Key Takeaways

Skadden

Merger Control Reviews: Spotlight on Internal Documents

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In a webinar held on March 25, 2021, Skadden antitrust/competition partners **Kenneth Schwartz** and **Ingrid Vandenborre** joined Charles River Associates vice presidents **Andrew Dick** and **Oliver Latham** to discuss the important role internal documents play in antitrust investigations worldwide and practical tips for document creation.

Antitrust regulators on both sides of the Atlantic have recently displayed an increased appetite for investigating transactions across industries, a trend that is expected to continue in the EU, the U.K. and, under the Biden administration, the United States. Given the increasing complexity of antitrust analysis, regulators tend to rely on companies' internal documents to understand the parties' intentions and likely effects of a transaction.

Accordingly, companies can benefit from better understanding antitrust concepts and processes and, particularly, how internal documents can be used to attack a deal from an antitrust perspective.

Types of Documents

There are two major categories of relevant documents: ordinary course materials and deal documents. Both types of documents are subject to review by the antitrust agencies in a merger review. Examples of ordinary course materials include regularly prepared business and strategic planning documents, sales and marketing materials, and customer call reports. Examples of deal documents include confidential information memoranda, bankers' books, financial models and board presentations. Companies must assume that every nonprivileged document on these subjects will be reviewed by the antitrust agencies at some point in the merger review process.

Mr. Schwartz and Ms. Vandenborre explained that, because ordinary course documents were not produced for the specific purpose of the merger review process, they are deemed by agencies to have greater value, as they highlight the company's views on competitive dynamics when businesspeople are not thinking about a potential deal or regulatory review. Mr. Schwartz and Ms. Vandenborre further explained that deal documents may cast light on the competitive aspects of the transaction and may be used to comprehend valuation, alternative deals and counterfactual scenarios.

Current Practice

Mr. Schwartz explained that in the U.S., internal documents have always played a central role in the merger review process. Where a transaction is reportable under the Hart-Scott-Rodino (HSR) Act, the parties are required to provide certain transaction-related documents (known as Item 4(c) and 4(d) documents) with their initial HSR

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filing. Item 4(c) and 4(d) documents are often the agency's first exposure to a transaction and can set the tone for their review. In this initial review period, the agency may send the parties a voluntary request for documents. If the agency decides to open an investigation, it will issue a request for additional material (known as a second request), which will extend the review period and require the parties to produce a broad set of documents, in addition to other materials.

Ms. Vandenborre added that in the EU, the EU Merger Regulation provides that, in support of their Form CO, merging parties must provide the European Commission (Commission) copies of documents prepared by or for any member of a company's board or for shareholders meetings. Similar document requirements apply in other jurisdictions.

The documents requirements are often supplemented with additional requests for contemporaneous documents. In *ArcelorMittal/Ilva*, *Qualcomm/NXP Semiconductors* and *Bayer/Monsanto*, the Commission indicated it reviewed respectively over 800,000, 1 million and 2.7 million internal documents as part of its in-depth investigations. In *Dow/DuPont*, internal documents were cited to substantiate the Commission's findings in relation to innovation in the agro-chemical sector. Commissioner for Competition Margrethe Vestager noted that internal documents can help the Commission "make better decisions, and understand the markets and companies' plans for the future." [1]

Ms. Vandenborre also explained that in the U.K., the Competition and Markets Authority (CMA) increasingly has examined the merger firms' internal documents as a part of its merger investigations. The revised CMA merger assessment guidelines[2] emphasize the use of internal documents as evidence in merger reviews to reveal anticompetitive intent or potential, particularly when other data or sources of evidence are scarce and market developments may be uncertain. The revised guidelines explain that "where internal documents support claims being made by merger firms or third parties that have an interest in the outcome of the CMA's investigation, the CMA may be likely to attach more evidentiary weight to such documents if they were generated prior to the period in which those firms were contemplating or aware of the merger, or if they are consistent with other evidence."

