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PLAYING MONOPOLY WITH THE FTC: "PLEASE, PASS GO: WE'LL COLLECT THE MONEY FROM YOU (MUCH) LATER"

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According to the Federal Trade Commission ("FTC"), it can, without any statute of limitations, seek millions of dollars in equitable relief back as far as the time of deal consummation for anticompetitive price increases, even if it previously chose not to investigate or challenge your deal (and collected your filing fee). By means of example:

Company A and B execute a purchase and sale agreement, the deal value requires a Hart-Scott-Rodino Act ("HSR Act") filing. The 30-day waiting period expires without any indication from the FTC that there are concerns about the transaction. The parties close. Five years later, the FTC investigates the transaction and finds the transaction anticompetitive. It files a complaint, eight years after the deal is consummated, seeking divestment of the assets necessary to restore competition. It also seeks a permanent injunction, preventing similar behavior in the future and disgorgement of alleged ill-gotten gains from monopolistic pricing in federal district court under the FTC Act ("Act") Section 13(b), since the deal was consummated seven years earlier. The parties settle for hundreds of millions of dollars or the court grants disgorgement.

Here, the FTC says it can recover "ill-gotten gains" from alleged anticompetitive practices, *e.g.*, maintaining monopolistic prices, under Section 13(b) of the FTC Act, that would not have occurred but for the deal closing.[1] This section of the Act does not specifically allow for monetary remedies. It does not outline how such remedies should be calculated. It also has no statute of limitations. And, there is no latches or waiver argument available despite the FTC's failure to take advantage of the HSR waiting period. The only basis for the FTC's current interpretation and use of Section 13(b) is judicial interpretation from the 1980s. Although the FTC has

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made infrequent use of its Section 13(b) authority to obtain monetary remedies in mergers, the fate of the agency's expansive interpretation of its authority now lies in the hands of the Supreme Court.

Federal Agencies, Like the FTC, Must Rely on Congressional Intent to Obtain Equitable Relief

Federal agencies do not have inherent equitable powers. That is, they cannot order a party to provide equitable monetary relief, such as disgorgement and restitution. Federal agencies, like the FTC, must go to federal court for such relief. Courts can grant equitable relief to federal agencies if Congress does so by statute. The FTC relies on the FTC Act for its authority. As discussed below, certain sections of the FTC Act explicitly provide that the FTC may seek injunctions, other equitable relief, and penalties. Most of these provisions have procedural safeguards and are bound by a statute of limitations.

Section 13(b) empowers the FTC to seek temporary restraining orders ("TROs") and preliminary injunctions if a company is violating, or is about to violate, any law that the FTC enforces, for example, Clayton Act Section 7.[2] Clayton Act Section 7 prohibits mergers and acquisitions that substantially lessen competition. Section 13(b) does not explicitly permit a court to grant equitable remedies or penalties; instead it explicitly authorizes only TROs and preliminary injunctions, which the FTC interprets to mean broad equitable relief. Section 13(b) is not constrained by a statute of limitations. When the FTC challenges consummated transactions, it typically does so under its Section 13(b) authority, alleging violations of Section 7 of the Clayton Act (if the deal is reportable under the HSR Act) and/or a violation of Section 5 of the FTC Act.[3] Neither of these statutes independently and specifically provides the FTC equitable monetary relief, absent an administrative proceeding or a trial in federal court.[4] The FTC must rely on Section 13(b) for such relief.

Therefore, defendants have questioned whether courts have authority to order equitable remedies, for any period of time, when the FTC seeks an injunction under Section 13(b). The Supreme

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Court just heard oral argument on this exact issue in *AMG Capital Management, LLC v. FTC* and the Supreme Court's decision will impact the FTC's powers to address consummated mergers. If it goes against the FTC, the *AMG Capital* case likely will not affect the FTC's authority to seek an order unwinding a consummated transaction, but it may reduce the FTC's leverage with parties by threatening monetary relief.

Statutory Background

In 1914, Congress enacted the FTC Act, creating the agency.[5] The FTC's goal: to protect consumers. Specifically, to protect consumers from unfair or deceptive acts or practices, and to protect consumers from unfair methods of competition. The Act provides methods by which the FTC can enforce the statutes, rules, and regulations it oversees. This includes an administrative pathway, in addition to standing to bring claims in federal court. Depending on the method by which the FTC brings its claims, it can seek a variety of remedies including an injunction, disgorgement, restitution, and at times, penalties.

The FTC did not always have as much latitude when it was created. In its infancy, the Act only provided for the FTC to exercise its authority in an administrative proceeding. At the time, the FTC had to bring its case before an administrative law judge ("ALJ"), and the ALJ had to issue an Initial Decision after an evidentiary hearing. The Commissioners then reviewed the Initial Decision and could issue a final Decision and Order. The FTC did not have an avenue to pursue its case in federal court.

The 1973 Amendments

Monetary Equitable Relief for Violations of FTC Administrative Orders*:* Congress first amended the Act in 1973. It gave the FTC the authority to pursue equitable remedies, including "mandatory injunctions and such other and further equitable relief as [courts] deem appropriate," from those violating the FTC's *administrative orders* in federal court.[6] By way of example, when merging parties agree to make a divestiture in order to consummate a main transaction, the FTC typically requires that the parties agree to a Decision & Order that sets forth the conditions of the settlement. The FTC can pursue monetary relief for violations of its orders.

Injunctive Relief: The 1973 amendment also added Section 13(b) of the Act, which provides the FTC the authority to seek injunctive relief in federal court if the defendant "is violating, or is about to violate" the Act.[7] The injunction provides the FTC the opportunity to mitigate any additional consumer harm while its administrative proceeding is taking place. Section 13(b) also provides that, "in proper cases," the court may issue a permanent injunction.[8] Section 13(b) does not explicitly provide for monetary remedies, in any form, including equitable ones, and it has no statute of limitations.

The 1975 Amendments

Two years later, in 1975, Congress amended the Act again.

Rule Promulgation: The amendment codified the FTC's authority to promulgate its own rules.

Penalties*:* Section 5(m) permits the FTC to seek penalties, in addition to equitable relief, in federal court, if the FTC establishes that a violator had "actual knowledge or knowledge fairly implied on the basis of objective circumstances" that his/her conduct violated a promulgated rule.[9] Moreover, the FTC could seek penalties if a party

knowingly violates a cease-and-desist order following an administrative proceeding, even if he/she/it was not a party to the original proceeding.[10]

Additional Remedies: Under Section 19, Congress granted the FTC the authority to seek relief in federal court "to redress injury to consumers" from certain past misconduct.[11] The amendment authorizes the federal courts to grant "rescission or reformation of contracts, the refund of money or return of property, the payment of damages, and public notification . . . ."[12] However, the FTC can only obtain these remedies under two circumstances. Rather than initiate an administrative proceeding, the FTC can go directly to federal court when a party has violated an FTC rule. The amendment also provides that the FTC can seek remedies if the FTC has previously issued a cease-and-desist order to the defendant after an administrative proceeding and then proves in court that a "reasonable man would have known under the circumstances" that the defendant's conduct "was dishonest or fraudulent."[13] The FTC must operate quickly under this provision in order to avail itself of these remedies given the short statute of limitations: the administrative proceeding must begin within three years of the violation, and the Section 19 action within one year of the final cease-and-desist order.

In sum, the FTC can seek equitable monetary remedies for a violation of an administrative order or rule, but there is no statute that explicitly authorizes monetary remedies when it seeks an injunction to enforce other antitrust laws, including the Clayton Act.

Chipping Away at Section 13(b)

Defendants have alleged that the FTC has improperly taken advantage of the authority it has in Section 13(b) for some time; however, only recently have courts questioned, and even curtailed, the FTC's authority. The attack has been twofold: 1) the FTC should not be able to obtain monetary remedies under Section 13(b) because Congress does not explicitly call for it in the statute, and 2) even if the FTC can obtain monetary remedies, the FTC cannot seek an injunction and remedies for behaviors that have occurred in the past and have now ceased. These arguments recently have gained traction, resulting in reversals in judicial precedent in circuit courts.

"Is Violating, or Is About to Violate"

One of the first major threats to the FTC's use of Section 13(b) arose out of its case against Shire ViroPharma ("*Shire*").[14] Shire manufactured Vancocin, a drug used to treat a life-threatening gastrointestinal infection. According to the FTC, Shire filed 43 meritless citizen petition filings with the U.S. Food and Drug Administration ("FDA") and instituted three federal court proceedings to forestall entry of a generic version of Vancocin from March 2006 to April 2012. Nearly five years later, in February 2017, the FTC filed suit in the U.S. District Court for the District of Delaware alleging a violation of FTC Act Section 5 (unfair methods of competition) and seeking remedies under Section 13(b). The FTC sought a permanent injunction and restitution and/or disgorgement of Shire's allegedly unlawful profits. Shire sought a dismissal, alleging that Section 13(b) only allows the FTC to obtain an injunction if a party "is violating" or "is about to violate" the law, neither of which fit the facts. It no longer had any open petitions to the FDA or active matters in federal court.[15] The district court granted Shire's motion to dismiss, finding it did not meet Section 13(b) requirements, and the Third Circuit panel affirmed.

