Antitrust Agencies Challenge Two Closed Acquisitions

2008-12-23

Last week, the Antitrust Division of the US Department of Justice and the Federal Trade Commission each brought suit in federal court seeking to undo previously completed transactions that had not been subject to the mandatory reporting and waiting period requirements of the Hart-Scott-Rodino Act (HSR Act). In each case, the agency asks the court to order the acquirer to sell the assets it purchased in an effort to restore the competition allegedly lost as a result of the transaction. The FTC's complaint also seeks disgorgement of assertedly illegal profits that the acquirer gained between the time of the acquisition and the complaint. These cases provide a stark reminder that even deals that are not reportable to the agencies can be investigated and challenged, and that the burden and risks of such investigations and litigation typically falls solely on the acquirer. Further, both cases also show that certain post-transaction conduct can increase the risk of both an investigation and a challenge.

The FTC's case, filed in federal court in Minnesota,[1] challenges the 2006 acquisition by pharmaceutical company Ovation of the US rights to the drug NeoProfen, which the FTC alleges is the only competitor to Ovation's drug Indocin for treating patent ductus arteriosus, a potentially fatal heart defect for some premature infants.[2] The complaint alleges that after it bought the rights to NeoProfen, Ovation raised the price of Indocin as much as 1300% and subsequently introduced NeoProfen at a price nearly identical to the new, higher price for Indocin. Because the purchase of the NeoProfen rights did not meet the HSR Act's filing thresholds, the deal did not receive an antitrust review before closing. The Commission claims that the transaction (a) violated Section 7 of the Clayton Act, which prohibits transactions that may substantially lessen competition, and (b) constituted an act of monopolization in violation of Section 5 of the FTC Act by maintaining Ovation's monopoly in drugs used to treat patent ductus arteriosus in premature babies.[3]

The Antitrust Division's case, filed in the Eastern District of Virginia, challenges the July 2008 acquisition by Microsemi Corporation from Semicoa, Inc. of assets used to develop and manufacture semiconductor devices used in military and space programs. The complaint alleges that since the transaction was completed, Microsemi has both raised prices significantly on those products for which it and Semicoa previously competed and threatened to impose on its customers less favorable service terms than had been available before the transaction.[4]

These cases are noteworthy for several reasons. First, both highlight the fact that the US antitrust agencies are free to--and regularly do--investigate transactions that are not reportable under the HSR Act.[5] Parties to transactions that may raise antitrust issues but do not meet the reporting thresholds need to consider the risks of a government investigation either before or after closing, though the risk of an investigation usually falls on the acquirer since any litigation is likely to occur after closing. The United States is not the only jurisdiction that may investigate consummated transactions. Accordingly, parties to transactions involving assets producing significant non-US sales will also want to consider the risk of investigation and challenge by other jurisdictions.

Second, the cases reflect that post-closing conduct can affect both the likelihood and the outcome of an investigation. Notably, both complaints allege that the acquirer raised prices significantly either immediately or shortly after closing; and the Microsemi complaint also alleges a threatened reduction of service levels. This sort of behavior tends to increase the likelihood of post-closing investigations. If reported in the press, significant price movements or service level changes may attract the attention of the agencies *sua sponte*. More likely, such conduct will anger customers, who (especially if sophisticated) may be willing and able to complain to antitrust authorities and get an investigation opened. Further, as these complaints shows, if the government opens an investigation, it may use the fact of the price increases as direct evidence that the transaction substantially lessened competition in violation of Section 7 of the Clayton Act.

Third, the FTC complaint serves a reminder that the Commission has authority to seek disgorgement of profits from post-acquisition price increases or service reductions allegedly resulting from violations of the antitrust laws. It has used this power sparingly in merger cases, but the disgorgement demand in *Ovation* is not unique.[6] Given that the Antitrust Division has not sought disgorgement in any Section 7 actions, the identity of the agency undertaking the investigation can affect the relief sought.[7]

Finally, it is notable that in both cases, the agency is seeking a complete divestiture of the assets acquired. For small transactions, the agencies will often view complete divestiture as the only possible effective relief, essentially unwinding the transaction. This will likely leave the acquirer without the assets and facing significant losses from a fire sale price for the divestiture and litigation costs and liability in follow-on private litigation. Given these potential costs, it is not surprising that the acquirer has not settled with the agency in either case.

Parties entering into non-reportable transactions are well advised to consider the scope of any competition risk and the implications of any measures designed to mitigate such risk. For instance, acquirers sometimes demand contractual protection against being required to close in the face of a pending competition investigation or payment components tied to profitable operation of the acquired business at some date certain after closing. Sellers, of course, have every incentive to ensure they get their money as quickly possible, and that any risk of an investigation falls squarely on the acquirer's shoulders. These competing considerations can sometimes become a significant negotiating issue and an important factor in how the parties value the transaction.

[1] The State of Minnesota has filed its own, nearly identical action.

[2] The FTC's Complaint can be found here.

[3] Commissioner Rosch filed an interesting concurrence when the Commission approved the complaint, expressing his view that Ovation's earlier acquisition of Indocin from Merck might be challenged under Section 7 of the Clayton Act because, among other things, Ovation, unlike Merck, chose to exploit Indocin's monopoly position by raising price significantly. Commissioner Leibovitz, in a separate concurrence, appeared to agree with Commissioner Rosch's views, at least to some extent, though he chose not to join Commissioner Rosch's statement.

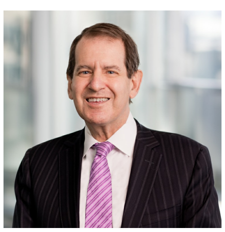
[4] The Antitrust Division's complaint can be found here.

[5] The Act requires that transactions that meet or exceed certain thresholds regarding the size of the transaction and size of the parties must be reported to the antitrust agencies, and the parties must abide by certain waiting periods before closing. Currently, most transactions valued in excess of $63.1 million must be reported.

[6] See, for example, *FTC v. Hearst Trust, et al.*, Civ. No.1:01CV00734 (D.D.C. 2001) in which the FTC challenged a consummated transaction alleging significant post-closing price increases and the acquirer agreed to pay $16 million in disgorgement to settle with the FTC.

[7] It is worth noting, however, that the filing of a government complaint is usually swiftly followed by the filing of private treble damages actions, which means that ultimately the financial penalty paid by the acquirer may be very similar regardless of whether the government seeks disgorgement.

Authors



Leon B. Greenfield

PARTNER

leon.greenfield@wilmerhale.com

+1 202 663 6972