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ValueAct: Activist Use of HSR Act's "Passive Investor" Exemption

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[On April 4, 2016,] the U.S. Department of Justice filed a complaint in federal district court alleging that two ValueAct Capital funds repeatedly violated the Hart-Scott-Rodino Act in amassing large equity positions in two oilfield services companies which have agreed to merge. The DOJ's complaint alleges that ValueAct's actions and statements of intention—including repeatedly meeting with both management teams, lobbying other shareholders to vote in favor of the proposed merger, promoting specific integration plans and executive compensation strategies, and proposing operational and strategic changes at the company to be acquired—were inconsistent with investment-only intent. The DOJ's complaint also took the extraordinary step of naming the ValueAct funds' general partner as a defendant.

The HSR Act and its rules require that parties to certain mergers and acquisitions notify the federal antitrust agencies of their proposed transactions and observe a waiting period before consummation. The rules create an exemption from the notice and waiting period requirements for acquisitions of up to 10% of the stock of a company if the purchases are made solely for the purpose of investment and the buyer "has no intention of participating in the formulation, determination, or direction of the basic business decisions of the issuer."

According to the DOJ's complaint, the two ValueAct funds acquired more than $2.5 billion in the two companies' voting securities, far in excess of the HSR Act's lowest notification threshold, in the months following their November 2014 agreement to merge. ValueAct did not file under the HSR Act on either company nor did it observe the applicable waiting period prior to making acquisitions in excess of the filing thresholds. In its complaint, the DOJ alleged that, because of ValueAct's actions and statements, ValueAct was not eligible for the passive investor exemption and thus violated the HSR Act.

Although nearly all defendants settle HSR Act violations in consent decrees, typically for a fraction of the total potential fine, ValueAct has said it will contest the DOJ's lawsuit. Given the

“seriousness” of the alleged current violation and ValueAct’s prior HSR violations, including one settled for $1.1 million in 2007, the DOJ’s complaint seeks a maximum fine and an injunction against future violations. In this case, the total fine could amount to nearly $20 million (based on the HSR Act’s maximum civil penalty of $16,000 for each day a person is in violation).

For decades the DOJ and the Federal Trade Commission have sought to curb what they perceive as overbroad or misplaced reliance on the HSR Act’s “investment-only” exemption by all types of investors. In recent years, the antitrust agencies have become more active in policing the HSR Act abuses of activist hedge funds, including enforcement actions against Biglari Holdings in 2012 andThird Point in 2015. The DOJ’s complaint against ValueAct represents their most forceful action taken to date in this area.