BNA's

BANKING REPORT

BNA Employee-Owned Since 1947

Dodd-Frank Act May Complicate Antitrust Review of Acquisitions

BY DAVID S. NEILL AND NELSON O. FITTS

With the exception of systemic risk considerations, the recently enacted financial reform legislation leaves intact the current antitrust review process for bank mergers. But the Dodd-Frank Wall Street Reform and Consumer Protection Act does create new antitrust review procedures for acquisitions of nonbank financial companies and nonbank subsidiaries of larger financial institutions. Those changes may complicate or lengthen the federal merger review process for financial institution acquisitions.

Dual Agency Review of Large Non-Bank FI Acquisitions

For the past decade — since the Gramm-Leach-Bliley Act permitted bank holding companies to participate in a broad range of nonbank financial activities pursuant to Section 4(k) of the Bank Holding Company Act — acquisitions relating to such nonbank activities were subject exclusively to review by the antitrust agencies (typically the Department of Justice) under the Hart-Scott-Rodino Act.[1] The Federal Reserve Board had no approval authority over these so-called ''4(k)'' activities. Following the financial reform bill, exclusive HSR coverage continues for small 4(k) acquisitions, but acquisitions of entities with more than $10 billion in assets are now subject both to the HSR Act *and* to premerger approval by the Federal Reserve Board.[2] For such large acquisitions, the financial reform bill requires applicants and the Board to follow the notice provisions of Section 4(j) of the Bank Holding Company Act that previously applied only to acquisitions involving activities ''closely related to banking.'' The Board's review criteria will cover the traditional 4(j) factors — including competitive considerations — as well as the reform bill's newly mandated evaluation of systemic risk. Thus, large 4(k) acquisitions are now subject to dual antitrust review by both the Justice Department and the Board under two distinct statutory regimes.

This new dual review poses two concerns. The first relates to timing and waiting periods. The Bank Holding Company Act's notice requirements provide that an application be filed at least 60 calendar days before consummation of the acquisition, although the Board may approve transactions to proceed before the expiration of the notice period. The HSR Act, by comparison, has a 30-day initial waiting period which the reviewing antitrust agency may — and frequently does — terminate early. Transactions raising competitive concerns may pose significant timing issues, since each of the foregoing waiting periods may be extended by the Board and the Justice Department, respectively, if those agencies require additional information or documents about competitive issues (or other concerns, in the Board's case) or demand divestiture remedies. The Board, in particular, has considerable discretion in determining

[1] Other activities ''closely relating to banking'' were long subject to Section 4(c)(8) of the Bank Holding Company Act. Following passage of the Gramm-Leach-Bliley Act in 1999, the Federal Trade Commission's Premerger Notification Office advised that acquirors of 4(c)(8) activities could choose whether to file notifications under the HSR Act with the antitrust agencies or 4(c)(8) applications with the Board. It is unclear at present whether or how the Dodd-Frank Act may affect that prior FTC interpretation.

[2] Section 163 of the financial reform legislation governs $10 billion acquisitions by either (1) bank holding companies with $50 billion or more in assets or (2) nonbank financial companies supervised by the Board on account of their systemic importance to the U.S. economy. Section 604(e) governs $10 billion acquisition of 4(k) businesses by financial holding companies. Both sections adopt the notice procedures already set forth in Section 4(j) of the Bank Holding Company Act, and both sections make clear that the new Board approval requirements do not exempt such 4(k) acquisitions from the HSR Act.

David Neill and Nelson Fitts are partners specializing in antitrust law at the firm of Wachtell, Lipton, Rosen & Katz in New York

 ISSN 0891-0634

whether notice requirements are met or whether the statutory notice period even begins to run.[3]

The new dual review introduces a second concern as to substantive antitrust analysis. If any given transaction raises competitive concerns, the Justice Department and the Board could reach different conclusions as to the nature and scope of those concerns and the remedies needed to resolve them. Indeed, such differences seem likely since the Justice Department and the Board have never before coordinated antitrust review or issued joint guidelines for analyzing nonbank acquisitions, and the Board has no prior experience evaluating competitive effects in the nonbank product lines at issue. In this regard, substantial differences between the Justice Department and the Board frequently arise under the current dual review system for bank mergers, under which each agency applies its own analytical methodology and focuses on different banking product lines — despite their 1995 adoption of joint antitrust guidelines for bank mergers. The current dual review of bank mergers often results in parties divesting assets up to the ''greatest common denominator'' required to satisfy both the Justice Department and the Board, and the Dodd-Frank legislation may lead to a similar result for nonbank businesses.

