# The Threshold

Newsletter of the Mergers & Acquisitions Committee

Volume XX

Number 1

Fall 2019

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## FROM THE CO-CHAIRS

To All Committee Members:

We have another great issue of The Threshold for you!

Our first article comes from Charles Tingley at Davies Ward Phillips & Vineberg LLP. The article details the Canadian Competition Bureau's recent focus on small acquisitions that do not meet merger notification thresholds. The article takes the reader through the recent challenge to the consummated Thoma Bravo/Aucerna acquisition and Bureau statements about acquisitions in digital markets. The article concludes with the potential implications of this new Bureau priority and provides practical advice for practitioners counseling their clients on this new development.

In our second article, Gabriel Araújo Souto from the ABA Antitrust Section Student Ambassador Program provides an overview of data portability considerations in M&A, including regulatory issues merging parties may face related to their data practices.

The issue closes with a summary from Kelsey Laugel of Kirkland & Ellis LLP of the ABA's recent comments on the FTC's proposed changes to the definition of a "foreign entity" for HSR purposes. We have included the ABA's full comments at the end of the issue.

Our next issue will be published for the Spring Meeting. As always, we encourage Committee members to consider submitting their original articles and letters to the editor for inclusion in The Threshold.

Enjoy the newsletter!

Mike and Joanna

Michael L. Keeley
Joanna Tsai
Committee Co-Chairs

# Small Mergers Are Big Deals for Canada's Competition Bureau

Charles Tingley[1]

The Canadian Competition Bureau is seeking and reviewing smaller acquisitions that may not exceed pre-merger notification thresholds under the Competition Act but that may nonetheless raise substantive competition issues. The Bureau's interest in evaluating smaller mergers (including non-notifiable transactions) is consistent both with its past enforcement practice and competition law issues of the day—specifically, concerns have been expressed by commentators in a number of jurisdictions about the acquisition of innovative start-ups by large digital players and the potential for such transactions to prevent future disruptive competition.[2]

## Getting the Message Out…

The Bureau has telegraphed a more pro-active enforcement approach to small and/or non-notified mergers. In May, the Commissioner of Competition announced that the Bureau had expanded its resources to monitor potentially problematic non-notifiable mergers and had established a "Merger Intelligence and Notification Unit" ("MINU") to carry out these responsibilities. The Commissioner reported that after only two months in operation, the MINU had

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[2] *See, e.g.*, *Unlocking Digital Competition: Report of the Digital Competition Expert Panel* (May 2019), *available at* https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/785547/unlocking_digital_competition_furman_review_web.pdf; Australian Competition and Consumer Commission, *Digital Platform Inquiry: Final Report* (June 2019), *available at* https://www.accc.gov.au/system/files/Digital%20platforms%20inquiry%20-%20final%20report.pdf; Jacques Crémer, Yves-Alexandre de Montjoye and Heike Schweitzer, *Competition Policy for the digital era: Final report* (April 2019), *available at* https://ec.europa.eu/competition/publications/reports/kd0419345enn.pdf; and United States Federal Trade Commission, Hearings on Competition and Consumer Protection in the 21st Century, Hearing #3: Antitrust Framework for Evaluating Acquisitions of Potential or Nascent Competitors in Digital Marketplaces (October 17, 2018), *available at* https://www.ftc.gov/news-events/events-calendar/2018/10/ftc-hearing-3-competition-consumer-protection-21st-century.

detected two transactions that raised potential competition issues.[3] More recently, in September, the Bureau followed-up with a formal media release noting the MINU's expanded responsibility for active intelligence gathering on non-notified merger transactions that may raise competition concerns and encouraging parties to such transactions to voluntarily engage with the MINU well in advance of closing.[4] The Bureau's news release also links to a webpage describing the MINU's responsibilities, which include assisting parties on interpretive issues relating to whether a transaction may be notifiable under the Competition Act.

**…And Driving it Home**

The Commissioner has backed-up his tough talk on small merger monitoring and enforcement with a number of recent enforcement-related actions or initiatives.

In June, the Commissioner challenged the completed acquisition by private equity firm Thoma Bravo of Aucerna, based on concerns that the acquisition would lead to an effective monopoly for the supply of specialized business software used by certain oil and gas producers in Canada.[5] The Commissioner and Thoma Bravo subsequently entered into consent agreements requiring Thoma Bravo to hold separate and divest one of the two overlapping software businesses.[6] Although the Commissioner clarified in a recent position

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[3] *See* Remarks by Commissioner of Competition Matthew Boswell to the Canadian Bar Association Competition Law Spring Conference 2019 (May 7, 2019), *available at* https://www.canada.ca/en/competition-bureau/news/2019/05/no-river-too-wide-no-mountain-too-high-enforcing-and-promoting-competition-in-the-digital-age.html.

[4] *See* Competition Bureau News Release, "Competition Bureau enhances information-gathering efforts on non-notifiable mergers" (September 17, 2019), *available at* https://www.canada.ca/en/competition-bureau/news/2019/09/competition-bureau-enhances-information-gathering-efforts-on-non-notifiable-mergers.html.

[5] *See* Competition Bureau News Release, "Competition Bureau challenges Thoma Bravo's acquisition of oil and gas reserves software firm Aucerna" (June 17, 2019), *available at* https://www.canada.ca/en/competition-bureau/news/2019/06/competition-bureau-challenges-thoma-bravos-acquisition-of-oil-and-gas-reserves-software-firm-aucerna.html.

[6] *See* Competition Bureau News Release, "Competition preserved in the supply of oil and gas reserves software in Canada" (August 20, 2019), *available at* https://www.canada.ca/en/competition-bureau/news/2019/08/competition-preserved-in-the-supply-of-oil-and-gas-reserves-software-in-canada.html.

statement[7] that the transaction was notified to the Bureau in advance of closing and subjected to a three-month review (according to the Commissioner's position statement, the parties completed the transaction despite being advised of the Bureau's concerns), it is notable that the size of the relevant software market in Canada was referred to in the Commissioner's filings as being "relatively modest" with annual revenues in the "tens of millions" of dollars. Indeed, the most recent fully litigated merger challenge in Canada (*Commissioner of Competition v. Tervita Corp.*) arose from a small $6 million acquisition in the oil-waste landfill business that fell below the pre-merger notification thresholds.[8]

More generally, Bureau personnel have been following up with parties to non-notified transactions to request confirmation of certain information, and the Commissioner has recently commenced at least one formal inquiry into a non-notified merger in connection with which he has obtained formal court orders to compel the production of relevant records.

In addition, the Bureau issued a statement in September requesting information from the public about potentially anticompetitive conduct in digital markets, including "creeping acquisitions" of actual or potential competitors.[9] This follows from a report published in late August in which the Bureau summarized highlights from its "Data Forum" held on May 30, 2019 to debate competition policy in the digital era.[10] In its report, the Bureau identified a debate about whether there is an "endemic merger problem" in the tech industry. While the Bureau acknowledged that start-ups are often in the market to be acquired

[7] *See* "Competition Bureau statement regarding Thoma Bravo's acquisition of Aucerna" (August 30, 2019), *available at* https://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04493.html.
[8] Despite its small size, the *Tervita* case resulted in judicial consideration from the Supreme Court of Canada. Interestingly, the only other merger challenge under the Competition Act to come before the Supreme Court of Canada (*Canada (Director of Investigation and Research) v. Southam Inc.*) involved a series of acquisitions that also were not subject to mandatory pre-merger notification.
[9] *See* "Competition Bureau call-out to market participants for information on potentially anti-competitive conduct in the digital economy" (September 4, 2019), *available at* https://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04494.html.
[10] *See* Competition Bureau News Release, "Competition Bureau publishes highlights from recent Data Forum" (August 30, 2019), *available at* https://www.canada.ca/en/competition-bureau/news/2019/08/competition-bureau-publishes-highlights-from-recent-data-forum.html.

based on incremental innovation that fits within pre-existing structures, the Bureau also highlighted a reference to the UK's Digital Competition Expert Panel as having reviewed numerous "under the radar" acquisitions and concluded that a number of problematic mergers were likely missed.

