Radical New Burdens for Marginal Benefit: Comment of the Global Antitrust Institute on Proposed HSR Rule Amendments

Abbott B. Lipsky, Jr., Antonin Scalia Law School, George Mason University

Alexander Raskovich, Antonin Scalia Law School, George Mason University

Bruce H. Kobayashi, Antonin Scalia Law School, George Mason University

John M. Yun, Antonin Scalia Law School, George Mason University

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RADICAL NEW BURDENS FOR MARGINAL BENEFIT:
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The Global Antitrust Institute ("GAI") submits this comment to the U.S. Federal Trade Commission ("FTC") in response to the FTC's Notice of Proposed Rulemaking ("NPRM"), "Premerger Notification; Reporting and Waiting Period Requirements."[1] This proposal would (1) amend the premerger notification form required pursuant to the Hart-Scott-Rodino Antitrust Improvements Act[2] ("HSR Form") and (2) implement the Merger Filing Fee Modernization Act of 2022.[3] This comment is based on the GAI's extensive experience and expertise in competition law and economics.[4]

We focus our discussion on the likely effects of the proposed changes to the HRS Form. The agencies' proposal to amend the HSR Form will, if implemented, substantially increase the burden on all merging parties to report their transactions, regardless of whether the transaction poses an anticompetitive risk. In Section I we review the market for corporate control and the benefits it can have for effective firm management, allocative efficiency of economic resources, and consumer welfare. In Section II we explain how, contrary to the FTC's view, the proposed changes will significantly increase the burden imposed on filing parties. This will impede the market for corporate control and consequently reduce productivity and inhibit innovation in other markets. In Section III we highlight potential conflicts between the proposed amendments to the HSR filing requirements and the Administrative Procedures Act.

I. The Market for Corporate Control

For years, scholars and policymakers around the world have recognized and accepted the market for corporate control as a phenomenon driving M&A strategy and decision-making.[5] The

[1] 88 FR 42178, June 29, 2023. Published in the *Federal Register* as RIN 3084-AB46.

[2] Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a.

[3] Merger Filing Fee Modernization Act of 2022, enacted as part of the Consolidated Appropriations Act, 2023, Pub. L. 117–328, 136 Stat. 4459 (Dec. 29, 2022).

[4] The GAI is a division of George Mason University's Antonin Scalia Law School and reports to the Dean of the Law School. In support of its mission, the GAI draws upon the independent expertise of the Law School faculty including Bruce H. Kobayashi, Paige V. and Henry N. Butler Chair in Law & Economics and former Director of the Bureau of Economics, FTC; Abbott B. Lipsky, Jr., Adjunct Professor, Director of Competition Advocacy for the GAI, former Acting Director of the Bureau of Competition, FTC, and former Deputy Assistant Attorney General for Antitrust, U.S. Department of Justice; Dr. Alexander Raskovich, the GAI's Director of Research; and John M. Yun, Associate Professor and former Acting Deputy Assistant Director, Bureau of Economics, FTC. The GAI is grateful for the generous contributions from the individuals, foundations, and corporations that enable the GAI to carry out its mission. Its finances are managed through the George Mason University Foundation, Inc., which is a 501(c)(3) corporation established to support the activities of George Mason University. More information may be found at https://gai.gmu.edu. The GAI gratefully acknowledges the substantial contributions to this comment by Scalia Law students Kendall Alford, Megan Dill, Anthony Cirri and Emily Polinski.

[5] Noah Joshua Phillips, Commissioner, Fed. Trade Comm'n, Competing for Companies: How M&A Drives Competition and Consumer Welfare, Opening Keynote at The Global Antitrust Economics Conference Concurrences & NYU Stern, at 6-7 (May 31, 2019) (transcript available on FTC public website https://www.ftc.gov/news-events/news/speeches/competing-companies-how-ma-drives-competition-consumer-welfare) (noting that corporate law has embraced this lesson more enthusiastically; hereinafter Phillips Keynote).

market for corporate control is best understood as competition among teams for the right to manage corporate assets.[6] The market operates when a relatively poorly managed firm, signaled by a lower or undervalued stock price, becomes an attractive target for acquisition by those who believe they can better manage the firm and increase its value.[7]

The market for corporate control creates value through (1) increasing the effectiveness of management, thereby improving resource allocation to the benefit of shareholders, and (2) commonly increasing the corporation's competitiveness in the market, thereby also benefiting consumers. The gains created by the market for corporate control are not dependent on anticompetitive reductions in output or increases in market share.[8] The market can (3) increase industry innovation by reducing barriers to entry for startups, and (4) encourage deconsolidation as a form of effective reallocation of resources.

