Practice Update

Intentions Matter: Acquiring Large Amounts of Voting Securities Can Trigger an HSR Filing Obligation

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Key Takeaways

- The method of acquisition of voting securities does not matter for HSR purposes.
- The civil penalties for individuals or companies that miss HSR filing obligations can be significant.
- Subsequent acquisitions of the same issuer's voting securities after the HSR requirements have been satisfied can trigger additional HSR filing obligations, even if previous acquisitions did not trigger a filing.

When one large company buys another large company in the United States, someone in the process, whether it's outside corporate counsel or a knowledgeable insider, will likely ask the question of whether or not an "HSR" or premerger antitrust filing is required. Someone will be tasked with analyzing the transaction, and a filing will be made, if necessary. That is standard practice and very rarely are filing obligations missed for these kinds of transactions. However, what is sometimes missed is that the same analysis needs to be applied whenever voting securities are acquired regardless of how they are acquired. Whether the securities are acquired as part of a transaction between two companies or by an individual on the open market, an antitrust filing

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could be required for any transaction that is sufficiently large.

The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 18a (HSR Act) requires that parties to acquisitions of voting securities meeting certain annually adjusted thresholds (the threshold currently starts at $119.5 million) file a notification with the Federal Trade Commission (FTC) and Antitrust Division of the Department of Justice (DOJ) and observe a statutory waiting period — typically 30 days — prior to consummating such transactions unless an exemption applies. The objective of the HSR Act is to give the federal agencies an opportunity to review the transactions, in advance of closing, and to determine whether such transactions may be anticompetitive. Parties must submit so-called HSR filings for transactions regardless of the structure of the acquisition and even if the transaction will have no impact on competition, unless an exemption applies. The HSR Act applies equally to companies, partnerships, trusts, and individuals whether foreign or domestic. Companies or individuals that fail to comply with the reporting requirements of the HSR Act are subject to potentially significant civil penalties (currently set at $51,744 per day until a corrective filing is made). Often, but not always, first-time offenders are not subject to a penalty and simply receive a warning letter that cautions them to avoid future violations. Unfortunately, there are plenty examples of unwary acquirers who have missed HSR filing obligations and paid significant, and avoidable, penalties as a result.

The FTC recently announced another example of a significant and avoidable penalty, and because of the egregious nature of the violation, the penalty is being imposed on a first-time offender. Ryan Cohen, managing partner of RC Ventures, LLC, and chairman and CEO of GameStop Corp., acquired more than 2 million Wells Fargo voting securities on the open market between June 2016 and September 2020. In particular, on March 22, 2018, Cohen

acquired 562,077 Wells Fargo voting securities on the open market, which put his aggregated holdings well above the HSR Act threshold. Unfortunately, Cohen did not make an HSR filing prior to any of his acquisitions, and now he has agreed to pay a $985,320 civil penalty for failing to file and observe the waiting period.

Initially, Cohen relied on the Investment-Only Exemption to avoid any obligation to file an HSR for his acquisitions. The Investment-Only Exemption is based on section (c)(9) of the HSR Act, 15 U.S.C. § 18a(c)(9), which exempts from the requirements of the HSR Act acquisitions of voting securities made "solely for the purpose of investment" if, as a result of the acquisition, the securities held do not exceed 10 percent of the outstanding voting securities of the issuer. "Solely for the purpose of investment" is further defined as follows: Voting securities are held or acquired "solely for the purpose of investment" if the person holding or acquiring such voting securities has no intention of participating in the formulation, determination, or direction of the basic business decisions of the issuer. As long as Cohen's holdings remained below 10 percent of the outstanding Wells Fargo voting securities and he showed no intention to participate "in the formulation, determination, or direction of the basic business decisions" of Wells Fargo, his acquisitions would not have triggered an HSR Act filing obligation.

At no point did Cohen's holdings of Wells Fargo voting securities exceed 10 percent of the outstanding Wells Fargo voting securities; however, on February 5, 2018, prior to his significant acquisition in March of that year, Cohen reached out to Wells Fargo's CEO regarding the contributions that Cohen believed he could make to Wells Fargo if he were to become a member of the board of directors. Cohen also made suggestions on how to improve Wells Fargo's operation. Cohen continued to have periodic communications with Wells Fargo's leadership through at least April 2020 regarding his

desire for a board seat and suggestions for improving Wells Fargo's business. Unfortunately, the FTC views these communications as evidence that Cohen had an intention to participate "in the formulation, determination, or direction of the basic business decisions" of Wells Fargo and therefore the Investment-Only Exemption was no longer available to Cohen with regards to his acquisitions of Wells Fargo securities after February 2018.

As a result, the FTC alleges that all of Cohen's acquisitions after February 2018 were subject to a filing obligation under the HSR Act, which he failed to make until January 14, 2021, when he made a corrective filing for the acquisition he made in March 2018. Based on this corrective filing, the violation period for failing to file ran from March 22, 2018, when he crossed the HSR threshold, until February 16, 2021, when the waiting period expired for his corrective filing, or 1,062 days. If the FTC had imposed the maximum civil penalty, they could have sought $46,507,104 from Cohen. Instead, the FTC reduced the penalty because the violation was inadvertent and Cohen was willing to settle the matter and thereby avoid prolonged investigation and litigation, and Cohen has agreed to pay a civil penalty of $985,320.

The good news for Cohen is that he only have to pay a fraction the maximum penalty he was facing, but this is likely cold comfort considering the penalty could have been avoided altogether with a timely HSR filing. Certainly filing an HSR notification and waiting 30 days would have be an annoyance, but rarely is it worth the risk of paying hundreds of thousands (or even millions) of dollars in civil penalties.

Generally, collecting the information and conducting the analysis necessary to determine if a particular transaction requires an HSR notification takes less than hour. Even if a filing is required, the potential civil penalty will always dwarf any legal fees, and the civil penalties are public. An HSR filing can be made

confidentially. In addition, once an HSR Act waiting period has expired, the acquirer can continue to acquire additional voting securities from the same issuer for up to five years without making another filing as long as the acquisitions do not cross a new HSR Act threshold. When it comes to the HSR Act it is far better to be safe than sorry, and there is no reason for you to become the next cautionary tale of avoidable mistakes.

Contact Austin A.B. Ownbey at 202.824.1734 or Austin.Ownbey@Akerman.com, or your Akerman lawyer for help with any of your HSR-related questions or concerns.

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