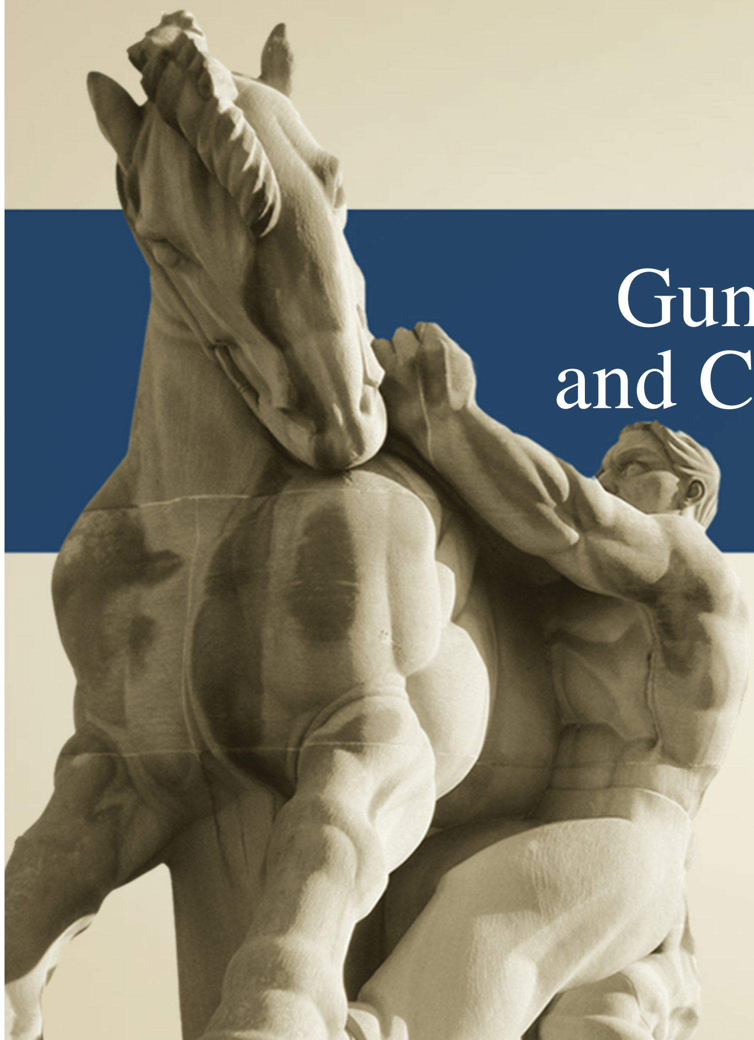

Gun-Jumping: The U.S. Experience and Challenges for the New Brazilian Merger Control Regime

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Gun-Jumping

- Coordination or integration between merging firms before the transaction is closed
  - Desire to coordinate is understandable and could be pro-competitive, BUT
  - Risks (1) anticompetitive behavior and/or (2) pre-merger integration
- Basic rule under U.S. antitrust laws: The firms are separate entities until they merge and must act accordingly
- Pre-merger planning vs. implementation of plan
- Trade-off between efficiency and effective merger control

Potential Benefits of Coordinated Planning

- Due Diligence: Merging partners need some inside information to know whether the deal will benefit shareholders
- Transition Planning: Studies show that a large percentage of mergers fail (35-60%). Successful mergers require:
  - Early planning
  - Use of transition teams
  - Identifying and incentivizing key managers
  - Quick integration
  - Frequent communications to stakeholders
- To be effective, both require communication and planning before the merger takes effect

Limits to Coordination: Two Risks

- Is there an illegal agreement in restraint of trade?
  - U.S.: Sherman Act § 1, FTC Act § 5
  - Brazil: Law No. 12,529/11, Art. 36 § 3 I & II?
- Has there been a violation of the pre-merger notification law?
  - U.S.: Hart-Scott-Rodino Act (Clayton Act § 7A)
  - Brazil: Law No. 12,529/11, Art. 88 § 4?
- Different analysis for each risk

Agreement in Restraint of Trade

- Usually analyzed under "rule of reason" as a joint venture
  - What are the benefits of the conduct?
  - What are the anticompetitive effects, and how do they balance against the benefits?
  - Is the conduct reasonably necessary to achieve the benefits?
  - Does the conduct go beyond what is reasonably necessary to achieve those benefits?
  - Are there alternate ways to realize the benefits?
- Most mergers (over 95%) raise no competitive issues, so coordination is unlikely to raise restraint of trade issues
- Caution: Conduct that is "*per se*" illegal (*e.g.*, price fixing) will be treated accordingly