Antitrust Review of FDIC Non-Bank Liquidation Transfers

The reform act grants the FDIC new authority to carry out orderly liquidations of nonbank financial institutions, mirroring its pre-existing authority with respect to insured depository institutions. The act applies disparate antitrust review procedures for FDIC liquidation transfers depending on whether they are structured as mergers or as asset sales. For merger transactions subject to the HSR Act, the reform act shortens the initial HSR waiting period to 15 calendar days from the normal 30 days.[4] Asset transfers, meanwhile, are addressed in a separate provision that is silent as to antitrust review procedures, but which enables asset transfers by the FDIC to occur ''without obtaining any approval, assignment or consent.''[5]

This disparate treatment of mergers and asset transfers appears to accommodate long-standing FTC interpretations of the HSR Act's exemption for ''transfers to or from a Federal agency'' under Section 7A(c)(4).[6] While the FTC deems asset sales made directly by the FDIC and other federal agencies *entirely exempt* from the HSR Act,[7] the FTC has taken the position that FDIC sales of voting securities of private corporations are not exempt.[8] The latter interpretation is rooted in a 1978 Statement of Basis and Purpose for the original rulemaking process under the HSR Act, which held that ''corporations controlled by [the United States and its agencies and political subdivisions] and engaged in commerce are entities, and may be subject to the requirements of the act.''[9] Even if that 32-year-old statement were consistent with the language of the HSR Act — which exempts all ''transfers to or from a Federal agency,'' without regard to form of transaction — the disparate treatment of asset and voting securities transactions is plainly at odds with modern FTC views. In 2005, the FTC expanded a regulatory exemption allowing parties to ''look through'' corporate forms to determine whether the underlying businesses are exempt from the HSR Act:

> The Commission has concluded that if the direct acquisition of an asset is already exempt, it appears logical to extend that exemption to an acquisition of voting securities of an issuer or of non-corporate interests in a[n] unincorporated entity whose only holding is that same asset.[10]

The logic of the FTC's 2004 statement would seem to invalidate its older interpretations and render all FDIC sales exempt under the HSR Act, regardless of form. But even if the FTC declines to reevaluate its historical view (and reconcile it with the more recent HSR rules), the Dodd-Frank Act's shortening of the HSR Act waiting period for mergers from 30 days to 15 days will reduce the timing disparity between FDIC merger and asset transactions.

Despite its consonance with long-established FTC interpretations of the HSR Act's federal agency exemption, the Dodd-Frank Act's disparate treatment of merg-

---

[3] Under the HSR Act, the Justice Department or the FTC may issue a Request for Additional Information and Documentary Material (''Second Request''), extending the waiting period until 30 calendar days after both parties substantially comply with the Second Request (often a two to three month process). Parties regularly agree to extend the second waiting period by 30 days or more. The Bank Holding Company Act provides that the Board generally must act on an application within 60 days of receiving a ''complete notification,'' but it may extend that period an additional 30 days. In practice, if the Board needs more time, it simply deems the notification incomplete and requests more information, effectively extending the waiting period indefinitely. Past practice in the bank merger arena has been for the Board (which controls timing of bank merger review using similar procedures) to accommodate Justice Department requests for more time to investigate competitive effects. If this practice bleeds over into nonbank mergers, then merger applicants could effectively lose the timing control they otherwise enjoy under the HSR Act, since the Board could extend the Bank Holding Company Act waiting period indefinitely at the behest of the antitrust agency. Such an extension could render meaningless the applicants' compliance with the Second Request and the expiration of the HSR waiting period.

[4] *See* Sections 210(a)(1)(G)(i)(I) and (ii). This shortened waiting period already applies in two other exigent circumstances: cash tender offers and certain acquisitions in bankruptcy. *See* 15 U.S.C. § 18a(b)(1)(B); 11 U.S.C. § 363(b)(2)(B).

[5] *See* Section 210(a)(1)(G)(i)(II).

[6] 15 U.S.C. § 18a(c)(4).

[7] *See* ABA Section of Antitrust Law, *Premerger Notification Practice Manual* (4th ed. 2007), Interp. 11 (''The fact that a government agency, such as the FDIC, is a corporation 'engaged in commerce,' does not change its status as a nonentity for purposes of the Act. The PNO's position is that the FDIC is a federal agency, and therefore, cannot be an entity under Section 801.1(a)(2).''); Interp. 12 (''If the government organization does not meet the criteria for an entity subject to the Act pursuant to Section 801.1(a)(2), the Section 7A(c)(4) exemption applies to all asset transfers to or from it. Any asset transfer, no matter the size of the assets involved, to or from a federal or state agency, as defined by Section 801.1(a)(2), is exempt from the reporting requirements of the Act.'').

[8] *See id*., Interp. 12 (''if a state or federal agency sells voting securities, . . . [t]he transaction will be subject to the Act if the acquired person, the issuer of the voting securities, is an entity under Section 801.1(a)(2) and otherwise subject to the Act.'').

[9] 43 Fed. Reg. 33,450, 33,456 (July 31, 1978).

[10] 69 Fed. Reg. 18,686, 18,693 (Apr. 8, 2004). The amended rule is 16 C.F.R. § 802.4(a).

