MAYER·BROWN

Gun Jumping

Pre-Closing Coordination

Richard M. Steuer
Partner

212-506-2530
rsteuer@mayerbrown.com

November 2012

Gun Jumping - What is it?

- Engaging in conduct that effectively transfers **beneficial ownership** or **operational control** of the acquired business before the regulatory waiting period expires. Examples include:
  - Transferring decision-making authority over the seller's prices and contracts
  - Physically occupying the premises of the seller
  - Assuming decision-making authority or influencing the seller's marketing activities
  - Integrating the seller's management and facilities into the buyer's

Gun Jumping - What is it?

- Exchanging **competitively sensitive** information that reduces competition before closing or if the transaction does not close.
  - Competition could be reduced if a rival can predict the disclosing party's competitive actions, or if the party disclosing the information would loose a competitive advantage if the transaction is not consummated.
  - Exchanging competitive sensitive information could support the conclusion that operational control or beneficial ownership has been transferred.

Gun Jumping - What is it?

- Examples of **competitively sensitive** information include
  - Current or future prices, fee schedules, pricing policies, pricing formulas, plans or other competitive terms of sale (*e.g.*, financing)
  - Current or future profit margins or profitability targets on specific products
  - Costs of specific products or processes, including input costs and production costs
  - Costs at production facilities, including capital, labor and maintenance costs

Gun Jumping - What is it?

- Examples of **competitively sensitive** information include
  - Strategies or policies relating to competition
  - Forward looking competitive information concerning future operations or strategies including: marketing plans, sales/promotional plans, strategic plans, capital investment plans, expansion plans, plant closures, budgets, new product plans, or any other materials concerning future operations or strategies
  - Status of negotiations with present or potential customers and suppliers
  - Plans or intentions to bid or not bid for the business of specific customers

Gun Jumping - What is it?

- Examples of **competitively sensitive** information include
  - Information about present customers, including costs, prices, profitability, marketing plans, product development plans, or other specific customer information
  - Proprietary technologies of a confidential nature
  - Information about specific research and development projects or initiatives
  - Any other business information that could be used to reduce competition

Gun Jumping - Why is it important?

- Improper pre-closing coordination can lead to a government investigation and an antitrust lawsuit:
  - An investigation is costly and could delay the closing even if the deal is cleared
  - Potential for large fines, and in some countries, *criminal* sanctions (individual and corporate) for pre-closing coordination resulting in serious violations like price fixing or customer allocation
- *U.S. v. Gemstar/TV Guide* – $5.7 million civil penalty for gun jumping (slow-roll customer contracts, divided customer segments, exchanged competitively sensitive information)
- *U.S. v. Computer Assocs.* – $638K civil penalty + conduct relief
- *Omnicare v. UnitedHealth Group*, 629 F.3d 697 (7th Cir. 2011).
- "Gun Jumping" is a potential concern under US and other antitrust laws (incl. Canada, China, EC, Russia, Australia)

Integration Planning – Minimizing Risk During Wait

- What is it?
  - Continuation of the due diligence process.
  - Planning for the consolidation of the business or assets after the transaction is consummated.
  - May require the involvement of persons involved in competitive decision making.
  - It is planning, not implementation.
- What are the risks?
  - Implementation and/or exchange of competitively sensitive information that potentially reduces competition, transfers beneficial ownership, or operational control.