A. *Effective Management*

As first articulated by Manne in 1965, "the potential return from a successful take-over and revitalization of a poorly run company can be enormous."[9] A 2019 study conducted by Gallup found that 70 percent of firm productivity depends on the quality of management.[10] Further, business innovation spurred by new management (e.g., new pricing schemes, integration, etc.) is essential to a thriving marketplace.[11] The market for corporate control can increase efficiencies, spur innovation, and create value in the market by allowing firms to compete through effective management. A market for corporate control increases the pool of bidders and the competitiveness of bidders within the pool.

B. *Consumer Welfare*

It is important to recognize that while the market for corporate control generates value for the company and shareholders, there is also empirical evidence that consumers receive gains from these improved outcomes.[12] Firms profit primarily by providing value to consumers – by competing to offer superior products at better prices. Therefore, new management seeking to create more value for shareholders commonly seek improvements in efficiency, resulting in increases in

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[6] Henry G. Manne, *Mergers and the Market for Corporate Control,* 73 J. POL. ECON. 110, 112 (1965). As first outlined by Manne, the basic idea of the market for corporate control was: "that the control of corporations may constitute a valuable asset; that this asset exists independent of any interest in either economics of scale or monopoly profits; that an active market for corporate control exists; and that a great many mergers are probably the result of the successful working of this special market." *Id.* at 112.

[7] A recent example is provided by activist investor Elliott Management's letter to the board of eBay, Inc., outlining why the stock was undervalued and how it could lead it to be valued 75 to 100 percent higher. *See* Press Release, Elliott Management Sends Letter to Board of Directors of eBay, BUSINESS WIRE (January 22, 2019), https://www.businesswire.com/news/home/20190122005513/en/Elliott-Management-Sends-LetterBoard-Directors-eBay.

[8] Michael C. Jensen & Richard S. Ruback, *The Market for Corporate Control: The Scientific Evidence*, J. FIN. ECON. 11 (1983) ("[The] gains created by corporate takeovers do not appear to come from the creation of market power.")

[9] Manne, *supra* note 6, at 113.

[10] JIM CLIFTON & HIM HARTER, IT'S THE MANAGER (Gallup 2019). *See also* Sam Walker, The Economy's Last Best Hope: Superstar Middle Managers, WALL STREET JOURNAL (Mar. 24, 2019), https://www.wsj.com/articles/the-economys-last-best-hope-superstar-middle-managers-11553313606 (quoting Gallup calling this conclusion "the single most profound, distinct and clarifying finding in its 80-year history.").

[11] JIM CLIFTON & HIM HARTER, *supra* note 10.

[12] Phillips Keynote, *supra* note 5.

output, profitable reductions in prices, better quality, and profitable opportunities for increased innovation.

C. Startup Innovation

Startups can help drive innovation and dynamic growth, and M&A activity can foster competition by providing a critical exit strategy for startups. Startups are often cited as examples of why antitrust enforcers need to intervene to prevent incumbent firms from gobbling up potential competitors.[13] Given that the vast majority of startups fail (primarily due to various managerial weaknesses),[14] acquisitions represent a critical exit path that spurs entrepreneurs to create startups by reducing the risks of failure. The adage that "barriers to exit are barriers to entry" illustrates an important point that the harder it is to exit, the higher the cost of entering an industry in the first place.[15] Reducing the availability of acquisition as an exit path can "deter not only innovation but the investment pipeline on which that innovation depends."[16]

D. Deconsolidation and Spin-Offs

A key benefit of the market for corporate control is facilitating the movement of resources to their highest-valued uses.[17] However, there is no ex-ante requirement that those resources be located within the same corporate domain. Such movement is frequently manifested through deconsolidation and spin-offs.[18] When the market for corporate control exerts pressure on a large company that is trying to manage too many business segments, deconsolidation through a spin-off may allow both the spun-off business and the retained units to play to their respective strengths and create additional value.

