A Case of Runaway Regulation

PREMERGER NOTIFICATION

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IN SEPTEMBER of last year, 100 pages of three-columned, small-print rules and regulations went into effect, subjecting hundreds of business transactions a year to new federal requirements. These were the final rules implementing Title II of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, which relates to "premerger notification" and the necessity for reporting certain mergers and acquisitions to the federal antitrust enforcement agencies. The 100,000 words produced by the regulation writers at the Federal Trade Commission (FTC) with the "concurrence" of the Department of Justice do not, as the number might indicate, inaugurate a new body of rules affecting the way business must be conducted, nor do they subject mergers to more rigorous antitrust standards. Rather, they deal with the procedural question whether an acquisition must be reported to the antitrust enforcement agencies, with the merging parties then required to wait thirty days (fifteen days for cash tender offers) before the transaction can be completed. Seldom have regulation writers created so much paperwork out of so little substance. Indeed, the FTC seems to take pride in acknowledging that it has transformed a simple notification program into a "new legal specialty, comparable to securities or tax law" (or so the director of the FTC's Bureau of Competition said in January 1977).

The new rules come at a time when the Carter administration is committed to "chopping down the thicket" of federal red tape and "gobbledygook." President Carter is pledged to a "continuing effort to cut down on unwarranted and unnecessary Government regulation and intrusion into the private free enterprise business sector." He has praised the Labor Department for reducing "nitpicking regulations" at the Occupational Safety and Health Administration, and commended the Defense Department for shortening the regulations on the purchase of towels from thirty pages to a paragraph. But it is doubtful he will be praising the antitrust agencies on this account.

Before the passage of Hart-Scott-Rodino, the FTC's merger notification program consisted of a two-page notice describing the program and a four-page form for sending in the required information in cases where the merger resulted in combined sales or assets for the merged company in excess of $250 million. Except for the mandatory waiting period, the new statutory provisions, while somewhat more detailed, continue essentially the same system, with the reporting requirements applying to a merger or acquisition in which one of the parties to the transaction has sales or assets of $100 million or more and the other has sales or assets of $10 million or more. By way of implementing regulations to carry out the expressed intent of Congress—to give the antitrust agencies a "fair and reasonable opportunity to detect and investigate large mergers of questionable legality before they are consummated," thereby providing them with a "meaningful chance to win a premerger injunction"—all that was needed was a few para-

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graphs describing the new law, defining its more important terms, and prescribing a simple form on which to supply the required data.

Instead, the premerger regulation writers have conjured up a complex world of "ultimate parent entities," acquisitions within acquisitions ("secondary acquisitions"), and four separate "notification thresholds" that can be crossed and recrossed by buying and selling various amounts of stock and assets, and that sometimes require the filing of additional premerger notification forms but sometimes not. On top of this, there is a lengthy form requiring remarkably complicated statistical calculations, including such things as 1972 sales figures transposed forward as if the reporting company manufactured and sold the same products in 1972 as it does today and, conversely, current sales figures transposed backward as if the company manufactured and sold the same products today that it did in 1972.

The inappropriateness of these rules is highlighted by the President's remarks of May 1978 to the Los Angeles County Bar Association in which he referred to the "over-lawyered" 10 percent of the population that requires the services of 90 percent of the lawyers. The premerger rules alone may render this estimate on the conservative side. In the same speech, the President put the case very well for preventing this sort of thing: "In trying to solve society's problems, our regulators have proposed unnecessarily detailed specifications and written regulations in the kind of gobbledygook that could employ a generation of law school graduates just to interpret them."

If the President has his way, the coming generation of "premerger notification" law graduates will be the last of its kind. But the gobbledygook writers will be going out in a blaze of glory, and it seems fitting to give some recognition to their final achievement. Set forth for all to see in these 100,000 words is the entire panoply of ploys, snares, and stratagems used by regulation writers for generations to consolidate and expand their regulated domain. Ambiguity, indirection, and confusion are important elements. But the indispensable requirement, however it be achieved, is to build in a need for further interpretation and "clarification" of the muddle that has gone before so that new generations of regulation writers, like lawyers, can succeed themselves, ever expanding the program as they come and go. The premerger regulation writers have improved some of the old techniques and invented a number of new and imaginative ones, and their effort should be recognized as a classic of its kind.

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Open Ends and Loopholes

Before turning in admiration to the regulations, we must pose a preliminary question. How is it that the premerger rules are so very long and detailed?

