12, 2023 and which both close after October 12, 2023 and meet the FSR thresholds will need to be notified to the Commission.

What are the Filing Thresholds?

For M&A transactions, a mandatory notification is required when the following two cumulative thresholds are met:

- at least one of the merging parties, the acquired party or the joint venture, is established in the EU and generates an aggregate revenue in the EU of at least EUR 500 million; and
- the parties to the M&A transaction solely or on a combined basis were granted financial contributions of more than EUR 50 million from non-EU countries in the three years preceding the conclusion of the agreement or the acquisition of a controlling interest.

The notification thresholds are not based on the level of subsidies (i.e., grants) that are liable to improve the competitive position in the EU of a party to the transaction. Rather, the notification requirement is based on a much wider concept of FFC, as described above.

Are Private Equity Companies also Affected?

Yes. "Financial contributions" are broadly defined and can be made by a wide variety of entities. Investments by a private equity ("PE") fund are included within the definition of a relevant "financial contribution", depending on whether such PE fund's actions can be attributed to the non-EU country in question. All relevant circumstances are taken into account in determining whether a PE fund's actions can, in fact, be attributed to a non-EU country.

The Commission has acknowledged that PE funds potentially within the scope of the FSR would need to gather information from multiple portfolio companies, which can be more burdensome than M&A

transactions that do not involve PE investors. As such, the Commission has lightened the notification burden applicable to PE funds by limiting their disclosure requirements for FFC to only the acquiring fund (or funds)—including its investors and portfolio companies—under certain conditions. However, in the case of foreign subsidies that fall within those categories identified by the Commission as most likely to distort the EU internal market, all funds and portfolio companies need consideration.

In any case, the analysis of FFCs for the purpose of determining the EUR 50 million notification threshold should still be carried out across all funds and portfolio companies.

It is also worth bearing in mind that in the case of non-compliance with the new rules, the Commission may look at the wider group structure to calculate a fine (see further discussion of fines below).

The Commission has acknowledged that more guidance on how these concepts apply in the PE context is required. It has indicated that this will soon be forthcoming.

Are Joint Ventures Implicated by the FSR?

It depends. The JV needs to hit a certain gross revenue (also called, "turnover") number and to act like an independent market player for the FSR rules to be triggered.

More specifically, in the case of the creation of JVs performing on a going-forward basis all the functions of an autonomous economic entity, the gross revenue threshold of the FSR will be met if the JV is established in the EU and the JV's gross revenue in the EU is at least EUR 500 million. However, in the case of the creation of a newly set-up JV (i.e., a "greenfield JV"), as it does not have any gross revenue of its own, this threshold is not met, and therefore a notification under the FSR is not required.

The analysis may be different when the JV is created via the change from sole to joint control of a pre-existing business or subsidiary or where there is a change in control in a joint control structure due to the entrance of new controlling equityholders or in the case where entities newly acquire joint control of a pre-existing entity or business. This is a complex area, and it is facts and circumstances dependent.

What Needs to be Reported?

The FSR requires the notification of FFCs.

A FFC is a measure taken by a non-EU government—including public entities and private entities acting under control of, or under entrustment or direction of that non-EU government—that transfers economic resources to a notifying company.

FFCs are widely defined and can include, for example, capital injections, grants, loans, loan guarantees, exclusive rights and tax incentives as well purchases from the non-EU government or sales to the government, including those made on market terms. They can also include, under certain circumstances, measures such as export taxes, for example on oil exports that depress domestic oil prices.

The FSR has not issued a finite list of FFCs that should be reported. The list is intentionally left open to cover all possible forms of financial contributions and to avoid circumvention

Such notification should cover financial contributions granted not only to the legal entities directly involved in a transaction but to all group entities of the companies concerned (except for investment funds, which benefit from a specific limitation under certain conditions).

The FSR and its Implementing Regulation further distinguish between FFCs that should be (i) notified in detail or (ii) declared through a simplified overview table.

Detailed notification is required for FFCs that, in the last three years, individually exceed EUR 1 million and are considered to be the most distortive subsidies ("high-risk" FFC). Examples of high-risk FFCs are unlimited guarantees for the debts or liabilities, export financing measures that are not in line with the Organisation for Economic Co-operation and Development arrangements, a subsidy directly facilitating a M&A transaction as well as a subsidy granted to a bankrupt undertaking.