**Implications**

In light of the foregoing, parties to proposed mergers of any size must assess whether they may have anticompetitive effects, even in small or niche markets in Canada, regardless of whether they are subject to mandatory pre-merger notification. Parties should also consider whether to voluntarily seek clearance from the Commissioner,[11] or be prepared to address, or possibly contest before the Competition Tribunal, any issues that the Commissioner may raise before or within one year of closing.

Relevant considerations to bear in mind when conducting this assessment include the following:

- Although resource constrained, the Bureau is capable of reacting quickly in order to challenge proposed or completed transactions and seek interim relief, as demonstrated in the Thoma Bravo/Aucerna matter, where the Commissioner was able to file a challenge within only two months of receiving complete responses from the parties to a supplementary information request (the Canadian equivalent to a Second Request) and within four months of being notified of the transaction.
- The relatively modest size of a relevant market should not be taken as a proxy for a low level of competition law risk—in some respects, the relative smallness of a market may itself raise threshold competition issues in some horizontal mergers, if it may act as a disincentive to future competitive entry, contributing to a possible finding that barriers to entry and expansion are relatively high. Indeed, this was the case in the Thoma Bravo/Aucerna matter, in which the Bureau

[11] Even if a proposed transaction is not subject to mandatory pre-merger notification, parties may apply to the Commissioner for a type of comfort that he will not challenge the proposed transaction (i.e., an advance ruling certificate or no-action letter), although such an application carries a fee that is currently C$73,584.

pointed to the relatively smaller market at issue as "limit[ing] the opportunities for entrants to recoup the sunk costs associated with the development and commercialization of a reserves software."

- Particularly in a digital context, acquisition targets operating in adjacent markets (vertical or otherwise) may be perceived as potential future competitors to the acquiring party, and consideration should be had of each party's future plans for potential expansion into new markets.
- In addition to conducting standard overlap and market share analyses, any internal documents discussing the rationale for the acquisition (including efficiencies, which may form the basis of a defence to otherwise anticompetitive mergers in Canada) and the market positioning of the parties should be carefully reviewed as part of the competition risk assessment.

**The Road Ahead?**

It is possible that the Bureau's renewed interest in non-notified transactions may lead to new initiatives, including proposals for legislative change. For example, the Bureau may follow the lead of some other jurisdictions in conducting retrospective analyses of certain mergers (including non-notified mergers) that were not challenged, in order to draw lessons about their competitive impacts and the relevant factors at play.[12] Similarly, experience that the Bureau may accumulate in monitoring smaller mergers (possibly including the results of any retrospective merger studies) could lead to future proposals by the Bureau to amend the Competition Act to facilitate the Bureau's ability to detect

[12] To the author's knowledge, the Bureau has not conducted formal merger retrospectives involving cases in which there was no agency intervention. In 2011, the Bureau published a summary of its Merger Remedies Study, which reviewed 23 merger transactions between 1995 and 2005 in respect of which the Bureau obtained a remedy in order to assess the effectiveness of the remedies. The summary is available at: https://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03392.html. The Bureau also signaled in its 2018-19 Annual Plan (see: https://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04356.html) that it would issue a white paper on merger efficiencies that, among other things, would analyze prior mergers to see whether claimed efficiencies materialized in line with the parties' pre-closing predictions. However, the Bureau's white paper, which was issued in draft in March 2018, did not contain such an analysis, and a final version of the white paper has not been issued.

and seek timely remedies for small transactions that raise competition issues. For instance, the Bureau may seek to extend the limitation period for challenging non-notified mergers[13] or to amend the thresholds for pre-merger notification to capture a larger number of potentially problematic transactions. However, the Commissioner's track record of enforcement with respect to small and non-notifiable mergers, and the Bureau's fresh commitment of resources to this part of its mandate, suggest that the current statutory regime in Canada is suitable as it relates to the Bureau's ability to review potentially problematic non-notifiable mergers.

[13] The current limitation period for challenging any transaction (notifiable or not) under the Competition Act's merger provisions is one year after substantial completion of the merger. This limitation period was introduced as part of a package of important amendments to the merger review regime in 2009 which, among other things, granted to the Commissioner significantly increased information gathering powers and longer statutory timeframes within which to conduct pre-closing review of notifiable transactions. Prior to the 2009 amendments, the limitation period under the merger provisions was three years after substantial completion of the merger.

# How Does Data Portability Affect M&A? An Operationalization Analysis Through M&A Phases

Gabriel Araújo Souto[1]

## 1. Introduction

Data portability is the possibility of transferring personal data to different platforms.[2] This possibility, enforced by the right to data portability,[3] aims to protect the data storage of users against the incompatibility of multiple platforms, that is, allowing interoperability between different services.[4] Data portability allows, for example, an Instagram user to transfer their data, such as photos and videos, directly to a competitor such as Pinterest, with no barriers to compatibility and preserving the personal data's integrity.

The imposition of data portability would require a certain level of interoperability between platforms.[5] This would benefit both unilateral and

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[1] Gabriel Araújo Souto is an ambassador of the American Bar Association Section of Antitrust Law's Law Student Ambassador Program.

[2] Barbara Engels, *Data Portability Among Online Platforms*, INTERNET POL'Y REVIEW, Vol. 5 Issue 2 (2016), *available at* https://policyreview.info/articles/analysis/data-portability-among-online-platforms.

[3] The General Data Protection Regulation ("GDPR") introduces the right to data portability, giving individuals greater control over their data. *See* Publications Office of the European Union. Article 20 of the Regulation (EU) 2016/679 (General Data Protection Regulation) (2016). The right to data portability not only serves a data protection purpose but also mitigates competing access issues by reducing switching costs and lock-in effect. The Brazilian General Data Protection Law ("LGPD") also standardizes the right to data portability. *See* Diário Oficial da União. Article 18 item V of the Law no. 13.709 (Lei Geral de Proteção de Dados) (2018)

[4] Nathan Sykes, *Frictionless Data: Why Ease and Portability Are More Important Than Ever*, DATACONOMY (Apr. 4, 2018), *available at* http://dataconomy.com/2018/04/frictionless-data-why-ease-and-portability-are-more-important-than-ever/.

