

## Expert Analysis

### Settlement of An HSR Act Violation Highlights the Limits on the 'Investment Only' Exemption

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On Sept. 25 the U.S. Department of Justice announced a proposed settlement of a civil complaint against Biglari Holdings Inc. related to alleged violations by Biglari of the Hart-Scott-Rodino Act.<sup>1</sup>

The complaint, which the DOJ brought on behalf of the U.S. Federal Trade Commission, alleged Biglari failed to comply with HSR pre-merger notification requirements when it acquired shares of Cracker Barrel Old Country Store Inc. in 2011.<sup>2</sup>

Biglari agreed to pay an \$850,000 fine to resolve the issues in the complaint.

#### BACKGROUND

Biglari is an investment fund that has ownership interests in restaurant chains, including Steak n Shake and Western Sizzlin. Cracker Barrel operates a chain of country stores and restaurants.

According to the complaint filed in the U.S. District Court for the District of Columbia, Biglari made multiple open-market acquisitions of Cracker Barrel voting securities between May 24, 2011, and June 13, 2011. The complaint also said on June 8, 2011, Biglari's acquisitions of Cracker Barrel shares exceeded \$66 million, which was the applicable HSR filing threshold at the time.

Biglari did not submit an HSR pre-merger notification form, however, for its acquisitions of Cracker Barrel shares prior to exceeding aggregate holdings totaling \$66 million. It appeared that Biglari attempted to rely on the "investment only" exemption to the HSR filing requirement because the holdings were less than ten percent of Cracker Barrel's outstanding securities. On June 13, 2011, Biglari filed a Form 13 D with the U.S. Securities and Exchange Commission with respect to its acquisition of Cracker Barrel voting securities. In the SEC filing, Biglari said its aggregate share acquisitions accounted for about 9.7 percent of the outstanding Cracker Barrel securities and that it planned "to communicate with the issuer's management and members of the board regarding the business, governance and future plans of the issuer."<sup>3</sup>

*Biglari Holdings Inc. attempted to rely on the “investment only” exemption to the HSR filing requirement because the holdings were less than 10 percent of Cracker Barrel’s outstanding securities.*

On Aug. 26, 2011, Biglari filed an HSR pre-merger notification form for an additional acquisition of Cracker Barrel shares. The acquisition of shares, once notified, received early termination of the HSR waiting period Sept. 22, 2011, which indicated that the transaction did not raise substantive antitrust concerns.

### ANALYSIS

The HSR Act and HSR rules provide certain filing exemptions to acquisitions of voting securities that otherwise meet the applicable thresholds. This includes an exemption for stock acquisitions made “solely for the purposes of investment,” as long as the acquirer does not hold over 10 percent of the issuer’s voting securities as a result of the acquisition.<sup>4</sup>

The HSR rules further limit the exemption by making it available only if the acquirer has “no intention of participating in the formulation, determination or direction of the basic business decisions of the issuer.”<sup>5</sup> Further, the government’s statements at the time the HSR rules were implemented say certain types of actions are inconsistent with holding securities solely for investment, including nominating a candidate for the board of directors, holding a board seat, proposing corporate action requiring shareholder approval, soliciting proxies or being a competitor of the issuer.<sup>6</sup>

The FTC concluded that Biglari’s acquisitions of Cracker Barrel shares did not qualify for the investment only exemption because of direct evidence that Biglari intended to become active in the management and direction of Cracker Barrel’s business.

Specifically, the complaint alleged that shortly after making the share acquisitions that exceeded the HSR threshold, Biglari CEO Sardar Biglari, contacted Cracker Barrel’s CEO to say he had ideas on how to improve Cracker Barrel’s business. More importantly, during a meeting with Cracker Barrel executives, Sardar Biglari requested seats on the Cracker Barrel board of directors for himself and another Biglari executive.

In light of these actions, the FTC alleged that Biglari violated the HSR Act by failing to submit an HSR notification form and observe the HSR waiting period before acquiring Cracker Barrel shares in excess of the \$66 million threshold. The penalties for HSR violations are civil penalties of up to \$16,000 for each day that an acquirer is in violation. Therefore, Biglari’s fine could have been over \$1.6 million (for the period between June 8 and Sept. 22, the day it received early termination of the HSR waiting period).

According to the settlement, however, the government determined a civil penalty of \$850,000 was appropriate to address the seriousness of the violation and deter future violations.

The final judgment has to be approved by a district court judge; however, because the settlement involves only the payment of civil penalties, the court’s entry of judgment should be straightforward.

### HIGHLIGHTS

The government has generally taken the position that a discussion between investors and management regarding the general direction of the company is allowable with the investment only exemption, absent other actions by the investor intended to influence the issuer’s business. The agencies have been consistent in denying the investment only exemption where the acquirer of shares has sought a seat on the

issuer's board of directors or advocated actions requiring shareholder vote. Therefore, the case is a strong reminder that stock purchasers, including private equity firms and activist share-holders, intending to influence the direction of a business should keep in mind the HSR pre-merger notification thresholds and filing requirements.

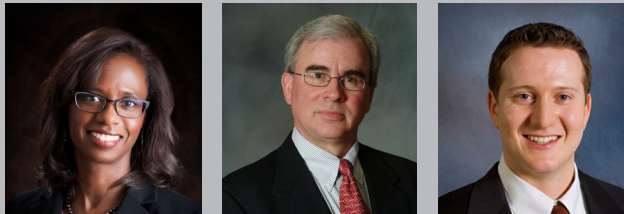
Although the DOJ's complaint does not provide details about the government's analysis of the investment only exemption, the case highlights the relatively high bar to claiming the investment only exemption.

More generally, the case reaffirms the FTC's position that exemptions to the HSR Act are to be applied appropriately and narrowly.

Finally, the fact that Biglari received a relatively significant fine, even though it was a first-time HSR violator, suggests that the FTC viewed this as a serious violation and perhaps intended to send a message to the investment community.

## NOTES

- <sup>1</sup> Press Release, Dep't of Justice, Biglari Holdings Inc. to Pay \$850,000 Civil Penalty for Violating Antitrust Premerger Notification Requirements (Sept. 25, 2012), *available at* [http://www.justice.gov/atr/public/press\\_releases/2012/287345.pdf](http://www.justice.gov/atr/public/press_releases/2012/287345.pdf). *See also* complaint and related case filings, *available at* <http://www.justice.gov/atr/cases/biglari.html>.
- <sup>2</sup> Press Release, Fed. Trade Comm'n, Biglari Holdings Inc. to Pay \$850,000 Penalty to Resolve FTC Allegations that it Violated U.S. Premerger Notification Requirements (Sept. 25, 2012), *available at* <http://www.ftc.gov/opa/2012/09/biglari.shtm>.
- <sup>3</sup> Biglari, SEC Form 13D, filed June 13, 2011.
- <sup>4</sup> See HSR Rule 802.9.
- <sup>5</sup> See Formal Interpretation No. 4, HSR Rules at n.3 (Jan. 17, 1979), *available at* <http://www.ftc.gov/bc/hsr/frmlintrps/fi04.shtm>.
- <sup>6</sup> See Statement of Basis & Purpose, HSR Rules, 43 Fed. Reg. 147 at p. 33465 (July 31, 1978), *available at* <http://www.ftc.gov/os/fedreg/1978/july/780731fr43FR33450.pdf>.



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