Mergers and Acquisitions

Center Forward Basics

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Overview

Mergers and acquisitions (M&A) are the combining of companies or assets through various types of financial transactions. They allow for businesses to grow or downsize in order to adjust their competitive position or improve the overall structure of their business. M&A also helps struggling companies to bring a product to market, expand new product lines, or share a product line in a new market. Additionally, M&A can also spur innovation by providing both entrepreneurs and investors a means to capitalize on the development of new products or services. Mergers and acquisition can benefit consumers by enabling firms to operate more efficiently or to offer product or service bundles for discounted prices. However, some mergers may also change market dynamics in ways that may lead to less competition, incentives to charge higher prices or offer fewer or lower-quality goods or services, and may dampen innovation. Transactions over a certain size (currently $101 million, but adjusted annually) are reviewed by either the Federal Trade Commission (FTC) or the Antitrust Division of the Department of Justice (DOJ) to ensure they comply with U.S. antitrust laws. Transactions that involve the transfer of control of a radio license also require review and approval by the Federal Communications Commission (FCC). This basic will explore the process, government review, and impact of mergers and acquisitions.

Center Forward Basics

Center Forward brings together members of Congress, not-for profits, academic experts, trade associations, corporations and unions to find common ground. Our mission: to give centrist allies the information they need to craft common sense solutions, and provide those allies the support they need to turn those ideas into results.

In order to meet our challenges we need to put aside the partisan bickering that has gridlocked Washington and come together to find common sense solutions.

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Mergers and Acquisitions

A merger occurs when two firms combine into a single new entity. An acquisition occurs when one company purchases a controlling interest in another company and becomes the new overall owner. Acquisitions often include consolidating another entity's stock, equity interests, assets, and liabilities under one new single entity. Mergers and acquisition can be structured in a variety of ways based on the relationship between the two companies involved in the deal. Common types of M&As include: :

- Conglomerate: a merger between firms that are involved in unrelated business activities.
- Horizontal Merger: a merger occurring between companies in the same industry. The businesses typically operate in the same market space and are often competitors that offer the same goods or services.
- Vertical Merger: a merger between companies that provide goods or services at different levels within an industry's supply chain for one specific finished product. Vertical mergers are typically pursued to increase synergies, reduce overall costs, and increase productivity and efficiency. These types of mergers, in particular, inherently enhance competition and rarely raise competitive concerns.
- Market Extension Mergers: a merger between two companies that deal in the same products, but operate in separate markets. This helps companies have access to a larger market and to an expanded client base.
- Product Extension Mergers: a merger between two business organizations with products that are related to each other and operate in the same market. This allows the merging companies to combine products and gain access to a bigger set of consumers.

Mergers & Acquisitions of Private Companies

The ability for a business to be merged or acquired is especially important for private companies that are not publicly traded. For many of these businesses, the future promise of being acquired is what drives investors to provide them with the capital needed to grow, innovate, and hire more employees. This is especially true for newer start-ups or businesses in the growth phase of their lifecycle. However, it is also true for companies that are not a fit for the public markets, or one company's assets that can better be deployed by another company rather than leaving the market. An example of such a transaction is Tate's Bakeshop, which was ultimately sold to Mondelez International.

Relatedly, as long-term investors in businesses (3-7 years on average), private equity (PE) firms and their funds are frequent participants in mergers and acquisitions. These funds often raise capital from pensions and other institutional investors to acquire and grow the value of businesses with the ultimate goal of eventually re-selling an improved business to another business or initiating an Initial Public Offering (IPO) of stock (e.g., Dunkin' Donuts). Additionally, PE and other private companies often participate in both mergers and acquisitions during strategic corporate divestitures as other private sector participants seek to strategically reduce assets or restructure.

Notably, the Biden Administration has taken a more aggressive approach towards antitrust policy on both merger review and litigation. The Administration has also suggested expanding the scope of antitrust oversight to heighten scrutiny of certain types of investors, including private equity transactions, without data or economic analysis beforehand in justification of the additional level of scrutiny. Several antitrust legislative proposals have been introduced in Congress that would impact mergers of public and private companies but none have passed both houses of Congress at this time.

Economic Impact

M&A transactions are a critical part of organic business growth. Growing a business through a merger or acquisition can offer various benefits, including:

- Access to markets that one company may not reach on its own or expansion of a company's reach from a local business to a regional or national one;
- Help for weakened or underperforming companies or business units. Mergers and acquisitions can help employees of a struggling business or business unit retain jobs that may be preserved in an acquisition versus employment losses due to bankruptcy;
- Diversification of the products, services, and long-term prospects of a business;
- The ability to obtain quality staff and additional skills, industry knowledge or sector expertise - for example, merging two businesses to solidify strong management or create more efficient production or distribution capabilities;
- Increase efficiencies or productivity through combining, for example, the different manufacturing process of both companies or their research and the development efforts;
- An improved balanced sheet through savings from reduced overall costs and overhead expenditures. Businesses in the same sector or location can combine resources to reduce costs, eliminate redundant facilities or departments and increase overall profitability;
- Mergers and acquisitions can allow for more secure and expanded employee benefits, including things like good wages, healthcare, and retirement benefits; and,
- Mergers and acquisitions can lead to increased investments in facilities and good-paying jobs, which lead to broader positive impacts in the communities where job creators operate.