[5] Paul De Hert et. al., *The Right to Data Portability in the GDPR: Towards User-centric Interoperability of Digital Services*, COMPUTER LAW & SECURITY REVIEW 196 (Apr. 2018), *available at* https://www.researchgate.net/publication/321198844_The_right_to_data_portability_in_the_GDPR_Towards_user-centric_interoperability_of_digital_services. *See also* Hogan Lovells, *Data Protection in M&A Transactions: A How-to-Guide*, HOGAN LOVELLS PUBLISH 4 (2015), *available at* https://www.hoganlovells.com/files/upload/10358_EUn_GMCQ%20Autumn%202_2015_E.pdf (explaining that in the US, for example, recent amendments to the Health Insurance Portability and Accountability Act ("HIPAA") allow the U.S. Department of Health and Human Services ("HHS") Office for Civil Rights to impose penalties of up to $1.5 million annually for data portability violations).

multilateral market platforms, as the flow of users would enable the network effect to be enhanced, even more with the practice of multihoming, as well as consumers by mitigating switching costs and lock-in effect.[6] To establish an effective form of data portability, technical measures should be in place to easily transfer user data from one platform to another.[7] To some extent, this would require a standard data storage format, such as Application Programming Interfaces ("APIs"),[8] and could be developed by consortia or international organizations to allow platforms to exchange and use such information mutually.[9]

Indeed, data sharing through APIs or common protocols between purchasers and targets is expected to have a profound market impact in terms of innovation and creation of new market opportunities for various stakeholders,[10] since M&A is already being affected by data protection pressures. These pressures are demonstrated by a 2018 research study by Merrill Corporation analyzing 539 M&A professionals, where 55% of them said they had worked on

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[6] *See* Carl Shapiro & Hal R. Varian, *Information Rules: A Strategic Guide to the Network Economy*, HARVARD BUSINESS SCHOOL PRESS 11-13 (1999) (explaining that the lock-in effect occurs when the consumer, dependent on the infrastructure or a particular service of a company, cannot switch to a competitor without substantial costs or material losses. In this sense, the absence of data portability has the potential to produce this effect to the consumer, since the latter may not be able to transfer its data to another platform, causing the user to remain using the service).

[7] Deloitte, *How to Flourish in an Uncertain Future, Open Banking and PSD2*, DELOITTE LLP PUBLICATIONS 8-9 (2017), *available at* https://www2.deloitte.com/content/dam/Deloitte/cz/Documents/financial-services/cz-open-banking-and-psd2.pdf (highlighting open standards of interoperability as important facilitators of competition). For example, the UK antitrust authority has demanded Open Banking standards in its attempt to increase competition in the retail banking market by allowing financial technology innovators to enter a market through access to APIs based on common technical standards. *Id.*

[8] *See* LIMSwiki, *Application Programming Interface*, LIMSWIKI ARTICLES (May 26, 2015), *available at* https://www.limswiki.org/index.php/Application_programming_interface (defining API as "a particular set of rules and specifications that software programs can follow to communicate with each other. It serves as an interface between different software programs and facilitates their interaction, similar to the way the user interface facilitates interaction between humans and computers.").

[9] Inge Graef et al., *Putting the Right to Data Portability into a Competition Law Perspective*, THE JOURNAL OF THE HIGHER SCHOOL OF ECONOMICS ANNUAL REVIEW 5 (2013), *available at* https://ssrn.com/abstract=2416537.

[10] Martin Koderisch, *GDPR – Overview of 'Data Portability,'* Edgar, Dunn & Company Blog (Aug. 1, 2017), *available at* https://edgardunn.com/2017/08/gdpr-overview-of-data-portability/.

deals that fell apart because of concerns about a target company's data protection policies and compliance with GDPR.[11]

Therefore, the implementation of data portability policies and tools by companies prior to M&A operations promotes less costly data transfer between companies and their customers.[12] Furthermore, it increases the efficiency of the operation as the migration of data will be less time consuming,[13] which can mitigate the potential loss of profit by the company's performance decline when data is critical to its operation. The steps to ensure an effective and compliant M&A operation considering data portability will be noted in the topic below.

## 2. The Importance and Operationalization of Data Portability in M&A

Personal data is an important aspect of most M&A transactions as almost every company stores information about its employees and customers.[14] Data is critical for some transactions.[15] To explain that, the analysis of the importance of data portability in M&A is structured in the form of a timeline, analyzing each stage of the transaction: (i) pre-signing, (ii) signing, (iii) signing to closing, and (iv) post-closing.

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[11] Nina Trentmann, *Data Protection Concerns Upend M&A Plans*, WALL STREET J. (Nov. 13, 2018), *available at* https://blogs.wsj.com/riskandcompliance/2018/11/13/data-protection-concerns-upend-ma-plans/.

[12] Richard Harroch, *The Importance of Online Data Rooms in Mergers and Acquisitions*, Forbes AllBusiness Blog (Aug. 15, 2016), *available at* https://www.forbes.com/sites/allbusiness/2016/08/15/the-importance-of-online-data-rooms-in-mergers-and-acquisitions/#26e6b0393566.

[13] *Id.*

[14] The importance of data in M&A can be illustrated by the acquisition of Nest by Google in early 2014. *See* Sophie Curtis, *What is Nest and Why Has Google Bought It?*, THE DAILY TELEGRAPH (Jan. 14, 2014), *available at* https://www.telegraph.co.uk/technology/google/10570414/What-is-Nest-and-why-has-Google-bought-it.html (describing that Nest, a producer of smart home devices such as thermostats and smoke detectors, was not competing with Google in any relevant markets when it was acquired by Google. However, this move by Google has strengthened its position regarding access to data on consumer behavior. The Nest acquisition may have impacted not only Google's ability to improve the relevance of existing services offered to users and advertisers on its search platform but also enabled Google to develop new products based on new insights gained from data analytics of Nest and by combining it with Google's information.).

[15] Hogan Lovells, *supra* note 5, at 3.

**(i) Pre-signing**

M&A operations look to combine customer databases to maximize transaction value, but this can raise privacy and data protection compliance issues. The operating efficiencies envisaged for an integrated business may be challenged by cross-border data transfer controls that prevent or restrict consolidation of data center and other operations.[16] Moreover, in a merger setting, remedies of data portability or data sharing may play a role as tools to prevent a merger from significantly impeding effective competition. For example, the European Commission ("EC") in the 2008 Thomson/Reuters merger decision, by approving the merger on the condition that the merging parties would divest copies of their databases containing financial information, together with relevant assets, personnel and customer base as appropriate, set a remedy that would allow purchasers of the databases to quickly establish themselves as a relevant competitive force in the market of the merged entity.[17]

Under US law, the pre-closing disclosure of personal data must comply with all relevant state laws, contractual restrictions, and promises made about the treatment of personal data in the target's published privacy policy.[18] For example, the FTC has made clear that it views the failure to comply with published privacy policies as a violation of Section 5 of the FTC Act.[19] In the European Union

[16] *See* Anca D. Chirita, *Data-Driven Mergers under EU Competition Law*, THE FUTURE OF COMMERCIAL LAW: WAYS FORWARD FOR HARMONISATION 22 (Jul. 13, 2018), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3199912 (explaining that "[i]n *Google/DoubleClick*, there were a number of competitive advantages for Google following the integration of DoubleClick's ad serving technology with ad intermediation services, Double Click's customer base among publishers and advertisers, and data about consumer behavior collected through ad serving. . . . A portability issue became apparent as advertisers had to transfer 'past' data from one system to another. It was, however, estimated that less than 1% of former customers would require the migration of historical delivery data upon switching.").
[17] Inge Graef et. al., *Data Portability and Data Control: Lessons for an Emerging Concept in EU Law*, SSRN Electronic Journal 1391 (Jan. 2017), https://www.researchgate.net/publication/322236453_Data_Portability_and_Data_Control_Lessons_for_an_Emerging_Concept_in_EU_Law.
[18] Daniel Ilan, *Privacy in M&A Transactions: Personal Data Transfer and Post Closing Liabilities*, Harvard Law School Forum on Corporate Governance and Financial Regulation (Nov. 10, 2016), https://corpgov.law.harvard.edu/2016/11/10/privacy-in-ma-transactions-personal-data-transfer-and-post-closing-liabilities/.
[19] *Id.*

("EU"), it is noticed the inclusion of the EC's standard contractual clauses on M&A to avoid potential Data Protection Authorities filings.[20]

Therefore, under US law, most of the focus is on the target's and purchaser's privacy policies and promises. But in the EU, the focus in review of post-acquisition practices is on the purposes for which the data was initially collected. The use of the data by the purchaser must be in a manner consistent with the specified purposes for which it was obtained by the target in the first place.[21] Apart from the regulatory compliance issues, the costs of integrating databases may be substantial and create transaction risk. Consequently, if the companies involved in the operation don't have an existing data portability infrastructure, it is fundamental to create a data protection "heat map" to identify areas of highest compliance risk on data portability for the target.[22] In that sense, it is important that a transfer or disclosure of personal data may occur in connection with an M&A transaction, including before consummation of the transaction, being advisable for the seller to enter into a data portability agreement with the purchaser concerning such obligations.