An Economist's Perspective

Dr. Dick described how agencies' economists and consulting economists retained by the merging parties make use of internal documents in a merger review. He explained that evidence relevant to a merger review comprises (i) business documents, (ii) testimony from market participants and (iii) economic analysis of data. Each category of evidence needs to be firmly connected to the two others: economic and data analysis are credible and convincing only if they reinforce, and are reinforced by, contemporaneous business documents and market participant testimony. He said that internal company documents provide a roadmap for where to look for economic evidence and how to understand and interpret what the company's data say.

Dr. Dick also discussed key roles that business documents play in the assessment of merger efficiencies. First, pre-deal documents discussing efficiencies, even if not quantified in detail, are critical because they support advocacy and economic arguments that efficiencies and synergies are the primary motivator of the merger. It is critical, early into an investigation, to place a counterweight or opposing view to agencies' speculation that elimination of competition or pursuit of higher prices are what motivated a deal. Second, contemporaneous documents that track the merging parties' success in achieving projected efficiencies from previous deals can be used by economists and counsel to help persuade antitrust agencies to give substantial weight to efficiency projections in their review of a pending transaction. Third, even if there are helpful premerger documents that discuss deal rationale or quantify merger efficiencies, they will be heavily discounted or ignored altogether if there also are very provocative documents that point to anticompetitive rationales as well. Dr. Dick concluded that it is extremely hard to overcome these types of deal rationale documents with efficiencies projections, because the implication is that even if prices might not rise as much but for the efficiencies created by the merger, prices still will go up nonetheless. In short, even the best efficiencies documents can be undermined or neutralized by provocative documents.

Internal Documents and 'Killer Acquisitions'

Dr. Latham said that agency economists increasingly use internal documents as central pieces of evidence to assess theories of harm in potential competition cases, *i.e.*, "killer acquisitions," in which the acquirer uses the acquisition to forestall a competitive threat, and "reverse killer acquisitions," in which the acquirer uses an acquisition to enter a market rather than doing so organically. He gave an overview of the three key categories of documents that are of greatest interest in such cases:

[1] Speech by Commissioner for Competition Margrethe Vestager on fairness and competition, Jan. 25, 2018.

[2] Merger assessment guidelines (CMA129), March 18, 2021 revised guidance, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/970322/MAGs_for_publication_2021_.pdf

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First, Dr. Latham identified documents setting out the deal rationale. Agencies will want to see whether the documents are telling a story consistent with a killer acquisition or reverse killer acquisition concern. "Smoking gun"-style quotes are a factor, but the broader industry narrative is as important. For example, are there economic forces or strategic trends that will encourage the buyer to enter the seller's business line in the foreseeable future? The second category involves any kind of "build/buy/partner" analysis. A key element that distinguishes a benign conglomerate transaction from a potential reverse killer acquisition is the extent to which the buyer has expertise and resource to enter organically in a short space of time. Agencies are likely to be skeptical of claims that a large incumbent cannot replicate what a small start-up does. Similarly, high barriers to organic build by the purchaser may be seen as the equivalent of saying that there are barriers for others to compete with the target as well. The third category includes valuation materials. Agencies will examine valuation materials in a way they had not before. (The new CMA merger assessment guidelines add this as a key piece of evidence they will explore.) Agencies will want to examine if there is an unexplained "deal premium" that is not justified by standalone value/synergies; they also will want to examine if any Discounted Cash Flow analysis assumes reductions in investment or growth for the target business or price increases. In addition, agencies will question an acquisition that is at a very large premium as compared to the last funding round, particularly if that premium is not explained by subsequent improvements in the target's business or deal-specific synergies.

Conclusion

One can see a real step change in the prominence given to document review and a real change in how economists are approaching the relative value of documentary and quantitative evidence. This is true in digital markets as well as in more traditional ones.

As such, companies always should be careful in their document creation and interactions with customers and competitors. Even when not contemplating a potential transaction, failure to consider antitrust implications when drafting documents may negatively affect a company's ability to enter into strategic transactions later on. It is important to adopt document creation guidelines and ensure businesspeople and outside advisers are aware of them, and to strive to conduct business and deal activities as if they are going to reviewed with 20-20 hindsight by a government agency.