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October 13, 2001

Antitrust Update:

The Department of Justice Brings Tough "Gun-Jumping" Case

The Department of Justice has just brought a case that should cause merging parties to take even greater precautions to ensure they do not improperly coordinate before closing. The DoJ complaint alleges violations both of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act) and of Section 1 of the Sherman Act.. We believe this case is of interest for three reasons. First, unlike previous gun-jumping cases, some of the conduct alleged here is arguably not dramatically different in kind from conduct that merging entities regularly undertake. Second, the case was brought long after the HSR waiting period had expired and the transaction had closed. Third, the case provides an object lesson in the pitfalls of antagonizing the antitrust agencies.

Under the HSR Act, parties to mergers over certain size thresholds must report the transaction to the U.S. antitrust agencies and then observe statutory waiting periods before they may close the deal. During the waiting periods, the parties must continue to operate as independent entities and may not act to effectuate the transaction. For example, the acquiring firm may not place its personnel in positions at the acquired firm, the parties cannot in any way hold out to the public that the transaction has closed, any contractual dealings between the parties must be at arm's-length, and, if the parties are competitors, they cannot cease to compete and should not share competitively sensitive information, except in limited, controlled circumstances. Failure to respect the waiting periods by engaging in this type of prohibited conduct, known as "gun-jumping," can subject the parties to sanctions under the HSR Act and, if they are competitors, under Section 1 of the Sherman Act (15 U.S.C. § 1) as well.

The exact limits on cooperation among merging parties during HSR waiting periods have long been a subject of uncertainty and some controversy. There is general agreement that traditional due diligence does not constitute gun-jumping, and that merging parties may engage in limited, controlled planning for future life together (as opposed to running there current business jointly) without running afoul of the HSR Act. When the transaction is among competitors, however, the parties must make efforts to limit the sharing and distribution of competitively-sensitive information. Additionally, it has traditionally been accepted that the acquiring party may insist that the acquired party refrain from activities outside the ordinary

scope of business -- *e.g.*, material transactions or changes in business operations -- to ensure that the acquiring party obtains the value for which it has agreed to pay. Beyond these basic principles, however, the few enforcement actions undertaken by the Department of Justice and the Federal Trade Commission have provided only limited guidance. That is largely because all previous enforcement actions have involved clear and egregious violations of the HSR Act, such as replacing the acquired firm's management with acquiring firm executives or dealing with customers as if the transaction has already closed. Furthermore, the few speeches on the subject by FTC and Department of Justice officials have provided only sketchy -- and sometimes contradictory -- guidance.

In this context comes DoJ's lawsuit against Computer Associates International Inc. ("CA"), filed on September 28, which alleges that CA engaged in gun-jumping during the HSR waiting periods for its 1999 acquisition of Platinum Technology International Inc. ("Platinum"), a company that competed with CA in the mainframe software industry. CA's actions during the HSR waiting period, according to DoJ, "prematurely reduced competition" between the merging companies.

DoJ is now, more than two years after closing, seeking $1.27 million in civil penalties, or $638,000 each from CA and Platinum, and to enjoin CA from similar conduct in the future. The complaint alleges that the violation began when the companies signed a merger agreement and continued for 58 days, ending when they entered into a consent decree with the government on substantive antitrust issues surrounding the deal and completed the merger. The proposed fine thus represents the maximum penalty available under the HSR Act, which provides for civil penalties of up to $11,000 per day.

The Department alleges that CA effectively completed the transaction while the government investigation was still pending, by taking various steps that restricted Platinum's ability to continue as an effective competitor until the closing. Because CA and Platinum were competitors, the Department alleges not only violations of both the HSR Act (which applies to all reportable transactions), but also violations of Section 1 of the Sherman Act (because the activities allegedly constituted illegal restraints on competition). The alleged violations include:

- Imposing "extraordinary" conduct of business restrictions on Platinum, including restrictions on ordinary-course activities such as setting the prices and terms Platinum could offer customers;

- Requiring Platinum to seek CA approval before granting customer discounts of more than 20% off list price or otherwise amending standard contract terms;

- Installing a CA division vice president at Platinum's headquarters to review and approve customer contracts; and

- Collecting competitively sensitive data and information on the day-to-day management of Platinum.

Some of the allegations (particularly the installation of a CA employee at Platinum's headquarters) may reflect the sort of plain HSR Act violations that have given rise to previous enforcement actions. But the most interesting (and potentially troubling) aspects of the Department's complaint are the allegations alleging conduct that may not be dramatically different from common practices in mergers and acquisitions. For instance, as noted above, acquirers routinely receive undertakings that the acquired firm will not materially deviate from its ordinary course of business between the signing and closing of the deal. Yet, the complaint -- especially the allegations concerning discount approvals -- suggests that (at least in DOJ's view) the line between an acquiring firm's legitimate interest in insuring the value of its purchase and impermissible meddling with the acquired firm's business pre-closing may be thin. Similarly (although it is difficult to tell on the face of the complaint) the allegations about sharing sensitive data and information on day-to-day management may relate to conduct that was not a patent violation of the HSR Act or Section 1.

At the heart of the CA complaint and many practical problems relating to pre-closing coordination is tension between legal restrictions on gun-jumping and powerful and legitimate business incentives to move forward quickly in planning for life after a merger. As the CA complaint well illustrates, this is a tension that cannot be resolved in the abstract, often involves complicated and fact-specific balancing, and requires close consultation with counsel to ensure that the parties are able to achieve the planning goals they set without risking sanctions for violating the HSR Act or Section 1. In this connection, a good rule of thumb is that *the parties should take no actions and share no information that they would not have done if the pending merger were not to take place, without first consulting counsel.* It is also important to note that this case was brought long after the transaction closed and after the substantive antitrust issues had been resolved, so parties should not assume that the end of the substantive antitrust investigation means that any potential gun-jumping liability has ended.

Another lesson to be taken from this enforcement action is the paramount importance to businesses and to their legal counsel of preserving good relations and credibility when dealing with antitrust enforcement authorities. The Department has had long-standing concerns about CA's veracity. In connection with a 1995 consent decree for its acquisition of Legent Corp., CA entered into a consent agreement with the Department that required CA to enter into certain licensing agreements, but CA subsequently dragged its feet on granting the licenses. CA's past behavior may have caused the Department to judge its behavior in this transaction more harshly.

CA has indicated that it will litigate this case. This, in and of itself is unusual: all previous gun-jumping cases have ultimately settled.

Finally, it should be noted that in an unrelated case announced just this week, the Hearst Trust agreed to pay $4 million to settle an FTC claim, brought earlier this year, that Hearst failed to produce required documents as part of its HSR filing for its acquisition of Medi-Span. Although such conduct does not constitute gun-jumping, it does reinforce that the U.S. antitrust enforcement agencies take HSR Act compliance very seriously and will pursue aggressively substantial punishments for violations.

Please contact any member of our U.S. antitrust practice at 202-663-6000 if you have any questions about this or any other issue.

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