**(ii) Signing**

If after the due diligence phase the parties reach an agreement for the transaction, they will sign a contract, which can be either a share purchase agreement, an asset purchase agreement, or a combination of both. In case specific infringements were spotted during the due diligence process, the buyer will have to consider whether it expects the seller to remedy such breaches pre-closing, or to bear fines or damages related to them. If an identifiable risk, such as lack of data processing agreements, is spotted during the due diligence phase, a price correction or a specific indemnity could be a solution.[23]

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[20] *Id.*
[21] *Id.*
[22] Hogan Lovells, *supra* note 5, at 4.
[23] Sarah De Wulf, *GDPR Meets Corporate: (New) Opportunities in an M&A Case*, Stibbe Blog (Aug. 16, 2019), *available at* https://www.stibbe.com/en/news/2019/august/gdpr-meets-corporate-new-opportunities-in-an-ma-case.

Due diligence of a potential target is necessary to ensure compliance at a target level, being fundamental to have strong and well negotiated confidentiality agreements and non-disclosure agreements.[24] If personal data is shared outside of the EU under a non-disclosure agreement, compliance with an adequate level of protection, standard model clauses, and data portability will need to be assessed.[25] Consequently, a previous data portability infrastructure between the parties involved in the operation would alleviate the need for interoperability standards agreements during this phase, reducing the risks of data transfer, avoiding data protection issues and complying with international data protection laws, which would facilitate cross-border data transfer as it would be easier to be internationally compliant if a stricter legislation is followed.

**(iii) Between Signing and Closing**

Integration between signing and closing may require the transfer of personal data between seller and buyer prior to the closing. But the scope of information at this moment can be sanctioned under gun jumping. For integration projects involving large amounts of data, buyer and seller may consider creating a governance framework to ensure that data protection concerns are reflected during each stage of the process. Under the principle of accountability, the seller must be able to register that data protection principles were conscientiously applied throughout the process, and what safeguards have been implemented to ensure that the whole process is reversible if the closing does not occur, which can be set through a data portability infrastructure that allows the vice-versa free flow of data transfer.[26]

During the period between signing and closing, antitrust authorities may request additional information.[27] If the parties' businesses involve the collection

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[24] Rabindra Jhunjhunwala et al., *Impact of GDPR on M&A Transactions in India*, FORTUNE INDIA (Sep. 13, 2018), *available at* https://www.fortuneindia.com/opinion/impact-of-gdpr-on-ma-transactions-in-india/102437.
[25] *Id.*
[26] Hogan Lovells, *supra* note 5, at 8.
[27] Inge Graef et. al., *supra* note 17, at 1390 (exemplifying that the EC, in its Facebook/WhatsApp merger decision made clear that it had not found any evidence suggesting that data portability

and aggregation of significant amounts of customer data, it is important to analyze whether the combination of those data sets creates a competitively significant barrier to entry that could harm competition.[28] Parties in transactions involving a combination of large sets of user data should be prepared to address potential arguments that the deal will foreclose or undermine smaller competitors.[29] A data portability policy could inform antitrust authorities about efforts made by parties to reduce lock-in effect and switching costs.[30]

**(iv) Post-closing**

Acquiring data assets through an acquisition does not automatically give a buyer rights to use the data. For example, in the US, regulators have made clear that buyers must continue to honor the privacy commitments made by the seller before closing. In the EU, the post-closing data processing operations are generally part of a broader set of technical and operational services covered by a transitional services agreement. After closing, the parties to the transaction will generally have to continue migration and integration efforts, a process that can last up to two years.[31] As part of transaction integration, parties will need to assess how data protection policies and practices of the acquirer and the target can

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issues would constitute a significant barrier to consumers' switching in the case of consumer communications apps. "Even though the [EC] did not consider restrictions on data portability to constitute barriers to switching in the specific circumstances of the case, the fact that these issues were investigated under merger review illustrates the potential of competition law to address data portability."). *See also* Daniel Ilan et. al., *supra* note 18 (explaining that in the US, "Although at the time of the acquisition WhatsApp's privacy policy contained an express provision stating that it reserved the right to transfer users' personal data to a third party in the event of a merger or acquisition, the FTC took the position that post-acquisition, WhatsApp must continue to abide by its original privacy policy (which promised not to share personal data with third-party companies for commercial or marketing use, except with users' consent or as part of programs or features to which users would be able to opt-in or opt-out of).").

[28] *See* Anca D. Chirita, *supra* note 16, at 31 (explaining that "in *Sanofi/Google/DMI JV*, the parties lacked the ability to lock-in patients by limiting or preventing the portability of their data. A similar approach was used in *Microsoft/LinkedIn*, specifically, that 'the merger does not raise competition concerns resulting from the possible post-merger combination of the data', including more specifically, personal and behavioral data.").

[29] Sarah De Wulf, *supra* note 23.

[30] *See* Anca D. Chirita, *supra* note 20, at 19 (elucidating that in TomTom/Tele Atlas, "customers had to reconfigure the new database when switching suppliers of navigable digital map databases. The EC that barriers to switching were relatively limited to the reconfiguration cost, including that of modifying production tools to handle different data formats.").

[31] Hogan Lovells, *supra* note 5, at 9.

be aligned,[32] integrating the acquired businesses into the buyer's data protection governance arrangements.

Under US law, a decisive factor in analyzing the legality of a transfer of personal data will be the promises contained in the target's published privacy policy.[33] In the EU, a transfer of personal data at closing as part of an M&A transaction requires showing that at least one of the grounds for transfer is found.[34] Additional steps may have to be taken in the case of transfers of data outside the European Economic Area (EEA). EU law imposes stringent regulatory constraints on the transfer of personal data outside the EEA to a country that is not deemed to have an adequate level of data protection, which includes the US, unless the transfer is to a company having self-certified under the EU-US Privacy Shield.[35] Therefore, a data portability policy should also be developed after post-closing, since it would benefit users of M&A companies who would like to migrate their data and reduce problems in international trade, as the transfer of international data could face restrictions under data protection regulations, such as the GDPR, which requires an adequate level of data protection from countries outside the EU.

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[32] Rabindra Jhunjhunwala, *supra* note 24.

[33] *See* Daniel Ilan et. al., *supra* note 18 (exemplifying that the FTC, through a settlement it reached with internet retailer Toysmart in 2000 (the "Toysmart Settlement") which allowed Toysmart, after it ceased operations, to transfer customer personal data to a third party in spite of its privacy policy stating that such personal data would "never be shared with a third party." As an alternative to the Toysmart Settlement, the FTC proposed in the RadioShack and Borders cases "requiring the target to obtain affirmative (opt-in) consent of the data subjects to the transfer of the data to the purchaser and to purge the data of those who did not consent.").