E. Implications for Antitrust

The market for corporate control has important implications for the appropriate scope and content of antitrust rules, because impairing the proper functioning of the market would itself degrade competition. If the goal of antitrust reform is to promote competition, then antitrust agencies should seek to take into account the adverse effects on market mechanisms, such as the market for corporate control, that higher compliance costs may engender. As engaging in M&A

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[13] *See, e.g.*, Note by the United States, *Start-ups, killer acquisitions and merger control*, OECD/DAF/COMP/WD (2020)23 (June 11, 2020), , https://www.ftc.gov/system/files/attachments/us-submissionsoecd-2010-present-other-international-competition-fora/oecd-killer_acquisiitions_us_submission.pdf.

[14] *See, e.g.,* The Top 20 Reasons Startups Fail, CB INSIGHTS (Feb. 2, 2018), https://www.cbinsights.com/research/startup-failure-reasons-top/.

[15] *See, e.g.,* STEPHEN MARTIN, INDUSTRIAL ORGANIZATION IN CONTEXT, 128-29 (Oxford U. Press 2009) (stating "Risk-adverse potential entrants will require a greater assurance of profitability before coming into a market, the greater the extent to which entry involves making sunk investments. In this sense 'barriers to exit are barriers to entry.'").

[16] Phillips Keynote, *supra* note 5 at 6-7.

[17] *Id.*

[18] *See, e.g.*, Mitigating Human Capital Risk and Unlocking Value From Spin-Offs, INSTITUTE FOR MERGERS, ACQUISITIONS & ALLIANCES (Oct. 13, 2016) https://imaa-institute.org/mitigating-human-capital-risks-unlocking-value-spin-offs/ ("Spin-offs . . . are increasingly popular as companies reexamine their business strategies and search for additional ways to boost shareholder returns"). *See, e.g.*, Analysis: YTD Spinoff Deal Count Is the Highest Since 2011, BLOOMBERG LAW ANALYSIS (Nov. 15, 2021) https://news.bloomberglaw.com/bloomberg-law-analysis/analysis-ytd-spinoff-deal-count-is-the-highest-since-2011 (finding that as of November 2021, there had been 205 spinoff transactions announced, the highest count since 2011 which had 227 spin-off deal announcements).

activities can be a high-risk, expensive proposition for any company, adopting HSR (and other) regulations that increase transaction costs for merging parties can have a chilling effect on those activities and therefore undermine competition to improve the management of firms.

This is not to say that the market for corporate control always functions perfectly or that M&A activity can never harm competition. However, unduly burdensome HSR regulation will distort the clear value-creation benefits, for both consumers and shareholders alike, of the market for corporate control, causing the HSR process to conflict with its intended purpose and with that of the antitrust laws more generally.

II. The Proposed Changes Increase Burdens on Parties

The proposed amendments require merging parties to submit many additional documents when filing their HSR Form. Providing additional information is burdensome for potentially merging parties. The additional burden may be worthwhile if the information thereby elicited allows the Agencies to resolve investigations into competitively benign transactions more quickly, thereby lessening resource costs for both the Agencies and the parties on net. On the cost side, the additional filing burdens discourage small transactions regardless of their anticompetitive potential. The benefits of the increased HSR filing burdens do not outweigh the costs, however.

The major cost is that procompetitive or easily cleared mergers may be discouraged from ever taking place due to the resource-intensive nature of providing such documents. In FY 2021, there were only 65 Second Requests issued out of 3,413 filed transactions (approximately 1.9 percent of all transactions).[19] While resources would be saved by asking for documents up front from approximately 2% of transactions that will require a Second Request, it would be more costly for approximately 98% of mergers up-front. In this section, we highlight the additional burden that some of the key proposals impose on filing parties.

