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FTC UPDATES GUIDANCE ON PREMERGER DUE DILIGENCE AND NEGOTIATIONS

(SHARING BUT NOT OVERSHARING)

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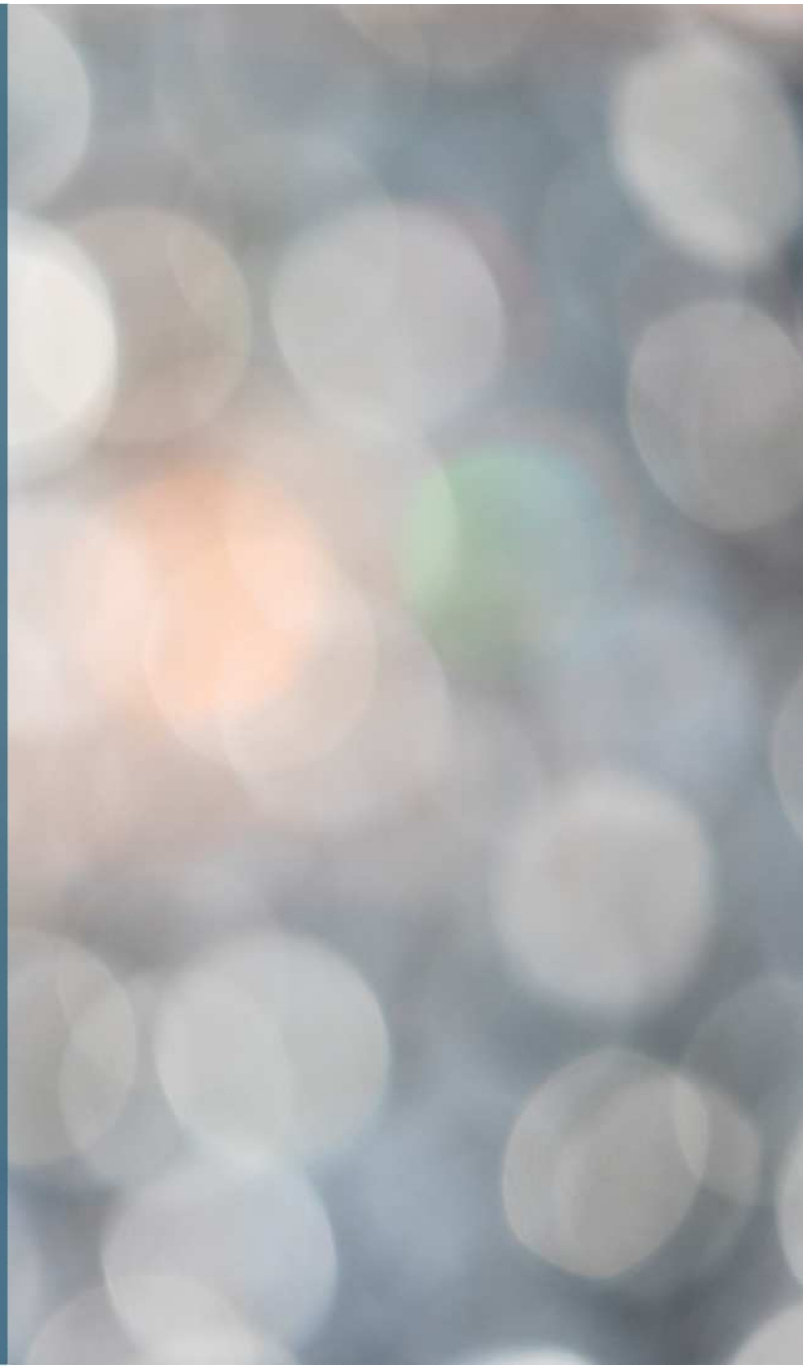

Agenda

Introductory comments

- Merger enforcement under Trump administration
- Overview of HSR Act and Sherman Act

Focus today: avoiding "information sharing" violations

- FTC's March 20 guidance on Competitively Sensitive Information (CSI) and violations of the merger review waiting period (gun jumping)
- FTC/DOJ guidance on information sharing more broadly
- DOJ's "employee no-poach" guidance and recent cases
- Practical points for staying out of trouble