Integration Planning – Minimizing Risk

- Establish integration planning protocols and procedures
  - Integration Planning Confidentiality Agreement
  - Confidentiality Protocol
  - Employee Compliance Agreements
  - Integration Planning Do's and Don'ts
  - Meetings Protocol
  - Data/Document Exchange Protocol
  - Clean Team Confidentiality Agreement
  - Clean Team Protocol
  - Clean Team Compliance Agreements

Legal Framework for Integration Planning

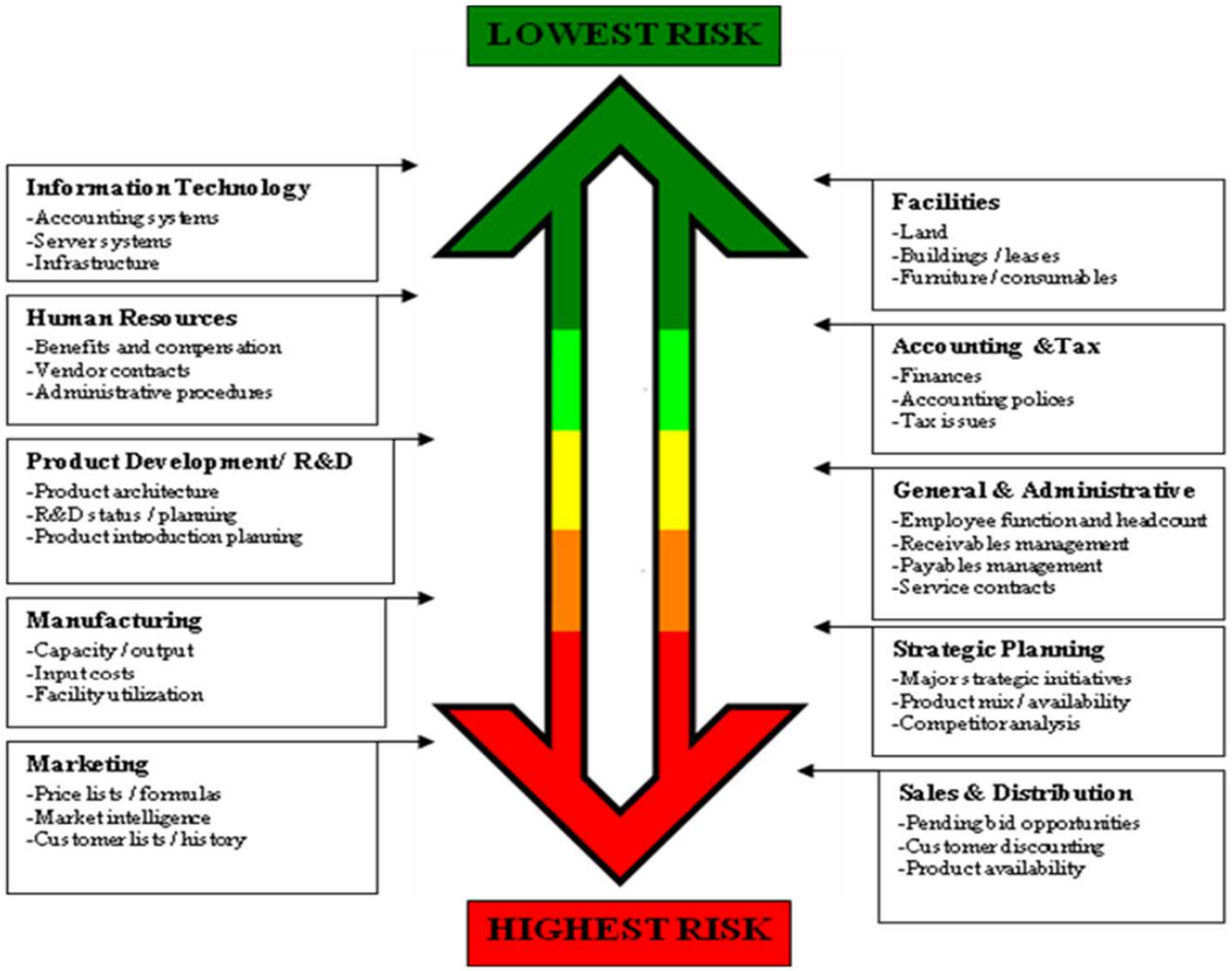
- Framework is necessary to protect the confidential information of both parties

- Framework also demonstrates sensitivity to potential gun-jumping issues if a government investigation or legal challenge arises

