

# Client Alert

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## DOJ Suit Against Activist Investor Highlights Narrow Interpretation of HSR “Investment Only” Exemption

By Jeff Jaeckel and Lauren Navarro

On April 4, 2016, the U.S. Department of Justice (DOJ) filed a civil antitrust lawsuit against activist investor ValueAct Capital (“ValueAct”). DOJ asserts that ValueAct improperly relied on the “investment only” exemption to the Hart-Scott-Rodino Act (the “HSR Act”) reporting requirements when it bought over \$2.5 billion worth of stock in Halliburton and Baker Hughes (collectively, “the Companies”) with the intention of influencing the business activities and strategies of the Companies. ValueAct has indicated that it may fight the DOJ lawsuit, but this action nonetheless underscores that investors should exercise care when relying on the investment-only HSR exemption, because the antitrust enforcement agencies show no sign of relaxing their narrow interpretation of the exemption and strict enforcement program against perceived violations.

### HSR INVESTMENT-ONLY EXEMPTION

The HSR Act imposes notification requirements and a statutory waiting period for transactions meeting certain size thresholds so that the antitrust enforcement agencies can undertake premerger review of such transactions. The HSR Act has a narrow exemption for acquisitions of less than 10 percent of a company’s outstanding voting securities if that acquisition is made “solely for the purposes of investment.”<sup>1</sup> DOJ and Federal Trade Commission (FTC) narrowly construe this exemption, however, as was underscored last year when another activist hedge fund, Third Point LLC, reached a settlement with the FTC over charges that it improperly relied on the exemption and failed to make a filing under the HSR Act.<sup>2</sup> In its public disclosures around that case, the FTC emphasized that the investment-only exemption applies only when an acquisition is solely for purposes of passive investment — that is, the investor must not intend to participate in any aspect of the company’s business decisions.<sup>3</sup>

### VALUEACT’S STOCK PURCHASE

On November 17, 2014, Baker Hughes and Halliburton – two large providers of oilfield products and services – announced a plan to merge the two companies in a transaction valued at \$35 billion. Following this announcement, ValueAct purchased over \$2.5 billion of the companies’ voting shares in open-market transactions but did not report the acquisition, relying on the investment-only exemption.

<sup>1</sup> 15 U.S.C. §18a(c)(9).

<sup>2</sup> See the FTC’s complaint against Third Point LLC, available at <https://www.ftc.gov/system/files/documents/cases/150824thirdpointcmpt.pdf>.

<sup>3</sup> See our previous alert describing the narrow application of the investment-only exemption and the Third Point LLC case available at <http://www.mofo.com/~media/Files/ClientAlert/2015/08/150831RecentFTCAction.pdf>.

# Client Alert

ValueAct is an investment firm that advertises a strategy of active, constructive involvement in the management of the companies in which it invests. According to ValueAct's website, its business model focuses on "acquiring significant ownership stakes in a limited number of companies," and "[t]he goal in each investment is to work constructively with management and/or the company's board to implement a strategy or strategies that maximize returns for all shareholders." DOJ pointed to this general language regarding ValueAct's investment strategy, contending it is inconsistent with the investment-only exemption, which requires the acquisition be solely for purposes of investment. Indeed, DOJ alleges that ValueAct specifically purchased shares in the Companies with the intent of influencing the Companies' business decisions as the merger unfolded:

ValueAct intended to use its position as a major shareholder of these companies to obtain access to management, to learn information about the merger and the companies' strategies in private conversations with senior executives, to influence those executives to improve the chances that the merger would be completed, and to influence other business decisions whether or not the merger went forward.

In light of this, DOJ asserts that ValueAct could not rely on the limited "investment-only" exemption to HSR notification requirements because ValueAct did in fact intend to influence the companies' business decisions.<sup>4</sup>

ValueAct replied in a statement that the firm takes its disclosures "extremely seriously" and that it plans to fight the lawsuit. The firm added, "[w]e have acted entirely properly and in compliance with the law. We fundamentally disagree with the Justice Department's allegations in this case." This case nonetheless illustrates the continued efforts of antitrust agencies to curtail reliance on the exemption, the precise boundaries of which remain unclear given that other recent defendants (like Third Point) have opted for settlement.

## KEY TAKEAWAYS

- **The Cautionary Tale of Websites.** In its complaint, DOJ quoted language from ValueAct's website regarding ValueAct's investment strategy. DOJ's reliance on such broad and generalized marketing statements should put investors on notice to be cognizant of how their services are advertised. The language stating that ValueAct supported "active, constructive involvement" in the management of the companies in which it invests says nothing about ValueAct's specific intentions or conduct with respect to its investment in the Companies, but it is being used in an effort to undercut the argument that the acquisition of Baker Hughes and Halliburton's shares was purely for "investment purposes." This is important to keep in mind as investors consider whether to invoke the exemption — specifically, whether there is publicly available information that an agency could claim contradicts the exemption requirements.
- **Repeat Offenders Beware.** It is noteworthy that this was not ValueAct's first reporting violation. The complaint explains how ValueAct has twice faced similar charges from federal regulators over prior disclosures, previously paying the government \$1.1 million to settle similar claims. This pattern appears to have furthered DOJ's resolve to pursue penalties against ValueAct. Indeed, DOJ asked the court to assess a civil penalty of at least \$19 million against the company. This outcome is consistent with language in the FTC's settlement with Third Point, where the FTC cited the fact that it was Third Point's first HSR violation as one of the reasons it chose not to seek civil penalties against the company.

<sup>4</sup> <https://www.justice.gov/opa/pr/justice-department-sues-valueact-violating-premerger-notification-requirements>.

## Client Alert

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- **Continued Scrutiny.** As this suit highlights, DOJ is not hesitant about closely scrutinizing whether an investor intends to influence a company's business decisions and therefore falls outside the exemption. As both this and the Third Point resolution make clear, investor intent is critical, and the regulatory agencies will not hesitate to ferret out illusory passive intent.

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