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Lessons from a $1.4 million HSR fine

By Thomas L. McLain

Fines for violations of the Hart Scott Rodino Act are not a common occurrence. However, when they do come along, they tend to be eye-popping. The most recent example resulted in an settlement agreement pursuant to which John C. Malone, CEO and Chairman of Discovery Holding Company, is to pay a $1.4 million civil penalty.

The central theme of the Complaint filed by the Federal Trade Commission ("FTC") against Mr. Malone is that he failed to file the required notification with the FTC and Department of Justice before acquiring voting securities of Discovery Holding Company ("Discovery"). Mr. Malone acquired the securities in a series of transactions beginning in August 2005 and continuing until April 2008. On June 12, 2008, Mr. Malone made a corrective filing with the FTC explaining that he had relied on a 2001 informal interpretation from the FTC that, unbeknownst to him, was replaced and disavowed by a February 07, 2005 informal interpretation issued by the FTC. The corrective filing established a waiting period that was to expire on July 14, 2008.

Had the fact pattern ended at this point, it is a reasonable assumption that civil penalties may not have been sought by the FTC. Based upon prior precedent and general procedures, provided that the reason for the missed filing is reasonable and there has been a demonstration of corrective actions taken to prevent future failures, the FTC has been reluctant to impose penalties. (See, Procedures For Submitting Post-Consummation Filings). In fact, on May 9, 1991, Mr. Malone made a corrective filing under the HSR Act for a previous acquisition made in 1985, and on July 2, 1991 the FTC decided not to seeking civil penalties. In any event, the penalties in effect during the time periods in question were $11,000 per day for each day during which there was a violation. [Note: as a result of a 2009 amendment, the daily penalties have been increased to $16,000 per day].

While the 1991 violation of the filing requirements under the HSR Act certainly did not help Mr. Malone's situation, the events occurring after his June 12, 2008 were far more problematic. On June 14, 2008, before the expiration of the HSR waiting period, Mr. Malone exercised options and acquired more shares of Discovery. These options would have expired before the end of the HSR waiting period on July 14, 2008, but Mr. Malone did not notify the FTC to ask whether it was permissible for him to exercise the options with an escrow arrangement prior to the expiration of the waiting period. There is no indication regarding how the FTC would have responded to the request, had it been made. However, this oversight seems to have weighed heavily in the FTC's decision to seek civil penalties.

The underlying HSR rules which resulted in a determination that a notification filing was required could themselves be the subject of an article. However, the purpose of this article is to provide a reminder of the stiff penalties that can be imposed for violations of the HSR Act and to examine some of intricacies of corrective filings. The series of events for Mr. Malone were indeed unfortunate and lead the FTC to seek to impose civil penalties. The result of the events was the entry of a consent judgment against Mr. Malone personally in the amount of $1.4 million. The consent judgment is testimony to the axiom that "bad fact lead to bad results." The primary lesson to be learned from Mr. Malone's problems is that one must always be mindful of the requirements of the HSR Act and that every merger or acquisition transaction must be weighed in light of those requirements.

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