Legal Framework for Integration Planning

- All requests for documents/data are sent to outside legal counsel for review. Counsel determines if the document/data falls into one of the three categories:
  - Green – documents/data can be shared directly between the integration teams
  - Yellow – documents/data subject to legal review prior to being exchanged between the integration teams
  - Red – documents/data may not be shared between the integration teams, but could be shared with a Clean Team
- All requests for meetings are also sent to outside legal counsel for review
  - Agendas to be approved and attorney attendance may be required depending on subject matter and participants
- *Clean Teams* established in cooperation with a consultant to review competitively sensitive (i.e., "red") information

Legal Framework for Integration Planning



Integration Planning – "Do's and Don'ts"

Do	Don't
Do conduct business as usual	***Don't*** meet with the other party's personnel regarding the proposed deal outside of the integration planning process.
Do continue to act as two separate companies.	***Don't*** take any action that might suggest to customers that they are dealing with a unified company (e.g., don't make joint sales calls to customers, operate out of each other's offices, or disseminate joint marketing material).
Do make unilateral decisions based upon the best interests of the company.	***Don't*** issue orders to, seek to exercise control over or attempt to influence the marketing or other conduct of the other party.
Do engage in necessary integration planning.	***Don't*** let information flow between the companies that would not have been exchanged as competitors, including current or future prices, costs, marketing plans or service decisions.
Do follow the integration process and obtain approval to meet with the other party as required.	***Don't*** use information obtained from the other party in the integration planning process for any purpose other than planning.
Do adhere to data request processes dictated by the integration planning team.	
Do refuse to receive information from the other party that is not needed for transition planning, or which you suspect or know is competitively sensitive prior to the formal closing.	

Integration Planning – Information Sharing

- The following information should not be shared without advance approval from the legal department:
  - Price information : selling or purchasing prices relating not only to actual prices charged but also the elements of pricing and pricing policy, price changes or current or future trading conditions
  - Capacity, costs, or production output per product line
  - Plans relating to current or future business investment, product, marketing and advertising strategies
  - Purchasing or bidding plans or other commercial strategies
  - Unpublished sales volumes or values and profitability figures for the past six months or future estimates
  - Market shares per product line
  - Individual dealings with customers or suppliers including the status or content of yearly negotiations

Integration Planning – Outside Contacts

- As a general matter, contact with people outside one's own company about the transaction is discouraged.
- Until closing, take no action that might suggest to customers, suppliers or distributors that they are dealing with a unified company. For example, do not make joint sales calls to customers or disseminate joint marketing material.
- If it is necessary to have a communication with an actual or potential distributor, customer or supplier about the transaction, it typically is appropriate to make the following points:
  - We are pleased to be [merging with] [acquiring] [being acquired by] the other party.
    - The acquisition provides us the opportunity to expand and serve customers more effectively.
    - We are committed to building the business and expect this to enhance our presence in a competitive business.
  - Until the transaction closes, however, the two of us will continue to compete.
  - It is premature to discuss business arrangements with customers, suppliers or distributors post-closing, but we will be in touch when our plans are more certain.
  - The transaction is expected to close on or about _____.

Step One: Premerger Coordination – What is it?

- Everything before closing, including
  - due diligence that occurs prior to the execution of the transaction agreement
  - drafting of the transaction agreement
  - integration planning that occurs pre-close
- Due diligence and integration planning necessarily involve the exchange of information

