WILMER, CUTLER & PICKERING

WASHINGTON • NEW YORK • BALTIMORE • NORTHERN VIRGINIA • LONDON • BRUSSELS • BERLIN

March 4, 2003

ANTITRUST UPDATE

New Department of Justice Actions on Gun-Jumping and Market Allocation Provide Guidance, Warnings

U.S. v. Gemstar–TV Guide and *U.S. v. Village Voice Media*

The Antitrust Division of the Department of Justice has recently issued two complaints that address critical issues for companies engaged in merger, acquisition, or joint venture discussions. First, in *U.S. v. Gemstar–TV Guide*, the Antitrust Division accused Gemstar and TV Guide of engaging in so-called "gun-jumping"—that is, ceasing competition and beginning to implement post-merger plans before closing their transaction. The Division alleged that the parties' conduct violated both the Hart–Scott–Rodino Act, 15 U.S.C. § 18a, and Section 1 of the Sherman Act, 15 U.S.C. §1. As discussed below, the complaint and settlement in *Gemstar*, which included a record $5.67 million fine, provide guidance as to acceptable conduct in the period between when merger discussion begins and when the transaction is closed.

The settlement order is particularly notable because it states that the sharing of current and future pricing information, even in the context of otherwise legitimate due diligence, may violate the antitrust laws absent strict limits on dissemination and strong confidentiality provisions. Because both the Department of Justice and the Federal Trade Commission have expressed renewed interest in pursuing gun-jumping violations, parties to transactions and their counsel should be aware of this new action.

In *U.S. v. Village Voice*, the Division challenged an agreement between two weekly newspaper chains to cease competing with one another in two different cities. While the parties have vigorously challenged the legal basis for the government's claims in various press statements, the conduct, at least as alleged, appears to constitute a clear violation. It is unclear whether the relief ordered can succeed in remedying the competitive harm that has occurred.

Gemstar

Until mid-1999, Gemstar and TV Guide competed vigorously in the development and sale of interactive program guides (IPGs), interactive on-screen tools that cable or satellite TV subscribers use to navigate their program choices through their remote controls. In advanced versions subscribers order pay-per-view movies and even products such as pizza through their IPG. IPGs are sold to cable and satellite system providers, such as Comcast or Echostar, which in turn offer them to subscribers. Prior to 1999, Gemstar and TV Guide had been engaged in protracted patent litigation. Beginning in June 1999, the parties renewed settlement discussions, which contemplated a possible joint venture to market the parties' respective IPGs and included an agreement on prices and terms for the joint IPG offerings. However, they were ultimately unable to agree on the JV, so instead they agreed to merge. That merger was announced in October 1999. The Department of Justice undertook an intensive investigation of the merger, which lasted through the spring of 2000. Ultimately, however, the government closed its investigation and the deal closed in July 2000.

The Hart–Scott–Rodino Act prohibits parties from consummating transactions reportable under the Act until the applicable waiting periods have expired. The government has stated that this means parties to a transaction may not take actions that would effectively transfer control or beneficial ownership of one of the entities before the end of the waiting periods. The Act also makes clear that parties to a reportable transaction are considered separate entities until the transaction closes, and that parties that are competitors prior to entering into the transaction are expected to continue to compete until closing.

In addition to the strictures imposed by the Hart–Scott–Rodino Act, Section 1 of the Sherman Act generally prohibits, *inter alia*, competitors from agreeing to limit competition among themselves. Thus, parties to a transaction who are competitors may violate Section 1 if they agree to limit their competitive activity or take steps (such as sharing competitively sensitive information) that have the effect of limiting competition between them prior to closing. It is important to note that while liability under the Hart–Scott–Rodino Act applies only to reportable transactions, Section 1 liability can reach any transaction, reportable or not.

The Antitrust Division alleges that, beginning in June 1999, Gemstar and TV Guide took actions that ended competition between them in the marketing and sale of IPGs and effectively transferred control of TV Guide's IPG business to Gemstar. Specifically, the Division alleged that the parties:

- Agreed at the highest executive levels to cease competing for two IPG contracts that were then up for bid;

- Ceased competing for these contracts and explicitly allocated the two customers between them;

- Agreed that TV Guide alone would negotiate with any other providers seeking new IPG contracts prior to closing, but solely on the basis of the prices and terms that Gemstar and TV Guide had agreed to during the joint venture negotiations;

- Shared and discussed information on prices and other terms regarding bids to specific customers and kept each other apprised of all aspects of negotiations with those customers;

- Exchanged contract and rate card information; and

- Acted on each other's behalf on IPG matters long before the merger closed.