Violation of Pre-Merger Law

- Legal standard
  - U.S.: was "beneficial ownership" obtained before pre-merger notification procedures ended
    - "Beneficial ownership" not defined by law
    - Totality of circumstances will be considered
    - Exercise of significant control equals beneficial ownership
  - Brazil: were "conditions of competition" preserved through clearance
- Competitive effects are not relevant
  - Violation of pre-merger law can be found even when the underlying transaction does not affect competition

A Careful Balance

- Merging firms are separate entities and must remain so until they merge
- Yet there is benefit in allowing due diligence and transition *planning*
- Agencies take these benefits into account when analyzing pre-merger conduct
  - Risk of under-enforcement
  - Risk of over-deterrence
  - Minimizing unneeded transaction costs
  - Promoting transparent enforcement

U.S. Enforcement Experience

- Seven cases between 1996 and 2006,* but none since then
- Agencies have explained their approach to gun-jumping in speeches to bar and business groups
- Bar and business awareness of the line

* *U.S. v. Qualcomm/Flarion* (2006)
U.S. v. Gemstar/TV Guide (2003)
U.S. v. Computer Assocs. Int'l (2002)
U.S. v. Input/Output, Inc. (1999)
In re Commonwealth Land Title Ins. Co. (1998)
In re Insilco Corp. (1998)
U.S. v. Titan Wheel Int'l (1996)

U.S. v. Titan Wheel Int'l (1996)

- Titan Wheel buys tire plant from Pirelli
- Titan Wheel takes control of the plant and Pirelli's competitively sensitive customer and supplier lists
- Filing made three days *later*
- Result:
  - Maximum fine for pre-merger violation
  - No FTC challenge on substantive grounds
  - Parties abandoned the transaction

In re Insilco Corp. (1998)

- Insilco agrees to buy Helmut Lingemann's aluminum tubing plant, which would lead to monopoly power in two markets
- Before clearance, Helmut Lingemann gave Insilco:
  - customer-specific pricing information;
  - pricing plans;
  - competitive strategies; and
  - price formulas
- FTC challenged the merger substantively and the data exchange

U.S. v. Computer Associates Int'l (2002)

- CAI agreement to purchase direct rival Platinum included pre-closing restrictions on Platinum:
  - CAI control over Platinum's operations, pricing, information management
  - Senior CAI employee assigned to Platinum's plant to review and approve contracts
  - Discounting and non-standard sales terms by Platinum – its normal strategy – required CAI's approval
  - CAI received competitively sensitive price information
  - Platinum prevented from attending trade show in competition with CAI
- DOJ required civil penalties, special conditions concerning future acquisitions, as well as certain divestitures

Three Scenarios with Potential Issues

- Spillover effects from ordinary due diligence and transition planning
- Planning for post-closing activities that require preliminary implementation pre-closing
- Joint marketing

Spillover Effects

- Transition planning may include discussions of pricing, marketing, sales force assignments, strategy, branding, narrowing product lines, investments, *etc*.
- This may lead to exchange of sensitive information and conformity of behavior to post-merger plans
- Possible solutions
  - Exchange of non-sensitive aggregated or historical data instead of current sensitive data
  - Creating a "clean team" to handle planning, separate from line operations
  - Use of consulting firms for planning
  - Just wait until the deal closes

Planning for Post-Closing Activities

- Typically arises when a party was considering a major investment (*e.g.*, a new plant) that would be unnecessary because of the merger
  - Prohibiting abandonment is inefficient
  - Capacity reduction could affect competition
  - If merger fails, abandoning party may be worse off
- Considerations
  - Multiple factors taken into account
  - Problems more likely when the decision resulted from pre-merger consultation instead of unilaterally
  - Purchase agreement may prohibit material changes in business

Joint Marketing

- Coordination in marketing, *e.g.*, price coordination, product allocation, is almost always illegal
- Joint advertisements that simply announce the merger (press conferences, announcements) -- less problematic
- Joint courtesy calls to customers -- potentially dangerous -- beware of spillovers

Conclusion

- Assessing restraint of trade issues
  - If an agreement is anticompetitive in the absence of a merger, the potential merger does not make it legal
  - If the agreement reduces the incentives of one firm to compete, it is likely anticompetitive
- Pre-merger notification issues
  - Pre-merger notification reflects a Congressional decision that some delay – and resulting inefficiency – is necessary to allow for merger review
  - Planning is OK if it doesn't cross the line
  - Most likely to be an issue in the less than 5% of cases that raise competitive concerns, where review period is longer