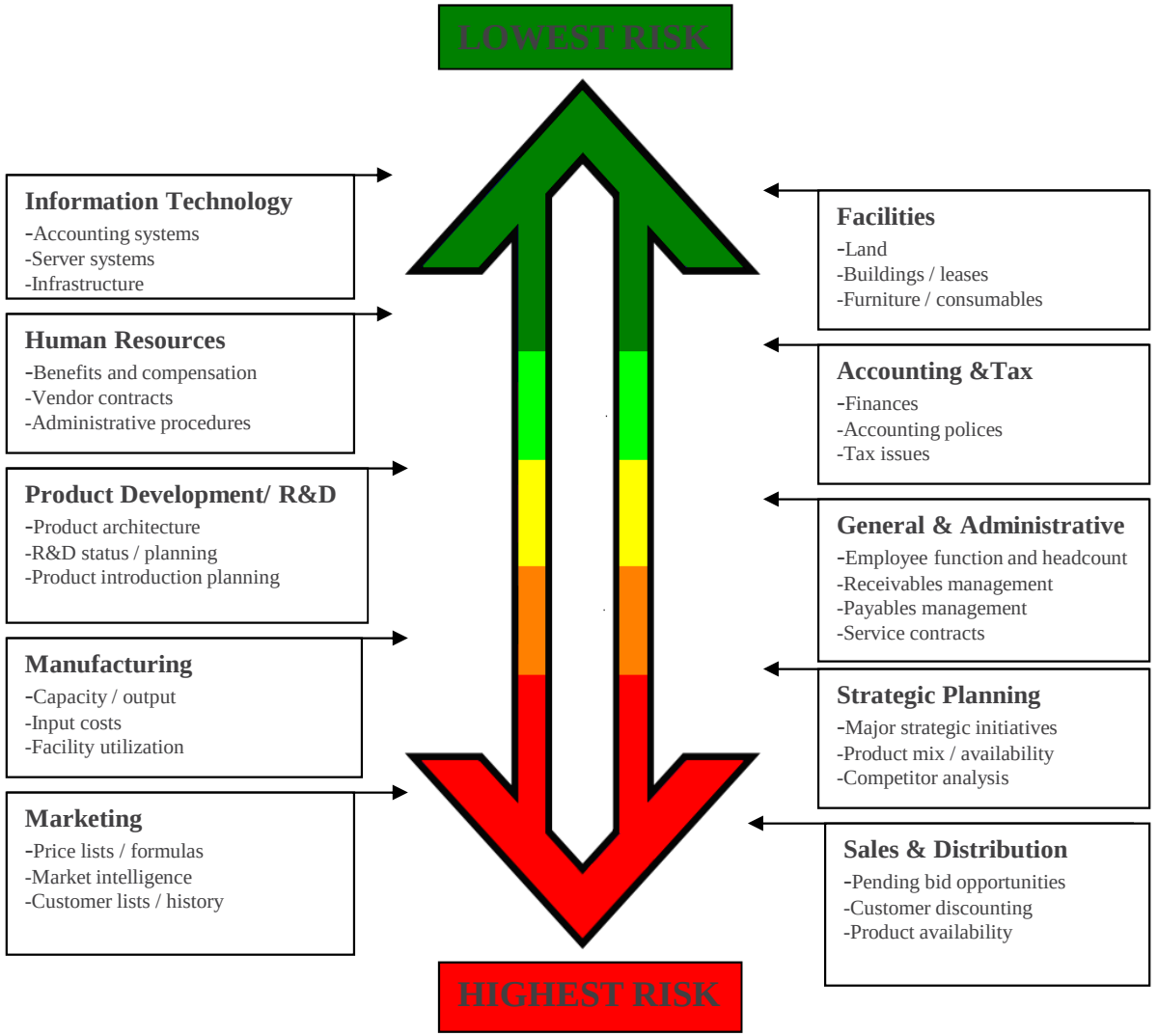
Due Diligence – Minimizing Risk at the Outset

- What are the first steps to take to prevent running afoul of the antitrust laws?
  - Understand the legal standards for the exchange of information
  - Enter into a NDA
  - Explore whether the transaction will have to be reported
- Why is this important?
  - Exchanging competitively sensitive information is permitted if it is reasonably related to an evaluation of the merits of a transaction (due diligence) and integration planning, and if the exchange is accompanied by protections preventing the recipient from using the information for commercial purposes