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The FTC conceded that Shire's allegedly illegal conduct stopped in 2012, and Shire even had divested Vancocin before the FTC filed its lawsuit. However, the FTC asserted that Shire was "about to violate" the law because its past conduct involving Vancocin made it more likely that the company would repeat the conduct in the future with respect to an unrelated drug. The Third Circuit disagreed, holding that the FTC cannot succeed under Section 13(b) with merely "a violation in the distant past and a vague and generalized likelihood of recurrent conduct."[16] Continuing to operate the business with similar products is not sufficient for the FTC to meet its pleading burden under Section 13(b).

Defining the Scope of Equitable Relief Provided for by an "Injunction"

Recently, some defendants have also successfully argued that the FTC is not entitled to monetary remedies under Section 13(b). As noted above, Section 13(b) does not refer explicitly to the FTC's authority to seek any monetary remedies. It simply states that the FTC can seek a preliminary injunction or "in proper cases," a permanent injunction. Absent longstanding judicial interpretation, the Court would not have the authority to exercise its equitable powers on the FTC's behalf as the statute currently reads.

Rather than discuss the history of the courts of equity, which may not be very interesting to some, suffice it to say that there is a long line of cases supporting the argument that if a court in equity can grant an injunction, it can also award monetary relief. Accordingly, courts have held that monetary equitable remedies are available under Section 13(b) because, once the court finds that it can grant an injunction, then all equitable remedies, including disgorgement and restitution, are at its disposal.[17]

A specter of change arose in December 2018 when the Ninth Circuit issued its opinion in *FTC v. AMG Capital Management, LLC* ("*AMG*"), a consumer protection case.[18] The court upheld longstanding precedent, finding that Section 13(b) "empowers district courts to grant any ancillary relief necessary to accomplish complete justice, including restitution."[19] However, Judge Diarmuid O'Scannlain issued a special concurrence to the majority opinion requesting the court to hear the case en banc and overturn prior circuit jurisprudence. Judge O'Scannlain reasoned that the forward-looking nature of Section 13(b), to prevent ongoing or imminent violations, would not adequately be addressed by "depriv[ing] a defendant of 'unjust gains from *past* violations.' "[20] He also found that other Sections within the Act, such as Section 19, which specifically allow the FTC to obtain monetary judgements for past conduct, suggested that Congress did not intend to empower the FTC to obtain monetary remedies under Section 13(b).[21] To hold otherwise may, to Judge O'Scannlain, be akin to granting the FTC penalties, rather than restitution.[22]

About eight months later, the Seventh Circuit reversed decades of precedent in *FTC v. Credit Bureau Center, LLC* ("*Credit Bureau*").[23] Despite the "injunctive language" in Section 13(b), the court could not find the implicit grant of equitable monetary relief. Similar to Judge O'Scannlain, the court noted that the language of Section 13(b) pertains to ongoing or imminent future conduct, finding that "[r]equiring ongoing imminent harm matches the forward-facing nature of injunctions."[24] In contrast, restitution is a "rem-

edy for past actions."[25] The court also could not presume that the word "injunction" was meant uniformly throughout the Act when other references to remedies specifically provide for both injunctions and "such other further equitable relief as [a court] deem[s] appropriate"[26] or "such relief as the court finds necessary . . . , [including] the refund of money or return of property."[27]

In July 2020, the U.S. Supreme Court consolidated, and agreed to hear, appeals in both cases, but on November 9, 2020, the Supreme Court vacated its prior grant of the Federal Trade Commission's petition for certiorari in *Credit Bureau*. Before drawing any conclusions, it is worth considering that Justice Barrett was on the Seventh Circuit when *Credit Bureau* was decided. She was not on the panel, but Justice Barrett did not dissent when she was required to review the overturned precedent. Therefore, the Supreme Court may have vacated the decision to avoid any conflict of interest, rather than imply how it would decide *AMG*.

The Court heard oral argument for *AMG* on January 13, 2021. It will likely be months until the Court issues a decision; the majority of decisions from the Supreme Court's 2020-2021 term will likely be released in June. Although it is possible to "over analyze" questions in oral arguments, several justices alluded to the possibility that the FTC may be overreaching its authority by seeking monetary remedies under Section 13(b). Specifically, some of the Justices did not find the existence of a grant of other forms of equitable relief in the text of Section 13(b). For example, Justice Kavanaugh and Justice Roberts focused on the difference between the powers held by Article III courts as compared to Article I executive agencies. Justice Kavanaugh stated that this is "a separation of powers case," in which the "Executive Branch of an independent agency [wants] to do good things, and sometimes [their] statutory authority is borderline . . . The problem is—is [sic] it results in a transfer of power from Congress to the Executive Branch to decide whether to exercise this new authority. That's a particular concern, at least for me, with independent agencies." In Justice Kavanaugh's words, "it seems the problem you have is the text." Although other Justices expressed concern that the FTC may lose its deterrent effect, Justice Kavanaugh simply inquired, "why isn't the answer here for the Agency to seek this new authority from Congress for us to maintain a principle of separation of powers?" Notably, Joseph Simons, Chairman of the FTC, asked Congress to do just that prior to oral argument, signaling the FTC's concern on how the Court may decide *AMG*, and the current status of *Shire* in the Third Circuit.[28]

Your Transaction, Re-Reviewed by the FTC, With a Hefty Price Tag

The vast majority of cases brought under Section 13(b), including *Credit Bureau* and *AMG*, are consumer protection cases, but the threat of the FTC applying Section 13(b) to transactions is real: The FTC has doubled the number of competition cases brought under the same statute in the last decade, coinciding with the FTC's revocation of its 2003 Policy Statement on Monetary Equitable Remedies in Competition Cases ("Policy Statement") in 2012.[29] The purpose of the Policy Statement was to identify the "appropriate circumstances" in which the FTC would seek monetary equitable remedies in competition cases pursuant to Section 13(b) of the Act. The Statement read that the FTC would seek such relief in "exceptional" circumstances.[30]

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However, the FTC may have found the Policy Statement to be suffocating its agenda. Indeed, it revoked the Policy Statement because "the practical effect of the Policy Statement was to create an overly restrictive view of the Commission's options for equitable remedies."[31] Its hands were artificially tied, and the FTC wanted to loosen the reins to crack down on anticompetitive behavior that may not otherwise stop absent a form of relief that would impact stakeholder behavior.

Absent new self-restraint or a decision by the Supreme Court that Section 13(b) does not provide for monetary remedies, the FTC continues to have authority to challenge, or threaten to challenge, consummated transactions under the statute. Moreover, although *Shire* is not before the Court, it raises questions as to whether the FTC will be able to pursue consummated mergers at all under Section 13(b). Once consummated, is there still an "ongoing" or "imminent" violation? The FTC may argue that ongoing price increases are an ongoing violation, but what if the defendant reverts back to original prices or argues that the input costs have increased? The FTC has used Section 13(b) to obtain monetary remedies in consummated mergers in the following examples:

- In *FTC v. Ovation Pharm., Inc.*,[32] the FTC challenged defendant's acquisition of a competing branded drug approved for the same indication as a drug in the defendant's existing portfolio. Upon acquisition, defendant allegedly raised the price of its existing drug nearly 1,300 percent, and then set the price of the acquired drug to match. The FTC alleged violations of Section 7 of the Clayton Act and Section 5 of the Act, seeking divestment and disgorgement.
- In *FTC v. Hearst Trust*,[33] the FTC alleged that Hearst Trust failed to substantially comply with the notification requirements under a subsection of the HSR Act. It further alleged that the transactions in question would substantially lessen competition under Section 7 of the Clayton Act. The FTC sought divestiture, disgorgement, and any monetary relief available under the HSR Act.
- In *FTC v. Mallinckrodt Ard Inc.*,[34] the FTC alleged that Mallinckrodt violated Section 5 of the Act and Section 2 of the Sherman Act by maintaining a monopoly unlawfully through the acquisition of the rights of a competing product in development, while raising the price of the product within its existing portfolio. The FTC sought divestiture and equitable monetary relief.

Under *Shire*, only *Hearst Trust* would have a clear showing of ongoing conduct out of the four cases above. Failure to meet substantial compliance under the HSR Act is a continuing violation, in which fines are assessed each day. The other three matters may not be considered ongoing since the transactions were consummated. The FTC would likely allege that the monopolistic prices would be a violation sufficient for Section 13(b), presuming that the parties do not lower prices prior to the FTC filing something in federal court, but that is a question for another day.

