The Mergers & Acquisitions Review

Fifth Edition

Editor
Simon Robinson

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Chapter 62

UNITED STATES

*Richard Hall and Mark Greene**

I OVERVIEW OF RECENT M&A ACTIVITY

The United States M&A environment still faces significant challenges as a result of the 2008 financial collapse, but the level of activity continued to increase through 2010. M&A activity still remains below its highest pre-credit crisis levels. However, during the 12 months ended 31 December 2010, US M&A volume exhibited an increase.[1] US M&A activity by dollar volume increased by 18.5 per cent from the previous period, reaching $1 trillion in total deal value. Moreover, the number of transactions increased by 2.9 per cent, with over 10,000 announced transactions.[2] Beginning in the second quarter of 2010, leveraged buyout ('LBO') activity re-emerged, rising to 15 per cent of the total deal value for the year ended 31 December 2010, a level not seen since the end of 2007.[3]

US M&A activity in the first quarter of 2011 increased nearly 117.3 per cent in total deal value over the first quarter of 2010, reaching $451.5 billion.[4] In the first quarter of 2011, however, LBO activity reversed course, capturing only 6.1 per cent of total

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1 Mergers & Acquisitions Review, Full Year 2010, Legal Advisors, Thomson Reuters (2011), http://online.thomsonone.com.

2 Id.

3 Mergers & Acquisitions Review, First Quarter 2011, Legal Advisors, Thomson Reuters (2011), http://online.thomsonone.com.

4 Id.

US-targeted M&A activity.[5] The US share of global M&A volume has remained steady since 2009, with approximately 34 per cent of announced deals by dollar volume.[6]

Much of the increase in US deal activity is attributable to a general strengthening in the US economy, even in some of the hardest-hit industries,[7] and depressed equity prices. These factors have provided shopping opportunities for buyers (primarily strategic) who have available unrestricted cash and hope to capitalise on expected economic recovery and growth. This has led to an unusually high number of hostile bids as acquirers attempt to exploit the weakened financial positions of their targets, and targets resist what they perceive to be insufficient offers.[8]

While the credit markets have recovered significantly, obtaining acquisition financing remains challenging. Relative to pre-credit crisis levels, this environment has resulted in lower levels of private equity activity and lower debt to equity ratios in the completed transactions.[9] In addition, financing-related issues have led to greater use of stock consideration among strategic acquirers, as well as more creative methods of reducing cash consideration, including earn-outs. Financing-related issues, combined with volatility in the equity markets, have sellers focused on certainty of closing and new developments with financing outs, such as utilising reverse break-up fees.

II GENERAL INTRODUCTION TO THE LEGISLATIVE M&A FRAMEWORK

M&A in the US is governed by a dual regulatory regime, consisting of state corporation laws (for example, the Delaware General Corporation Law) and the federal securities laws (primarily, the Securities Act of 1933 and the Securities Exchange Act of 1934). The Securities and Exchange Commission ('SEC') is the regulatory agency responsible for administering the federal securities laws. The federal securities laws, including proxy rules governing the solicitation of approval of shareholders of a publicly held target company, apply in the context of a merger. The federal securities laws relating to tender offers apply in the context of an offer to purchase shares of a publicly held target company. In addition to these laws, an acquisition or merger will implicate fiduciary duties, as developed and applied in the state of incorporation of the target company.

Unlike certain other jurisdictions, the US patchwork of federal and state regulation of acquisitions is not focused on the substantive question of regulating changes of control

5 Id. (notable LBOs for the first quarter of 2011 include Blackstone's $9.4 billion acquisition of Centro Properties Group and Apax Partners $3.8 billion buyout of Smiths Medical).

6 Mergers & Acquisitions Review, Full Year 2010, Legal Advisors, *supra* note 1.

7 Nick Bunkley, G.M. Earns $865 million as Sales Rise 40 Percent, N.Y. Times, 17 May 2010, www.nytimes.com/2010/05/18/business/18auto.html?ref=business.

8 Michael Erman, Hostile Bids Set to Rise Again in 2011, Reuters (6 January 2011) (more than $260 billion in hostile bids were launched in 2010, doubling the 2009 total).

9 See Janet Morrissey, Private Equity Deals: Posed for a Comeback?, (15 October 2010) (private equity firms remain under pressure to exit investments made before the 'Credit Crisis' and to utilise capital, although such firms are still waiting for market conditions to stabilise).

of target companies. Rather, US regulation focuses on disclosure, ensuring that common shareholders of target corporations are given the time and information required to make a fully informed decision regarding the acceptance of a tender offer or vote in favour of a merger.

Under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 ('the HSR Act'), an acquirer is normally required to make a filing with US antitrust authorities prior to completing the acquisition. Generally, the HSR Act requires notification if the size of the transaction exceeds $66 million (adjusted annually for inflation); the requirement was increased from $63.4 million in 2010.[10]

The US does not have a general statutory review process governing foreign investment in the US. Under the Exon-Florio Amendment to the Defence Production Act, however, the President, through the Committee on Foreign Investment in the US ('CFIUS'), has the power to investigate, prohibit or unwind transactions involving investments by non-US entities that threaten to impair national security.[11] The 1992 Byrd Amendment also requires CFIUS to conduct a thorough Exon-Florio review whenever CFIUS receives notice of a non-US government-led takeover of a US business that may affect national security.[12]

There are also additional industry-specific statutes that may require advance notification of an acquisition to a governmental authority. Examples of sensitive industries include airlines, broadcast licences, electric and gas utilities.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

i 'Poison pill' jurisprudence

Yucaipa American Alliance Fund II, L.P. v. Riggio et. al.

In *Yucaipa American Alliance Fund II, LP v. Riggio et al*, the Delaware Court of Chancery upheld Barnes & Noble's 'poison pill,' which is triggered when a shareholder acquires over 20 per cent of the company's outstanding stock.[13]

The court upheld the 'poison pill' to ensure that stockholders would receive the benefit of a control premium, preventing billionaire investor Ronald Burkle, the potential acquirer, from taking control of the company through a 'creeping acquisition.'[14] In response to corporate activities led by Leonard Riggio, the founder and largest shareholder of Barnes & Noble, such as the acquisition of Barnes & Noble College Booksellers, Burkle voiced his displeasure with the company's corporate direction and

10 Updates to the Hart-Scott-Rodino Antitrust Improvements Act of 1976, Fed. Trade Comm'n, http://www.ftc.gov/opa/2011/01/claytonsimon.shtm.

11 50 US C. app. Section 2170.

12 Pub. L. No. 102-484 (1992).

13 *Yucaipa Am Alliance Fund II, LP v. Riggio et al*, 1 A.3d 310, 312 (Del. Ch. 2010) (Notably, the poison pill also is triggered when two or more shareholders enter into an arrangement to acquire, hold, vote or dispose of any voting securities of the company).

14 Yucaipa, 1 A.3d at 313.

stated his intent to buy up to a 50 per cent stake in the company, along with proposing additional M&A activity and a joint venture with Hewlett Packard.[15]

In *Yucaipa*, the court applied existing 'poison pill' jurisprudence, concluding that 'when a pill both prevents a tender offer and unfairly tilts the electoral playing field against an insurgent [...] this court should not hesitate to enjoin its operation'.[16] In *Yucaipa*, the court found that the pill was reasonable and not preclusive because it provided Burkle an opportunity to prevail in a proxy contest as the pill likewise capped Riggio from increasing his interest in the company.[17] Interestingly, in this case the pill was upheld, in part, to protect the rights of the shareholder to receive a control premium, rather than protect control of the corporation itself. While the *Yucaipa* ruling indicates the strength of 'poison pills,' its impact outside the context of protecting control premium remains unclear.

Air Products and Chemicals, Inc v. Airgas, Inc

In *Air Products and Chemicals, Inc v. Airgas, Inc*, the Delaware Court of Chancery upheld a 'poison pill' used to thwart Air Products' $5.8 billion offer to acquire Airgas.[18] The duel between Air Products and Airgas spanned more than 16 months and was the subject of much public debate. Although John McGlade, the CEO of Air Products, initially engaged management of Airgas to inquire into its interest in a friendly combination, these relations quickly chilled as Airgas' board rebuffed the invitation as clearly inadequate and opportunistic based on the company's depressed stock price. Due to Airgas' unwillingness to meet and discuss a combination, Air Products elected to engage Airgas' shareholders directly through a hostile tender offer.