[34] *See* Franz Urlesberger, *Does the Right to Privacy Play any Role in Merger Control Proceedings?*, Schonherr Blog (2018), *available at* https://www.schoenherr.eu/publications/publication-detail/does-the-right-to-privacy-play-any-role-in-merger-control-proceedings/ (showing that "[a]nother recent example of data protection rules coming into play within the competitive assessment came to light during the EC's assessment of an envisaged joint venture between Sanofi and Google. The joint venture was meant to offer services for the management and treatment of diabetes, including data collection, processing, and analysis. In its competitive analysis, the EC addressed concerns voiced over the ability of the parties to lock-in patients by limiting or preventing the portability of their data towards alternative services. The [EC] dismissed these claims by inter alia pointing to the GDPR, which will provide the users with the right to request portability of their personal data . . . In light of this, the EC considered the power of locking-in patients to the services of the joint venture to be unlikely in the foreseeable future.").

[35] Daniel Ilan et. al., *supra* note 18.

## 3. Conclusion

Considering the efficiencies of a previous data portability policy and infrastructure between the companies entering into an M&A process, prior to signing, a purchaser's due diligence will involve a risk analysis of transfer and disclosure of data related to the M&A transaction. The seller should consider entering into a data portability agreement with the purchaser with respect to such obligations, defining and categorizing the types of data related to the operation identifying which data should be considered portable before the M&A transaction, as well as running a comparative test confronting the M&A's portability risks in light of data protection compliance. On signing, the parties should perform a deep examination of the data portability infrastructure between the companies to reduce the risks of data transfer and comply with international data protection laws. Between signing and closing, a thorough data portability report, which can be made under a data protection impact assessment, and a risk assessment related to data transfer should be made to inform antitrust authorities about efforts made by parties to reduce any lock-in effect and switching costs. After the transaction closes, it is important to develop and implement tools for customers and employees to download their data to have data mobility compliant with the most rigorous data protection frameworks across the globe.

# Summary of ABA Comment on FTC Amendments to Pre-Merger Notification Rules

Kelsey Laugel[1]

On December 30, 2019, the ABA Antitrust Law Section submitted comments to the FTC's proposed amendments to the premerger notification rules regarding the definition of a foreign entity for purposes of the Hart-Scott-Rodino ("HSR") Act. The HSR reportability of certain transactions can hinge on the availability of certain exemptions that require one or more entities to be classified as foreign.

Under the HSR Rules, one criteria in defining an entity as "foreign" is that it cannot have its principal offices in the United States. See 16 C.F.R. § 801.1(e)(2)(i)(A). The Statement of Basis and Purpose accompanying the HSR Rules defines principal office as "that single location which the person regards as the headquarters office of the ultimate parent entity." 43 Fed. Reg. 33,450, 33,461 (July 31, 1978). Current informal guidance from the FTC indicates that the location of officers is also key in determining whether an entity is foreign.

Under the proposed amendments, a company's principal offices would be in the United States if (1) 50% or more of its officers reside in the United States or (2) 50% or more of its directors reside in the United States or (3) 50% or more of the company's assets are located in the United States. The ABA provides commentary and the following suggested revisions with respect to each of these three proposed thresholds: (1) the residency of officers test should be based on the officers' principal places of work rather than the officers' residences as this is easier to determine and more relevant to the conduct of the business; (2) the residency of directors test should be entirely omitted as it bears little relation to the location of the offices of an entity, is an uncertain and burdensome determination, is inconsistent with ICN and OECD best practices, raises potential

[1] Kelsey Laugel is an associate in the Antitrust & Competition group of Kirkland & Ellis LLP.

data privacy concerns, and has the potential of discouraging companies from selecting board members that reside in the United States; and (3) certain exemptions should be incorporated into the asset rule such that non-operating assets are exempted, there is a carve-out for companies that do not have any owned or leased property in the United States, and the asset determination is based on book value rather than a fair market valuation analysis.

Alternatively, the ABA proposes a test whereby parties are vested with the responsibility to determine in good faith whether a company's principal offices are located in the United States based on the totality of the circumstances, analogous to the "nerve center" test in *Hertz Corp. v. Friend*.

The ABA's full comments follow.

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December 30, 2019

**Via Electronic Link:**

Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, DC 20580-0002

SUBJECT: Federal Trade Commission "16CFT parts 801 and 803: Amendments to the Premerger Notification Rules, Notice of Proposed Rulemaking, Matter No. P989316"

Dear Sir/Madam:

On behalf of the American Bar Association Antitrust Law Section, I am pleased to submit the attached comments in response to the request for public comments on "16 CFR parts 801 and 803: Amendments to the Premerger Notification Rules, Notice of Proposed Rulemaking, Matter No. P989316".

Please note that these views are being presented only on behalf of the Antitrust Law Section. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and should not be construed as representing the policy of the American Bar Association.

If you have any questions after reviewing this report, I will be happy to provide further comments.

Sincerely,

Brian R. Henry
Chair, Antitrust Law Section

attachment

**COMMENTS OF THE AMERICAN BAR ASSOCIATION ANTITRUST LAW SECTION TO THE FEDERAL TRADE COMMISSION ON 16 CFR PARTS 801 AND 803: AMENDMENTS TO THE PREMERGER NOTIFICATION RULES, MATTER NO. P989316**

December 30, 2019

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*The views stated in this submission are presented on behalf of the Antitrust Law Section. They have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and therefore should not be construed as representing the policy of the American Bar Association.*

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The Federal Trade Commission ("Commission or "FTC") proposes amendments to the premerger notification rules to clarify the location of an entity's "principal offices." Where an entity has its principal offices is one factor in determining whether an entity is a U.S. or foreign entity for purposes of the Hart-Scott-Rodino ("HSR") Act. Some exemptions in the HSR rules require one or more entities to be foreign. Thus, changing the current definition of "principal offices" to classify additional entities as US instead of foreign will affect the reportability of certain types of transactions that have previously been exempt.

As is, the HSR rules state that an entity is foreign if it (1) is not incorporated in the United States, (2) is not organized under the laws of the United States, and (3) does not have its *principal offices* in the United States. A natural person is considered to be a foreign person if he or she is not a citizen of the United States and does not reside in the United States.

At this time, there is only informal guidance from the FTC's Premerger Notification Office ("PNO") regarding the definition of "principal offices." This guidance states that the location of directors and board meetings is generally not relevant in determining the location of principal offices; the location of officers is key.[1] The Commission's current position is consistent with the original position taken by the Commission in its 1978 Statement of Basis of Purpose promulgating the HSR rules, which state that: "principal offices refers to that single location which the person regards as the headquarters office of the ultimate parent entity. This location may or may not coincide with the location of its principal operations."[2]

Under the FTC's proposed amendments, a company's principal offices are within the United States if any of the following apply:

1. 50 percent or more of the officers[3] reside in the United States;

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[1] Interpretation 156, ABA Premerger Notification Practice Manual (5th Ed. 2015), citing Commission Informal Interpretations 0709017, 1003003 and 0803016.

[2] 43 Fed. Reg. 33,450, 33,461.

[3] Existing HSR informal interpretations indicate the relevant officers for HSR purposes, as described in Example 1 to paragraph (e)(1) of the FTC's notice of proposed rulemaking, "the individuals in positions that are

2. 50 percent or more of the directors reside in the United States; or
3. 50 percent or more of the company's assets are located in the United States.

An entity is a foreign issuer if the entity satisfies none of the three criteria above.[4] Several exemptions within the HSR rules rely on the definition of principal offices to determine whether an entity is a U.S. entity or a foreign entity:[5]

- 16 C.F.R. § 802.50(b) – an exemption for the acquisition of foreign assets valued below $359.9 million where the buyer's parent and the seller's parent are both foreign entities and have less than $198 million in combined US sales and less than $198 million in combined US assets.
- 16 C.F.R. § 802.51(a) – an exemption for the acquisition of a foreign entity with less than $90 million in US sales and less than $90 million in US assets.
- 16 C.F.R. § 802.51(b) – an exemption for the acquisition of a minority stake in a foreign entity where buyer's parent is also a foreign entity.
- 16 C.F.R. § 802.51(c) – an exemption for the acquisition of a foreign entity valued below $359.9 million where the parents of buyer and seller are both foreign entities and have less than $198 million in combined US sales and less than $198 million in combined US assets.