The most obvious impact of a Supreme Court decision against the FTC in *AMG* would be curtailing the amount of remedies the FTC can obtain. The FTC would have to rely on other laws that provided monetary remedies (if one fits the facts), and those statutes have statutes of limitations or limited applicability. In the *Mallinckrodt* matter, for example, the FTC filed its complaint

in 2017; however, the acquisition in question closed in 2013. If the FTC could no longer obtain disgorgement under Section 13(b), it may only be able to seek a portion of the monetary remedies that it could obtain under Section 13(b) because it may be restricted by a statute of limitations of less than four years. Indeed, the FTC is aware that "in certain circumstances, obstacles, such as statutes of limitations, prohibitions against suits by indirect purchasers, or standing requirements, may hinder the filing of a treble damages suit [brought by a private plaintiff]" and as a result, the FTC is taking upon itself the duty to "seek monetary remedies 'because other remedies are likely to fail to accomplish fully the purposes of the antitrust laws.' "[35] The FTC also claims that the specter of monetary remedies has a "deterrent effect," discouraging violations before they occur. In practice, the FTC might lose some leverage to obtain settlements such as divestitures in consummated mergers because it no longer has the threat of monetary remedies.

The most unsettling cases, although rare, are those in which a deal was reportable, no investigation ensued, and yet the FTC, many years later, raises concerns that the deal should have never been permitted to close. Although consummated deals are reviewable, parties should be permitted to have some level of expectation that a review under the HSR Act will not be revisited absent extraordinary circumstances, and certainly not result in monetary remedies. Challenges to consummated transactions, particularly those that seek monetary remedies, diminish the value of that stability and may, in some cases, distort business decisions

The views and opinions set forth herein are the personal views or opinions of the author; they do not necessarily reflect views or opinions of the law firm with which she is associated.

ENDNOTES:

[1]15 U.S.C. § 53(b).

[2]*See* 15 U.S.C. § 53(b) (permitting the FTC to seek preliminary and permanent injunctions in federal court to restrain violations of any statute overseen by the FTC).

[3]See 15 U.S.C. § 21 (allowing the FTC to enforce Section 7 via an administrative process); *id.* § 45(b) (allowing the FTC to pursue violations of Section 5 of the FTC Act administratively).

[4]"Under Section 5(b) of the FTC Act, the Commission can initiate an administrative proceeding to halt unfair or deceptive practices, unfair methods of competition, or violations of other laws enforced through the FTC Act. Generally, only injunctive relief is available through Section 5(b), and only through a final order—preliminary injunctions are not available, and monetary relief cannot be awarded under current practice, except in a settlement." Chopra, R. and Levine, S, "The Case for Resurrecting the FTC Act's Penalty Offense Authority," at 12 (Nov. 3, 2020).

[5]Federal Trade Commission Act ("Act"), 15 U.S.C. §§ 41 *et seq*.

[6]15 U.S.C. § 45(l).

[7]*Id.* § 53(b).

[8]"Proper" may read a bit ambiguously; however, the FTC has said that a proper case is one in which there is a violation of a rule or statute enforced by the FTC, other than the Act itself, or any conduct previously declared unfair or deceptive by the FTC in an administrative proceeding.

[9]*Id.* § 45(m)(1)(A).

[10]*Id.* § 45(m)(1)(B).

[11]*See* 15 U.S.C. § 57b.

[12]*Id.*

[13]*Id.*

[14]*Federal Trade Commission v. Shire Viro-*

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Pharma, Inc., 917 F.3d 147, 2019-1 Trade Cas. (CCH) ¶ 80681 (3d Cir. 2019).

[15]Shire also alleged that its petitioning activity was immune from antitrust challenges under the Noerr-Pennington doctrine. *Id.* at 153.

[16]*Id.* at 159.

[17]*See, e.g., Porter v. Warner Holding Co.*, 328 U.S. 395, 66 S. Ct. 1086, 90 L. Ed. 1332 (1946) (holding that a reference to "permanent or temporary injunction, restraining order, or other order" permitted district courts to use "all inherent equitable powers," including monetary remedies such as restitution).

[18]*Federal Trade Commission v. AMG Capital Management, LLC*, 910 F.3d 417, 2018-2 Trade Cas. (CCH) ¶ 80595 (9th Cir. 2018), cert. granted, 141 S. Ct. 194, 207 L. Ed. 2d 1118 (2020).

[19]*Id.* at 426 (9th Cir. 2018).

[20]*Id.* at 432 (citing *F.T.C. v. Commerce Planet, Inc.*, 815 F.3d 593, 599 (9th Cir. 2016), for additional opinion, see, 642 Fed. Appx. 680, 2016-1 Trade Cas. (CCH) ¶ 79526 (9th Cir. 2016)) (emphasis added).

[21]*Id.* at 431.

[22]*Id.* at 433 (referring to the Supreme Court's most recent decision in *Kokesh v. S.E.C.*, 137 S. Ct. 1635, 198 L. Ed. 2d 86, Fed. Sec. L. Rep. (CCH) P 99733 (2017)). The import of the *Kokesh* decision is beyond the scope of this article, however, the Court described three characteristics that can be used to ascertain if disgorgement is a penalty.

[23]*Federal Trade Commission v. Credit Bureau Center, LLC*, 937 F.3d 764, 2019-2 Trade Cas. (CCH) ¶ 80883 (7th Cir. 2019) (rejected by, *Federal Trade Commission v. Zurixx, LLC*, 441 F. Supp. 3d 1216, 2020-1 Trade Cas. (CCH) ¶ 81123 (D. Utah 2020)) and cert. granted, 141 S. Ct. 194, 207 L. Ed. 2d 1118 (2020), vacated, 2020 WL 6551765 (U.S. 2020) and cert. denied, 141 S. Ct. 195, 207 L. Ed. 2d 1118 (2020).

[24]*Id.* at 779. (citing 11A CHARLES ALAN WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 2942, at 47 (3d ed. 2013) ("[I]njunctive relief looks to the future and is designed to deter . . . .").

[25]*Id.*

[26]15 U.S.C. § 45(l).

[27]15 U.S.C. § 57b(b).

[28]Questions for the Record from the Honorable David N. Cicilline, Chairman, Subcommittee on Antitrust, Commercial and Administrative Law of the Committee on the Judiciary, Joseph Simons (June 2019) (Simons asked for Congress to "clarify Section 13(b) to reaffirm the Commission's longstanding authority to secure all types of equitable relief, including restitution and disgorgement. In addition, Congress should revise Section 13(b) to clarify that the Commission may sue in federal court to obtain equitable relief even if conduct is no longer ongoing or impending when the suit is filed.").

[29]Policy Statement on Monetary Equitable Remedies in Competition Cases, 68 Fed. Reg. 45,820 (Aug. 4, 2003).

[30]The FTC must show that the violation in question is "clear;" that the basis upon which the FTC calculated the amount of relief is "reasonable;" and there is a "value" to seeking such relief over other forms of relief, *i.e.*, simply an injunction, as permitted under the statute.

[31]Statement of the Commission, Effecting the Withdrawal of the Commission's Policy Statement on Monetary Equitable Remedies in Competition Cases (July 31, 2012), 77 Fed. Reg. 47,070 (Aug. 7, 2012).

[32]No. 08-6379 (D. Minn. Dec. 16, 2008).

[33]No. 1:01-cv-00734 (D.D.C. Apr. 4, 2001).

[34]No. 1:17-cv-00120 (D.D.C. Jan. 25, 2017).

[35]Antitrust Modernization Commission, Report and Recommendations, at 95-96 (April 2007).

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CONTESTED VIRTUAL SHAREHOLDER MEETINGS: A NEW FRONTIER

By Igor Kirman, Sabastian Niles and Natalie Wong

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Even prior to the COVID-19 pandemic environment, virtual shareholder meetings, also known as VSMs, had been on the rise in recent proxy seasons as public companies sought to increase the attendance of their investor base, decrease administrative costs of holding a physical meeting and embrace the use of technology in engaging with investors. VSMs, like in-person shareholder meetings, occur in settings that can be placed on a spectrum from least contested to most contested: ranging from routine management-only proposals on the ballot, to Rule 14a-8 shareholder proposals in which proponents solicit using the company's proxy cards, to withhold-the-vote campaigns against the company's recommended director slate, to full-fledged proxy contests in which companies and dissident shareholders battle over which directors will be elected to the board. This last context—the fully contested VSM—is the focus of this article.

From the first major use of virtual capabilities at an annual meeting in 2009, by Intel Corporation, using technology pioneered by Broadridge Financial Solutions, the number of VSMs has been on the increase. The use of hybrid[1] or virtual-only annual shareholder meetings more than doubled from 93 meetings in 2014 to 187 meetings in 2016, and has steadily increased to 236, 285, and 326 meetings in 2017, 2018, and 2019 respectively.[2] This steady rise became a torrent in 2020, as companies turned to hybrid or, more frequently, virtual-only annual shareholder meetings due to the COVID-19 pandemic, shelter-in-place regulations and public health considerations. Broadridge reported hosting close to 1,500 virtual-only and hybrid shareholder meetings on its platform during the 2020 proxy season.[3]

Yet companies have traditionally been reluctant to use VSMs for contested proxy fights, involving multiple proxy cards and competing director slates, due to the extra complexity and high stakes of such meetings, which present a slew of legal risks that are absent from non-contested situations. Another challenge has been, until recently, the absence of a commercial platform for implementing contested VSMs. But, being as necessity is often the mother of invention, the pandemic led some companies, starting with TEGNA Inc. in April 2020, to conduct their contested VSMs virtually. Given that the year ahead will likely see an elevated number of VSMs and an increase in shareholder activism, we expect that the need to conduct proxy fights on digital platforms will continue. Looking beyond 2021, when it is hoped safety concerns will diminish and companies could return to the annual meeting choices they had pre-pandemic, the questions—and opportunities—raised by VSMs will remain. This article discusses some of the benefits and considerations involved in conducting contested shareholder meetings virtually.