The central issue in Air Products is whether a board:

> *'acting in good faith and with a reasonable factual basis for its decision, when faced with a structurally non-coercive, all-cash, fully financed tender offer directed to the shareholders of corporation, [may] keep a 'poison pill' in place so as to prevent the stockholders from making their own decision about whether they want to tender their shares' or, more simply, 'who gets to decide when and if the corporation is for sale?'*[19]

The Court found that the power to 'defeat an inadequate hostile tender offer ultimately lies with the board,' so long as the board meets its burden under Unocal.[20] Airgas' board feared that opportunistic shareholders would tender their shares to Air Products, even though independent advisers for the target provided information indicating a much higher valuation. Moreover, at trial, Airgas acknowledged that its shareholders were well advised and knowledgeable about the terms of the tender offer and the position of the

15 Id. at 317.

16 Id. at 337.

17 Id. at 313.

18 *Air Prods and Chems, Inc v. Airgas Inc*, 16 A.3d. 48 (Del. Ch. 2011).

19 Air Prods., 16 A.3d. at 54.

20 Id. at 55.

company's board.[21] Nonetheless, the board felt it necessary to defend its pill, ensuring that its shareholders could not elect to sell.

Although Chancellor Chandler's opinion suggests he is uncomfortable with his decision, Chandler upheld the company's pill: '[w]hile corporate democracy is a pertinent concept, a corporation is not a New England town meeting; directors, not shareholders, have responsibilities to manage the business and affairs of the corporation.'[22] The Court found that Airgas' board articulated a legitimate threat to the corporation: in light of information provided by the company's board and independent advisers, its shareholders may tender their shares anyway. Thus, the Court found that the use of a 'poison pill' to protect the company from the shareholders' ill-advised tendering of their shares was a proportional and reasonable response to the threat posed by the tender offer.

eBay Domestic Holdings, Inc. v. Newmark, C.A.

In eBay Domestic Holdings, Inc v. Newmark, CA, the Delaware Court of Chancery struck down Craigslist's 'poison pill' and right of first refusal.[23] This is the first time a Delaware court reviewed the validity of a 'poison pill' installed by a closely-held company. Craigslist is a privately held company with three shareholders: Craig Newmark ('the founder'); James Buckmaster ('CEO'); and eBay. In 2004, eBay purchased a 28 per cent interest in Craigslist for $32 million upon the sale by Philip Knowlton, one of the founding members of Craigslist.[24] Knowlton sold his shares because the founder and CEO, in accordance with their view of the corporate culture, refused to make business decisions that sought to maximise profits.

In response to the sale by Knowlton to eBay, the founder and CEO entered into a voting agreement, whereby both agreed to vote their shares in a manner that guaranteed each would continue to be reelected to the Craigslist board. eBay, on the other hand, entered into a relationship with Craigslist with the intent to acquire the company outright. As eBay's management realised it would be unable to entice the other stakeholders to sell, eBay, in compliance with the terms of the stock purchase agreement, sought opportunities to compete with Craigslist. Because Craigslist does not operate solely as a profit-maximizing enterprise, the founder and CEO believed eBay's actions and aggressive behaviour threatened the corporate culture of Craigslist. Thus, the founder and CEO of Craigslist adopted defensive measures, including a staggered board, rights plan and a right of first refusal ('ROFR').[25]

The court, applying the 'business judgment rule', allowed Craigslist's use of a staggered board. The court found that the use of a staggered board was a reasonable

21 Id. at 106.

22 Air Prods., 16 A.3d. at 102 (quoting *Paramount Commc'ns, Inc v. Time Inc*, 571 A.2d 1140 (Del. 1990)).

23 *eBay Domestic Holdings, Inc v. Newmark, et al*, 16 A.3d 1 (Del. Ch. 2011).

24 Knowlton received $16 million in consideration for the transaction, while the Founder and CEO of Craigslist each received $8 million for their cooperation with the transaction and certain minority investor protections.

25 eBay, 16 A.3d at 20.

response to the risk eBay may misuse confidential information in its competitive endeavours.[26]

The ROFR defence allowed Craigslist to dilute eBay's ownership and preclude eBay from nominating one of the company's three directors. Shareholders electing to offer a ROFR to the company were granted one additional share for every five shares owned.[27] When triggered, the ROFR would cause dilution of the non-electing shareholder's interest. This was detrimental to eBay, as the founder and CEO were certain to make the election and eBay would choose to keep their shares unencumbered.

The 'poison pill' prevented, in effect, eBay's ability to transfer its entire stake to a third party. Although the Court acknowledged 'poison pills' can be used to protect corporate assets, the Court refused to accept a pill designed to protect future corporate culture.[28] The founder and CEO argued that once they were incapacitated and their shares passed to heirs, the valuable 'Craigslist culture' would be lost. The Court found that the company needed to make a specific showing that the 'Craigslist culture' will at some point provide shareholder value in order to justify protecting the future asset with a defence mechanism.[29] Although, in this case, the rights plan was rejected by the Court, the opinion suggests closely-held companies can implement pills if proper procedures and protections are put in place.

Freeze-out jurisprudence

In the case *In Re CNX Gas Corporation Shareholders Litigation*, Vice Chancellor Laster of the Delaware Court of Chancery sets forth a unified standard of review for a controlling stockholder's two-step freeze-out transaction.[30] CNX Gas Corp ('the CNX') was a majority-owned subsidiary of CONSOL Energy Inc. ('CONSOL'), which had been publicly traded since its IPO in 2005. T Rowe Price, however, held a significant block of CNX's publicly-held shares.[31]

In connection with the two-step freeze-out transaction, CONSOL negotiated an agreement with T Rowe Price to tender its shares of CNX at a set price.[32] As a result of the tender offer, CNX formed a special committee of independent directors to evaluate CONSOL's tender offer; however, the special committee did not have authority to negotiate with CONSOL.[33] Given the special committee's inability to negotiate with CONSOL and the agreement with T Rowe Price, CONSOL's tender offer would most likely be successful. Thus, minority shareholders moved for a preliminary injunction to block the tender offer.

26 Id. at 36 (eBay pursued a competitive endeavour with the website www.kijiji.com).

27 Id. at 24.

28 Id. at 34.

29 eBay, 16 A.3d at 34.

30 *In Re CNX Gas Corp S'holders Litig*, No. 5377 VCL, 2010 WL 2291842 *1, 1 (Del. Ch. 5 July 2010).

31 Barry Bryer, CNX and the Unified Standard, The Deal Magazine (10 September 2010).

32 *In re CNX*, No. 5,377 VCL, 2010 WL 2291842 at *3-4.

33 Id. at *5-6.

In re CNX is important to practitioners because it endorsed a 'unified standard' of review for two-step freeze-out transactions initiated by a controlling shareholder. The court held that a two-step tender offer led by a controlling shareholder will be reviewed under the business judgment standard of review only if the following two conditions are met: (1) the tender offer must be negotiated and recommended by a special committee of independent directors; and (2) a majority of unaffiliated shareholders vote affirmatively for the tender.[34]

Chancellor Laster found the business judgment standard inappropriate in this case because the special committee did not have requisite authority to negotiate the tender offer and the agreement with T Rowe Price raised questions about the ability of the minority shareholders to have a real voice in the transaction.[35] Thus, Chancellor Laster applied the entire fairness standard of review and granted the injunction.[36]

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

i Deutsche Börse bid for NYSE and London Stock Exchange and Toronto Stock Exchange merger

One of the most closely followed US deals with foreign involvement of the past year was the proposed Deutsche Börse AG ('Börse') and New York Stock Exchange Euronext ('NYSE') $10 billion all-stock merger of equals.[37] In an attempt to prevent the Börse and NYSE merger, Nasdaq and the IntercontinentalExchange ('ICE') made a joint $11.3 billion competing bid for the NYSE. The US Department of Justice ('DoJ'), however, announced it would challenge Nasdaq-ICE's bid with an antitrust lawsuit, causing Nasdaq-ICE to withdraw its bid.[38] Even after DoJ rejection, Nasdaq-ICE continued to interfere with the pending deal, warning NYSE shareholders of 'rushed judgment'.[39]

In a similar transaction announced one week prior to the Börse-NYSE merger, the London Stock Exchange ('LSE') and TMX Group, Inc. (the parent company of the Toronto Stock Exchange ('TSE')) progressed towards a $3.3 billion merger. These efforts were met with a Canadian-led interloping bid by The Maple Group Acquisition Corporation ('the Maple Group').[40] The Maple Group seeks to prevent the LSE-TSE

34 Id. at *13.

35 Id. at *14.

36 Id. at *1.

37 Deutsche Börse will issue 0.47 of a share for each NYSE share, yielding approximately a 10 per cent premium for NYSE shareholders. Deutsche Börse will also hold 10 of the 17 seats on the combined board, as its shareholders will hold approximately 60 per cent of the joint company. See Michael De la Merced, New York and German Exchanges to Merge in $10 Billion Deal, N.Y. Times (15 February 2010).