Merger Enforcement Trends

Reviews are taking longer and **some issues have become harder**

- Average length of second request investigation was ~12 months in 2017 (up from 7 months just five years ago)
- Resolving mergers with consent decrees is becoming more challenging
  - Failed, high-profile divestitures have embarrassed both agencies; has caused increased scrutiny of divestiture buyers, viability of divested businesses, etc.
  - Agencies increasingly insist on upfront buyers
  - DOJ & FTC also concerned about failed or failing relief; there is particular concern about the regulatory burden of behavioral relief
  - Greater insistence that buyer conduct adequate due diligence and have sufficient transition services
- Agencies' approach to vertical deals' remedies is in flux
  - FTC speeches suggest that divestitures will be preferred; required one recent divesture; but last week, accepted a complex remedy with no divestiture
  - DOJ has made similar speeches; sued AT&T/Time Warner rather than accept a "behavioral" consent decree

HSR Act and Sherman Act Overview

HSR Act: governs mergers, acquisitions, and business combinations

Until expiration of a waiting period, prohibits companies "gun jumping" (even if the parties do not compete) by:

- Transferring "control" of operations from seller to buyer
- The buyer altering the seller's ordinary-course business operations
- Otherwise "scrambling the eggs" – point is to maintain the status quo

Sherman Act: general antitrust law

- Prohibits monopolization and unreasonable restraints of trade
- Applies to both the merger and non-merger context
- Greater scrutiny for agreements between competitors but also applies to vertical agreements
- In the preclosing context, restricts sharing CSI without safeguards and ceasing to compete

Who is your competitor?

- Any entity with whom you compete for sales (downstream) or inputs (upstream, e.g., materials, feedstocks and employees)

HSR Act and Sherman Act Overview

Penalties under the laws

- HSR Act - potential fines of $40k+ per person per day
- Sherman Act - treble damages, payable to private plaintiffs (including in class actions), plus criminal sentences and fines if cartel conduct is proved

Examples of consequences

- US: Flakeboard/Sierra Pine - $5 million in fines and disgorged profits
- EC: Altice/PT Portugal - €124.5 million fine
- Fines can occur despite the deal ultimately being cleared

Practical considerations

- Gun jumping concerns can extend the length of the merger-review process and may increase agency skepticism of the underlying deal
- Distraction and expense of discovery/investigations processes
- Reputational harm
- Debarment from some government contracts or other opportunities

FTC's March 20 "Gun Jumping" Guidance

Competitively sensitive information includes information that:

- you believe a knowledgeable person could use to forecast your competitive responses
- the disclosure of which would eliminate a competitive advantage, or
- you believe is significant to competition (use your judgment)
- not formulaic

Examples of competitively sensitive information

- Customer-specific names, prices, costs, margins, sales, & strategies
- Supplier-specific names costs and strategies
- Methods of targeting or bidding for customers
- Current purchases of significant feedstocks
- Recent product-specific prices and variable costs
- Capacity utilization
- Forward looking business strategy (large capital projects are unlikely to fall within this category)
- Employee-specific wages/salaries
- Product or technology roadmaps (unless announced publicly)

Each party should thoughtfully define its own CSI

FTC's March 20 "Gun Jumping" Guidance

On March 20, 2018, the FTC issued the first guidance in this area since 2005

- The guidance sets out three major themes …
  - Parties should create, maintain, and monitor a program that allows for diligence and planning but that prevents CSI from being used commercially
  - Companies and counsel should ensure that the protections are being followed
  - Counsel and the parties must not only monitor compliance and stop any breaches of the protocols, but also are advised to self-report violations to the government
- … and makes specific demands:
  - Parties must redact customer names and other information to ensure other parties cannot "reverse engineer" withheld information
  - Use electronic controls in data rooms
  - "Clean teams should not include any personnel responsible for competitive planning, pricing, or strategy" (this is a change from older guidance)

Information Sharing – Non-Merger Guidance

US agencies have a safe harbor for formal information "exchanges."