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Virtual Shareholder Meetings: The Rise of the Machines

The concept, legal groundwork and technology to host virtual shareholder meetings have existed for several years, beginning with Delaware amending its business corporation laws to permit such meetings in 2000. Most states now permit virtual-only or hybrid meetings. At least 33 states permit virtual-only meetings and 45 states permit hybrid meetings.[4]

In 2020, a major evolution in the regulatory framework for VSMs occurred as a result of the pandemic. Much of this was done in "real time" as pandemic concerns and shelter-in-place orders were being promulgated just as the annual spring proxy season was getting under way. Delaware took the lead and issued an emergency order in April 2020 that allowed companies to change scheduled in-person meetings to VSMs without having to re-notice such meetings so long as the company filed the notice of change with the SEC and posted a copy on its website.[5] A number of other states followed,[6] and the staff of the SEC issued guidance in April 2020 permitting issuers to change the format of their shareholder meetings to a virtual-only meeting or hybrid meeting without mailing additional solicitations if they issued a press release announcing such change, filed the press release as definitive additional soliciting material with the SEC, and took all reasonable necessary steps to inform other intermediaries and market participants of such change.[7]

Shareholder Reactions

While the VSM has been seen as a welcome technological development by many companies, a growing group of institutional shareholders, proxy advisory firms and activists alike have cautioned that the VSM may restrict the full shareholder participation that an in-person meeting would otherwise afford. There is a growing suspicion that the VSM format permits the Board and management to "cherry pick" and reword innocuous questions and comments, gives them discretion over which questions to answer, and restricts follow-up comments by limiting each shareholder to one question.[8] There has been meaningful pushback against these suspicions as well, and a number of institutional and retail investors are supportive of the opportunities that a well-run and fair VSM could provide. The Council of Institutional Investors, among several other interest groups that prefer in-person attendance, has publicly expressed that the near-universal VSMs conducted during the 2020 proxy season were a "poor substitute for in-person shareholder meetings, notwithstanding the potential for virtual technology to expand participation."[9] Proxy advisory firms ISS and Glass Lewis have also cautioned that VSMs need to be conducted in a way that allows for comparable rights and opportunities for shareholders to participate electronically as they would have during an in-person meeting, and institutional investors such as BlackRock and State Street, among others, have expressed similar views.[10]

Companies and investors also now recognize that by providing for virtual attendance, what would typically be a physical meeting attended, at most, by employees, union representatives where applicable, a handful of local retail holders, localized interest groups and proponents of shareholder proposals (where applicable), the meeting may become a virtual forum akin to another "investor day," where analysts and other institutional investor representatives focus the dialogue on the company's business and financial

performance. This business focus is often apparent as part of a general "Q&A" session at the end of the VSM. It remains less common for companies to provide a "Q&A" session after each proposal, or two "Q&A" sessions for proposal and non-proposal matters. Whether companies and shareholders prefer a more robust discussion of business issues, rather than the items relating to corporate governance and shareholder proposals, varies based on the circumstances.

Finally, activist investors and proponents of shareholder proposals in particular have sometimes asserted that during VSMs, their live participation may be limited, their questions risk being ignored, and that their engagement rate would be much higher in an in-person meeting.[11] Companies have generally disputed these assertions and have pointed to ways in which they have tried to replicate, as much as possible, the engagement of an in-person, given the constraints of a digital platform.

Contested Virtual Shareholder Meetings

Contested meetings, due to their high stakes and adversarial nature, have traditionally been fraught with the potential for every action by the company to be examined and potentially challenged in court. As a result, even as some companies migrated to virtual-only annual meetings, prior to 2020 none chose to do so for proxy contests—whether in connection with an unsolicited takeover effort, activism, or other situations involving competing proxy cards. In 2020, however, a number of companies, led initially by TEGNA Inc., faced proxy contests and had no choice but to conduct contested VSMs in light of the COVID-19 pandemic. In all, there were 13 proxy contests that went to a shareholder vote in the 2020 proxy season and 25 board seats won through a contested election, compared to six proxy contests and four board seats won in 2019.[12] In addition to the TEGNA proxy contest, which TEGNA won, other notable contests included the partially successful attempt by Senator Investment Group and Cannae Holdings to replace the entire board of CoreLogic (they ended up replacing a minority of the board); Starboard's control slate at GCP Applied Technologies that was backed by GCP's largest investor and periodic activist 40 North; and GameStop's loss of two director seats to nominees advanced by Hestia Capital Partners and Permit Capital Enterprise Fund. These contests hold several lessons and observations for the future use of VSMs in contested situations

Attendance and Shareholder Access

One significant benefit of VSMs is that they make it easier for all constituents, including shareholders, to attend the meeting by allowing them to do so from their homes, without the need to travel to what is often an out-of-state location. In the 2020 proxy season, Broadridge reported an average of 146 attendees for VSMs with shareholder proposals and 37 attendees for VSMs without,[13] both significant increases in number from in-person meetings. These also translate to a greater amount of questions asked and answered, and to a lesser extent, a larger number of votes received at the meeting itself. In this regard, a case can be made that VSMs contribute to shareholder access and engagement. In particular, especially with the rise of index funds that hold major positions in most publicly-traded companies, especially companies in the S&P 500, VSMs enable index funds that would normally not be well positioned to attend many in-person meetings in their portfolio to have a more practical opportunity to do so.

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Design and Technical Considerations

Key features of the VSM platform in a contested situation should include the registration of shareholders and permitted guests of the company and the dissident in advance of the virtual meeting (including the ability to submit evidence needed to establish the identity of the foregoing), as well as the ability of shareholders to inspect the company's shareholder list online and vote by ballot. In addition, the dissident in a proxy fight should be given the opportunity to present their nomination or proposal unless the company and the dissident agree to waive such opportunity and be given the opportunity to ask questions like other shareholders during the meeting itself. In implementing VSM procedures in a legally protected and compliant manner, Delaware companies may rely on DGCL § 211(a), which provides that a company may conduct a VSM "subject to such guidelines and procedures as the board of directors may adopt." In response to the COVID-19 pandemic, most of the other states granted issuers temporary relief through executive orders or emergency legislation to allow VSMs, with conditions substantially similar to the requirements set forth in DGCL § 211(a). That said, not all of these orders or legislation are permanent, and some have expired (and need to be renewed to apply), so a non-Delaware company will need to check the applicable state corporate statute, as well as its organizational documents, to determine whether a virtual-only VSM is permitted (and what the applicable requirements and parameters are). On a federal level, an issuer should also take into consideration the guidance issued by the staff of the SEC, which requires issuers to "disclose clear directions as to the logistical details of the 'virtual' or 'hybrid' meeting, including how shareholders can remotely access, participate in, and vote at such meeting" and, with respect to Rule 14a-8 shareholder proposals, encourages issuers to "provide shareholder proponents or their representatives with the ability to present their proposals through alternative means, such as by phone."[14]

When TEGNA hosted the first contested VSM in April 2020, it faced technical obstacles, in large part because Broadridge and other VSM platform providers had yet to develop contested VSM platforms. TEGNA eventually had to develop and customize its own contested VSM platform in collaboration with third party service providers, while managing the considerations listed below. Since then, at least one commercial provider, Corporate Election Services ("CES"), has emerged to provide a contested commercial platform and Broadridge is working on its own. At the moment, the Broadridge platform reportedly will include a call center equipped to handle management and dissident voting instructions, with live operators taking instructions from shareholders during the contested VSM. Broadridge will then provide voting reports to the inspector of elections after the conclusion of the contested VSM. Since such a delay may prove to be unattractive in contested situations, we expect that companies will seek alternatives until Broadridge is able to automate the tabulation of votes in contested VSM, something which it says it is also working on.[15] Due consideration must also be given to technical difficulties that may interrupt the VSM or prevent it from starting, and the company should adopt a contingency plan and be able to communicate this plan in advance. In addition, it is possible that hackers may attempt to hijack or disrupt a VSM, as has occurred in other contexts. Companies should clearly communicate how shareholders can seek technical support

where they have individual technical issues in accessing the VSM. In addition, companies need to be prepared for the possibility of full-scale technical failures that may occasion a need to postpone or adjourn the meeting. Companies should consult with their organizational documents and applicable state law in this regard, and try to anticipate (and possibly disclose) these possibilities in advance. Even though in theory video could be available for VSMs, and the demand for this is growing, almost all companies that have held contested VSMs have made them audio-only to minimize data usage and the possibility of technical failures. Finally, in the event that an adjournment needs to take place, companies need to consider in advance whether they will be able to delay or reconvene the VSM. When planning meetings on a commercial platform, the platforms—and associated staff—book up, so a company seeking a last-minute adjournment may find that it has no slots available. Companies that believe this to be a possibility may need to reserve commercial platforms for backup plans. Companies should consult state laws as to how notice of a reconvened meeting should be disseminated.