Congress must take part—perhaps even a large part—of the blame. Since the mid-1950s, the antitrust agencies had sought not only a premerger notification procedure, but also an automatic stay provision enabling the government to prevent consummation of transactions merely by certifying to a federal district court that the public interest required delay of consummation until the actual legality of the merger had been determined. This automatic premerger injunction provision was necessary to overcome the "wholly inadequate remedy" of divestiture that always was "long-delayed" after the government prevailed on the merits of the case and almost invariably "failed to restore the competitive conditions existing before the merger"—to quote from Senate Report 94-803 (I, May 6, 1976). Thus, the provision was contained in the premerger notification bill that Senators Hart and Scott introduced into the Senate in March 1975, and its enactment was urged by the Antitrust Division of the Department of Justice as "crucial to an effective enforcement program."

Unfortunately for those who favored the bill, the Ford administration (as Deputy Attorney General Harold Tyler advised the Senate Judiciary Committee in February 1976) opposed the premerger injunction provision. That fact, together with some serious filibustering by Senators Allen, Hruska, and others, led to the

final compromise in Hart-Scott-Rodino by which the government was merely given the option of an early federal court hearing on a preliminary injunction with no automatic stay provision of any kind.

Deprived by Congress of its primary raison d'être, the premerger legislation was reduced to a notification device, supposedly giving the antitrust agencies "a fair and reasonable opportunity" to investigate "large mergers" of questionable legality before they were consummated. Even this modest congressional objective was based upon dubious statistical premises. Without citing any source for its numbers, the Senate Report noted that the premerger legislation would cover less than 100 transactions a year out of the "approximately 3,000 mergers that have occurred annually in the course of the past several years." A half year's reporting under the premerger regulations has demonstrated that these figures were far too low. From September 5, 1978, through the third week of March 1979, by the FTC's own count, the antitrust agencies received filings on 560 transactions (*Legal Times of Washington*, April 2, 1979). If this pace continues, the FTC and the Antitrust Division will be receiving data for more than ten times the number of transactions forecast by Congress—and very few of these transactions will involve "large mergers of questionable legality." Before passage of Hart-Scott-Rodino, Congress had fair warning that if the FTC had to investigate all mergers of more than $100 million "the fruits of our efforts might not be worth the cost"—this from no less an authority than FTC Chairman Lewis Engman. Congress paid no attention, and as Engman predicted, the antitrust agencies are bearing the costs of processing an avalanche of largely meaningless paper. Far larger costs are being borne by the firms required to provide complex data to the antitrust agencies—usually for relatively small mergers and acquisitions having little or no antitrust significance.

To make matters worse, Congress not only presented a broad and ambiguous statute to the FTC's regulation writers, but also allowed them freedom both to define the terms used and to prescribe such other rules as may be "necessary and appropriate to carry out the purposes" of the legislation. And, as if this were not sufficiently open-ended, Congress also gave them the opportunity to obtain from reporting parties "such documentary material and information as is necessary and appropriate" to determine whether an acquisition violates the antitrust laws. The potential for expansive regulation writing is self-evident.

While Congress can and should be held accountable for enacting a vague and loopholed statute, with an excessive delegation of authority, the regulation writers must take equal responsibility for the length and complexity of the premerger rules. It is an unalterable phenomenon of bureaucratic behavior that any authority delegated to regulation writers will be exercised to the fullest.[1] In transforming two pages and 2,000 words of the premerger statute into 100 pages and 100,000 words of rules and regulations, the premerger regulation writers were following what can be termed a "Regulation Writer's Law," not unlike Parkinson's, that implementing regulations tend to expand so as to explain, interpret, and establish procedures for complying with every possible meaning of every word of the governing statute. On top of this, of course, a good regulation writer can find ways to go beyond any possible meaning of the statutory words.

Premerger Notification Ploys, Snares, and Stratagems

The devices used by the premerger notification writers are so numerous that anything more than a brief attempt at cataloging them by type, with an occasional example or two, would produce an exegesis nearly as long as the regulations themselves. They range from the traditional word games—expansion by over-broad

[1] In providing that the FTC obtain the "concurrence of the Antitrust Division in implementing the premerger regulations, Congress may have hoped to produce some restraint and balance in the final rules. But this, too, proved to be a miscalculation. According to former Deputy Assistant Attorney General Joe Sims, the FTC viewed the premerger notification statute as a device for obtaining as much information as possible from as many reporting firms as could be included. In contrast, according to Sims, the Antitrust Division pressed for more exemptions (particularly so as to eliminate many of the smaller transactions) and advocated a shorter initial notification form, with more detailed information and documents only being required if the acquisition appeared to present problems under the antitrust laws. With a few exceptions, such as some limitations on foreign transactions advocated by the Antitrust Division, the FTC's viewpoint largely prevailed.

definition of terms and by finding ambiguity or double meaning where there is none—to some highly innovative techniques for confusing what appears to be clear and for obtaining data and documents Congress specifically said may not be obtained.

