

CLIENT ALERT

Alleged “Transactional Device” For Avoiding Merger Filings Subject of DOJ and EU Fines

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Earlier this summer, the U.S. Department of Justice (the “DOJ”) filed a proposed final judgment against Canon Inc. (“Canon”) and Toshiba Corp. (“Toshiba”), imposing a \$2.5 million civil penalty against each party.¹ The DOJ, which filed a complaint based on a referral from the Federal Trade Commission (“FTC”),² alleged that the parties strategically structured the sale of a Toshiba subsidiary to Canon to circumvent the filing requirements of the Hart-Scott-Rodino Act (“HSR Act”).³ The public comment period on the proposed final judgment runs until August 25, 2019.⁴

The antitrust authorities of the European Union (“EU”) also imposed a \$31.8 million fine on Canon as the acquiring party for avoiding the corresponding EU merger regulation.⁵ The European Commission found that the transactions structured by Canon and Toshiba “breached the notification requirement and standstill obligation.”⁶

¹ Proposed Final Judgment at 3, *U.S. v. Canon Inc. et al.*, No. 1:19-cv-01680 (D.D.C. June 10, 2019) [*hereinafter* Canon Proposed Final Judgment].

² Press Release, *Fed. Trade Comm’n, Canon Inc., Toshiba Corporation Agree to Pay \$5 Million for Violating Federal Antitrust Laws* (June 10, 2019), available [here](#) [*hereinafter* FTC Press Release].

³ *Id.*

⁴ *United States v. Canon Inc. and Toshiba Corporation*, Proposed Final Judgment and Competitive Impact Statement 84 Fed. Reg. 123 (proposed June 26, 2019).

⁵ European Commission Press Release IP/19/3429, *Mergers: Commission Fines Canon €28 Million for Partially Implementing Its Acquisition of Toshiba Medical Systems Corporation Before Notification and Merger Control Approval* (Jun. 27, 2019), available [here](#) [*hereinafter* EC Press Release].

⁶ *Id.*

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The *Canon* matter provides a good reminder that antitrust regulators in the U.S. and Europe continue to police merger-notifications rules vigorously and do not permit the avoidance of those requirements. FTC Commissioner Bruce Hoffman promised that the agency would be “vigilant in seeking relief against attempts to circumvent the HSR Act’s filing requirements.”⁷ EU Competition Commissioner Margrethe Vestager added, “Our merger assessment and decision-making depends on the [European Commission’s] being sure that companies are not jumping the gun and implementing mergers without our approval.”⁸

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Parties may not structure transactions for the purpose of avoiding the HSR Act.⁹ Section 801.90 of the HSR Rules states that “[a]ny transaction(s) or other device(s) entered into or employed for the purpose of avoiding the obligation to comply with the requirements of the act shall be disregarded, and the obligation to comply shall be determined by applying the act and these rules to the substance of the transaction.”¹⁰

A review of the facts of the *Canon* matter in light of Rule 801.90 is instructive. Toshiba began the process of selling Toshiba Medical Systems Corp. (“TMSC”) in December 2015, after it was forced to restate its earnings for several years and incur a significant accounting charge.¹¹ Given Toshiba’s financial position, it sought to recognize the proceeds from the sale *before the end of its fiscal year on March 31, 2016*.¹² Filing premerger notification and receiving the necessary clearance under the HSR Act within such a timeframe would have been difficult, if not impossible.¹³

As an alternative, Toshiba and Canon engaged in a multi-step acquisition process.¹⁴ First, on March 8, 2016, Toshiba and Canon caused the formation of MS Holding Corp. (“MS Holding”).¹⁵ Second, on March 15, 2016, Toshiba altered the corporate ownership structure of TMSC.¹⁶ Toshiba formed “new classes of voting shares, a single non-voting share with rights custom-made for Canon, and options convertible to ordinary shares.”¹⁷

⁷ FTC Press Release.

⁸ EC Press Release.

⁹ Complaint 20, *U.S. v. Canon Inc. et. al.*, No. 1:19-cv-01680 (D.D.C. June 10, 2019) [*hereinafter* Canon Complaint].

¹⁰ 16 C.F.R. § 801.90.

¹¹ Canon Complaint 3.

¹² *Id.* 3-4.

¹³ *Id.* 4.

¹⁴ *Id.* 5-7.

¹⁵ *Id.* 28(e-h).