38 Azam Ahmed, Nasdaq Drops a Bid to Buy Rival NYSE, N.Y. Times (17 May 2011).

39 Jacob Bunge, ICE, Nasdaq Warn Against Rushed NYSE Shareholder Vote, Wall St. J. (10 May 2011).

40 The Maple Group includes TD Bank Financial Group, Bank of Nova Scotia, Canadian Imperial Bank of Commerce and the National Bank of Canada, among others. Laura Board, Banks,

merger to maintain domestic ownership of the TSE. On 15 May 2011, the Maple Group offered C$3.6 billion for TMX Group, which represents a 23 per cent premium over the LSE bid. Moreover, the Maple Group hopes that upon its successful bid, TSE will then merge with its primary domestic competitor.[41]

Recently, the global marketplace has witnessed significant consolidation of the world's preeminent exchanges.[42] The Börse-NYSE and LSE-TSE mergers are noteworthy for several reasons, among them deal size, competitive implications and nationalist consequences. Both the Börse-NYSE and LSE-TSE mergers were challenged by interloping domestic bids. The TSE board quickly rejected the interloping bid, and the Nasdaq-ICE bid was swiftly challenged by the DoJ for its anti-competitive implications.

Commentators, including US Senator Charles Schumer, have voiced concerns that an international merger between the NYSE and Börse could threaten the perception of New York as the world's financial centre, particularly if the combined name of the entity does not lead with NYSE.[43] Similarly, the Maple Group consortium is concerned with losing its preeminent exchange, the TSE. Although many items remain unsettled, it appears that consolidation of the world's pre-eminent exchanges will continue to be headline news throughout 2011.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

i Social media sector

Approximately 10 years following the 'dot-com bubble,' the US is experiencing tremendous deal activity in the social media sector. Deal activity in the social media space for the 12 months ended 30 March 2011 includes Microsoft's acquisition of Skype, AOL's acquisition of The Huffington Post, Google's rebuffed offer for Groupon and its pending IPO, venture capital investments in Facebook and Twitter and initial public offerings ('IPOs') by LinkedIn (along with speculation of IPOs by Facebook, Twitter and other social media giants).

Microsoft-Skype acquisition

On the heels of the expiry of the 2002 antitrust judgment against Microsoft, the software giant announced an $8.5 billion takeover of Skype Technologies SA ('Skype'). The Skype acquisition is Microsoft's largest acquisition in its history.[44] The sale to Microsoft will

Funds Launch Canadian Fightback for TMX, Deal Pipeline (16 May 2011).

41 Ahmed, *supra* note 38.

42 Id.

43 Michael De la Merced, Deal on NYSE-Deutsche Börse Nears, N.Y. Times (14 February 2011), at 2.

44 Flynn, Mary Kathleen Flynn & Andrew Bulkeley, Microsoft Snaps up Skype for $8.5 billion Deal Pipeline (10 May 2011).

yield Silver Lake Management LLC a 300 per cent gain since it acquired 70 per cent of Skype from eBay for $1.9 billion 18 months prior.[45]

The Skype acquisition represents a shift in direction for Microsoft, as it moves from its core focus on operating systems to social media applications. Microsoft hopes that its acquisition of Skype will help it compete with Apple and Google with respect to tablets and other handheld devices.

AOL-The Huffington Post Acquisition

In early February 2011, AOL announced its $315 million ($300 million in cash, $15 million in stock) acquisition of The Huffington Post, a news commentary site that attracts approximately 25 million monthly visitors.[46] AOL's acquisition of The Huffington Post is the company's first significant transaction since it was spun off from Time Warner in late 2009.[47] Although the acquisition has been met with mixed reaction, commentators have viewed it as AOL's attempt to attract traffic with quality content and news gathering ability, while departing from the company's roots as a dial-up internet service provider.[48]

Google/Groupon bid and Groupon's pending IPO

Making headline news, Groupon, an online coupon start-up company, declined Google's $6 billion takeover offer, which included $700 million in performance bonuses for management of the company.[49] Groupon, through a grassroots marketing campaign of 3,000 sales members, offers its members deep discounts to local stores, restaurants and nearby events.[50] Google's desire to compete in the local advertising market, along with the opportunity to learn more about consumer spending habits, was the impetus for the offer.[51]

Although executives at Groupon have not publicly stated a rationale for turning down the Google offer, Groupon is moving forward with an IPO aimed to raise $750 million, which values the company at as much as $25 billion.[52] The Groupon IPO has been targeted to 'go to market' as early as the second half of 2011.[53] On the other hand,

45 Id.

46 Robin Abcarian, Can Huffington Help AOL?, Belleville News Democrat (21 February 2011).

47 Verne Kopytoff, AOL's Latest Imperative, The Int'l Herald Tribune (9 February 2011).

48 Id.

49 Evelyn M. Rusli & Jenna Wortham, Google's Groupon Gambit, N.Y. Times (1 December 2010).

50 Id.

51 Id.

52 Anupreeta Das & Gina Chon, Groupon Files for IPO, Wall St. J. (2 June 2011); Douglas MacMillan, 'Groupon Said to Discuss IPO Valuation of up to $25 billion', *Bloomberg Businessweek* (June 2, 2011).

53 Groupon IPO May Value Company at $15-$20 Billion, Reuters (14 April 2011), www.reuters.com/article/2011/04/15/us-groupon-idUSTRE73E02S20110415.

Google is expected to move to acquire either LivingSocial or BuyWithMe, the second- and third-largest companies in the local social media space.[54]

In addition to the bid for Groupon, there have been additional investments in local social media, including eBay's $75 million acquisition of MoLi.com[55] and Amazon's $175 million investment in LivingSocial.[56] In transactions reported 1 June 2011, LivingSocial acquired two social media entities, Dealissime, a French daily deal site, and SocialMedia.com, a marketing company.[57] The move bolsters LivingSocial's global footprint and helps it compete with Groupon's larger marketing team.

Interest in Twitter acquisition and IPO

In addition to the bids for Skype, Groupon and The Huffington Post, Twitter Inc. has allegedly engaged in preliminary discussions with suitors such as Facebook, Google and Apple. Reportedly, Facebook offered $500 million for the fledgling Twitter entity in 2008, but negotiations quickly broke down (Twitter is an online microblogging service). Twitter, a privately held company, estimates its 2011 revenues will reach up to $110 million.[58]

Although actively sought after, Twitter executives have indicated greater interest in seeking an IPO rather than a sale of the company. In the meantime, Twitter has been able to raise up to $360 million in venture funding led by investment firm Kleiner Perkins Caulfield & Byers.[59]

LinkedIn IPO

In a transaction depicting the market's receptivity to social media, LinkedIn Corp.'s IPO tripled in its first day of trading.[60] After soaring past initial expectations, the company at one point held a first-day valuation of approximately $10 billion. LinkedIn, a company founded in Reid Hoffman's living room in 2002, is the world's largest professional network on the internet with more than 100 million members in over 200 countries.[61] Moreover, LinkedIn reports that, on average, it adds one new member every second.

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54 Groupon Rejects Google: What Local Businesses Need to Know, Mktg. Profs Daily Fix (28 January 2011). Google also launched Google Offers, an entity designed to compete with Groupon, on 1 June 2011.