Expansion by Definition and Self-Created Double Meaning. A time-tested technique for regulatory expansion is to define the terms of the statute broadly enough to cover everything the regulators deem reasonable and permissible. An obvious example in the premerger notification rules is the inclusion of new joint ventures. As was pointed out in a number of comments that the FTC received on the proposed rules, no mention of joint ventures is made in either the statute or its legislative history, an omission that contrasts with the explicit references to joint ventures in another section of Hart-Scott-Rodino. It was even pointed out that the premerger statute is in the present tense and assets or securities cannot be acquired in the present from a "person" who will only exist in the future. Not deterred in the slightest by such rudimentary logic, the regulation writers merely responded that Section 7A(d)(1) gave them the power to define the terms of the act and that is all they had done. (For these and their other comments and responses, see *Federal Register*, July 31, 1978.)

A somewhat more subtle technique was used to overcome the fact that several statutory tests must be met before a merger or acquisition is covered, which obviously would reduce the regulator's domain. Specifically Section 7A(a)(2) states that the "person" from whom securities or assets are being acquired must have total sales or assets of $10 million or more, while Section 7A(a)(3) states that the securities or assets purchased must amount to 15 percent or more of the "acquired person" before notice need be filed. The regulation writers neatly minimized the effect of this limitation by finding that "the Act itself uses the term 'person' in at least two different senses," although this double meaning has not been apparent to anyone else. The device of attributing ambiguity or double meaning to a word enabled them to maximize coverage by defining "person" as the largest possible entity (the "entire corporate structure") when measuring the size of the acquired person, and as a smaller entity (for example, the subsidiary corporation that issued the stock to be acquired) when measuring whether 15 percent or more of the acquired "person" was purchased. As might be expected, a number of commentators criticized the use of different definitions of the same term, particularly when these definitions are being applied within the same subsection of the statute. The regulation writers disposed of these objections by noting that "demands for consistency were not constructive to the extent that they fail to suggest a way to apply the 15 percent test of 7A(a)(3)(A) when shares of one corporation of a multicorporate person are to be acquired." In other words, to insist that the same meaning be given to the same word in the same subsection of the statute is not "constructive" if it does not permit the regulation writers to extend their dominion.

There is a certain Orwellian quality to all this. In *Nineteen Eighty-Four,* "double-think" is to hold two contradictory beliefs in one's mind simultaneously and accept both of them, and it is not surprising perhaps that a few years short of 1984 a word can be given different meanings simultaneously so that an "acquired person" is the entire corporation or a subsidiary of the same corporation, depending on one's needs. Both for Orwell and for the regulation writers the key to power is to be able to define your own terms as you go along.

Finding Legislative Intent, Both as "Manifest" and through a Negative Pregnant. Another useful method for expanding any field of regulation is to discover a "legislative intent" for something that is desired but cannot be justified any other way. The regulation writers effectively employed this device in subjecting acquisitions made long before the passage of Hart-Scott-Rodino to the requirements of the act—which would be questionable ex post facto law if enacted by Congress. By way of an example, the premerger regulators pointed hypothetically to corporation A's seeking to acquire $1 million of the stock of corporation X after the regulations have gone into effect, but already holding $19 million of the same company's stock, purchased at a much earlier date. Since Section 7A(a)(3) of the statute specifies that coverage depends on the acquiring company's holding $15 million of stock "as a result of" the acquisition, it would seem to be elemen-

tary that the $1 million stock purchase need not be reported. Not so, according to the regulation writers, and they overcome the hurdle by "deeming" the earlier $19 million purchase to be part of the later $1 million purchase.

Outlandish? Clearly it is, but the premerger regulators had no trouble finding that the Hart-Scott-Rodino Act "manifests an intention that the agencies should be informed of large securities holdings whenever an acquisition takes place, and the rule is faithful to that intention." Exactly where such ex post facto congressional intent manifests itself they do not say, but good regulation writers, while famous for their verbosity, can also be taciturn when the occasion demands.