The most frequently used exemptions described above are 802.51(a) and 802.51(b). The FTC's proposed change will not affect the reportability of transactions that would have been exempt under old 802.51(a) because another exemption, 802.4, does not require the existence of a foreign issuer. Under 802.4, the acquisition of an entity holding US and foreign assets will be exempt if the entity's foreign assets generated less than $90 million in US sales and the entity's US assets are valued below $90 million. The acquired entity need not qualify as a foreign entity under the HSR rules. Because 802.4 can exempt all transactions that would be exempt under 802.51(a), the principal value of 802.51(a) has been to lessen the burden on parties trying to determine whether an exemption applies. Analysis under 802.4 requires separating an entity's assets into U.S. and non-U.S. assets and identifying sales generated by U.S. versus non-U.S. assets. While some companies may keep this information in the ordinary course of their business, the process of gathering and organizing the data in the way that the FTC requires is often time

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either (a) provided for in the entity's articles of incorporation or by-laws, or (b) appointed by the board of directors." Premerger Notification; Reporting and Waiting Period Requirements, 84 Fed. Reg. 58,348 (Oct. 31, 2019) (to be codified at 16 C.F.R. §§ 801, 803). The Section recommends including this definition of officer in the final amendment.

[4] The FTC proposes a distinct test for non-corporate entities. For entities without officers or directors, such as limited partnerships, the FTC proposes looking to persons who perform the same function as officers and directors. If those positions are filled by contracting with a third party instead of using natural persons, such as through a general partner or investment manager, the FTC proposes that no residency test is required. If any such managing entity is incorporated under US law or organized under the laws of the United States, then the officers/directors are deemed to reside in the United States and the entity will be a U.S. entity. Past guidance indicated that the location of a general partner or investment manager was not relevant to whether a non-corporate entity is a U.S. entity. *See* Notice of Proposed Rulemaking, 84 Fed. Reg. 58,348 (Oct. 31, 2019) at 58,350.

[5] All of the thresholds used herein are the inflation-adjusted thresholds for 2019. *See* Revised Jurisdictional Thresholds for Section 7a of the Clayton Act, 84 Fed. Reg. 7,369, at 7369-70 (Apr. 3, 2019).

consuming. Because the information needed for 802.51(a) is more readily available, it is easier to administer. Under the FTC's proposed rule, as noted below, it will be more difficult to determine whether an entity is foreign in order to use 802.51(a).

The proposed rule has a different effect on the exemption provided by 802.51(b). The minority investments previously exempt under 802.51(b) cannot necessarily be exempted using 802.4. Thus, under the proposed rule, some transactions that were previously exempt would be reportable, as further explained in Part 2.

The Section welcomes the FTC's attempt to clarify the definition of principal offices. The Section agrees with the FTC that the "principal office" concept can be "hard to define and difficult to apply to modern globalized businesses." Moreover, the Section is in broad agreement with the principles that seem to underpin the proposed amendments: a company's "principal location" should be based on the location of its operating assets and brainpower. However, the FTC's proposed amendments are likely to increase ambiguity and uncertainty, increase the burden on some companies, and lead to divergent filing determinations for certain transactions that are virtually identical. The Section proposes changes to the proposed amendments to ameliorate these concerns.

1. **The Section respectfully recommends that the FTC's officer test should be based on the officers' principal place of work rather than the officers' residences.**

Although there are likely to be exceptions, the work location of a majority of a company's officers is likely to correlate significantly with a company's principal offices.[6] That said, the relevant location of officers—a reason the company might have a material nexus with the United States—should be based upon the officers' principal workplace, not their residence. Where officers primarily conduct business is more relevant than where they spend their time not conducting business. For that reason, the Section respectfully urges the FTC to base the officer test upon the company's location at which a majority of its officers primarily conduct business.[7]

We recognize that an officer's principal place of work may not always have a quick answer. Business travel, working from home, and working out of multiple offices could complicate the analysis. However, determining an officer's principal place of work is likely to be less burdensome than determining residence, and less intrusive.[8]

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[6] Although all corporate officers perform important functions, some corporate officers are likely closer to a company's core operations. For example, the responsibilities of a company's CEO, CFO, and COO are likely more relevant to the company's core operations than a Chief Information Officer, Chief Human Resource Officer, or a Chief Compliance Officer.

[7] While this test may be administrable for friendly transactions, it may not be possible to determine the identity of the officers, as that term is defined under the HSR rules, in hostile transactions. To resolve this issue, the FTC could consider limiting the officer analysis for the purposes of determining whether a company is a foreign issuer to top-level officers (i.e., Chairman, CEO, President, COO, and CFO, if those titles or their equivalent exist). *See supra* note 6.

[8] Similar concerns described in Section 2 of this submission regarding the determination of a director's residence apply to the determination of an officer's residence.

2. **The Section respectfully recommends that the FTC should omit the proposed amendment related to directors.**

As noted above, the proposed rules attempt to clarify when a person or entity is a United States or a foreign person or issuer. Under the proposed amendment, a person or entity would be deemed to have its principal offices in the United States if 50 percent or more of its directors reside in the United States. The proposed rule related to directors bears little, if any, connection to the location of an entity's principal offices, fails to meet International Competition Network ("ICN") and Organisation for Economic Co-operation and Development ("OECD") standards related to assertion of jurisdiction only over transactions with a material nexus to the reviewing jurisdiction, and is likely to be burdensome in some cases.[9]

The residency of an entity's directors bears little, if any, relationship to the principal offices of an entity. In general, a board of directors is responsible for a corporation's high-level management.[10] In practice, to discharge that duty, directors are responsible for (1) appointing officers who run the day-to-day operations and propose strategies to implement corporate plans; (2) supervising officers; and (3) making certain high-level corporate decisions (e.g., M&A, adopting an annual budget, or dissolving the company). Although directors serve an important function, unlike officers who manage a company's day-to-day operations, non-executive directors are generally not involved in the day-to-day operations of a company. Therefore, directors need not reside in the same country as a company's principal office (nor near any office of the company, for that matter). Because directors can and do reside in many global locations, it has become increasingly common for boards of directors to conduct meetings telephonically or via internet services such as Webex.[11] In any given year, a director might not, and has no obligation to, visit a corporation's principal offices to discharge his or her duties.

Corporations select directors for a variety of reasons. Those reasons include industry knowledge, expertise related to a particular need of the corporation (e.g., legal, HR, M&A experience, or financial knowledge), ability to help raise funds for a startup, regulatory or political expertise, or knowledge related to particular business segments, among others. With the exception perhaps of community boards of nonprofit entities such as charities or hospital systems, a board member's residence is may not be a relevant consideration for his or her selection or service. Indeed, a corporation may select a director precisely because he or she has experience in particular far-flung markets. Because a director's residence does not necessarily bear any relation to the location of a corporation's principal offices, the proposed 50% of directors rule fails as a proxy for a corporation's principal offices.

Many directors are otherwise unaffiliated with a company and serve as officers or directors for one or more unaffiliated companies, universities, or other organizations. Indeed,

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[9] INT'L COMPETITION NETWORK, RECOMMENDED PRACTICES FOR MERGER NOTIFICATION AND REVIEW PROCEDURES (2018), *available at* https://www.internationalcompetitionnetwork.org/wp-content/uploads/2018/09/MWG_NPRecPractices2018.pdf; OECD, COUNCIL RECOMMENDATION ON MERGER REVIEW (2005), *available at* http://www.oecd.org/daf/competition/mergers/40537528.pdf.