All other FFCs need to be declared by means of an overview table if the individual FFC is above EUR 1 million and granted by a non-EU country that granted in aggregate FFCs of at least EUR 45 million in the three years prior to the concentration.

However, note that all FFCs granted in the three years prior to the conclusion of the agreement or the acquisition of a controlling interest (including the sale of products or services to a public entity at market terms) count for determining whether the EUR 50 million threshold is met that triggers the notification obligation.

Substantive Assessment?

The Commission will focus in its assessment on foreign subsidies that distort competition in the EU.

The FSR explicitly lists categories of foreign subsidies that are most likely to distort the internal market, such as a subsidy directly facilitating a M&A transaction. Foreign subsidies are also likely to cause distortions if granted in markets characterized by overcapacity, or leading to overcapacity, by sustaining "uneconomic assets" or by encouraging investment in capacity expansions that would otherwise not have been built. Under the FSR, a foreign subsidy granted to a beneficiary that shows a low degree of activity in the EU (measured in terms of EU revenue) is less likely to cause distortions than a foreign subsidy granted to a beneficiary that has a more significant level of activity in the EU.

The Commission will particularly focus on sizeable subsidies (i.e., subsidies in absolute terms or in relation to the size of the market or to the value of the investment). In addition, the Commission is likely to focus primarily on subsidies granted by China, Japan, the United States and, in some cases, South Korea and Saudi Arabia due to these economies having a large enough budget to grant sizeable subsidies. The Commission has already explicitly identified subsidies granted under the U.S. Inflation Reduction Act as a major area of concern and is expected to follow its extensive existing practice under the EU anti-subsidy trade defense rules when considering distortion under the FSR.

What is the Review Timetable?

The FSR review timetable is similar to the one under the EU Merger Regulation. As such, parties are encouraged to speak to the Commission early on, at the "pre-notification" stage before the formal phase 1 review period of 25 working days. In case of substantive concerns, the Commission may open a phase 2 review, which will last up to 90 working days (with a possible extension).

The Commission must approve the notifiable transactions under the FSR before the closing of the affected M&A deals.

It is not currently clear when remedies can be offered and accepted, especially at phase 1. As a practical matter, early engagement with the Commission on this point, as well as the review timetable more generally, is encouraged.

Does the analysis run in parallel to merger control and other regulatory filings?

Yes. The FSR creates an additional layer of regulatory compliance and deal conditionality for sizeable transactions separate and apart from potential merger control and foreign direct investment clearance.

However, the FSR and merger reviews at the Commission level have aligned timeframes, allowing the two notifications to run efficiently in parallel. Parties and their advisors should speak to the Commission as soon as possible to ensure that both regulatory regimes–FSR and merger control–are synched up in terms of timing, data requests and analysis.

Note that a M&A deal may require an FSR filing with the Commission while the same deal may undergo merger control scrutiny only at the EU member state level in cases where the Commission has no merger review jurisdiction. In addition, the same M&A deal may require foreign direct investment scrutiny in one or more EU member states.

Do Fines Apply?

Yes. Fines of up to 10% of the preceding financial year's turnover apply for companies that fail to notify a transaction, implement a notified merger or acquisition before the lapse of the review periods or who try to circumvent the notification requirements.

As under the EU Merger Regulation, the Commission is authorized to impose fines on the entities for breaching certain procedural requirements, such as supplying incorrect information or failing to supply required information. The fines for infringements of procedural requirements may reach 1% of the aggregate turnover in the preceding year or 5% of the average daily aggregate turnover in the preceding year for each day of the violation.

What Should Parties Consider in M&A Deals Specifically?

Parties should specifically consider the following in M&A transactions:

- **Deal planning**: If the deal requires FSR clearance, the transaction will also be subject to a "standstill obligation" under the regime, meaning that the transaction cannot close until the notification process has cleared. This time frame needs to be built into the deal timeline and corresponding agreement terms.
- **Include FSR provisions in corporate documentation**: All transactions signed after July 12, 2023 and that will not be closed by October 12, 2023 will need to be notified under the FSR procedures if the thresholds are met. All such deals should include provisions relating to FSR clearance (and potentially commitments with respect to what must be done in order to seek clearance) in their conditions precedent and other relevant corporate documentation.
- **Adopt stringent data collection mechanisms**: Under the FSR, the data collection burdens on parties to a relevant merger are significant (see further discussion below). Parties need to consider how to best to collate records of the required data on FFCs received from their investors, and by their portfolio companies and other group investments, in order to assess their likely exposure to filing obligations under the FSR.
- **Carefully consider whether the FSR applies to financial contributions from countries where loans, utilities and land-use rights are provided at non-market terms**: This is especially relevant when such conditions have been found in past European decisions, such as in the area of anti-subsidy investigations. The same applies to manufacturing inputs sourced from sectors with a significant state ownership or those acting under entrustment and direction from a foreign government (e.g., batteries, steel, aluminum, chemicals). Such contributions are unlikely to benefit from a waiver for the less-detailed summary reporting.