For an example of another "legislative intent" device—what may be called the negative pregnant—we turn again to the matter of joint ventures. As noted, the regulation writers had some difficulty in defining joint ventures into the statute since such transactions are nowhere referred to in the statute's premerger section or in the legislative debates or reports. They were able to turn this omission to their advantage by asserting that "nothing in the act's legislative history indicates that Congress did not intend for the act to reach acquisitions of voting securities in connection with the formation of new corporations," including joint ventures. Of course, the same may be said for a lot of other things Congress did not mention, and it might be wondered why this simple ploy is not used more often to expand regulatory coverage. The answer is that power grabs based on a legislative negative pregnant or on a finding of "manifest" legislative intent cannot be used too often without giving the game away. The premerger notification writers used them only when there was nothing else available.

Creating Confusion by Specifying Clear Lines for Noncoverage and Then Muddying Them Up. As we have said, one method by which regulation writers expand their domain is to be as obscure and complex as possible so that the regulators and their expanding staffs will be called upon repeatedly to clarify the confusion they themselves have wrought. The premerger notification writers are masters at this. For pure subtlety and indirection in creating confusion and thereby expanding jurisdiction, nothing quite equals their performance in drafting Rules 802.20 and 801.10.

First, in what appears to be a most magnanimous gesture of jurisdictional forbearance, they eliminated from coverage all asset acquisitions in which the acquiring corporation does not purchase assets valued at more than $10 million. As they were careful to point out, this limitation, as embodied in Rule 802.20, eliminated the "reporting and waiting period requirements with respect to certain relatively small acquisitions that are clearly reportable under the act." Ordinarily, good regulation writers do not give up any part of their jurisdiction quite so easily without a quid pro quo, and careful examination reveals that while they gave away a little with one hand, they took back a great deal more with the other.

The taking back came in Rule 801.10, where their stratagem revolved around the method by which the acquired assets must be "valued." It is not the acquisition price of the assets alone that determines the value, but rather the acquisition price or the "fair market value" of the assets, whichever is higher—with the acquisition reportable if either is greater than $10 million. As an added touch, this fair market value determination is required to be made by the acquiring company's board of directors or by someone directly accountable to the board. With this fair market value provision, the regulation writers quietly imposed a requirement that there be a fair market value determination for each asset acquisition made by a $100 million corporation, no matter how small the acquisition price.

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So smoothly and inconspicuously was this done that we hardly notice the disappearance of the supposedly clear-cut $10 million exemption for asset acquisitions. Similarly, the 15 percent limitation in Section 7A(a)(3) of the statute has been left far behind. Now, each time an asset acquisition of whatever size or percentage is considered by a large corporation, the

company's top executives must become involved with premerger notification. Notice again that the fair market value determination must be made *whether or not* the acquisition is covered by the premerger statute or the regulations. By stealth and indirection, the regulators have extended their domain to include transactions completely outside the statute. This is expansive regulation writing at its best.

Expansion by Intimidation. One not-so-subtle device used by the premerger notification writers is pure and simple intimidation. Characteristically, they do not bother to make threats with the civil penalty provision of the statute (which is common to many federal statutes and rarely used). The statutory scheme provides them with a much more formidable weapon, and they make good use of it. Bluntly put, it is: "If you do not comply with our regulations and give us what we want, you will have a lawsuit and not an acquisition." To make the threat stronger, the lawsuit would concern not the legality of the acquisition, but only whether there had been compliance with the statutory requirements of notification, as interpreted (and expanded upon) by the regulation writers.

The premerger regulators found their opening for this device in what appears to be a routine provision of the statute, one specifying that the waiting period begins when the "completed" notification forms are received, or (to the extent that the forms are not completed) on the reception of "a statement of the reasons for . . . noncompliance." Aware of this potential loophole and anxious to forestall any possibility that the antitrust agencies might be able to delay and abort acquisitions by insisting on very technical "complete" compliance with the requirements before the waiting period started to run, Congress specifically required only "substantial compliance," and not "absolute and complete compliance." Moreover, alert to the ways of regulation writers, Congressman Rodino placed on the record a carefully prepared statement of legislative intent in order to make it clear that the regulators would have very little room to maneuver in order to delay the running of the waiting period. "A broad and liberal interpretation of the doctrine of 'substantial compliance' should protect the rights of the Government as well as the parties to the proposed merger." Congressman Rodino then went on to remind the regulation writers:

> It was, after all, the prospect of protracted delays of many months—which might effectively "kill" most mergers—which led to the deletion, by the Senate and the House Monopolies Subcommittee, of the "automatic stay" provisions originally contained in both bills. To interpret the requirement of substantial compliance so as to reverse this clear legislative determination clearly constitutes a misinterpretation of this bill [*Congressional Record,* September 16, 1976].