[10] *See e.g.*, 8 DEL. CODE ANN. § 141 (2019).

[11] In some cases, corporations hold board meetings at unaffiliated locations hosted by a third party.

many individuals serve on multiple boards. Although companies may have information about how to contact a director by mail, companies do not track the residence of their directors in the ordinary course of business. As the FTC notes in the Notice of Proposed Rulemaking, it has not provided guidance about the meaning of "residence." The FTC proposes three potential alternatives: (1) primary tax residence; (2) country of residence for more than half the year; or (3) location of at least half of the real property owned by the director. For (2) and (3), there are likely situations in which a director does not reside in any country for more than half of a year or no country is the site of at least half of a director's real property. In most cases, the location of a director's primary tax residence, country of residence for more than half of a year, or location of real property is driven by personal or professional priorities (e.g., tax minimization, another job, etc.) unrelated to the company for which he or she is a director. Because these factors bear no relation to a corporation's principal offices, they should not affect whether a company is subject to an HSR filing obligation.

Any similar attempt to define residence is likely to be fraught with uncertainty and undue complication. Without clear guidance related to how to determine residency, corporations will be uncertain about whether a filing is required unless they go through the potentially burdensome exercise of collecting personal information from directors that is unrelated to their service to the company in order to make this determination. Therefore, the 50% of directors rule fails to meet the ICN Recommended Practices for Merger Notification and Review Procedure I.E. that "mandatory notification thresholds should be based on objectively quantifiable criteria."

The cost and burden are magnified if the transaction is hostile or involves stock purchases on the open market. If a target refuses to cooperate by providing information about its directors that is not publicly available, how will the buyer know whether it has a filing obligation?

A few examples highlight the flaws in the proposed rule:

- **Example 1.** A company determines that under 802.51, it is a foreign issuer and does not have an HSR filing obligation because its officers reside outside the United States, 90% of its assets are outside the United States, and 2 of its 3 directors reside outside the United States. On that basis, it negotiates and executes a transaction agreement, with related risk-shift obligations, interim operating covenants, and other provisions. Days before the transaction is set to be consummated, a director passes away, changes his or her residence to the United States from a foreign country, or resigns for personal reasons, such that 50% of the company's directors now reside in the United States. An unexpected HSR filing would therefore be triggered.

- **Example 2.** Same factual scenario except that pursuant to the transaction agreement, the buyer plans to retain two of the company's three directors in the post-transaction entity. One of the remaining directors resides in the United States and one resides abroad. Immediately prior to consummation of the transaction, the seller plans to reorganize the corporation for tax purposes, which will result in resignation of the third director, who resides outside the United States. Therefore, for a split second prior to closing, 50% or more of the corporation's directors reside in the United States. Would the FTC require an HSR filing in this circumstance? Unclear.

- **Example 3.** Company A and Company B are competing to acquire 40% of Company C, a foreign issuer. The purchase price is expected to be $500 million. Company A has just $1 million in U.S. sales, but $100 million in U.S. assets as a result of non-operating real property holdings. More than 50% of Company A's assets are outside the United States and all of its officers reside outside the United States  We understand that Company A would be considered a U.S. issuer and therefore have an HSR filing obligation because 2 of its 3 directors reside in the United States Company B has the same facts except that it has $300 million in U.S. sales and 2 of its 3 directors reside outside the United States. It would seem an odd result that a company with 300 times the sales volume in the United States would not have a filing obligation merely because it has fewer directors residing in the United States.

As the FTC notes in the background to the proposed amendment, the "foreign exemptions" are intended to exclude certain foreign transactions from the HSR Act's requirements "when there is only a limited nexus with U.S. commerce." Based on the Examples 2 and 3 above, two nearly identical transactions can lead to different results based not on the substantive factors or the nexus to the jurisdiction (e.g., the effect of the transaction in the jurisdiction, sales in the jurisdiction, or assets in the jurisdiction), but merely because the company has chosen directors that happen to reside in or outside the United States. The 50% of directors rule is inconsistent with ICN and OECD best practices, which provide that "jurisdiction should be asserted only over transactions that have a material nexus to the reviewing jurisdiction."[12]

The ICN also recommends that "determination of a transaction's nexus to the reviewing jurisdiction should be based on activities within that jurisdiction as measured by reference to the activities of at least two parties to the transaction in the local territory and/or by reference to the activities of the acquired business in the jurisdiction."[13] Example 3 demonstrates that the assertion of jurisdiction regarding the 50% of directors rule is related only to the activities of the buyer, which also is inconsistent with the ICN's recommended best practices.

Finally, the Section notes two other potential concerns. First, obtaining and processing the confidential and personal information of directors may raise data privacy issues in certain jurisdictions, hampering a company's ability to determine whether a filing is required. Second, the rule may disincentivize some companies from selecting board members that reside in the United States  Companies should select board members based on the merits of their service, and the proposed amendment may have the unintended consequence of discouraging foreign

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[12] ICN, RECOMMENDED PRACTICES FOR MERGER NOTIFICATION AND REVIEW PROCEDURES, at 3 (2018), *available at* https://www.internationalcompetitionnetwork.org/wp-content/uploads/2018/09/MWG_NPRecPractices2018.pdf. OECD recommendations are similar, "Assert jurisdiction only over those mergers that have an appropriate nexus with their jurisdiction."  OECD, COUNCIL RECOMMENDATION ON MERGER REVIEW, at 2 (2005), *available at* http://www.oecd.org/daf/competition/mergers/40537528.pdf.

[13] ICN, RECOMMENDED PRACTICES FOR MERGER NOTIFICATION AND REVIEW PROCEDURES, at 4 (2018), *available at* https://www.internationalcompetitionnetwork.org/wp-content/uploads/2018/09/MWG_NPRecPractices2018.pdf

companies from selecting U.S. citizens for their boards. In sum, the Section recommends that the FTC refrain from including the proposed amendment related to directors.

3. **The Section respectfully recommends that that the FTC incorporate exemptions to the 50% of assets rule to achieve its objectives and to be consistent with prior PNO guidance.**

The proposed rule regarding an entity's principal offices being located in the United States if 50% or more of the entity's assets are located in the United States makes sense in principal as a baseline rule. However, the Section proposes incorporating the following two exemptions to accommodate practical considerations and to be consistent with prior PNO Guidance.

First, we propose including a carve-out for companies that do not have any owned or leased property in the United States. This would be consistent with Informal Interpretation 0803016, in which the PNO explains that an entity's principal offices need to be determined when a company has offices both in the United States and outside the United States[14] This also makes practical sense; if the core purpose of the rule is to determine where an entity's principal offices are located, then it follows that an entity cannot have offices in the United States if it neither owns nor leases property in the United States, and if an entity has no offices in the United States, then that entity's principal offices cannot be in the United States.

Second, we propose including an exemption for non-operating assets. Once again, if the core purpose of the rule is to determine where an entity's principal offices are located, non-operating assets have no bearing on an entity's operations and thus the location of such non-operating assets has no bearing on the location of an entity's principal offices. For example, consider a foreign company with foreign officers, directors, and mostly foreign assets except that it owns U.S. real property unrelated to its operations. Under the current proposed rule, such an entity could technically be deemed to have its principal offices located in the United States even though the only thing tying it to the United States are non-operational assets that have no relation to its nexus of operations and even though it is a foreign entity for all other purposes and under all other tests. To avoid such false positives and to be consistent with prior PNO guidance, we suggest excluding companies that do not have any owned or leased property in the United States and excluding exempt assets from the proposed rule change.