However, in limited circumstances there can also be downsides to certain mergers and acquisitions, including:

- Concerns regarding reduced competition, where a merger or acquisition may also create an incentive or ability to raise price, reduce output, or diminish innovation. Uncertainty and confusion among the employees and/or risk of employment reductions.

Regulatory Oversight

Since 1976, there has been a robust and detailed process required to notify the government of significant mergers and acquisitions for review. The FTC and the DOJ enforce the nation's antitrust laws—complementing each other in enforcement and merger reviews by generally focusing on those industries and markets where they have each developed expertise. The agencies review more than a thousand M&A filings each year and 95% of the filings have no underlying competitive issues. While there are some exemptions, current law largely requires any deals valued at $101 million or more to be reported to the agencies for review—allowing a preliminary review and potential extended review. Notably, the Clayton Act prohibits the transactions when the effect "may be substantially to lessen competition, or to tend to create a monopoly." To evaluate whether a transaction violates this standard, the agencies focus on whether the proposed transaction will significantly create or enhance market power or facilitate its exercise in a market. Often, antitrust concerns can arise with proposed horizontal mergers between direct competitors. The Hart-Scott-Rodino Act enables antitrust agencies to examine the likely effects of proposed transactions before they take place, and the agencies may take formal legal action to modify or to stop the merger. On occasion, the agencies have allowed some aspects of a deal to advance while eliminating other components that may present a competitive threat by way of a consent decree with the merging parties which requires either structural remedies (e.g., divestitures) or behavioral remedies (e.g., changes to the merging parties' conduct after the merger). Additionally, many states have their own antitrust laws and may also review a proposed transaction. In recent years, some states have increased such merger reviews.

The divestiture landscape is another place where the regulators have taken a very aggressive posture — increasingly saying that a third-party purchaser that buys a divested asset must agree to let the FTC and DOJ approve any subsequent sale of that asset over the next 10 years, even though there are no competitiveness concerns with the third-party purchaser and this buyer is not one of the merging parties that raised competitiveness concerns.

Additionally, revisiting past mergers and acquisitions could potentially threaten future growth and create instability in markets. Specifically, reviewing past transactions and applying a different analytical approach or a heightened level of scrutiny risks undermining predictability and could slow economic growth. As a solution, the government could focus any retrospective enforcement on identifying any deals where the original analysis relied on flawed or incomplete information (e.g., where it was withheld by the parties). Also, it could be harmful to employees, suppliers, and many others in local economies for regulators to revisit their decisions either not to challenge prior transactions, or to resolve their concerns about such transactions through negotiated settlements, based on new or evolved thinking on what they now believe could or should have been done previously.

For mergers in which a radio license or other authorization granted by the FCC will be transferred to a new owner, the FCC also must review and approve the transaction. In such cases, the FCC will launch a public comment proceeding in which any interested party can participate by filing formal or ex parte comments. The FCC's standard for approving mergers and acquisitions is different from the DOJ and FTC's antitrust standard. Rather, the FCC can only approve a transaction if it finds that it is in the "public interest." In M&A transactions in which the FCC is involved, the FCC typically coordinates its review closely with the DOJ or FTC.

Links to Other Resources

- Bloomberg – A Misguided Assault on Mergers
- Ernst & Young – Six ways private equity will help drive value in M&A
- Forbes – The Impact of the Coronavirus Crisis on Mergers and Acquisitions
- Department of Justice - Merger Enforcement

- Federal Trade Commission – [Mergers]
- Federal Trade Commission – Regarding the Statement of the Commission on Use of Prior Approval Provisions in Merger Orders
- Federal Communications Commission – Review of Significant Transactions
- The Hill – Democratic lawmakers push for merger freeze in next coronavirus relief package
- Investopedia – Mergers and Acquisitions – M&A
- Minority Business Development Agency – Benefits of a Merger or Acquisition
- Politico – House antitrust chairman proposes merger ban during pandemic
- Real Clark Markets – Elizabeth Warren and AOC Get Everything Wrong About M&A
- SIFMA – Global Capital Markets & Financial Institutions Primer
- SIFMA – Markets Matter: US Capital Markets are the Largest in the World