¹⁶ *Id.* 5, 28(i).

¹⁷ *Id.* 6.

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On March 17, 2016, Toshiba sold to Canon TMSC’s special non-voting shares and options for \$6.1 billion, thereby realizing before the end of its fiscal year on March 31, 2016, the inflow of proceeds that it was seeking.¹⁸ At the same time, Toshiba transferred the voting shares of TMSC to MS Holding in exchange for \$900.¹⁹ On December 19, 2016, after having filed HSR notification and observed the requisite waiting periods, Canon exercised its options to acquire the ordinary shares and, on December 21, 2019, Canon obtained formal control of TMSC’s voting shares.²⁰

The agencies claimed that Canon had effectively acquired beneficial ownership of TMSC on March 17, 2016, when Canon acquired the options to purchase TMSC voting securities without having complied with HSR requirements.²¹ Canon exercised direction and control over MS Holding during its formation. The DOJ alleged that Canon had “caused the creation of MS Holding; it participated in the selection of the principals of MS Holding; it briefed the proposed principals of MS Holding about the transaction; it participated in the drafting of the formation documents of MS Holding; it commented on the appropriateness of the name MS Holding; it reviewed, commented on, and approved the share transfer agreement between MS Holding and Toshiba; and it commented on draft questions and answers regarding MS Holding.”²²

In addition, the DOJ alleged, MS Holding “had no meaningful risk of loss or benefit of gain in connection with its ownership of the Class A [voting] shares. It was to be paid a fixed amount that did not go up or down depending on the financial performance of TMSC.”²³ MS Holding was created “for the specific purpose of acquiring and holding certain of TMSC’s shares pending antitrust clearance for Canon’s proposed acquisition of TMSC.”²⁴

According to the DOJ, “MS Holding did not act as an independent owner of TMSC during the period it nominally controlled TMSC through its ownership of the Class A shares.”²⁵ “Neither the Defendants nor the principals of MS Holding expected MS Holding to be involved in the operation of TMSC during the period that MS Holding nominally controlled the Class A shares. Indeed, Canon itself has admitted that ‘TMSC’s management board ran TMSC’s day-to-day business during the time MS Holding’ controlled the Class A shares.”²⁶

¹⁸ *Id.* 28(j).

¹⁹ *Id.* 6, 28(k).

²⁰ *Id.* 28(l)-(m).

²¹ *Id.* 27-30.

²² *Id.* 31.

²³ *Id.* 32.

²⁴ *Id.* 16.

²⁵ *Id.* 33.

²⁶ *Id.* 34.

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The acquisition of beneficial ownership of the TMSC shares, the absence of any genuine risk of loss or benefit of gain to MS Holding, and MS Holding’s failure to act as an independent owner of TMSC formed the basis for the application of the non-circumvention prohibition of Rule 801.90.

Canon and MS Holding eventually filed HSR Act notifications on April 26, 2016, to allow Canon to exercise the options to acquire the TMSC voting shares,²⁷ which Canon eventually did on December 21, 2016. These filings were neither timely nor effective to cover the alleged transfer of beneficial ownership to Canon that occurred on March 17, 2016.²⁸

In addition to being fined in the United States, Canon was subsequently fined \$31.8 million by the EU antitrust authorities, on June 27, 2019, for avoiding EU merger reporting obligations as well.²⁹ EU Competition Commissioner Margrethe Vestager stated, “This is a procedural breach of our merger review . . . [o]ur merger assessment and decision-making depends on the [European Commission’s] being sure that companies are not jumping the gun and implementing mergers without our approval.”³⁰ The EU fine was a unilateral penalty imposed by the European Commission, unlike the US fine, which arose from a settlement struck between the companies and the U.S. agencies.³¹

Both the bar and the enforcement agencies recognize that the HSR regulations are highly technical. The *Canon* matter nevertheless underscores that the antitrust regulators will apply the non-circumvention prohibition in Rule 801.90 to parties that use those technicalities to structure a transaction to avoid an HSR filing when the transaction in substance transfers beneficial ownership of stock or assets that would otherwise require a filing.

²⁷ *Id.* 37. While the acquisition of an option is exempt from filing obligations pursuant to 16 C.F.R. § 802.31, the exercise of an option (or other convertible security) can trigger a filing obligation.

²⁸ *Id.* 37.

²⁹ EC Press Release.

³⁰ *Id.*

³¹ *Id.* FTC Press Release.

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