A. *Transaction Details/Agreements, Non-Transaction Specific Agreements, and Draft Item 4(c) Documents*

The proposed amendments will require all filing parties to produce drafts of Item 4 documents, as well as ordinary course reports that relate to competition.[20] There are seemingly few benefits to requesting additional documents on agreements up-front. In addition to the 4(c) documents submitted through the pre-merger notification process, the agencies can request additional information from the parties on a voluntary basis so they can conduct their initial thirty-day investigations.[21] Although these additional productions are voluntary, filing parties are highly incentivized to produce them in order to avoid the issuance of a resource- and burden-intensive Second Request.[22] Further, agency staff have a history of working with filing parties in "the pull

[19] Fed. Trade Comm'n and U.S. Dep't. of Justice Antitrust Division, Hart-Scott-Rodino Annual Report: Fiscal Year 2021, https://www.ftc.gov/system/files/ftc_gov/pdf/p110014fy2021hsrannualreport.pdf

[20] 88 Fed. Reg. 42178, at 42213-14.

[21] Fed. Trade Comm'n, Guidance for Voluntary Submission of Documents During the Initial Waiting Period, https://www.ftc.gov/enforcement/premerger-notification-program/hsr-resources/guidance-voluntary-submission-documents ("Staff generally has requested these documents and information in a 'voluntary request letter' or 'access letter' during the initial waiting period and prior to any issuance [of a Second Request]").

[22] SecondSight Law, Comment Letter on the Notice of Proposed Rulemaking on Premerger Notification; Reporting and Waiting Period Requirements Under Section 7A(d) of the Clayton Act, at 2-3 (August 27, 2023), https://www.regulations.gov/comment/FTC-2023-0040-0488.

and refile" process to allow staff additional time to work with merging entities to get all information they believe they need to make their decision regarding a Second Request.[23]

B. *Competition Narratives*

The proposed amendments also ask for merging parties to weigh in on antitrust concerns via narrative responses. Both parties would be required to explain the ownership structure of the parties, business operations, transaction rationale, horizontal competitive effects, vertical and horizontal supply relationships, and potential labor market overlaps.[24] This is a "fundamental shift" in the HSR process, placing more of the fact-finding burden on parties and less on agencies.[25] As a result of this requirement, parties will have to expend significant additional resources for preparations for meeting HSR burdens ex-ante (possibly including extensive additional antitrust counseling), reducing their incentive to enter the deal at all.[26]

Additionally, the introduction of these narratives could lead to a higher rate of rejection of HSR filings given the much wider scope for potential disputes regarding compliance.[27] Regardless, the requirement of up-front submissions of competition narratives would shift more of the burden of discovering competitive effects to the parties rather than the agencies, when it is highly unlikely that such narratives will be of any value except in a very small category of cases.

C. *Prior Acquisitions*

The proposed amendments would also require filing parties to report all prior domestic acquisitions, in industries where the merging parties have horizontal overlaps, across a 10-year period irrespective of transaction size.[28] For most parties, identifying all prior transactions that fit these criteria will involve significant engagement of company personnel and legal counsel. With such a breadth of time covered by the HSR requirements, it is easy to imagine a scenario where the personnel with relevant "institutional knowledge" have left the company.

Most pointedly, this amendment will drastically increase the costs associated with compiling a compliant HSR filing with little to no added benefit to the agencies' investigative work. The FTC cites acquisitions by "five of the largest technology companies" as evidence that the change is necessary to identify potential issues or roll-up strategies.[29] However, it is unlikely that the agencies will gain any insights from the vast majority of parties who will have to report this information that is not already obtained through the current HSR reporting requirements.