   ISSN 0891-0634

ers and asset transfers generated confusion among commentators and within Congress itself. For instance, the American Antitrust Institute voiced concern that the reform act's language enabling FDIC asset transfers ''without obtaining approval, assignment or consent'' could be interpreted to exempt FDIC asset transfers from the HSR Act — apparently ignoring the fact that such asset sales *have always been exempt*.[11] Rep. John Conyers (Chairman of the House Judiciary Committee and a House conferee on the bill) may have further obscured the new legislation in remarks published in the Congressional Record.[12] Without referencing the language regarding no ''approval'' or ''consent,'' Rep. Conyers concluded that the bill's silence as to specific review procedures for asset sales would subject those sales to *full* HSR review, denying asset deals even the shortened 15-day waiting period applied to FDIC merger transactions.[13] He admirably went on to encourage the antitrust agencies and the FDIC to establish an ''informal arrangement'' to expedite the processing of all FDIC liquidation transfers — mergers and asset sales alike. Rep. Conyers's interpretation of the legislation could not be correct, however, unless Congress were to repeal the HSR Act's exemption for federal agency transfers — which the Dodd-Frank Act clearly did not do — or the FTC were to reverse decades of regulatory precedent and untenably claim the FDIC is not a ''Federal agency'' for purposes of the HSR Act.[14]

Bank Merger Guidelines Remain Intact

On Aug. 19, the Justice Department and the FTC substantially revised the Horizontal Merger Guidelines under which they have operated since 1992. The revised Guidelines de-emphasize the role of traditional market definition and market concentration tests and elevate various alternative means for determining whether mergers would lessen competition. To the extent market concentration indices — in particular the Herfindahl-Hirschman Index (''HHI'')[15] — will still be used, the revised guidelines relax the safe harbor thresholds used to screen mergers for competitive concerns. The 1992 guidelines used HHI to classify markets as ''unconcentrated'' (below 1,000), ''moderately concentrated'' (between 1,000 and 1,800), and ''highly concentrated'' (above 1,800) and establish safe harbors based on the change in HHI and the level of concentration caused by a proposed merger. The revisions relax the concentration classifications by raising the HHI boundaries for ''moderately concentrated'' markets to 1,500 and 2,500 and making corresponding adjustments to the safe harbor thresholds.

Since 1995, bank mergers have been subject to a different set of antitrust guidelines, as set forth in an interagency agreement between the DOJ and the bank regulatory agencies entitled ''Bank Merger Competitive Review.'' Recognizing that competition from nonbank financial companies impinged on ''banking'' sufficiently to blur product market definitions, the 1995 bank merger guidelines set forth special banking safe harbors somewhat more relaxed than those established by the 1992 Horizontal Merger Guidelines — sanctioning all concentrations with post-merger HHIs less than 1,800 or HHI increases less than 200 points. With some exceptions, the 1995 bank guidelines generally adopted the Federal Reserve Board's predefined geographic markets as a starting point, obviating the need to define such markets from scratch.[16]

It is noteworthy, therefore, that the DOJ staff in its Aug. 19 press release announcing the new Horizontal Merger Guidelines advised that it does not plan to revise the bank merger guidelines in concert with the revisions to the Horizontal Merger Guidelines or as a result of the financial reform legislation. Thus, whereas for 15 years the DOJ has applied more relaxed safe harbor standards to bank mergers than to industrial and nonbank financial company mergers, in some respects the agency will now be more tolerant of concentration in the broader economy than in banking markets. The reasons for this reversal are unclear, but may reflect the challenges of altering an interagency agreement with the banking regulators, particularly in light of ''too big to fail'' criticisms leveled during the financial crisis (see related report in the News section).

[11] *See* letter dated May 11, 2010 from the American Antitrust Institute to Hon. Harry Reid, available at http://www.antitrustinstitute.org/archives/files/HSR%20Exemptions%20Letter.5.11_051120102213.pdf.

[12] Rep. Conyers's remarks are available at http://op.bna.com/bar.nsf/r?Open=jtin-88hncz.

[13] Review under the HSR Act technically does not constitute ''approval'' by the reviewing antitrust agency; the HSR Act merely prevents consummation of the proposed transaction pending the parties' notification and substantial compliance with any Second Request, enabling the agencies to seek an injunction against the transaction if they see fit. Even if the Justice Department and the FTC allow an acquisition to proceed, they are not estopped under the Clayton Act from later suing to unwind the transaction.

[14] It should also be noted that subjecting FDIC transfers of *non-bank* assets to HSR waiting periods would contrast sharply with the current procedures applied to FDIC transfers of *banking* assets. Under the Bank Merger Act, federal bank regulators reviewing third-party acquisitions of banking assets held in FDIC receivership may invoke ''probable failure'' authority to enable immediate consummation of the transactions without waiting for any Justice Department antitrust review. That ''probable failure'' authority for banking assets appears to remain intact under the reform bill. Thus, were it valid, Rep. Conyers's view of the financial reform legislation would create an anomalous procedural disparity between bank and nonbank asset transfers from FDIC receivership.

[15] The HHI is calculated by summing the squares of the market shares of all the competitors in the market and determining how much the index would increase as a result of the proposed merger.

[16] Within this framework, however, the DOJ and the FRB apply different methodologies for weighting thrifts and credit unions in calculating market shares and weigh qualitative mitigating factors (such as troubled banks) differently, such that they often reach different conclusions as to required divestitures. Moreover, the DOJ frequently second-guesses FRB geographic market definitions that the DOJ believes to be too large.