55 MoLi.com is a social network, which allows members to manage multiple profiles from a single account. MoLi, www.moli.com (last visited 1 June 2006)

56 Tiernan Ray, Does Google's Groupon Deal Make Sense?, Barron's (6 December 2010), at 27.

57 Tricia Duryee, Bonjour! LivingSocial Goes After Groupon in France, All Things Digital (1 June 2011) (The financial terms of the acquisitions have not been released.).

58 Spencer E Ante, Twitter as Tech Bubble Barometer, Wall St. J. (10 February 2011).

59 Mary Kathleen Flynn, Twitter Reportedly in Takeover Talks, Deal Pipeline (10 February 2011).

60 The offering priced at $45 per share and reached a daily high of $122.70 before closing at $94.25, yielding a 109 per cent one-day gain.

61 LinkedIn, http://press.linkedin.com/about/ (last visited 25 May 2011).

In a uniquely marketed deal, the underwriting syndicate drastically limited the number of shares offered to the market with the hope of creating artificially strong demand and a large opening day 'pop.' With its initial valuation of $4 billion, the LinkedIn IPO is the largest US IPO since the Google offering in 2004.[62]

Although the IPO has been a success, as indicated by the market's receptivity to the offering, some commentators have criticised the bookrunners for underpricing the transaction. The underpricing created a windfall for favoured 'buy-side' clients, who experienced over a 100 per cent one-day return, which came directly from the pockets of LinkedIn and its investors. Founder Reid Hoffman has retained a 20.1 per cent interest in the company.

Facebook, venture capital and its contemplated IPO

In early 2011, Goldman Sachs ('Goldman'), along with Russian investment firm Digital Sky Technologies, led a venture capital round that raised $500 million for Facebook, the popular social networking site. Goldman, in connection with its investment, created a 'special purpose vehicle' ('SPV') to allow certain 'buy-side' clients to invest $1.5 billion in Facebook.[63]

The SEC, however, requires companies with more than 499 investors to disclose certain financial results to the public, which may create issues for the Facebook-Goldman venture. Goldman's position is that its SPV will allow the Goldman investors to be treated as one investor, circumventing the SEC rule.[64]

The Goldman investment fuels discussion as to when and whether Facebook's IPO will 'go to market.' Given Facebook's strong liquidity, coupled with the capital injection from the Goldman-led venture, commentators do not believe an IPO is imminently necessary, but is nonetheless forthcoming.

ii Energy and power sector

In the US, M&A activity during the last three quarters of 2010 remained focused on the energy and power sector, which had a total deal value of $205.6 billion.[65] In the first quarter of 2011, the energy and power sector remained active with a deal volume of $58.7 billion and more than 15.5 per cent of market share, led by Duke Energy's $26 billion acquisition of Progress Energy.[66] It is unclear, however, how the current volatility of oil prices due to conflict in the Middle East will influence the energy and power sector in the US.

62 On 28 January 2011, LinkedIn filed an S-1 with the stated aim of raising up to $175 million. See Olaf De Senerpont Domis, LinkedIn Aims for IPO, Deal Pipeline (27 January 2011).

63 Dan Primack, What Does Goldman's Investment in Facebook Mean?, CNN Money (3 January 2011) (the Goldman investment values Facebook at approximately $50 billion).

64 Id.

65 Mergers & Acquisitions Review, Full Year 2010, Legal Advisors, *supra* note 1.

66 Mergers & Acquisitions Review, First Quarter 2011, Legal Advisors, *supra* note 3.

VI FINANCING OF M&A MAIN SOURCES AND DEVELOPMENTS

While the credit markets have re-emerged, they have not yet reached the pre-credit crisis heights of 2007. Over the last four quarters, availability of financing for LBOs has been on the rise. For the year ended 31 December 2010, the US experienced approximately $57 billion in LBO deal volume, comprising 64 per cent of global LBO deal volume.[67] As of 30 March 2011, LBO deal volume totalled $41.5 billion, which is a 23 per cent increase relative to the first quarter of 2010.[68] For the year ended 31 December 2010, LBOs constituted approximately 15 per cent of US-targeted M&A, compared to more than 30 per cent in late 2006.[69]

Credit markets are returning to normal following the 'credit crisis'.[70] Improved market sentiment and increased volume have helped mitigate obstacles to securing financing commitments and have also improved commitment terms for acquirers. Utilisation of junk bonds has taken the lead in funding LBOs. In fact, commentators believe that the process of securing financing is currently exhibiting some of the competitive, precedent-based and time-compressed characteristics witnessed during the last LBO boom.[71]

In 2010, private equity firms were flush with capital for dealmaking with an estimated $490 billion in 'dry powder'.[72] Market participants expect an uptick in LBO deals because of 'dry powder', and private equity firms are eager to put their capital to use.[73] However, large private equity firms are experiencing a great deal of competition from corporate bidders, who are often able to make more attractive bids. Additionally, lending institutions have demanded that private equity firms provide a greater equity mix, which, for the most part, has kept large LBOs off of the table.[74] According to Blackstone President Tony James, equity-mix levels in 2006 and 2007 were typically 15 per cent to 20 per cent, while the 'new normal' is 25 per cent to 40 per cent.[75]

Currently, private equity deal size is typically in the $3 billion to $5 billion range, which is significantly smaller than the deal size witnessed in 2006 and 2007.[76] Nonetheless, the price of mergers has been on the rise. As of May 2011, the average price paid for an asset in the US is 13.2 times EBITDA, which is higher than the last three

67 Mergers & Acquisitions Review, Full Year 2010, Legal Advisors, *supra* note 1.

68 Andrew Bary, LBO Hunt: Who's Next?, Barron's (18 April 2011).

69 Mergers & Acquisitions Review, Full Year 2010, Legal Advisors, *supra* note 1.

70 Joy Ferguson, High Yield Market Ready for Quick Uptick in M&A, Reuters News (5 May 2011).

71 Jason Kyrwood, Return of the Froth, Daily Deal (25 April 2011).

72 Richard Kellerhals, LBOs Seen Driving Leverage Loan Volume, 77 Inv. Dealers' Digest 1 (2011) (levels of 'fresh powder have only been higher in 2009, when levels reached 521 billion).

73 Id.

74 Joe Mantone, 'LBO Market Shows Signs of Life', *SNL Sec. & Invs. M&A* (1 March 2011).

75 Id.

76 Megan Davies, 'LBOs of up to $15 Billion Possible, *Reuters News* (3 March 2011).

years.[77] Moreover, the average leverage multiple for US LBOs through April 2011 has risen to 10.6 times EBITDA from 8.9 times EBITDA for 2010.[78]

Although credit markets are improving, strategic and financial buyers continue to face challenges obtaining financing, resulting in a significant number of deals that include consideration in the form of stock. The use of stock, in addition to reducing the amount of cash needed to consummate a deal, allows the target's shareholders to participate in the potential upside of the combined entity, which can be helpful in deflecting criticism that the acquirer is not paying full value by buying at a depressed stock price.

VII EMPLOYMENT LAW

i 'Say-on-pay' and 'say on golden parachute' shareholder votes

The intense focus on executive compensation that emerged last year has not abated; in fact, it has been strengthened by new regulations promulgated by the SEC implementing the expansive Dodd-Frank finance reform legislation passed last year by the US Congress. The new regulations are aimed at increasing shareholder participation in matters of executive compensation and corporate governance. Under the regulations, which apply from the beginning of 2011 to most US public companies, shareholders are entitled to increased disclosure regarding, and an advisory vote on, the material components of these companies' executive compensation programmes ('say-on-pay'). Further, these companies must provide their shareholders with detailed disclosure and, under certain circumstances, an additional advisory vote, with respect to golden parachute and other compensation arrangements related to M&A transactions. Specifically, companies must now disclose in proxy statements soliciting shareholder approval and in consent solicitations in connection with M&A transactions all potential transaction-related payments to executives of the target and the acquiror. These payments could include payments resulting from deal consummation (e.g., option cash-outs) as well as contingent payments (e.g., severance). Moreover, the company generally must provide its shareholders with an advisory vote on these arrangements. However, the vote is non-binding and does not create an additional condition to closing or affect the validity of the compensation arrangements.