But the premerger notification writers wasted little time in setting about to misinterpret this "clear legislative determination" in as many ways as possible. Instead of adopting a "broad and liberal interpretation" of the "substantial compliance" phrase, they have specified that anything "less than a complete response potentially is not substantial compliance," and that any failure "to supply a complete response will be construed narrowly." Instead of following Chairman Rodino's admonition that a government request for data "that could not be compiled or reduced to writing in a relatively short period of time . . . would not constitute a failure to substantially comply," the regulation writers look unkindly upon any objection based on the burdensomeness of the demands for data: "That it will be costly or burdensome to obtain requested information will not necessarily excuse a failure to comply substantially. . . ."

While these may be rhetorical threats and nothing more, they reveal an unwillingness on the part of the regulation writers to adhere even to the few restrictions placed upon them by Congress. At this point, would anyone have the temerity to decline to compile an obviously burdensome and time-consuming request for data, and then claim that there had been substantial compliance? Clearly, since the threats might become real at any time, the answer is no.

Even more boldly, the regulation writers disregarded the congressional directive to keep their hands off materials protected by what Congressman Rodino called a "legitimate privilege." Both the House Report accompanying Hart-Scott-Rodino and Rodino himself stated *for the record* that withholding privileged material would not constitute failure "to substan-

tially comply" with premerger notification, nor could it serve as an excuse for any claim that the waiting period had not begun.

The premerger notification writers paid no attention. Singling out the most "legitimate" privilege of all, the attorney-client privilege, they announced that they "declined to follow" any suggestion that "documents protected by the attorney-client or other privileges should be exempt from disclosure. . . ." When "allegedly privileged" documents are withheld, they went on to state, it will be decided on a "case-by-case basis" whether "a reporting person has substantially complied with the act and rules." It would be surprising, and indeed shocking, for Congress itself to attempt to repeal such a well-recognized privilege and, of course, it did not do so. The premerger regulation writers were far more adventurous. Is it to be supposed that they thought such a clearly prohibited expansion of their power would go unchallenged? Apparently so and, as we have observed, the premerger statutory scheme provides a potent means for intimidation. When an executive is faced with the choice of fighting a lawsuit to preserve the attorney-client privilege or of completing a potentially profitable acquisition upon which much time and effort has been spent, it is a good bet that he will choose the latter.

An *in terrorem* effect may be present even if the threat to force disclosure of privileged documents is never exercised. An acquisition-minded company could well be deterred from seeking a comprehensive antitrust analysis from counsel for fear the analysis might have to be given to the regulators—or the merger delayed because the analysis was withheld. Ironically, overreaching by the regulation writers could thus increase rather than lessen the number of mergers and acquisitions of questionable legality, since merging companies following this seemingly prudent course may not receive, let alone document, adequate legal advice before completing their transactions.

How to Keep the Regulation Writers at Bay

So far, the premerger regulation writers have ignored the President, gone even beyond the broad authority delegated to them by Congress, and would seem to have little fear of challenge from those "reporting persons" whom they are regulating. An obvious inquiry at this point is how to insert some semblance of fairness and reason into this runaway regulation. One simple remedial measure would be to raise the dollar amount on reportable transactions to a more realistic level. For example, a return to the FTC's earlier merger notification figure of $250 million in sales or assets for the combined company (with a $50 million minimum for each party to the transaction) would go far to eliminate the need for reporting inconsequential transactions. Congress can and should take the lead in insisting upon this modification, and the Antitrust Division might be able to precipitate congressional action by withholding its concurrence from the next annual report the FTC must submit to Congress. (Submission of a separate Antitrust Division report calling for a sharp decrease in coverage would be even better.)

Such a step would be beneficial, but the 100,000-word muddle of complex and confusing regulations would remain. This raises the more fundamental question whether there is perhaps some prospect of curtailing regulation writers in general and the premerger notification writers in particular? It seems apparent that the only realistic hope for chopping down the premerger regulatory thicket is through decisive action by the executive branch. The administration, through the recently created Regulatory Council (and, if enacted, through the Regulation Reform Act of 1979), must carry forward its commitment to abolish unwarranted government regulations—and the premerger notification rules are an inviting first candidate. Another helpful step would be to impose length limitations on all interpretative regulations—for example (though this may be Utopian), no more words than the underlying statute itself. As a goal, this seems preferable to the fifty words of explanation for every word of the premerger statute achieved by the premerger regulation writers. Finally, the administration or Congress (or both) should adopt a "sunset" provision requiring that regulations terminate after a specified period (say, three years) and that, if another round of regulations is necessary, they must be equally concise and should be written by a new group of regulators.

If this kind of chopping down of unnecessary regulations ever got under way, there is no telling how many regulation writers (and lawyers) might have to look for other lines of work. ■