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Proactive Management of Antitrust Risk Amidst the Q1 M&A Slowdown

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Compared to 2021's record level deal activity, the first quarter of 2022 has registered a dip in global M&A. Analysts report that for January through March of 2022, global M&A is down by approximately one-fifth relative to the same period last year when measured by both deal value and volume metrics. The total value of pending and completed deals announced in Q1 2022 is the lowest since the second quarter of 2020. Big deals are still being signed, including a range of high profile deals in the largest mega-deal bracket (i.e., deals valued at $10B or more), a category that includes, among others, Microsoft/Activision Blizzard ($68B) and TD Bank/First Horizon ($13.4B). Yet, during the early months of 2022, large and mid-market deals—those valued between $1B and $5B—declined 40% relative to last year.

A host of complex factors influence M&A activity at any given time, from inflation to global conflicts to liquidity factors to prevailing regulatory dynamics. To be sure, the current regulatory climate around antitrust issues presents a challenge for deal makers. Progressive leadership at the Federal Trade Commission (FTC) and the Department of Justice Antitrust Division (DOJ) (together, the Agencies) have articulated and begun to execute a broad anti-consolidation agenda, increasing uncertainty and heightening risk associated with the U.S. merger clearance process. Similar trends are playing out across the global antitrust enforcement community. This shift has implications for the costs, timeline, and business disruption associated with the merger clearance process, particularly in light of the Agencies' movement towards disfavoring settlements. But unlike many of the factors that contribute to M&A trends, which are exogenous and uncontrollable by deal parties, concerns about antitrust risk can be assessed and managed.

Gibson Dunn is working actively with clients to ensure that unpredictability around the merger control process under the Biden administration does not create unnecessary barriers to lawful M&A transactions. In this climate, the clear and certain allocation of risk and articulation of regulatory obligations in transaction agreements is paramount. Where appropriate, merging parties should prepare to defend their transactions through federal court litigation in the event that the Agencies adopt theories of harm that depart from standing law or are inconsistent with business realities. Finally, parties should give broad consideration to the implications of Agency non-merger enforcement activity (i.e., investigative studies, conduct enforcement actions, and rulemakings) on potential transactions, and vice versa.

Heightened Uncertainty and Risk Associated With Merger Clearance in the U.S. and Beyond

Since coming to leadership, FTC Chair Lina Khan and Assistant Attorney General Jonathan Kanter of the DOJ have pursued a top to bottom reconsideration of the antitrust agenda. Through rulemaking, promises of tougher enforcement activity, and rescission and (eventual) replacement of key policy documents, the Agencies are seeking to broaden antitrust enforcement and, in so doing, discourage M&A activity. These policies stem, in part, from the Agencies' belief that corporate consolidation has "harmed open markets and fair competition" under overly permissive enforcement regimes in the past decades.

Among the Agencies' most significant departures from past merger review practice is their reconsideration of the Horizontal Merger Guidelines and withdrawal of the Vertical Merger Guidelines, which they deemed "narrow and outdated." Historically, agency staff, as well as deal makers and advisors interpreting the merger laws, have relied heavily on the Horizontal Merger Guidelines and, to a lesser extent (due to their recent revision and the less developed state of vertical merger enforcement), the Vertical Merger Guidelines. Now, the relevancy of the past guidelines is in doubt, but the content and scope of new guidelines is also unknown. What is clear from Agency commentary is that new guidelines are likely to substantially expand the scope of merger enforcement and very well may embrace novel and untested theories of harm, including greater scrutiny of "non-horizontal" transactions (e.g., conglomerate mergers and cross market mergers), examination of the incentives created by the involvement of investment firms, and a newfound emphasis on harm to workers and small businesses.

The Agencies' shifting policy around merger remedies is another source of unpredictability and increased deal risk. In recent remarks, AAG Kanter expressed concern that the Agencies' historical approach to merger remedies has been ineffective. He went on to say that under his leadership the DOJ may be less willing to resolve competitive concerns through divestitures, particularly when a deal involves "innovative markets" or "evolving business models." Instead, when enforcers "conclude[] that a merger is likely to lessen competition, in most situations" the Agency "should seek a simple injunction to block the transaction," rather than trying to cure the harm through divestitures. Accordingly, relative to past practice, merging parties may find the Agencies unreceptive to settlement negotiations. At the least, parties will face more resistance and likely need to offer broader divestiture packages. And even where merger settlements are available, the Agencies have revived the practice of including in consent decrees prior notice and approval requirements in respect of future transactions, with the effect of complicating settlement negotiations and burdening future deals.