Although these shareholder votes are non-binding, they have significant normative force and, thus far, have had a considerable impact. The increased pressure on companies has produced enhanced dialogue with shareholders. Indeed, in advance of its annual meeting this year, Occidental Petroleum, which was one of the first US companies to receive a majority 'no' vote on its 'say-on-pay' resolution last year, took the unusual step of scheduling a 'fifth analyst call' between its directors and key shareholders to discuss

77 Megan Davies, Plain Vanilla LBOs Few and Far Between, Reuters News (29 April 2011) (the last time asset prices eclipsed 13.2 times EBITDA was 2007, when the average price was 14.3 times EBITDA).

78 Id.

compensation and other corporate governance matters.[79] This move was not without controversy, and it remains to be seen whether other companies will follow this trend in the coming months.

To date, at least 30 companies have failed to obtain majority approval of their 'say-on-pay' resolutions. By contrast, over 500 companies have received favourable votes of greater than 90 per cent. The role of proxy adviser firms continues to be significant, with the recommendations of such firms having a demonstrable impact on the vote outcome. The existing data shows that companies for which a proxy adviser firm issued unfavourable vote recommendations either received majority 'no' votes on their 'say-on-pay' resolutions or received favourable votes by a margin substantially lower than companies for which a favourable recommendation had been issued. In addition, the stakes for the vote have risen in light of the developing trend of strike lawsuits being filed against companies that receive majority 'no' votes.[80] As of the end of May 2011, at least five such suits have been filed, and legal analysts expect more to follow despite some uncertainty over whether such suits lack merit.

VIII TAX LAW

i Enacted legislation

Denial of foreign tax credits for certain asset acquisitions

A US taxpayer can step up the tax basis of a foreign target's assets for US tax purposes, but not for foreign tax purposes in connection with certain acquisitions of interests in a foreign target. This can be achieved by the purchase of stock in a foreign corporation where an election is made under Section 338(g) of the Internal Revenue Code, the purchase of interests in a partnership where an election under Section 754 is available or generally, where an acquisition of interests in a foreign target is treated as an asset acquisition for US tax purposes but as a stock acquisition for foreign tax purposes due to entity classification ('check-the-box') elections. In such transactions, the foreign corporation will often have a lower tax basis in its assets for foreign than for US tax purposes, and will be subject to foreign tax on the basis of a higher taxable income than exists for US tax purposes. Taxpayers have taken advantage of this disparity in order to obtain a US foreign tax credit for foreign taxes paid on the higher amount of foreign income, while only having to report in the US the lower amount of income as determined for US tax purposes. Recent legislation enacted Section 901(m) to deny a foreign tax credit for foreign taxes on foreign income that is not subject to US taxation because of the step up in tax basis for US tax purposes.

79 See Sarah Johnson, Giving Shareholders More Say, CFO Magazine (1 June 2011), www.cfo.com/article.cfm/14577235/c_14577475.

80 See, for example, Dena Aubin, 'Lawsuits Over Say-On-Pay Votes up Ante for Boards', *Reuters* (12 May 2011), www.reuters.com/article/2011/05/12/ceo-pay-lawsuits-idUSN1230190120110512.

ii Pending legislation

Elimination of 'boot-within-gain rule'

Under current law, if a tax-free reorganisation involves closely-held corporations with common shareholders, any cash ('boot') distributed to shareholders of the target corporation may be considered to have the effect of the distribution of a dividend. In that case, the gain that is otherwise recognised by a target shareholder is taxable as dividend income rather than as capital gain. However, although the boot is treated as a dividend, it is only taxable to the extent of the gain realised on the exchange (the 'boot-within-gain rule'), even though the full amount of a dividend would be taxable under general tax principles. Legislation proposed in the Obama Administration's 2012 Budget ('the 2012 Budget'), if enacted, would repeal this rule by requiring the shareholder to recognise dividend income up to the earnings and profits of the corporation, without regard to the gain realised on the exchange.[81] This legislation is intended, in part, to prohibit a technique that US parent corporations have used to repatriate earnings from foreign subsidiaries on a tax-free basis.

Taxation of 'carried interests'

Under current law, managers of investment funds can receive a 'profits interest' or 'carried interest' in the fund in exchange for their services and receive their share of the income of the fund at capital gains rates. There have been different versions of 'carried interest' legislation proposed by Congress; if enacted, they would generally treat a portion of the income received in respect of such a 'profits interest' as ordinary income rather than capital gains.

In the 2012 Budget, the Obama Administration has proposed its own version of such legislation, which provides a set of special rules for any person who holds an 'investment services partnership interest' ('ISPI').[82] An ISPI is a carried interest in an 'investment partnership', which is defined to be a partnership where the majority of the assets are investment-type assets (certain securities, real estate, interests in partnerships, commodities, cash or cash equivalents or derivative contracts with respect to those assets), but only if over 50 per cent of the partnership's contributed capital is from partners in whose hands the interests constitute property held for the production of income. Gain recognised on the sale of an ISPI would also generally be taxed as ordinary income, not as capital gain.

Service partners who invest capital in an investment services partnership would, in certain instances, be allowed to allocate income between the invested capital and the carried interest. Invested capital for these purposes excludes the proceeds of any loan or other advance made or guaranteed by any partner or the partnership.

Commentators believe that the prospects of 'carried interest' legislation, in light of the Republican-controlled House, is fairly slim. However, none of the proposed legislation to date has included a grandfather clause and thus taxpayers, in structuring their current

81 Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2012 Revenue Proposals (February 2011).

82 Id.

arrangements, may want to pay attention to the details of the Administration's proposed legislation.

iii Treasury department regulations

Final 'Killer B' regulations

If a US corporation has a foreign subsidiary, active income of the subsidiary generally is not taxed in the US until repatriated to the US. In recent years, US taxpayers have developed structures designed to permit them to repatriate funds from foreign subsidiaries (including foreign targets in M&A transactions) without paying any US tax. For example, the 'Killer B' structure involved a foreign subsidiary purchasing US parent stock for cash and then using that stock to acquire stock of a related or unrelated target in a tax-free reorganisation. The initial purchase of the US parent stock for cash allowed money to be paid from the foreign subsidiary to the US parent tax-free. The Treasury Department recently finalised regulations that are designed to shut down 'Killer B' and similar transactions. The final regulations are stricter than the proposed regulations in certain respects, for example covering a transaction where the foreign subsidiary purchases US parent securities rather than stock.[83]

iv Published guidance

Economic substance doctrine

In 2010, Congress enacted legislation to codify the judicial 'economic substance doctrine', which courts invoke to deny tax benefits generated by transactions that lack true economic substance. The newly enacted Section 7701(o) provides that, in the case of any transaction to which the economic substance doctrine is relevant, the transaction will be treated as having economic substance only if (1) the transaction changes the taxpayer's economic position in a meaningful way (ignoring the transaction's US Federal income tax effects) and (2) the taxpayer has a substantial purpose for entering into the transaction (apart from the transaction's US Federal income tax effects). The legislation also imposed a 20 per cent strict liability penalty for any underpayment of tax by reason of a transaction lacking economic substance (40 per cent if the taxpayer does not adequately disclose the relevant facts of the transaction in the return).

The IRS recently issued guidance on Section 7701(o), stating that the IRS will analyse each prong of the two-prong conjunctive test by applying cases under the common-law economic substance doctrine and will generally continue to apply the economic substance doctrine in the same fashion as it did prior to the enactment of Section 7701(o).[84] The IRS has also indicated that it does not intend to issue general administrative guidance regarding the types of transactions to which the economic substance doctrine applies, including private letter rulings as to whether any transaction complies with the requirements of Section 7701(o).