The FSR regime is new, and the Commission itself has acknowledged that it will need some time to work out how to operate the new rules in practice. There may be, for example, some flexibility by the Commission regarding the timeframe during which commitments can be offered. Businesses should plan their engagement with the Commission strategically and consider what waivers they can offer the Commission in terms of protection of confidential information to speed up both the FSR and merger reviews.

It is also critical for parties to keep up to date on the adoption of the FSR into practice. The Commission has emphasized that the applicable rules and regulations in the FSR field will evolve as practice and experience grow so it will be important to closely follow developments as this new regime goes into effect.

How should companies collect the required data?

Businesses will need to gather information on their group-wide receipts of non-EU State financial contributions over a rolling three year period for three main reasons:

- to check whether they trigger the thresholds for mandatory notification of M&A transaction under the FSR;
- to be able to fill in the required notification forms if the thresholds are met; and
- to be able to respond to any *ex officio* investigation carried out by the Commission.

Parties will need to gather, on an on-going basis, an extensive amount of information on FFC. This is similar to the process many companies follow to comply with EU merger control—corporates collect data on an on-going basis and know their geographic group-wide breakdown of turnover, so that they can assess to the relevance of merger control when they enter into M&A deals. With respect to the FSR, companies need to collect information on FFCs in order to determine whether the regime applies; and if it does, then the information will need to be further refined.

In terms of putting into place internal mechanisms to help with the necessary data collection under the FSR, companies should generally be able to combine an annual turnover breakdown request from its internal teams with a request for FFC data. The list of operating subsidiaries and controlled JV investments should generally be the same for both data collection exercises. It follows that the identification of the relevant corporate "group" for FSR purposes should follow the same approach used for the group-wide turnover breakdown—meaning, the ultimate parent, all subsidiaries and all interests in JVs where the group is able to exercise control and/or material influence for merger control purposes.

To assist in putting into place such internal processes, we have developed a template that is designed to capture, in a single place, the information required to assess whether a notification triggered for the relevant M&A transaction, as the case may be. The template is intended as a basis to capture the necessary FSR data from potentially extensive numbers of group entities. In any given M&A transaction, as with merger control, there will be a need for some dialogue and follow-up questions with the Commission, during which process, the parties can benefit from the advice of counsel who have experience working with the Commission.

What Boards Need to Know Regarding the Forthcoming Artificial Intelligence-Related Legal Frameworks and What They Can Do to Prepare

By: Dominique Shelton Leipzig and Camila Panama

Currently, there are artificial intelligence ("AI")-related legal frameworks pending or proposed in 37 countries across six continents. Even within each particular country, multiple governmental agencies are claiming AI as within their jurisdictional reach. For example, in the United States, the Consumer Financial Protection Bureau, Department of Justice, Equal Employment Opportunity Commission, Food and Drug Administration, Federal Trade Commission and the Securities and Exchange Commission each has issued guidance or otherwise indicated through enforcement activity that they view AI as within their respective purview of current regulatory and enforcement authority. In a world where AI, particularly generative AI, continues to weave its way into, among other things, businesses, marketing and public relations efforts, internal administrative actions and hiring processes, it may be prudent for boards of directors to understand the key implications of the new laws and their possible effect on the company's use of AI. While the first of the many new AI-related laws is not anticipated to go into effect until 2025, now is the time for boards to begin gaining familiarity with the key requirements coming down the pike and to consider a pro-active approach to compliance.