Outside of the merger context, the Agencies are taking action that is likely to have second-order effects for M&A. For example, the FTC is actively deploying its Section 6(b) authority, which enables the agency to conduct wide-ranging studies without a specific law enforcement objective. Section 6(b) scrutiny of particularly industries or issues (such as non-reportable technology transactions or particular healthcare sectors) is likely to create obstacles for mergers that coincide with the area of FTC scrutiny. For example, enforcers may be inclined to look more closely at a transaction that relates to an area of active study in order to further their study objectives. In addition, political or PR concerns may enter into the Agencies' calculus about clearing mergers in an industry that is under active 6(b) scrutiny. The same is true for mergers in industries that are being investigated or prosecuted for anticompetitive practices; such mergers may face more intense and searching scrutiny.

Once the new merger guidelines are issued and AAG Kanter and Chair Khan's new policies develop a track record of implementation, we will have a more precise understanding of the operative analytical framework and its implications for M&A transactions. But the practical consequences of Chair Khan and AAG's Kanter's antitrust rewrite are already playing out and the trajectory is unlikely to change: merging parties are bearing more second request risk, broader and longer investigations, less opportunity to resolve competitive concerns with settlements, and greater risk of enforcement action.

Practical Considerations for Dealmakers and Advisors

In light of antitrust's gating function, it is fair to question whether the current antitrust climate has to some extent played a role in the Q1 M&A dip. Yet dealmakers have a range of tools to accommodate and manage the risk engendered by the current regulatory environment. Antitrust considerations should be raised in the earliest phases of deal negotiations. As transaction agreements are negotiated, **clear articulation of regulatory obligations and risk allocation remains critical** in the effort to keep merging parties aligned and ultimately hold deals together when Agency scrutiny comes to bear. Before agreeing to particular efforts standards in purchase agreements in respect of obtaining antitrust approvals, parties should appreciate the possibility that those efforts standards may ultimately require time-consuming and costly litigation.

In some transactions, merging parties are unwilling to carry on if a second request is issued and their agreement reflects that fact. The signal that such a contractual provision sends to the Agencies and the incentives that it creates should be weighed carefully.

Appreciating that merger reviews are likely to be more time consuming, onerous, and costly (whether because the Agencies require more engagement and advocacy during the first 30 days, require a pull-and-refile, or issue a broad second request), **parties should consider building flexibility or extra time into transaction timetables**. For cross-border deals that may be subject to scrutiny in jurisdictions that move slowly or, like the U.S., are broadening their approach to merger enforcement, a sophisticated multi-jurisdiction analysis should be conducted early on so that deal timing can be formulated accordingly. The likelihood of protracted reviews should also be contemplated during deal financing.

Transaction rationale and economics should take account of the Agencies' heightened skepticism of merger remedies and the possibility of the FTC imposing a prior approval clause in those consents that are achievable. Transactions in which divestiture of a full business is feasible will have a better chance of resolving Agency concerns with a remedy, whereas transactions involving dynamic markets are expected to face more settlement resistance.

In light of the FTC's new practice of warning merging parties that they may keep investigations open beyond the expiration of the HSR Act waiting period, **contractual language formulating closing conditions based on the status of antitrust review should be worded precisely**. Likewise, in the context of cross-border transactions that must be notified in ex-U.S. jurisdictions that do not have a statutory bar on closing before the review is complete, merging parties should agree as to whether they will close the deal during an ongoing review, with the buyer bearing the risk of future action by competition authorities.

Even deals that do not present any facial competitive issue may face an uncertain regulatory path if the parties do business in a sector that is the subject of Agency interest, as evinced by 6(b) studies, the Executive Order on Promoting Competition in the American Economy, conduct investigations or enforcement activity, or the Agencies' political agenda. Parties doing deals in these industries should actively consider this layer of risk in consultation with antitrust counsel, so as to ensure that all possible risks are understood and mitigated.

Finally, where possible, **merging parties should consider including commitments to litigate** in their transaction agreement to signal to the Agencies that they are committed to closing and will not be backed off by onerous second requests or a protracted review. Ultimately, merger guidelines and other enforcement policy statements do not bind federal courts. In the event that the Agencies depart significantly from established law and economics, merging parties may have good prospects of vindicating their deals in federal court.

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding the issues discussed in this update. Please contact the Gibson Dunn lawyer with whom you usually work, any member of the firm's Antitrust and Competition or Mergers and Acquisitions practice groups, or the following:

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