Dissident's Right to Speak; Questions and Answers

A key consideration for companies using a virtual platform for contested VSMs is how best to permit dissidents, or other shareholders, the ability to make their views known on such a platform, whether it be through an allotted amount of time to speak, or through the "Q&A" session. As noted above, we have seen some companies adopt some (if not all) of the following restrictions in contested VSMs (similar to restrictions adopted at in-person contested meetings): (i) only permitting shareholders of record to submit questions, (ii) limiting questions to one question per shareholder, (iii) requiring that questions be submitted in writing and in advance and not in real time during the meeting (eliminating the ability of the shareholder to respond to or follow up on management's responses) and/or (iv) giving management the ability to "group" questions by topic and rephrase in their own discretion. In general, having too many restrictions in contested situations is risky and could open companies to challenge by the dissident or other shareholders. In the interests of full and fair disclosure, a growing number of companies undertake to post the transcript of the VSM and/or unanswered questions (in some cases, together with responses) on their website after the VSM. Most companies in contested proxy situations give dissidents the right to speak live for a short period of time, and typically have the dissident call in to make a prepared speech, all by advance agreement. Ultimately, companies will need to balance shareholders' desire for enhanced participation in a VSM with the need to keep the meeting orderly and moving on time, but where possible should seek to consider and accommodate reasonable requests from the dissident.

Cross-Functional Planning and Support

Planning and implementing an effective contested VSM requires the cooperation of a multidisciplinary task force, including in-house information-technology and legal personnel and third-party experts and advisors such as outside counsel, proxy solicitors and public-relations advisors. The critical importance of conducting dry runs, testing the platform and making any necessary adjustments prior to the VSM webcast cannot be overstated. Without sufficient trial and error, companies run the risk of technological failures or human error derailing the VSM, which is especially a significant risk to run in a contested

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election. The use of a commercial platform should alleviate some of the technical needs, but testing remains a necessity even with a commercial platform. Companies should also consider updating corporate governance documents to authorize virtual meetings, updating annual meeting rules, agendas and proxy materials, and otherwise working with their VSM task-force to execute a VSM in compliance with state law and best practices.

Physical Contested Meeting Parallels

Veterans of proxy fights and activism campaigns will be familiar with dynamics unique to proxy fights, such as "war rooms," in-person delivery of voted proxies to the inspector of elections by each side's proxy solicitor, "snake pits" and real-time, high-pressure communication and consultation by representatives of the two sides with each other.

Many of these concepts remain relevant in the virtual realm but require adaption—for example, since there are not separate "war rooms" set up alongside in-person presence for both parties to observe the contested meeting and communicate with the inspector of elections in real time, alternative means of communications for both parties are needed. If a dissident wishes to have the opportunity to address shareholders at the meeting, a separate phone line may be made available to enable this, to be activated during the period when such remarks are scheduled. If each side's team members are not physically together for a contested VSM and related webcast, they will need to use phone lines (or other means, such as Zoom conferences, text messaging or other communication platforms) to communicate amongst themselves during the VSM and discuss various questions or issues that may arise.

Communication Between the Company and the Dissident

As with a physical meeting, representatives of the company and the dissident should communicate prior to the VSM, including as to how the VSM will be conducted and the handling of requested accommodations that may be sought by the dissident. In fact, such communications are even more important in the VSM context, especially since dissidents may be suspicious of company motives since virtual platforms under a company's control are less well-understood than physical meeting spaces and procedures. It is prudent to begin such discussions a little earlier than for physical meetings, given the novelty (for now) and complexity of the issues to be discussed. Sometimes, the parties will enter into agreements for the conduct of the meeting. As discussed more fully below, it also may make sense to involve the inspector of elections in some of these discussions, so that both parties understand the rules and mechanisms (including, while not legally required, prudent backup plans) for submitting votes.

Role of the Inspector of Elections

Since the inspector is not physically present to receive proxies from the two sides in the proxy contest (or attending shareholders), advance coordination with the inspector is needed to determine the process for submitting all proxies and ballots before the polls close. Where the parties use a commercial platform like CES, the platform is designed to take care of the communication with the inspector of elections; thus, a shareholder voting at the meeting presses a button on the website, and the platform communicates that vote to the inspector of elections. However, the shareholder seeking to vote at the

meeting itself (as opposed to prior to the meeting) still needs to obtain a legal proxy to do so and upload that to the platform in advance. Where the parties are not using a ready-made product like CES, arrangements must be made directly with the inspector of elections. The company and the dissident might agree that the inspector of elections may receive each side's master ballots by email, to be held in escrow until the polls open on the meeting date, and that the inspector of elections may accept all other proxies by email until the polls close. In any event, it is crucial that the procedures to be used are properly documented and aligned on between the parties, given the possibility of either party challenging the preliminary voting results.

Inching Toward a "Universal Ballot"?

"Attendance" at a VSM, even if remotely, permits shareholders the flexibility of voting for both management and dissident nominees. The SEC's "bona fide nominee" rule effectively means that shareholders largely vote on either the company's or the dissident's proxy card, but cannot "mix and match" votes unless they vote on a ballot that is provided at the meeting (which includes all nominees) and have the legal authority to do so. Under the corporate laws of most states, including Delaware, for a meeting held solely in a physical location, voting by ballot at the meeting requires in-person attendance by the shareholder of record or a proxy holder for such shareholder. Since it is easier to attend a VSM, more shareholders can attend and vote by ballot, which allows them to "split the ballot." But voting by ballot at the meeting under current SEC and state law frameworks is still more cumbersome than voting by proxy due to the administrative burden and execution risks of obtaining legal proxies, especially when ownership is split across multiple accounts. Advance registration requirements for a VSM setting may also add a timing consideration. As the United States is seeing more early "mail in" voting (which can be analogized to pre-VSM proxy voting), the question of whether VSMs will encourage a move in the opposite direction—towards more voting on "election day"—is still an open one.

One knock-on effect of this potential trend is that more "election day" voting may reduce advance visibility into the likelihood of shareholder approval or rejection of a particular matter. Having shareholders more able and likely to vote *at* an annual meeting can reduce both sides' visibility into voting results, which is particularly critical if the contest seems close and the parties are considering settlement. Of course, this uncertainty will arise only if shareholders choose to vote in meaningful numbers at the VSM itself, which remains an open question.

Conclusion

As we head towards the 2021 proxy season and beyond, whether contested VSMs will become a permanent fixture in the public company shareholder engagement landscape will depend not only on the perceptions of various stakeholders—the institutional investors, proxy advisory firms, activist investors, and the board and management itself—but also on the state of commercially-available technology and platforms to host these meetings, as well as how companies are able to manage risks. The experiences of the 2020 proxy season have shown some of the key considerations—both positive and negative—involved in hosting contested VSMs on a virtual platform. It has also shown that with a bit of diligence and care, such meetings can be handled effectively.

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ENDNOTES:

[1]A hybrid virtual meeting gives shareholders the option to attend and vote virtually, unlike an in-person meeting with live streaming (in which only in-person attendees can vote).

[2]Broadridge Financial Solutions, Virtual Shareholder Meetings: 2020 Mid-Year Facts and Figures, *available at* https://www.broadridge.com/_assets/pdf/broadridge-am_00315_br_20-203401-bfs-vsm_brochure_082520.pdf.

[3]Broadridge Financial Solutions and PricewaterhouseCoopers LLP, ProxyPulse: 2020 Proxy Season Review, October 2020, *available at* https://www.pwc.com/us/en/governance-insights-center/publications/assets/pwc-and-broadridge-2020-proxy-season-review.pdf.

[4]Rutgers Center for Corporate Law and Governance Council of Institutional Investors Society for Corporate Governance, Report of the 2020 Multi-Stakeholder Working Group on Practices for Virtual Shareholder Meetings (December 10, 2020) at p.4 and Appendix C, *available at* https://cclg.rutgers.edu/wp-content/uploads/VSM-Working-Group-Report-12_10_2020.pdf.

[5]State of Delaware, Executive Department, Tenth Modification of the Declaration of a State of Emergency for the State of Delaware due to a Public Health Threat (April 6, 2020).

[6]These include New York, Massachusetts and California. See State of New York, Continuing Temporary Suspension and Modifications of Law Relating to the Disaster Emergency, Exec. Order No. 202.8 (Mar. 20, 2020); Commonwealth of Massachusetts, Order Regarding the Conduct of Shareholder Meetings by Public Companies, COVID-19 Order No. 19 (Mar. 30, 2020); Executive Dep't of State of California, Executive Order N-40-20 (Mar. 30, 2020).