The Purpose of the New AI Legal Frameworks and Potential Consequences of Non-Compliance

The new AI legal frameworks are designed to balance the interest in encouraging innovation with concerns about human rights and civil liberties, privacy rights, anti-discrimination interests, consumer safety and protection, intellectual property protection, information integrity, security and fair business practices. For example, in the European Union, if the proposed law goes into effect in its current form, non-compliance may result in monetary penalties that, in some cases, project to be larger than the General Data Protection Regulation's highest fine levels of 4% of a company's gross revenue—the new European Union Parliament legislation proposes a monetary fine of up to 7% of a company's gross revenue for non-compliance. Additional potential consequences of non-compliance include reputational damage, and, in certain cases based on the pending or proposed laws, personal liability.

Action Items for Companies to Consider

With so many AI-related laws pending or proposed all over the world by a variety of different regulatory bodies, it is unsurprising that not all of these new rules are precisely aligned. However, there are key overlapped themes among the majority of these pending or proposed laws. Generally, the new AI legal frameworks call for categorizing the risk level of each of the company's use cases for AI, with such

categories including: (a) prohibited use, (b) high risk and (c) minimal or low risk. If “high risk” AI is present, then the pending or proposed laws generally require that such AI systems are required to undergo continuous testing, monitoring and auditing in areas including privacy, cybersecurity, intellectual property, antitrust, algorithmic bias, accuracy and consumer product/health/safety. There are over 70 “high risk” use case categories across the various AI-related frameworks, including AI use cases relating to pharmaceuticals, medical devices, manufacturing, personal finance, employment, health and critical infrastructure, among many others. These “high risk” use case categories are broadly defined—for example, simply stating “employment” and not going into further specificity, so we expect that most companies that use generative AI will have at least some instances of “high risk” use and, therefore, may need to comply with the required testing, monitoring and auditing depending on which laws they are ultimately subject to, among other factors. Once the various new laws take effect, they will generally require companies to put into place, or update accordingly, their AI-governance policies and enterprise risk management (“ERM”) programs.

By way of example, many companies have been using or gearing up to use AI-technology to help with their employee hiring processes, utilizing AI to do tasks such as routine resume screening of applicants. Across various use cases in recent years, inherent bias in AI models used for resume screening has resulted in applicant pools in which women and minorities were disproportionately screened-out, as compared to when such screening is performed by humans. While AI screening can certainly increase efficiency, it may result in biased outputs—the new AI laws seek to keep this in-check.

Which Legal Framework Will Go Into Effect First?

The European Union Artificial Intelligence Act (the “EU AI Act”) was approved by the European Parliament on June 14, 2023 and is likely to be the first among the various pending or proposed AI-legal frameworks to go into effect. The final version of the EU AI Act is currently being negotiated among the relevant EU-regulators, and it is anticipated that, at the earliest, the final version of the EU AI Act will go into effect in 2025. For more details, see our Legal Update, “European Parliament Reaches Agreement on its Version of the Proposed EU Artificial Intelligence Act”.

What Can Directors Do to Prepare for the Forthcoming Effectiveness of Applicable AI-Legal Frameworks?

Step 1: Stay Current on the Relevant Legal Landscape. There are over 198 AI-related laws and draft pieces of legislation pending or proposed in jurisdictions around the world, many of which implicate board accountability. While directors cannot know the details of each piece of legislation, boards of directors should consider asking for information about the key legal requirements that apply to the company and being briefed on the best practices for directors with respect to compliance and oversight. The AI legal frameworks, much like the AI they seek to govern, are continually evolving. With the risk of significant monetary fines, reputational damage and potential personal liability, it is prudent for directors to be well-positioned to ensure the company’s compliance and proper oversight of AI-related risks.

Step 2: Ask Management the Right Questions. In exercising their oversight role, boards of directors should consider asking thoughtful and strategic questions about the company’s use of AI to ensure that internal processes line up with both company strategy and legal requirements.

Boards can consider asking management: (1) How are we using AI? (2) How are we testing, monitoring and auditing for accuracy, fairness, elimination of bias, privacy, separate and distinct for cybersecurity, product safety, IP and antitrust considerations? (3) How can we review and approve governance policies for AI that include human review by management? (4) How are we identifying and mitigating any new cyber-related risks introduced by AI use cases? (5) Are we developing AI in accordance with putative legislative and regulatory expectations?

Step 3: Continue to Monitor "Mission Critical" Risks and Keep Records. Consistent with directors' fiduciary duties with respect to overseeing the company's "mission critical" risks, it may benefit directors to be educated about the company's AI risk exposure, as well as potential business and financial impacts. For purposes of establishing a solid oversight record, relevant topics would ideally be documented in board meeting agendas and resulting discussion recorded in meeting minutes.