83 See Treas. Reg. § 1.367(b)-10.

84 See I.R.S. Notice 2010-62, 2010-40 IRB 411 (9 September 2010).

Deductibility of 'success-based' fees for acquisitions and reorganisations
Businesses are generally not allowed to deduct any amount paid for property having a useful life substantially beyond the taxable year. In the case of an acquisition or reorganisation of a business, costs incurred to facilitate the transaction are presumed to produce long-term benefits and generally must be capitalised. For an amount that is contingent on the successful closing of a transaction (a 'success-based' fee) – generally investment banking, and in certain cases legal, fees – the taxpayer may rebut this presumption by keeping sufficient documentation to support the allocation of a portion of the fee to activities that do not facilitate the transaction. There has been uncertainty over the type and extent of documentation required to support such an allocation. The IRS has issued guidance that simplifies the allocation method by providing a safe harbour for taxpayers to deduct 70 per cent of a success-based fee and to capitalise the remaining 30 per cent, if an election is made and certain reporting requirements are met.[85]

Recapitalisations in conjunction with spin-off transactions
One of the requirements for a tax-free spin-off is that the distributing corporation ('Distributing') must hold stock in the corporation to be spun off ('Spinco') representing at least 80 per cent of the total combined voting power of all classes of stock entitled to vote and at least 80 per cent of the total number of shares of all other outstanding classes of stock. To meet this requirement, Distributing may acquire control of Spinco in anticipation of a spin-off through a tax-free recapitalisation in which Distributing receives high-vote stock.

In the past, the IRS ruling position has been that the recapitalisation must constitute a 'permanent realignment' of the voting rights of the corporation, so that there could not be a plan at the time of the spin-off to undo the higher vote of the high-vote stock. However, the IRS has recently adopted the position that a recapitalisation into control is permissible as long as there is no binding contract to undo the high-vote position after the spin-off; a plan to do so is permissible. For example, in IRS private letter ruling 201116001, the IRS sanctioned tax-free treatment of a spin-off where (1) before the spin-off, Spinco recapitalised its classes of stock so that distributing would meet the 80 per cent control requirement and (2) after the spin-off, Spinco had a plan (but no obligation) to propose a shareholder vote on a transaction that would reduce the voting power of the stake that was distributed.[86] Thus, it is now easy to avoid the 'control' requirement for a spin-off by recapitalising into control before the spin-off, with a plan to recapitalise back after the spin-off.

Calculating limitations on net operating losses
If a corporation with net operating losses ('NOLs') has an 'ownership change', Section 382 limits the amount of the corporation's pre-change NOLs that can be used to offset post-change taxable income. An ownership change occurs if any 5 per cent shareholders have increased their ownership in the loss corporation stock by more than 50 per cent

85 Rev. Proc. 2011-29, 2011-18 IRB 746 (8 April 2011).

86 See, for example, I.R.S. Priv. Ltr. Rul. 201116001 (22 April 2011).

over generally a three year period. Section 382 applies special rules for less than 5 per cent shareholders ('small shareholders') and aggregates such small shareholders into one 5 per cent shareholder, generally referred to as the 'public group.' However, more than one 'public group' may be deemed to exist after certain transactions, such as tax-free reorganisations under Section 368, and keeping track of multiple 'public groups' can be quite complex.

In Notice 2010-49, 2010-27 IRB 10 (11 June 2010), the IRS asked for comments on simplifying the way that small shareholders are taken into account in determining ownership changes. The IRS suggested two potential methods (under an approach called the 'Purposive Approach') for simplifying the existing rules. Both methods would result in considerable simplification and likely reduce the circumstances in which an ownership change would occur.

In addition, the ownership percentage of a shareholder under Section 382 is based on the value of stock owned by the shareholder compared to the value of all outstanding stock of the corporation. When a corporation has two or more classes of stock outstanding (e.g., common and preferred stock), it is not clear how to determine changes in percentage ownership of the stock held by a particular shareholder. The issue arises because the preexisting stock owned by a particular shareholder may represent a different percentage of the total value of the outstanding stock at different times, due to changes in the relative value of different classes of stock. Logically, in determining a shareholder's increase in percentage ownership in the corporation under Section 382, changes in percentage ownership arising from changes in the relative value of preexisting stock held by the shareholder should be disregarded. The IRS recently provided interim guidance on how to take such fluctuations in stock value into account in determining ownership shifts of loss corporations. The IRS described two methodologies and stated that, until final rules are issued, either method is acceptable.[87]

v Case law

Poison pill plans to protect net operating losses

In recent years, some corporations with NOLs have implemented poison pills that are activated by 5 per cent stock purchases in order to avoid triggering an 'ownership change' under Section 382, which would limit the use of their NOLs (as discussed above). These differ from traditional anti-takeover poison pills that are typically activated by stock purchases ranging from 10 per cent to 20 per cent.

The Delaware Supreme Court recently affirmed an important decision that supports the legality of 5 per cent poison pills.[88] Selectica Inc ('Selectica') created a 5 per cent 'poison pill' to protect a $160 million NOL asset. The pill was later activated by a Selectica shareholder that increased its ownership holding to 6.7 per cent. Selectica filed suit in the Delaware Chancery Court seeking a declaratory judgment upholding the validity of its 5 per cent 'poison pill.' Despite expert testimony at the trial stating that at least 90 per cent of pills had triggers of 15 or 20 per cent, the court ruled in Selectica's

87 See I.R.S. Notice 2010-50, 2010-27 IRB 12 (11 June 2010).

88 *Versata Enters., Inc. v. Selectica, Inc.*, 5 A.3d 586 (Del. 2010).

favour and the Delaware Supreme Court affirmed. This decision is likely to encourage other corporations to protect NOL attributes with similar 'poison pill' arrangements.

IX COMPETITION LAW

The past year has been a busy one in US merger enforcement. The Department of Justice ('DoJ') and the Federal Trade Commission ('the FTC') released revised Horizontal Merger Guidelines ('the pre-merger Guidelines'), the blueprint by which they analyse proposed mergers; the FTC proposed significant revisions to the Hart-Scott-Rodino ('the HSR') pre-merger notification form, imposing some substantial new reporting requirements while paring others; the DoJ released an updated Policy Guide to Merger Remedies; and the DoJ investigated several high-profile proposed mergers. This section provides an overview of the major developments.

i New Horizontal Merger Guidelines

In August 2010, the DoJ and the FTC released revised Horizontal Merger Guidelines.[89] This is the first time since 1992 that the Guidelines have been revised, though the 2006 DoJ/FTC Commentary on the Guidelines previewed a number of the current revisions.[90]

The change generating the most discussion relates to the agencies' drive to de-emphasise formal market definition in favour of direct effects evidence in their competitive effects analysis, particularly in unilateral effects cases. Direct effects evidence can include business documents, evidence related to existing competition between the merging firms, and the effects of prior mergers in the same market, among other things. The agencies have long incorporated such evidence into the early stages of their merger analyses, but the inclusion of new language in the guidelines appears to signal their intention to focus on such evidence.

For the first time, the guidelines contain a section on how the agencies generally analyse the likely effects of a proposed merger on incentives to innovate.[91] Although the discussion on innovation lacks specific guidance, the presence of this new section reflects the growing importance of innovation markets to the US economy and reflects the need for antitrust doctrine to keep pace with the new challenges such markets present.

ii HSR reform proposals

In August 2010, the FTC announced significant proposed changes to the Hart-Scott-Rodino Notification and Report Form ('the Form') that parties to mergers and acquisitions that meet a certain threshold must file before they can consummate

89 Fed. Trade Comm'n, Horizontal Merger Guidelines For Public Comment (20 April 2010), www.ftc.gov/os/2010/04/100420hmg.pdf.

90 Fed. Trade Comm'n & U.S. Dep't of Justice, Commentary on the Horizontal Merger Guidelines (March 2006), www.justice.gov/atr/public/guidelines/215247.htm.

91 Horizontal Merger Guidelines Section 6.4 (2010).

proposed transactions.[92] The new Form would eliminate some categories of information that the FTC has found are not useful in its initial screening process, but it would also contain two new categories of required information that could substantially increase the aggregate burden on some filers.

The FTC has proposed, under Item 4(d), three new categories of documents that must be produced along with the Form. These documents, which the FTC has said would substantially aid the merger screening process, include all offering memoranda that reference the acquired entity or assets; certain kinds of competition-relevant analyses prepared by third-party advisers such as consultants and investment bankers; and certain studies, analyses and reports that evaluate synergies or efficiencies from the proposed transaction.[93] Only such documents prepared in the previous two years must be produced. Nonetheless, Item 4(d) could add substantially to burden associated with document collection.