[7]U.S. Securities and Exchange Commission, Staff Guidance for Conducting Shareholder Meetings in Light of COVID-19 Concerns (Updated Apr. 7, 2020).

[8]A September 2019 report from Institutional Shareholder Services (the "ISS 2019 Update") undertook to evaluate whether companies shifted to virtual-only meetings in an effort to discourage facing shareholders in person about poor governance practices. The ISS 2019 Update concluded that there does not seem to be a link between governance structure and company meeting format, and that companies with virtual-only meetings appear no more likely to have poor governance practices. The ISS 2019 Update further observed that dissent levels on key voting items do not appear to vary materially for both physical and virtual meeting shareholders.

[9]Council of Institutional Investors et. al., Virtual and Hybrid Meetings: Concerns from 2020 Proxy Season (July 6, 2020) *available at* https://www.cii.org/files/issues_and_advocacy/correspondence/2020/Virtual%20Meetings%20Letter%20_%20Corrected%20Copy_.pdf.

[10]*See* Council of Institutional Investors, Corporate Governance Policies (Updated September 22, 2020), *available at* https://www.cii.org/files/policies/09_22_20_corp_gov_policies.pdf ("Companies incorporating virtual technology into their shareowner meeting should use it as a tool for broadening, not limiting, shareowner meeting participation. With this objective in mind, a virtual option, if used, should facilitate the opportunity for remote attendees to participate in the meeting to the same degree as in-person attendees.") *See also* BlackRock Investment Stewardship, Proxy Voting Guidelines for U.S. Securities effective as of January 2021, *available at* https://www.blackrock.com/corporate/literature/fact-sheet/blk-responsible-investment-guidelines-us.pdf ("We expect shareholders to have a meaningful opportunity to participate in the meeting and interact with the board and management in these virtual settings; companies should facilitate open dialogue and allow shareholders to voice concerns and provide feedback without undue censorship."); State Street Global Advisors, Proxy Season Review (Q2 2020), *available at* https://www.ssga.com/library-content/products/esg/asset-stewardship-report-q2-2020.pdf. ("When conducting an AGM virtually, we expect companies to preserve all of the rights and opportunities afforded to shareholders in a physical meeting.")

[11]In one extreme such assertion, for example, prominent shareholder "gadfly" activist John

Chevedden alleged in a voluntary filing with the SEC with respect to a company that management cut his remote connection as his shareholder proposal was being read. Goodyear Tire & Rubber Company Shareholder Alert, voluntary submission by John Chevedden pursuant to Rule 14a-6(g)(1) promulgated under the Securities Exchange Act of 1934, filed with the SEC on April 7, 2020.

[12]FactSet; Activist Insight.

[13]*Supra* note 1. For example, the TEGNA contested virtual meeting had over 100 attendees.

[14]*Supra* note 7.

[15]The Independent Steering Committee of Broadridge Newsletter, January 2021, Volume 16, *available at* https://www.broadridge.com/resource/news-from-the-independent-steering-committee-of-broadridge#article3.

SEC DIVISION OF CORPORATION FINANCE ISSUES SPAC DISCLOSURE GUIDANCE

By Mark S. Bergman, John C. Kennedy, Raphael M. Russo, and David Curtiss

Mark Bergman is a partner in the London office of Paul, Weiss, Rifkind, Wharton & Garrison LLP. John Kennedy and Raphael Russo are partners, and David Curtiss is counsel, in Paul Weiss' New York office. This is adapted from a piece that originally appeared on the Columbia Law School Blue Sky Blog.
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The Staff of the Division of Corporation Finance recently issued CF Disclosure Guidance: Topic 11—Special Purpose Acquisition Companies.[1] This guidance highlights disclosure considerations for SPACs at both the IPO and business combination stages, with a focus on disclosures around conflicts of interest and the differing economic interests of SPAC sponsors, directors, officers and their affiliates (collectively, "SPAC Insiders") as compared to the interests of the SPAC's public shareholders.

IPO Disclosure Considerations

In an effort to elicit better disclosures when a SPAC goes public, the guidance poses questions for SPACs to address in the IPO registration statement on the following topics of concern to the Staff:

- *conflicts of interests*—especially on the part of the SPAC Insiders, with regard to fiduciary and contractual relationships they have with entities other than the SPAC and competition for business combination opportunities, and the potential for conflicts in the business combination transaction itself;

- *the limited time that a SPAC has to complete a business transaction and its impact*—including the financial incentives of the SPAC Insiders to complete a transaction, their influence over the approval of any transaction, the ability to amend governing documents to facilitate a transaction, the ability to extend the timeline to complete a transaction, and the prior SPAC-success track record of the sponsors, directors and officers;

- *the compensation and role of the underwriters*—including any deferral of underwriting compensation until completion of the business transaction, what additional services the underwriters may be providing, any conflict of interest the underwriters may have (especially if providing additional services given deferred IPO underwriting com-

pensation), and the timing, conditionality and manner (*i.e.*, cash or other consideration) of the payment of compensation to the underwriters;

- *the economic terms of SPAC Insider investments*—including the securities ownership of SPAC Insiders and the prices at which they acquired those securities (and the terms, amount and impact of any concurrent offering in which they may be participating), and any conflicts of interest arising from their securities ownership, compensation arrangements and relationships with affiliated entities that may create a financial incentive to complete a business transaction even if not in the best interest of other public shareholders—the Staff specifically asks SPACs to clearly disclose that "if the SPAC fails to complete a business combination transaction, some of all of the sponsors,' directors,' and officers' and their affiliates' securities would have no value and the sponsors, directors, officers and their affiliates may incur a substantial loss on their investment"; and

- *the terms of SPAC issuances to its sponsor and others in private financings*—including how, if applicable, the terms of different classes of securities compare to the rights, terms and risks of public securities offered in the IPO, the impact of any of these offerings (especially of convertible securities) on the SPAC's capital structure, whether the SPAC will seek additional funding and how the price and terms of any securities the SPAC may issue in the future could compare to the securities offered to the public in the IPO and whether the SPAC Insiders may participate, or have an interest, in the financing, and the terms, and potential dilutive effect, of any forward purchase agreement (including whether the commitments are irrevocable).

Business Combination Disclosure Considerations

The guidance also poses specific questions for SPACs to address in the business combination context to elicit clearer disclosure in the business combination filing with the SEC on the following topics:

- *additional financing*—whether additional financing is necessary to complete the business combination, how the terms of any financing may impact public shareholders, and, if the additional financing involves the issuance of securities, the material terms of such securities, including how the pricing and terms compare to, and differ from, the IPO, the financing's impact on the capital structure and if convertible securities are to be issued, the terms of conversion and the impact on beneficial ownership of the combined company, and whether the SPAC Insiders are participating in the financing;

- *interests of SPAC Insiders in evaluating the transaction and other opportunities*—including detailed information regarding the identification and evaluation of the proposed transaction, detailed information regarding the negotiations over the nature and amount of consideration, the material factors considered by the board in its approval of the transaction, how the board evaluated the interests of the SPAC Insiders, whether there are any conflicts of interest of the

SPAC Insiders and how the SPAC addressed these conflicts, any interest the SPAC Insiders have in the target company (including the timing and acquisition cost thereof), detailed information on how the SPAC Insiders will benefit (including quantifying any compensation payments or investment returns), and the total percentage ownership interest the SPAC Insiders may hold after the combination (including after the exercise of warrants and conversion of convertible debt); and

- *underwriters services and fees*—including disclosure of all services and the timing, conditionality (*i.e.*, contingency) and manner (*i.e.*, cash or other consideration) of the payment of compensation to the underwriters, and any conflict of interest the underwriters may have (especially if providing additional services given deferred IPO underwriting compensation).

ENDNOTES:

[1]Available *here*: https://www.sec.gov/corpfin/disclosure-special-purpose-acquisition-companies.

TECH M&A IN 2021: MOVING FROM STRENGTH TO GREATER STRENGTH?

Technology was among the saving graces of 2020, whether the sector's performance in equities or M&A. This year could see even more of the same, at least in regard to tech company acquisitions.

In late January, *The M&A Lawyer* spoke to **Eric McCrath**, a partner in the San Francisco office of Morrison & Foerster LLP and co-chair of Morrison & Foerster's Global Corporate Department, about his firm's most recent Tech M&A Leaders' Survey. Its findings suggest a substantial tech M&A boom could occur in 2021, building on last year's already-strong performance.

The Survey, conducted in December 2020 and whose 89 respondents were primarily U.S.-based investment bankers (39%) or C-level/M&A executives (39%), found that its participants greatly expect a wave of tech M&A deals. Two-thirds of respondents (66%) anticipate a rise in tech acquisition activity, the largest percentage to predict that since the firm's April 2014 survey. Only about 6% said they believed tech M&A activity would decrease in 2021.

"We should continue to see a lot of consolidation in the semiconductor space, in the fintech space," McCrath said. "There's a large crop of private companies in the AI and security space that I believe will also be part of ongoing M&A activity. I think we'll continue to see a lot of cross-border activity—there are hints of more of that as we go forward this year."