D. *Identification of Co-Investors, General Partners/Creditors/Other Influential Entities*

The proposed changes would require the acquiring party to disclose all minority stakeholders, including limited partners, that hold 5% of the voting securities or non-corporate

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[23] *Id.*
[24] 88 Fed. Reg. 42178, at 42214.
[25] The Impact of the FTC's Proposed Changes to Hart-Scott-Rodino Filing Requirements, SIDLEY (JULY 10, 2023), https://www.sidley.com/en/insights/newsupdates/2023/07/the-impact-of-the-ftcs-proposed-changes-to-hsr-filing-requirements.
[26] *Id.*
[27] *Id.*
[28] 88 Fed. Reg. 42178, at 42202-04.
[29] *Id.* at 42203.

interests of the (i) acquiring entity, (ii) any entity directly or indirectly controlled by the acquiring entity, (iii) any entity that directly or indirectly controls the acquiring entity, and (iv) any entity within the acquiring person that has been or will be created in contemplation of, or for the purpose of effectuating, the transaction.[30] These additional disclosure requirements could cause a substantial decrease in fundraising and deal volume, and they disproportionately impact private equity.[31]

These changes discourage investments unrelated to the transaction under review as individuals may not want their identities disclosed to the FTC/DOJ and would be reluctant to provide funding to future transactions. Therefore, the proposed disclosure requirements substantially burden transacting parties and may also have the effect of depriving consumers and the economy of potentially pro-competitive transactions.

Additionally, the identities of limited partners are considered highly confidential among investment firms. The proposed changes will force transacting companies to figure out ways to appease both the Agencies and investment firms who may be uncomfortable disclosing their identity. The new requirements are so broad that companies will be forced to expend substantial time and resources navigating the "direct or indirect" "control or controlled by" tests when determining which minority stakeholders, they will need to disclose.

III. Administrative Concerns About the Proposed Revisions

It is unclear whether the Agencies' proposals are necessary to increase the "efficiency" of the pre-merger screening process. The agencies' proposal raises potential issues under the Administrative Procedures Act because the substantial costs parties must bear to comply with the proposed changes to the HSR form do not nearly justify any benefits obtained by requiring the additional information.

Most of the transactions reported to the agencies do not raise anticompetitive concerns that justify the increased burden required to comply with the proposed changes. In 2021 alone, 3,520 merger transactions were reported to the agencies under the HSR act.[32] Of these reported transactions, the agencies required additional information in approximately two to four percent of reported transactions. Further, the agencies collectively brought thirty-two merger enforcement challenges - approximately one percent of the total number of transactions reported.[33] These statistics demonstrate that since the vast majority of transactions reported are not anticompetitive, imposing the additional burdens of the proposed amendments on *all* filed transactions would outweigh any potential benefits aimed at shifting the burden of identifying anticompetitive mergers to the parties themselves. This is particularly so when that burden is sufficient to impede the market for corporate control, with resulting adverse economic impact on that market and on others in which the transacting parties may compete.

The Agencies typically have thirty days to review the HSR Form and all supporting documents and to identify transactions that warrant an in-depth investigation into the transaction's

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[30] *Id.* at 42188.
[31] Proposed HSR Changes: What Fund Manager Need to Know, SCHULTE ROTH + ZABEL (July 14, 2023) https://www.srz.com/resources/proposed-hsr-changes-what-fund-managers-need-to-know.html.
[32] Fed. Trade Comm'n and U.S. Dep't. of Justice Antitrust Division, Hart-Scott-Rodino Annual Report: Fiscal Year 2021, https://www.ftc.gov/system/files/ftc gov/pdf/p110014fy2021hsrannualreport.pdf.
[33] *Id.* (reporting that the FTC challenged 18 transactions and the DOJ challenged 14 in 2021).

competitive effects. Given this short time period, it is not feasible for the agencies to review copious amounts of documentation, so the additional information elicited by the new filing burden is of very limited value to the Agencies.

An agency must have sound reasons for changing a rule. Agencies must demonstrate that they have examined the available data and must offer a cogent explanation for the change, identifying a rational connection between the facts found and the choice made.[34] Considering the statistics reported by the agencies, the available data does not support an increase in the burden on all filing parties. Thus, the new HSR rules could be subject to challenge under the Administrative Procedures Act on various grounds.

[34] *Motor Vehicle Manu. Ass'n. v. State Farm*, 463 U.S. 29 (1983).