The other major revision to the form calls for reporting regarding 'associates', entities that are not under common control with the filing entity but have a management or oversight relationship with that entity. This requirement could be particularly burdensome for private equity firms and for banks that may manage dozens of limited partnerships, each holding minority investments in many firms. The proposed associated entity reporting requirements were the focus of sharp criticism from these interests during the public comment period, which closed in October 2010.

Some observers expected the FTC to issue the new Form and Rules in the first quarter of 2011.[94] As of this writing, however, the FTC has taken no further action.

iii New DoJ policy guide to merger remedies

On 17 June 2011, the Antitrust Division ('the Division') released an updated version of its Policy Guide to Merger Remedies ('the Guide')[95], the first such update since 2004. Assistant Attorney General Varney cited changes in the merger landscape, including 'increasing transnational mergers and complex vertical transactions,' as the impetus for

92 Fed. Trade Comm'n, PreMerger Notification; Reporting and Waiting Period Requirements; Proposed Rule, 75 Fed. Reg. 180, 57110 (17 September 2010), www.ftc.gov/os/2010/08/100812hsrfrn.pdf. The proposed changes do not alter the 'Size of Transaction' thresholds, which following the annual GNP-based adjustment that became effective on 24 February 2011 are $66 million (when size of person requirements are also met) and $263.8 million (size of person irrelevant), respectively.

93 Id. at 57110 (stating that the addition of Item 4(d) would 'capture additional information that would significantly assist the Agencies').

94 See, for example, Neal R Stoll & Shepard Goldfein, Form Over Substance: Anticipating Amended Hart-Scott-Rodino Rules, N.Y. L.J. (Mar. 8, 2011) ('We understand that the amendments to the HSR rules will be published in the Federal Register by the end of March.').

95 Dep't of Justice, Department of Justice Antitrust Division Policy Guide to Merger Remedies (June 2011), www.justice.gov/atr/public/guidelines/272350.pdf.

the new Guide.[96] The new Guide appears consistent with observed Division practice over the last several years.

The most significant change is the Division's embrace of conduct remedies for preventing competitive harm. The 2004 Guide stated that 'structural remedies are preferred' and that 'conduct relief is appropriate only in limited circumstances'.[97] By contrast, the 2011 Guide recites no preference for structural remedies and observes that 'conduct remedies are a valuable tool for the Division' that can 'preserve a merger's potential efficiencies, and, at the same time, remedy the competitive harm that would otherwise result from the merger.'[98]

This language is consistent with the remedies utilised by the Division in three recent vertical mergers, *Google-ITA*,[99] *Ticketmaster-Live Nation*,[100] and *NBC Universal-Comcast*.[101] In each of these cases, the Division employed complex conduct remedies, including nondiscrimination provisions (*NBC Universal-Comcast*), mandatory licensing (*Google-ITA* and *Ticketmaster-Live Nation*), and ongoing development obligations (*Google-ITA*), to protect competition while allowing efficiencies from the transaction to be realised. Indeed, the new Guide recognises that conduct remedies may be a particularly useful tool for the Division in vertical mergers,[102] which have recently been the subject of increased scrutiny, particularly in the high-tech, media, and communications sectors.

Two additional changes are worthy of note. First, when a structural remedy entails divestiture of less than an existing business unit, the Division may now require either an up-front buyer or a crown jewel provision.[103] These requirements, which the Division traditionally has disfavoured, bring its remedies policy more closely in line with that of

96 Press Release, Dep't of Justice, Antitrust Division Issues Updated Merger Remedies Guide (17 June 2011), http://www.justice.gov/atr/public/press_releases/2011/272365.pdf.

97 Press Release, Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies, Section III (A) (October 2004), http://www.justice.gov/atr/public/guidelines/205108.pdf.

98 Press Release, Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies, Section II (October 2004), http://www.justice.gov/atr/public/guidelines/205108.pdf.

99 Press Release, Dep't of Justice, Justice Department Requires Google Inc. to Develop and License Travel Software In Order to Proceed With Its Acquisition of ITA Software Inc. (8 April 2011), http://www.justice.gov/opa/pr/2011/April/11-at-445.html.

100 *Dep't of Justice, Competitive Impact Statement, U.S. v. Ticketmaster Entm't, Inc. & Live Nation, Inc.* (25 January 2010), http://www.justice.gov/atr/cases/f254500/254544.pdf.

101 Press Release, Dep't of Justice, Justice Department Allows Comcast-NBCU Joint Venture To Proceed With Conditions (18 January 2011), http://www.justice.gov/atr/public/press_releases/2011/266149.pdf.

102 Dep't of Justice, Department of Justice Antitrust Division Policy Guide to Merger Remedies, Section II (B) (June 2011), http://www.justice.gov/atr/public/guidelines/272350.pdf (Conduct remedies can be an effective method for dealing with competition concerns raised by vertical merger and are also sometimes used to address concerns raised by horizontal mergers (usually in conjunction with a structural remedy)).

103 Dep't of Justice, Department of Justice Antitrust Division Policy Guide to Merger Remedies, Section IV (A)(2)(b) (June 2011), http://www.justice.gov/atr/public/guidelines/272350.pdf.

the FTC. Second, enforcement of Division consent decrees will now be the responsibility of the newly created Office of the General Counsel.[104] Previously, enforcement of consent decrees remained with the Division staff responsible for reviewing the transaction. This again brings the Division more in line with the FTC, which has long had a Compliance Division dedicated to merger remedies enforcement.

iv Three high-profile transactions

Finally, it is instructive to consider three high-profile mergers reviewed by the DoJ in the past year. Two of these (*UAL/Continental* and *Google/ITA*) were cleared, while the third (*AT&T/T-Mobile*) remains under investigation.

UAL/Continental Merger[105]

The Obama DoJ's August 2010 clearance of the combination of UAL Corp and Continental Airlines with targeted divestitures demonstrated that the agency will act swiftly and without regard to public pressure when the logic of the underlying merger is compelling.

UAL and Continental were both 'network' airlines, with relatively broad national coverage routed through 10 hubs. Those networks were, however, largely complementary. This raised the threshold question of whether the relevant antitrust markets were national or local. The DoJ continued its established practice of evaluating airline combinations by city-pair markets, rejecting the notion of a national market for air travel. When examined in this light, the merger of UAL and Continental raised possible competition concerns on a very limited number of routes and at Newark Airport, where both airlines had a strong presence. The latter concerns were remedied through the divestiture of 18 pairs of takeoff/landing slots to low-cost competitor Southwest Airlines. In the end, the DoJ cleared this $3 billion merger after an investigation period of less than four months.[106]

The Newark divestitures did not resolve the concerns of a coalition of state attorneys general led by Ohio Attorney General Richard Cordray, which continued to investigate the merger. With closing imminent, UAL Continental entered into an agreement with the Attorney General committing to maintain operations at Continental's Cleveland hub at certain target levels over five years, subject to adjustment if UAL/Continental demonstrates that its Cleveland operations are generating substantial losses.[107] The

104 Dep't of Justice, Department of Justice Antitrust Division Policy Guide to Merger Remedies, Section V (A) (June 2011), http://www.justice.gov/atr/public/guidelines/272350.pdf.

105 The authors of this chapter are members of Cravath, Swaine & Moore LLP, which advised UAL Corp. on the merger and represented UAL Continental in merger-related litigation.

106 Press Release, Dep't of Justice, United Airlines and Continental Airlines Transfer Assets to Southwest Airlines in Response to Department of Justice's Antitrust Concerns (27 August 2010), www.justice.gov/atr/public/press_releases/2010/262002.htm.