Separately, the Section also respectfully recommends that, for the purposes of this rule, the determination of the value of an entity's assets be based on the book value of those assets. The book value of assets is an objective measurement that is used consistently across most companies.[15] The Commission's proposed rule requires that the board of directors of the acquiring entity determine the Fair Market Valuation ("FMV") of assets. An FMV analysis is not required in all transactions (e.g., acquisitions of voting securities when the acquisition price has

[14] Federal Trade Commission, Informal Interpretation 0803016, (Mar. 27, 2008), *available at* https://www.ftc.gov/enforcement/premerger-notification-program/informal-interpretations/0803016.

[15] In open market purchases under 16 C.F.R. § 801.30, buyers in many cases do not have access to the target's book value information. Either by rule or through an example in the Statements of Basis and Purpose, the Section recommends that buyers can rely on good faith estimates of book value if actual book value is unavailable.

been determined). This can be a complex and burdensome exercise in some cases, particularly where intangible assets such as goodwill or intellectual property account for much of a business's value. Moreover, FMV analyses are not required by any other competition authority in what is usually an already extensive filing analysis.

In addition, the FTC has provided informal guidance related to FMV analysis required under 16 C.F.R. § 801.10. Under the proposed amendment, those informal interpretations would apply to the FMV calculation of U.S. assets to determine the location of principal offices. While those informal interpretations may make sense in the context of valuing assets to be acquired, some are inapt as a proxy for principal location. For example, in Informal Interpretation 1703001, the FTC determined that clinical trial data were an asset that needed to be included in the FMV of U.S. assets because the data were "inextricably linked to the value" of U.S. IP even though the data were collected and stored outside the United States, the company had no tangible U.S. assets or offices, the company had less than $1 million in U.S. revenue, and the company was a foreign entity.[16] Even if this guidance makes sense for the purposes of valuing the U.S. portion of a transaction, it makes little sense as a proxy for a company's principal location.[17]

Additionally, FMV is altogether more susceptible to subjectivity and, therefore, potential ambiguity**.** Because an FMV analysis is the Buyer's obligation per § 801.10 and dependent on the Buyer's judgment, requiring the use of an FMV creates a potential situation where a Seller does not know or have visibility into whether they are a U.S. entity. Similarly, because FMV is a somewhat subjective determination, it can result in the Buyer and Seller not agreeing on the outcome, creating unnecessary uncertainty. It is also possible that a target might be deemed a U.S. entity based on one buyer's FMV, but a foreign entity based on another buyer's FMV. To resolve some of these issues, the Section recommends making it Seller's responsibility to determine the location of the principal offices of its UPE.

Even in a friendly transaction when both parties are working collaboratively, such ambiguity would be particularly prevalent when determining the location of intangible assets, let alone the ambiguity an FMV determination would present in a hostile deal. As such, a rule that requires an FMV determination has the potential to create false positives. For example, consider a company that has foreign manufacturing operations, foreign tangible assets (such as real property), and foreign executives and directors, but that has a significant amount of U.S. intellectual property. Under an FMV analysis, at least by value, a significant portion of its assets could then be classified as U.S. assets purely because of the U.S. intellectual property. The company could then necessarily be determined to have its principal offices in the United States even though the only thing tying its operations to the United States is intangible intellectual property. To avoid such false positives due to ambiguity and to remain sensitive to practical considerations, we suggest using book value rather than fair market value when requiring a valuation of a company's assets under the proposed rule change.

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[16] Federal Trade Commission, Informal Interpretation 1703001, (Mar. 1, 2017), *available at* https://www.ftc.gov/enforcement/premerger-notification-program/informal-interpretations/1703001.

[17] A similar problem exists with the application of Informal Interpretation 1907004 to the proposed amendment. Federal Trade Commission, Informal Interpretation 1907004, (July 11, 2019) ("Goodwill should be allocated according to sales (in/into versus outside the US). So if 80% of Y's sales were US sales, 80% of its goodwill is a US asset.").

4. **Conclusion**

Contrary to the assertion that "the proposed amendments should make it easier for entities to evaluate whether a given transaction will qualify for the foreign exemptions," the proposed amendments are likely to increase ambiguity and uncertainty, increase the burden on some companies, and lead to divergent filing determinations for transactions that are virtually identical.

Although the Section agrees with the FTC that the "principal office" concept can (in certain circumstances) be "hard to define and difficult to apply to modern globalized businesses," in our experience that is not the case in the majority of situations. Indeed, in practice today, it is easier for companies to apply the rules related to 16 C.F.R. § 802.51(b) than to conduct the fair market valuation assessment required under 16 C.F.R. § 802.4. Absent evidence that some number of problematic transactions with appropriate nexus to the United States are evading HSR review because of the existing principal office exception, the Section is not convinced that any change to the current rules needs to be made.[18]

However, should the FTC decide that amendments to the current rule are necessary, the Section proposes two alternative rules to replace the proposed amendments. A company's principal offices are in the United States if:

- The principal workplace of more than 50% of a company's officers[19] is in the United States; *and*
- More than 50% of the book value of a company's non-exempt assets are in the United States.

While no rule is likely to be perfect, the Section's proposed rule is clear, administrable, based on objective criteria, and not likely to lead to discriminatory treatment of similarly situated transactions.

The Section proposes an alternative test in which the PNO vests the filers with the responsibility to determine, in their good faith judgment, whether the company's principal offices are in the United States, based on the totality of the circumstances, analogous to the Supreme Court's "nerve center" test in *Hertz Corp. v. Friend*. In that case, the Court held:

> we conclude that "principal place of business" is best read as referring to the place where a corporation's officers direct, control, and coordinate the corporation's activities. It is the place that Courts of Appeals have called

[18] Of course, the Section acknowledges that there may be examples to the contrary, but notes that there is not likely to be a perfect test. *See e.g.*, *Hertz Corp. v. Friend*, 559 U.S. 77, 95 (2010) ("[In determining principal place of business,] [w]e recognize that there may be no perfect test that satisfies all administrative and purposive criteria.)." However, the FTC and DOJ have authority to (and do) investigate transactions regardless of whether an HSR filing is required.

[19] *See supra* note 6.

> the corporation's "nerve center." And in practice it should normally be the place where the corporation maintains its headquarters—provided that the headquarters is the actual center of direction, control, and coordination, i.e., the "nerve center," and not simply an office where the corporation holds its board meetings (for example, attended by directors and officers who have traveled there for the occasion).[20]

The PNO relies on companies to make similar good faith determinations, for example, in calculating the fair market value of assets, or determining whether the entity is an exempt foreign government or agency under 16 CFR 801.1(a)(2) and the related informal interpretations. Under a proposed alternative rule, a company must determine whether its principal offices are located in the United States based upon the totality of circumstances in light of the varied considerations:

- The principal workplace of more than 50% of a company's officers[21] is in the United States.
- More than 50% of the book value of a company's non-exempt assets are in the United States.
- More than 50% of a company's revenue is derived from sales in or into the United States.
- More than 50% of a company's employees work primarily in the United States.
- The company holds itself out as principally located in the United States.

Although this alternative test is not based upon a bright line rule, the Section submits that most companies could make this determination without additional burden.

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The Section appreciates the opportunity to comment on the proposed amendments and is available to respond to any questions that the FTC may have with respect to any of the issues discussed in this comment.

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[20] 559 U.S., at 92-93. This approach would harmonize the principal location concept in the HSR rules with corporate law and the *Hertz* case.

[21] For a definition of officers, *see supra* note 3.

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