HSR Compliance: The Consequences of Being Lackadaisical … A $720,000 Fine

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MacAndrews and Forbes' (M&F) settlement with the Department of Justice (DOJ) on June 20, 2013, provides a good reminder that simply surviving the Hart-Scott-Rodino (HSR) Act waiting period or receiving an early termination is not the end of HSR premerger notification compliance. The settlement demonstrates the need to be continually vigilant of HSR compliance matters, including, e.g., time periods and size of transactions. M&F agreed to pay $720,000 to settle charges that it violated the premerger notification and waiting period requirements of the HSR Act when it acquired voting securities of Scientific Games Corporation (SG) in a follow-on acquisition.

The DOJ simultaneously filed a complaint against M&F and a settlement on behalf of the Federal Trade Commission (FTC) on June 20, 2013. The complaint alleges that M&F violated the HSR Act by the acquisition of additional SG voting securities in June 2012. M&F first acquired SG voting securities during the five-year statutory period beginning February 9, 2007 (the date on which M&F received early termination notice of its premerger notification). The five-year period expired on February 9, 2012, several months before the June 2012 acquisitions.

The HSR rules generally permit a person to continue to acquire voting securities of the same issuer for a period of five years after expiration of the waiting period (whether by natural expiration or early termination) provided that such subsequent acquisition does not cause the acquiring person to exceed the next notification

threshold. If a subsequent acquisition will cross the next notification threshold, then, prior to the acquisition, a new HSR notice must be filed. This triggers a new waiting period. In the case of M&F, its June 2012 acquisition of additional SG voting securities did not exceed the next threshold. However, it did occur outside of the five-year statutory limit. Consequently, M&F should have filed a new HSR notification prior to the acquisition. In an unsuccessful attempt to self-correct this filing omission, M&F filed a corrective HSR notification on August 16, 2012, after a review of its portfolio by its HSR counsel.

This latest incident may not have led to the penalty if it was only an isolated incident of M&F. However, on May 13, 2011, M&F previously made a corrective HSR filing in connection with a follow-on acquisition of voting securities in SIGA Technologies, Inc. (SIGA). On June 22, 2010, M&F filed a premerger notification to acquire SIGA voting shares in an amount between the then current size of the transaction thresholds of $63.4 million and $126.9 million. The waiting period expired on July 22, 2010. After the expiration of the waiting period, M&F acquired 2.6 million SIGA voting shares and on January 7, 2011, M&F acquired an additional 600,000 SIGA voting shares through a cashless exercise of a warrant. According to the complaint, the value of the shares at the time of the cashless exercise of the warrant significantly increased from the prices that M&F paid for the initially acquired shares. Consequently, the cashless exercise of the warrant caused the value of M&F's holdings in SIGA to exceed the then in effect $126.9 million threshold. However, M&F did not provide notification and observe an additional waiting period, as was required by the HSR Act, prior to crossing the threshold. Again, it was only after a review of the M&F portfolio by HSR counsel in May 2010 that M&F realized the need to file a preacquisition notification. As noted above, M&F made a corrective filing on May 13, 2011, and indicated in the cover letter that the failure to file and observe the waiting period was inadvertent. Apparently, this attempt at a corrective filing was accepted but the subsequent attempt was not, as evidenced by the complaint and settlement.

This settlement demonstrates a number of items:

- **HSR Strict But Reasonable Enforcement**. The FTC and DOJ appear to be taking a strict position regarding HSR notification compliance, but have shown some understanding and leniency for an isolated inadvertent violation. In both instances of non-compliance by M&F, it appeared to self-report the non-compliance by filing corrective filings. Regardless of these

good-faith attempts, after the second corrective filing, the FTC and DOJ fined M&F a significant sum. It also is possible that if the SIGA violation had an anti-competitive impact, the government may have not shown its initial leniency.

- **HSR Continuing Compliance**. The settlement illustrates that HSR compliance does not end with expiration of the waiting period or the date of early termination. In both instances of non-compliance, M&F initially complied with its HSR notification requirements. It was only after the passage of time and the appreciation in the value of the investment that the need for subsequent notification arose. M&F presumably knew that it was making investments in the two entities over a period of time and should have adjusted its HSR compliance accordingly.
- **HSR Compliance Program**. M&F could have avoided legal troubles with the SEC and FTC in the first instance if it had a basic HSR compliance program in place that was consistent with its business model. M&F's business model appears to include the periodic acquisition of securities in portfolio companies. As a result, its HSR compliance program should have included checks prior to any follow-on investments to make certain, e.g., that the size of the transaction or time limitation requirements were not violated.

The M&F settlement provides an excellent example of why clients need to review their HSR compliance program or establish one.