107 See Jay Miller, Continental, United airlines agree to keep Cleveland Hopkins hub for at least five years, Crain's Clev. Bus. (5 June 2011), www.crainscleveland.com/article/20100913/FREE/100919958.

agreement contains substantial penalties for noncompliance and gives the Attorney General the right to commission an independent audit at company expense.[108]

Also shortly before closing, a group of travel agent plaintiffs filed a Section 7 action in California seeking a preliminary injunction halting the merger.[109] Following a two-day evidentiary hearing, the district court denied the injunction, rejecting plaintiffs' assertion of a national air travel relevant market, as well as relevant markets for business travelers and for airport pairs.[110] After closing, the district court's decision was affirmed by the Ninth Circuit.[111]

Google/ITA merger

Google's proposed $700 million acquisition of travel software maker ITA was initially the subject of criticism by rival travel sites, a coalition of state attorneys general and the generally pro-intervention American Antitrust Institute.[112] These critics argued that the acquisition of the leading producer of airfare pricing and shopping systems by the leader in online search threatened to distort competition in a developing market, potentially leading to the foreclosure of rival travel search firms.[113]

Although the DoJ considered seeking an injunction blocking the deal, the agency ultimately cleared the transaction subject to a consent decree.[114] Among other undertakings, Google committed to continue licensing the ITA software to competitors on commercially reasonable terms and agreed to an arbitration process to quickly settle licensing disputes. Google also agreed to implement an internal firewall to prevent abuse of commercially sensitive data gathered from ITA's customers. Finally, Google agreed to continue developing both ITA's current travel search product as well as its next-generation product at existing levels.[115]

108 A copy of the final executed agreement may be found at media.cleveland.com/business_impact/other/Final%20Agreement%20%282%29.pdf.

109 See Complaint, *Malaney, et al. v. UAL Corporation, et al.*, CV 10 2858 (N.D. Cal. 29 June 2010).

110 Order Denying Motion for Preliminary Injunction, *Malaney, et al. v. UAL Corporation, et al.*, CV 10 2858 (N.D. Cal. 27 September 2010).

111 *Malaney, et al. v. UAL Corporation, et al.*, CV 10 2858 (9th Cir. 23 May 2011) (unpublished).

112 See, for example, Randy Stutz, An Examination of the Antitrust Issues Posed by Google's Acquisition of ITA, Am. Antitrust Inst. (18 February, 2011), www.antitrustinstitute.org/sites/default/files/Google-ITA%20AAI%20White%20Paper2.18.11.pdf.

113 Id. at 11 ('The DoJ should ... examine whether the transaction likely may have significant foreclosure effects, preventing either existing or future market entrants from competing.')

114 See Amir Efrati, U.S. Prepares Possible Case Against Google-ITA Deal, Wall St. J. (14 January 2011) ('The Justice Department is laying the groundwork for a potential court challenge to Google Inc.'s acquisition … Justice Department staff lawyers have begun preparing legal documents for us in a possible court challenge … but no decision has been made, one of the people familiar with the matter said.')

115 Press Release, Dep't of Justice, Justice Department Requires Google Inc. to Develop and License Travel Software in order to Proceed with its Acquisition of ITA Software Inc., www.justice.gov/

The Google/ITA consent decree could test the limits of the DoJ's 'fix-it-first' process for addressing competitive concerns raised by mergers that nonetheless have the potential to bolster competition. Under 'fix-it-first', the DoJ negotiates targeted divestitures, licensing agreements and other binding commitments designed to remedy competitive threats identified during the agency's investigation. The DoJ can later sue to enforce the terms of the decree if necessary. The 'fix-it-first' approach has occasionally been criticised as requiring too much ongoing agency supervision, but in this instance, 'fix-it-first' appears to have provided a suitable remedy. After the consent decree was announced, FairSearch, a coalition of ITA competitors that had initially opposed the deal, pronounced itself satisfied with the consent decree, calling the result 'a clear win for consumers'.[116]

AT&T/T-Mobile Merger

On 20 March 2011, AT&T announced its proposed $39 billion acquisition of mobile telephone service competitor T-Mobile, a division of Deutsche Telecom.[117] This transaction will present a number of issues at the cutting edge of merger analysis. The deal would combine horizontal competitors in an already highly concentrated industry, raising both short-run and longer-run competition issues. The technological sophistication of the industry and the possible effect of the deal on adjacent markets such as those for handsets and chipsets are additional sources of complexity. In addition, the DoJ and the FCC, which have dual jurisdiction, will review the transaction under different standards: the DoJ under Section 7 of the Clayton Act and the FCC under its broader 'public interest' mandate.

As with the merger of UAL and Continental, market definition promises to be a central issue. While there are only four companies offering national network coverage, many cities have smaller providers that offer less-inclusive plans. Defining markets locally so as to include these local firms would make these markets appear more competitive. Opponents of the merger will argue that the relevant market should be national, not local, and therefore include only the four national service providers (AT&T, Verizon, T-Mobile and Sprint). With the market so defined, a merger of any two of these four providers is presumptively anti-competitive under the Horizontal Merger Guidelines. The elimination of T-Mobile as an independent competitor also raises concerns because of T-Mobile's history as an aggressive discounter of wireless services – 'maverick' whose market presence tends to constrain the pricing behaviour of the other national providers.

As with Google's acquisition of ITA, AT&T's proposed acquisition of T-Mobile will also raise longer-term issues concerning the competitive incentives of the remaining

atr/public/press_releases/2011/269589.htm.

116 See Press Release, FairSearch, FairSearch.org Applauds DoJ for Protecting Consumers, Challenging Google-ITA Deal (8 April 2011), www.fairsearch.org/google-ita/update-fairsearch-org-applauds-doj-for-protecting-consumers-challenging-google-ita-deal ('Today's decision by the Justice Department to challenge Google's acquisition of ITA Software is a clear win for consumers.').

117 AT&T to Acquire T-Mobile USA from Deutsche Telekom, Bus. Wire (20 March 2011).

firms. Such 'dynamic competition' concerns have become increasingly important in merger analysis in recent years as the US economy grows more dependent on the technology sector for growth. The post-merger wireless market would contain two 'mega-firms', AT&T and Verizon, as well as a considerably smaller competitor, Sprint; with AT&T's and Verizon's large installed bases of customers, they could become the gatekeepers through which much of the industry's innovation must flow to reach consumers.[118]

Agency review of the deal is expected to take a year or longer. The FCC has named respected former DoJ A ttorney Renata Hesse, a partner in the Washington office of Wilson Sonsini Goodrich & Rosati, to lead its review.[119] The New York Attorney General[120] and the California Public Utility Commission[121] have opened their own investigations.

X OUTLOOK

While M&A activity remains below its highs of 2006 and 2007, it is steadily approaching its pre-'boom' levels. Improved credit markets and depressed equity prices have driven the uptick in M&A activity and have provided favourable buying opportunities for acquirers. In addition, private equity and LBO activity have begun to show signs of life as the credit markets strengthen. Significant uncertainty remains, however, and recent economic destabilisation in Europe and political instability in the Middle East may create additional challenges for the US financial system.

118 See Professor Andrew I. Gavil, Howard University School of Law, Remarks before the House Judiciary Committee, Subcommittee on Intellectual Property, Competition, and the Internet, How Will the Proposed Merger Between AT&T and T-Mobile Affect Wireless Telecommunications Competition (26 May 2011), http://judiciary.house.gov/hearings/pdf/Gavil05262011.pdf (describing effects on innovation in upstream markets from increased concentration of wireless providers).

119 See Press Release, Fed. Commc'ns Comm'n, Renata Hesse Named Senior Counsel to the Chairman for Transactions (17 May 2011), www.fcc.gov/document/renata-hesse-named-senior-counsel-chairman-transactions.

120 See Press Release, New York Office of the Attorney Gen., A.G. Schneiderman to Undertake Thorough Review of AT&T, T-Mobile Merger (29 March 2011), www.ag.ny.gov/media_center/2011/mar/mar29a_11.html.

121 Shayndi Rice, California Regulators Move to Investigate, AT&T, T-Mobile Deal, Wall St. J. (27 May 2011).

Appendix 1

ABOUT THE AUTHORS

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Richard Hall is a partner in Cravath's Corporate Department and is the Practice Leader of the Firm's Merger and Acquisitions practice. His practice focuses on mergers and acquisitions, particularly in the international arena and natural resources sector, and corporate governance advice. Mr Hall has represented non-US companies in their acquisitions of US companies, US companies in their acquisitions by non-US companies, and non-US companies in their combinations with other non-US companies. He has also advised in the areas of unsolicited activity, takeover defence and in general corporate matters. Mr Hall received a BComm with honours in 1984 and an LLB with honours in 1986 from the University of Melbourne, and an LLM from Harvard University in 1988. He joined Cravath in 1988 and became a partner in 1996.

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