A tech M&A boom this year will be owed in great part to 2020, when the sector proved invaluable during the COVID-19 crisis. For example, someone who had never heard of Zoom in 2019 was using it as a lifeline for work a year later. "There was a real tech resilience in the face of the pandemic," McCrath said. Where retail, for example, was hard hit, "there was a lot of strength in tech that was focused on security measures, around home offices, having employees deploy remotely."

A solid majority (61%) of respondents said

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they believed that private equity spending on tech targets would increase in 2021, nearly double the number who said that in the 2019 survey (as Morrison & Foerster noted, PE spending on tech targets rose to $108 billion last year, a performance boosted by $27 billion reported in December 2020 alone).

And roughly 66% of respondents said tech purchases by special purpose acquisition companies (aka "blank check companies") would also increase. As in other sectors, SPACs emerged from seemingly out of nowhere last year to become a significant buyer, with 35 acquisitions of tech targets reported. By contrast, there were only six SPAC tech purchases in 2018.

"The numbers say it all," McCrath said. Earlier in the previous decade, SPACs "had been a flavor, but not necessarily the focus of a lot of attention." That changed dramatically in 2020. A selling company's bankers and lawyers were now almost required to consider SPACs as one option, due to the huge uptick in volume. That trend is likely to continue, in the short-to-medium-term at least. "Momentum builds on momentum. [SPACs] will likely be bigger this year because of their greater exposure and the greater sense of them being something to look at."

More Deals, Lesser Valuations?

The survey found that the outlook for deal valuations, however, is less bullish than for deal activity. Only about 35% of respondents said they anticipated an increase in valuations for sales of privately-held tech companies in 2021.

In particular, survey respondents were divided on whether PE firms would pay higher or lower multiples for tech companies in 2021. Roughly 39% expect them to pay more, while 28% predict less. As Morrison & Foerster noted, "the vaguely optimistic outlook comes on the back of a tough year for selling assets to sponsors. Leveraged buyout firms paid a median 2.9x trailing revenue for their tech acquisitions in 2020, the lowest since 2016."

There was consensus, however, that competition would push up pricing on PE acquisitions. About 63% of respondents expect contested deals among PE firms to increase M&A prices, and 61% said the drive to beat other strategic acquirers could propel multiples in 2021.

And many (69%) respondents said there would be a favorable exit environment for PE assets in the next three years. About 64% of respondents said they expected strategic acquirers to deliver such exits this year, along with bankruptcies (61%) and secondary sales (54%) also expanding.

The survey also assessed how the pandemic had affected tech dealmaking over the past year. Asked which impacts of COVID they had encountered in at least one M&A deal they had worked on, roughly 53% of respondents said due diligence had been delayed, 39% said the buyer postponed negotiations, 27% said that a buyer ended or suspended negotiations and had yet to resume them, and 26% said that a buyer renegotiated the deal price. Only 9%, however, said the buyer terminated its acquisition agreement.

McCrath said that "there was a little bit of a learning curve in the first couple of months [of the pandemic], as people figured out how to set up their specific comfort zones." In terms of due diligence, "there was a greater focus, I believe, on bringing in legal specialists who could assess and help do penetration tests on target companies in M&A diligence. That was naturally increasing in

any event, but in this past year there's been a lot of focus on that, in terms of better assessing risks associated with target companies."

ANTITRUST M&A SUGGESTIONS FOR THE 117TH CONGRESS

By Makan Delrahim

Makan Delrahim, Assistant Attorney General for the Antitrust Division at the Department of Justice, left his position upon the start of the Biden administration. This is excerpted and adapted from his final address, delivered on January 19, 2021 at a virtual event hosted by Duke University.

Today is my last day as the Senate-confirmed Assistant Attorney General of the Antitrust Division at the Justice Department . . . Some of you may have read that I started my career as a patent lawyer. When I pivoted to antitrust, it was more of an esoteric specialty. While John D. Rockefeller and Standard Oil have rightly earned their places in American business history, few had a true appreciation for antitrust as a discipline that polices the industrial relations of firms for the betterment of consumers broadly defined. Today, antitrust is at the forefront. Spurred by the social, political, and economic crises of our time, today we are all participants in a spirited public discussion about the goals and limits of antitrust. In many ways, 2020 was an inflection point in that conversation—and perhaps a signal that we have pivoted from discussion to action . . .

Undoubtedly, I have had a unique perch from which to participate in and observe this critical period. Over the last three and a half years, I have wrestled with difficult civil and criminal enforcement decisions; overseen victories and painful losses; witnessed the promise of public and nonpublic investigations while being inspired by the tenacity of the Division's staff; and engaged antitrust thought leaders with whom I agree and many with whom I vigorously disagree. This work has challenged me in important ways. On some matters, I have reassessed certain intellectual priors and re-considered arguments that I once thought out of the question. I have retreated to first principles to explain why some fashionable policies would be bad for consumers. I have stretched to consider whether worthy welfare goals could be achieved by better means. Most consequentially, I have asked and empowered the men and women of the Antitrust Division to approach problems both big and small differently, and they have had the grace and intellectual rigor to consider those directives.

The transition of power is an important opportunity to share lessons and insights because, regardless of politics, I root for the success of this great institution and for its forthcoming stewards. In addition to being available to them in any way that I can, I want to share some of my considered conclusions with the public—a testimony of a kind to the policymakers in Congress and both domestic and international antitrust enforcers who will lead through the next few years. I hope these suggestions will make enforcement more administrable, empower consumers, and offer increased clarity to businesses, both established and the ever-important start-up.

I offer two major theses. *First*, antitrust enforcers and policymakers can continue to do more to accomplish reliably the results that our traditional effects-based analysis dictate. Thoughtful legislative changes can effectuate these goals.

Second, some of the current debate about online

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platforms and digital markets is focused on principles that are foundational to trust in a market-based economy.

Policy solutions have ranged from direct command-and-control regulation by creating yet another regulatory agency to oversee the digital technology industry, to wholesale calls for breakup of companies with a certain size, to more laissez-faire self-regulation by industry itself. The events of recent days have laid bare the extraordinary influence of tech giants in matters of public policy. But if we don't find a way to harness that market power into partnership with democratic policy-making, we risk devastating outcomes for our civil democratic society . . .

Legislative Reforms

Congress serves two important roles: oversight and law-making. Rooted in the separation of powers, our system works best when checks and balances are robust. While the executive and judicial branches have been active, the public is best served when Congress uses the power allotted to it by the framers. As the first article of the Constitution, its importance can't be overstated.

Undoubtedly, one of the more consequential events that coincided with my tenure as AAG was the 116th Congress in both chambers using its oversight, including subpoena, power to investigate market power in digital markets. That work culminated in a body of public record and the issuance of the House report summarizing the Antitrust Subcommittee's findings and recommendations. While I believe some of its suggested reforms require further consideration, several are quite sensible.

On the legislative front, I was extremely pleased that Congress passed, and the President signed into law, several important antitrust reforms that will strengthen the Division's enforcement efforts.

I am most proud that Congress saw the need for additional resources for the Antitrust Division. Despite rising costs, shrinking headcount, and more resource-intensive investigations, funding effectively has decreased each year for at least 10 years. The recent omnibus appropriations bill contained the first enhancement to our budget in more than 10 years. This represents one of the most important pieces of support for the antitrust mission: it will allow us to hire additional staff that we need to effectively enforce the laws. I hope that the new Congress also will pass bipartisan legislation to bring merger filing fees current with inflation, and consider allocating further increases to the Division's enforcement budgets.

These latest developments enhance the Division's ability to carry out our mission, but more should be done. Congress would be well suited to consider immediately some simple legislative reforms to improve the predictability and efficiency of antitrust enforcement to make consumers better off and protect free markets.

I offer recommendations for Congress to consider this term.

Burden-Shifting Legislation on Excessive Consolidation

First, Congress should pass legislation to introduce bright line rules and alter the burdens of proof in civil merger cases in order to effectively combat certain excessive market concentration. This recommendation is grounded in the Division's actual experience investigating and challenging the Sabre/Farelogix and Visa/Plaid mergers in court.

Indeed, we at the Division have studied and have drafted burden-shifting legislation to advance consideration of this issue.[1]

The proposed legislation would amend the Clayton Act to address acquisitions of nascent competitors by dominant firms.

Specifically, I propose that for firms with more than 50% market share in any defined market, there should be a presumption that further acquisitions in that same market are anticompetitive, which can be rebutted by the merging companies if they can show by a preponderance of the evidence that:

- the parties combined post-transaction would not be able to exercise market power; or
- the anticompetitive effects of the transaction are insubstantial, or outweighed by the procompetitive benefits of the transaction.

The presumption should apply regardless of the size of target company, helping to address situations in which dominant firms engage in acquisitions of smaller firms to maintain and solidify their market power, not by superior business acumen, but by acquisition.

Under this proposal, the Government still would bear the burden of:

- defining the market in which there may be a substantial lessening of competition;
- proffering the merged firm's shares in that market; and
- rebutting cognizable, merger-specific procompetitive efficiencies.