The parties settled the government's complaint against this conduct, paying a $5.67 million penalty, which was based on the statutory fine under the Hart–Scott–Rodino Act of $11,000 for each day of violation (there is no provision for financial penalties for a civil violation of Section 1). The settlement also restricts Gemstar's conduct relating to future transactions. These restrictions provide a useful guide to pre-closing "no-nos." The parties may not (and thus all merging parties should not):

1. Enter into any agreement with a potential or actual merger partner regarding the price of competing products prior to closing;

2. Enter into any agreement to delay or suspend competitive sales efforts prior to closing;

3. Enter into any agreement to allocate markets or customers prior to closing; or

4. Disclose or seek disclosure about current or future prices or contract offers, *except* in legitimate due diligence efforts where the information is reasonably related to the discovering party's understanding of future earnings and economic prospects and the disclosure is made solely subject to a non-disclosure agreement that explicitly prohibits disclosure of that information to any employee of the recipient responsible for pricing, sales or marketing of competing products.

The settlement order does state that parties to a transaction can agree that one or both of them will continue to operate in the ordinary course pending closing and will refrain from taking action that would

have a material adverse effect on the value of the business.

Based on the allegations in the complaint, the conduct here significantly exceeds what is generally understood to be permissible coordination pre-closing. Generally parties to a transaction can engage in post-merger planning before closing, but they cannot implement any of those plans; nor, if they are competitors, may they actually stop competing or coordinate on sales opportunities (unless they might have done so prior to entering into the merger agreement and those joint arrangements are fixed on an arm's-length basis and on commercially reasonable terms). Parties should also not share any competitively sensitive information except when absolutely necessary for due diligence or post-merger planning purposes and then only under restrictive confidentiality agreements.

Generally we advise that parties to a merger should not enter into any agreements or share any information that they would regret if the transaction ultimately collapsed. If that rule is followed, parties will rarely run afoul of the gun-jumping rules. However, the government's views about disclosure of pricing and contract information, even in due diligence, should be noted and followed with care, particularly when the parties to the transaction are competitors.

Village Voice

Village Voice Media and New Times Media are two chains that produce "alternative" weekly newspapers in a variety of cities. Until October 2002, they each offered publications in Cleveland and Los Angeles that competed against one another for advertising and readership. According to the government's complaint, in October, Village Voice and New Times reached an agreement whereby New Times agreed to close its Los Angeles paper in exchange for $9 million and Village Voice's agreement to close its Cleveland paper. Some assets of the closed papers were exchanged, but these assets constituted only a small portion of the total assets of the closed papers. In addition, the parties entered into reciprocal non-compete agreements under which each promised not to reopen the closed papers and to take steps to ensure that no third party could use assets of the closed papers, such as the trademarks, equipment, and retained personnel, to create a new competitive publication in either city.

The Antitrust Division, along with the states of California and Ohio, charged in a civil action that the agreement between Village Voice and New Times was a *per se* illegal market division agreement. The government recognized that in certain circumstances territorial non-compete agreements can be legal if ancillary to a legitimate business transaction. But here there was, the government alleges, no such legitimate agreement; rather, the government alleges that the sole purpose of the underlying transaction and the continuing territorial restrictions was to eliminate competition.

To remedy this violation, the settlement order requires each of the parties to sell within 30 days the assets of its respective closed newspaper to a government-approved buyer that will be in a position to use those assets to open a new newspaper in the affected city. If the parties cannot effectuate either of the sales within 30 days, the unsold assets will be turned over to a trustee for sale. The parties are also prohibited from enforcing their reciprocal non-compete provisions and any non-competes imposed on their employees and must release advertisers who may have signed long-term contracts from those arrangements if they wish to advertise in the newly reformed competitive papers.

It is uncertain what real impact the remedial decree will have in this case. It is simply not clear that viable buyers can be found or that the assets to be sold can, at this stage, meaningfully assist a new owner to restart competitive papers in the affected cities. Indeed, an executive of one of the defendants has openly ridiculed the decree as being painless (statements which will certainly not endear these companies to the Department of Justice). It is also not clear whether the parties will face any significant penalties from private suits; the papers were shut down for only a limited period before the government acted, and so the damages period likely would be found to have been short.

Given that this case was pled principally as a *per se* illegal market allocation agreement (the complaint also alleges that the same conduct constituted a rule of reason violation), the government could have brought a criminal case against the company and possibly even against individual executives. That would have allowed the government to seek significant fines and possibly jail time for any convicted individuals. However, the criminal case would have taken far longer to resolve, meaning that the assets of the closed papers would have wasted even more and been even less subject to revival. Similarly, the states that joined the complaint might have been able to seek civil penalties under state law; however, such an effort could also have led to the sort of delay in resolution that would have been faced by the criminal action. There appears, therefore, to be some tension between the desire for quick restoration of competition and the desire for effective deterrents to future conduct. In any event, it will be interesting to watch whether the relief obtained by the government is, in fact, successful in restoring competition in either or both of the affected cities, and whether the parties face private legal challenges to their conduct.

* * * * *

Please contact us at (202) 663-6000 if you have any questions.

Robert Bell	**Jim Lowe**
Lee Greenfield	**Doug Melamed**
Veronica Kayne	**Thomas Mueller**
William Kolasky	**Ali Stoeppelwerth**