Due Diligence – Minimizing Risk

- What information is safe to exchange between competitors?
  - Publically available information
  - General information
- What information raises concern if exchanged between competitors?
  - See above slides

Due Diligence – Same Risk Hierarchy



Due Diligence – Minimizing Risk

- What safeguards can be used to prevent the information from being used for commercial purposes?
  - A NDA limiting the use of the information (*e.g.*, evaluating the proposed transaction) and prohibiting the use of the information for any commercial purposes (*e.g.*, revenue data shared with accounting, not marketing)
  - Physically segregate and limited access to the information exchanged
  - Use third-parties consultants or former employees to collect, evaluate, and aggregate sensitive data (*e.g.*, a clean team)
  - Consider removing employees from decision-making authority if given access to sensitive information

Due Diligence – Minimizing Risk

- What provisions should a NDA contain?
  - Key provisions might include
    - Identify the legitimate purposes for using the competitively sensitive information
    - Limit who may receive the information
    - Describe what may be done with the information
  - More recent consent decrees have prohibited the disclosure of competitively sensitive information to employees directly involved in or responsible for the marketing, pricing, or sales of any competing product or service.
  - The key goal is to prevent the commercial use of competitively sensitive information.

Transaction Agreements – Minimizing Risk

- Ordinary course of business provisions
  - Provisions that require the seller to operate its business in the ordinary course consistent with past practices along with a list of schedule of contracts, expenditures, or other conduct deemed to be the ordinary course.
    - Restricting the seller from operating inconsistently with existing business plans or budgets
  - Overly restrictive provisions that effectively limit operations in the ordinary course, can raise antitrust concern.
    - Restricting deviations from standard contracts when the seller has a history of doing so.
    - Setting a capital expenditure that is too low such that it impedes ordinary course operations.

Transaction Agreements – Minimizing Risk

- Ordinary course of business provisions
  - Want to set the minimum threshold above that made in the ordinary course and at a level that would constitute a material adverse change in the seller's business.
  - Want to avoid creating a mechanism for periodic communications about the seller's ordinary course of business. Routine communication and a change in conduct creates the wrong impression.
  - These types of provisions specify, for example, (1) classes of expenditures, (2) investments, (3) contracts, (4) divestitures, and (5) the level of indebtedness.

Transaction Agreements – Minimizing Risk

- Ordinary course of business provisions
  - A buyer has the right to require the seller to obtain written permission before:
    - Declaring or paying dividends or distributions of the seller's stock
    - Issuing, selling, pledging or encumbering the seller's securities
    - Amending the seller's organizational documents
    - Acquiring or agreeing to acquire other businesses
    - Mortgaging or encumbering the seller's IP or other material assets outside of the ordinary course
    - Making or agreeing to make large new capital expenditures
    - Making material tax elections or compromising material tax liabilities

Transaction Agreements – Minimizing Risk

- Ordinary course of business provisions
  - A buyer has the right to require the seller to obtain written permission before:
    - Paying, discharging, or satisfying any claims or liabilities outside the ordinary course
    - Commencing lawsuits other than routine collection matters
    - Offering enhanced rights or refunds to customers contingent on a change of control of the seller's business
  - A buyer can require prior approval where conduct outside the ordinary course of business will diminish the benefits of the transaction.

Transaction Agreements – Minimizing Risk

- Material adverse change (MAC) provisions
  - Provisions that require the seller to represent and warrant at closing that between execution and closing, the business has not been altered in a materially adverse way.
  - Overly restrictive provisions that effectively limit operations in the ordinary course, can raise antitrust concern.

Transaction Agreements – Minimizing Risk

- Key questions to ask:
  - Is the prohibited conduct outside the ordinary cause of business?
  - Will the prohibited conduct cause a material adverse change to the business?
  - Will the restriction on the prohibited conduct reduce competition before closing or if the merger does not close?
  - Will the restriction on the prohibited conduct transfer operational control or beneficial ownership?

Concluding Remarks

- Thank you!