The existing legal standards on these topics (*e.g.*, market definition, efficiencies) would remain unchanged, facilitating administrability and predictability.

The goal here is to create a bright-line rule for merging parties and for courts, allowing for better business planning by private parties and better litigation planning by federal antitrust enforcers.

Clarifying the Reach of *Ohio et al. v. American Express* (2018)

Second, I urge Congress to provide much-needed clarity on the reach of the Supreme Court's 2018 decision in *Ohio et al. v. American Express*. The law that has developed as a result creates confusion and may result in uncertainty and unnecessary litigation for businesses.

The issue on appeal was how to prove Section 1 liability for two-sided "transaction" platforms like credit cards, where merchants and store owners are on one side of a platform run by American Express, and customers are on the other. Credit cards, of course, are just one type of two-sided transaction platform. Under the majority opinion, certain digital platforms may qualify as two-sided as well.

The Solicitor General's brief explained that to show behavior is illegal, plaintiffs should have to prove harm to only one side of the platform. If the platform wants to rely on offsetting benefits on the other side, the defendant should bear the burden of proof. Instead, the Court's opinion requires the plaintiffs to not only show harm, but to somehow preemptively disprove that there are benefits anywhere else on the platform.

The *American Express* decision, in my view, obfuscated the legal standard in rule of reason cases. Among other things, it incorrectly raised the standard for plaintiffs to prove antitrust cases

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by paving the way for defendants and courts to wrongly assert that every market is a two-sided platform. This is a classic example of bad cases leading to bad law. In only two years, we already have seen unbridled defense arguments and confused decisions by the lower courts, including in the Division's case to block Sabre's acquisition of Farelogix. For these reasons, among others, the opinion has been criticized and recognized as creating a significant barrier to antitrust enforcement against platforms.

Legislation should codify the approach to two-sided markets as reflected in the Department's briefs and largely adopted by Justice Breyer in his dissent. Specifically, Congress should consider allowing a plaintiff to establish a prima facie violation by proving harm on only one side of a multi-sided platform, and importantly, allowing procompetitive benefits on either side of the market, but place the burden of showing such benefits on the defendant . . .

Modernized Pay Scale for Federal Antitrust Agencies

Congress should consider a modernized pay scale for the attorneys and economists of the federal antitrust agencies. This pay scale does not need to be bespoke, but modeled after one already used at the Securities and Exchange Commission. The simple truth is that there is great competition for the technical expertise of antitrust attorneys and industrial organization economists at the antitrust agencies.

Such a change, in my view, is well-justified and would ensure that the agencies are able to both retain and recruit top talent, especially as they compete with a handful of dominant technology firms in the same talent pool. I would suggest, however, that with the new salary structure, Congress demand performance accountability by requiring that employees who are rated in the bottom 5% each year are dismissed.

International Attaches in Beijing and Brussels

Congress should authorize the placement of antitrust experts at the U.S. Mission in Beijing and the U.S. Mission to the European Union in Brussels. In an inter-related world, antitrust enforcement increasingly is an international endeavor. Today, there are nearly 140 antitrust agencies across the globe. The Department of Justice spends considerable resources engaging with our enforcement partners on cartel, merger, and conduct enforcement almost on a daily basis. Given the importance of China and the E.U. to the global economy and to the United States, it would benefit both U.S. enforcers and the United States economy for the Department of Justice to have permanent attachés to focus on competition issues in those two regions. This also can be achieved through personnel details to the two regions through an agreement with the Office of the United States Trade Representative, which already has a presence in each other's missions.

Specialty Antitrust Courts

Finally, Congress should consider and implement a pilot for a specialized antitrust court to hear government enforcement actions, a view echoed by one of my predecessors turned legendary professor and Court of Appeals Judge, the Honorable Douglas H. Ginsburg.[2]

When the government brings an enforcement action to stop an anticompetitive merger or remedy anticompetitive conduct, we sometimes have been confronted by generalist judges who lack

experience with antitrust law or economics. Some have even voiced discomfort with the idea of deciding a case because antitrust law often deals in the counterfactual—the "but for" world—such that courts must make informed predictions about the future. As a result, antitrust enforcers devote significant resources to educating courts, an exercise that is sometimes wasteful, may lead to trial delays, and is ill-suited for rapidly evolving industries like the technology sector. Even companies find it difficult to police their conduct and M&A strategies in this framework, thereby undermining the deterrence goals of antitrust enforcement.

For that reason, a specialty district court where the government can bring civil antitrust cases may be a solution. This court would be modeled on Foreign Intelligence Surveillance Act, or FISA, with current Article III judges selected by the Chief Justice of the United States among interested and experienced district court judges across the country who can develop antitrust expertise and help expedite antitrust cases. Yet unlike FISA courts, proceedings and decisions should be open to the public.

Above all, these reforms are legislative solutions that could improve predictability for enforcers and businesses, and reduce waste, while expanding transparency and avoiding error costs.

ENDNOTES:

[1] Department of Justice Legislative Proposal Amending Section 7 of the Clayton Act,15 U.S.C.A. § 18 (Section 7 of the Clayton Act, 15 U.S.C.A. § 18, is amended as follows: (1) After the second paragraph, ending "the effect of such acquisition, of such stocks or assets, or of the use of such stock by the voting or granting of proxies or otherwise, may be substantially to lessen competition, or to tend to create a monopoly," inserting the following: "The United States or the Federal Trade Commission may initiate a proceeding to enjoin a transaction prohibited by this section. In such a proceeding, it shall be presumed that the effect of a transaction may be substantially to lessen competition, or to tend to create a monopoly, if a) The transaction would combine persons that compete in the same market, such that the elimination of competition by agreement between them would constitute a violation of any of the antitrust laws; and b) Any party to the transaction has a pre-transaction share of the market that is greater than 50%. The defendants may rebut this presumption only if they demonstrate by a preponderance of the evidence that a) The combined parties' post-transaction would not be able to exercise market power; or b) The anticompetitive effects of the transaction are insubstantial, or are clearly outweighed by the procompetitive benefits of the transaction in the relevant market. This presumption shall not limit any other presumption courts have created or used or may create or use in resolving cases under this section.").

[2] Ginsburg, Douglas H. and Wright, Joshua D., Antitrust Courts: Specialists Versus Generalists (July 3, 2013). Fordham International Law Journal, Vol. 36, No. 4, pp. 788-811, May 2013, George Mason Law & Economics Research Paper No. 13-42, *available at* https://ssrn.com/abstract=2289488 (last accessed January 19, 2021).

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FROM THE EDITOR

A New Antitrust Regime Starts to Take Shape

As of press time for this issue, President Biden had yet to announce his nomination to head the Department of Justice's Antitrust Division. Ongoing speculation over the most likely candidates suggests that dealmakers, particularly in the technology sector, should prepare to contend with a more activist federal regulator. But they may also have relatively merger-sympathetic officials in the DOJ's top spots.

As per Reuters, two former Obama administration officials are among the front-runners to replace Makan Delrahim as Assistant Attorney General. These are Renata Hesse, a former Acting AAG and currently a partner at Sullivan & Cromwell, where she helped to advise Amazon on its acquisition of Whole Foods, among other deals. And Juan Arteaga, former Deputy Assistant Attorney General at the DOJ, and currently a partner at Crowell & Moring. Arteaga aided in the investigation and trial that resulted the rejection of the DOJ's challenge to AT&T's acquisition of Time Warner, the first litigated vertical merger challenge in half a century. Progressive groups have reportedly advocated for Jonathan Kanter, known for his criticism of Big Tech companies. Former FTC Commissioner Terrell McSweeny is also in the mix.

Market observers cited reports that during the Biden transition, his team allegedly discussed its antitrust policy priorities, with an emphasis on regulators bringing cases "even if you're going to lose," as per Reuters. Topics discussed during the transition also included, reportedly, prospective changes in merger guidelines, increased antitrust enforcement funding and a push for more retrospective scrutiny of mergers.

As for Delrahim, he left his position on January 19. His tenure surprised critics at times: his division's AT&T and Visa cases were fairly aggressive enforcement actions that unlikely would have occurred in either of the Bush administrations, for example. Yet his division also allowed the T-Mobile/ Sprint merger that the Obama administration had opposed.

In his farewell speech, excerpted elsewhere in this issue, Delrahim offered antitrust-related suggestions to the Democratic-controlled 117th Congress. These included "legislation to introduce bright line rules and alter the burdens of proof in civil merger cases in order to effectively combat certain excessive market concentration," a recommendation "grounded in the Division's actual experience investigating and challenging the Sabre/Farelogix and Visa/Plaid mergers in court." He also called for specialized antitrust courts as a remedy for the status quo, in which "antitrust enforcers devote significant resources to educating courts, an exercise that is sometimes wasteful, may lead to trial delays, and is ill-suited for rapidly evolving industries like the technology sector. Even companies find it difficult to police their conduct and M&A strategies in this framework, thereby undermining the deterrence goals of antitrust enforcement."

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