At the board level, policies can be used to ensure that underlying data and AI-technology is evaluated like any other asset of the company. For more details on director duties and recommended precautions, see our Legal Update, "Generative Artificial Intelligence and Corporate Boards: Cautions and Considerations".

Step 4: Evaluate the Need for AI-Related Substantive Trainings and/or Experts. With an ever-evolving technological landscape, use cases and opportunities, the world of AI is far from static. As AI becomes more critical to the business, it is important that boards be kept generally apprised of any key corresponding risks. While this should not require a detailed technological understanding of all things AI, a certain level of understanding may be helpful to fully understanding the risks. If a board does not have board members with AI experience, it may consider retaining third party advisors to support the board, in addition to any relevant education that may be able to be provided in-house, either through management briefings or by elevating leaders proficient in AI-related issues to the board. In cases where AI is integral to the company's business and no current board members are sufficiently versed in the field, boards may consider adding a director with the relevant substantive experience and skillset.

Step 5: Be Proactive with Compliance. It is prudent for top-level management and boards to understand use cases for AI and associated risks for the company, and to develop an appropriate governance framework that adequately addresses the relevant legal requirements. As AI-use cases continue to rapidly advance, companies that streamline effective AI-governance early on will be better positioned to move quickly to integrate new use cases while also complying with the AI-related laws that will come into effect.

Contact Us

Feel free to contact any of the below listed authors, editors or your regular Mayer Brown attorney contacts.

Editorial Board

Martha McGarry
Partner, New York
+1 212 506 2305
mmcgarry@mayerbrown.com

Andrew Noreuil
Partner, Chicago
+1 312 701 8099
anoreuil@mayerbrown.com

Camila Panama
Partner, New York
+1 212 506 2764
cpanama@mayerbrown.com

Authors

Gail Levine
Partner, Washington DC
+1 202 263 3335
glevine@mayerbrown.com

Nikolay Mizulin
Partner, Brussels
+32 2 551 5967
nmizulin@mayerbrown.com

Dr. Andrea Pomana
Partner, Brussels / Frankfurt
+32 2 551 5980 / +49 69 7941 0
apomana@mayerbrown.com

Dominique Shelton Leipzig
Partner, Los Angeles
+1 213 229 5152
dsheltonleipzig@mayerbrown.com

William Stallings
Partner, Washington DC
+1 202 263 3807
wstallings@mayerbrown.com

ACKNOWLEDGEMENTS

The authors would like to thank Emanuil Stoichev, Alexander Dussault and Danielle Marino, Associates at Mayer Brown, and Andrew Stanger, Professional Support Lawyer at Mayer Brown, for their assistance with this *M&A, Activism and Corporate Governance Quarterly Review.*

Mayer Brown is a distinctively global law firm, uniquely positioned to advise the world's leading companies and financial institutions on their most complex deals and disputes. With extensive reach across four continents, we are the only integrated law firm in the world with approximately 200 lawyers in each of the world's three largest financial centers—New York, London and Hong Kong—the backbone of the global economy. We have deep experience in high-stakes litigation and complex transactions across industry sectors, including our signature strength, the global financial services industry. Our diverse teams of lawyers are recognized by our clients as strategic partners with deep commercial instincts and a commitment to creatively anticipating their needs and delivering excellence in everything we do. Our "one-firm" culture—seamless and integrated across all practices and regions—ensures that our clients receive the best of our knowledge and experience.

Please visit mayerbrown.com for comprehensive contact information for all Mayer Brown offices.

Mayer Brown is a global services provider comprising associated legal practices that are separate entities, including Mayer Brown LLP (Illinois, USA), Mayer Brown International LLP (England), Mayer Brown (a Hong Kong partnership) and Tauil & Chequer Advogados (a Brazilian law partnership) (collectively the "Mayer Brown Practices") and non-legal service providers, which provide consultancy services (the "Mayer Brown Consultancies"). The Mayer Brown Practices and Mayer Brown Consultancies are established in various jurisdictions and may be a legal person or a partnership. Details of the individual Mayer Brown Practices and Mayer Brown Consultancies can be found in the Legal Notices section of our website. "Mayer Brown" and the Mayer Brown logo are the trademarks of Mayer Brown.

© 2023 Mayer Brown. All rights reserved. Attorney Advertising. Prior results do not guarantee a similar outcome.