But it is narrow, and requires three factors:

- Neutral gatherer: compiler of the information must be a neutral third party, not an employee or agent of a competitor
- Old: price or other CSI must be "dated." Healthcare industry information should be at least three months old; no guidance specifically tailored for the energy industry.
- Aggregated: at least five participants must provide the data underlying each statistic shared; no single provider's data can contribute more than 25% of the "weight" of any statistic shared; and the shared statistics must be sufficiently aggregated that no participant can discern the data of any other participant

Conduct outside the safe harbor is not necessarily unlawful, but is risky

- US agencies view conduct outside the safe harbor as unlawful unless the parties can prove the "necessity" of a departure from the guidance
- *Detroit Medical Center* case: exchange of recent nurse-wage info, even via a hospital trade association, prevented a defense summary judgment

Particular risk for price announcements and "price leadership"

- The Supreme Court's *Twombly / Iqbal* legal standard prevents plaintiffs from bringing antitrust claims unless they can plead more than mere "parallel" pricing or capacity adjustments. This standard has reduced abusive lawsuits but not eliminated them.
- Some plaintiffs have survived motions to dismiss by showing price or capacity announcements that were accompanied by other factors that plaintiffs characterize as "signaling": an "offer" of a price/capacity "fix," which is "accepted" by parallel conduct.
- Ways to reduce risk:
  - Avoid conditional statements: "if a competitor does X, we will do Y"
  - Avoid detailed discussion of "the industry's" moves or competitors' price, capacity, or other competitively important terms and conditions
  - Be careful when making forward-looking statements about the companies' own price and capacity moves (even if not stated conditionally as to competitor moves)
  - Consider timing. Coincidence between competitors' statements and price/capacity changes has helped some cases survive dismissal, and justify massive discovery.

Particular risk for sharing wage information or making "no poach" agreements

- In the 2010 "high tech hiring" cases, DOJ sued and settled with several tech firms, and prohibited "no-poach" or "mutual no-hire" agreements
  - DOJ's suit and settlements were under civil law
  - DOJ then issued a threat: future conduct will be prosecuted criminally
- This year:
  - In February 2018, AAG Makan Delrahim predicted cases "soon," and chose the ABA's Cartel conference to make this statement
  - On April 3, 2018, DOJ announced a suit and settlement against Knorr-Bremse AG and Westinghouse Air Brake Technologies Corporation
- Such sharing and certain non-compete terms must be included in HSR Act filings; therefore, will be subject to close DOJ and FTC review
- So, be aware that information sharing regarding terms or conditions of employment can be as risky as sharing information on sales
  - Can lead to evidence of *per se* illegal agreements not to compete
  - Could even lead to criminal prosecutions, alleging employment "cartel" conduct

Practical advice – merger context

Counsel all relevant personnel before the deal

- All business people involved in the transaction (including Board Members)
- Ask your counterparty to invoke similar antitrust protections
- Advise consultants and financial advisors that all best practices, particularly document drafting, apply just as strongly to them
  - You may want antitrust counsel to review drafts of teasers and offering memoranda, since these need to be filed with the HSR form

Limit the number of people on the deal team

- Also, assign one or two people to serve as the points of contact (POCs) between the parties
- POCs should be the only people sending, receiving and logging requests (your electronic vendor can be involved)

Have antitrust counsel review diligence requests and responses

Practical advice – information exchange

Delay exchanges involving competitively sensitive information until parties have confidence that they will come to terms

Provide older or aggregated information first

- aggregate over time (customers, geography or product) to ensure that a knowledgeable business person receiving the information cannot discern the competitively sensitive information;
- provide more detailed information as diligence progresses

Consider the number of customers at your facility and breadth of distribution when considering how to disguise information

Establish a clean team if competitively sensitive information is necessary to resolve a diligence issue

- Clean team structure: Select a subset of the diligence team who are not involved in competitively sensitive activities (sales and procurement), for example:
  - Business development, financial and operational personnel
  - Knowledgeable persons from other geographies
- The clean team members will be permitted to share results, but not underlying clean team data, to the diligence team (antitrust counsel should review clean team reports)
- Clean team members will not be able to be involved in competitively sensitive activities if the transaction does not close
- Consider documenting the clean team procedure
- Do not deviate from the protocol

Practical advice – document creation

Draft all documents expecting the government to review them

- The HSR form requires the submission of all documents prepared by or for an officer or director evaluating the transaction with respect to competition, markets and market shares
- This includes documents prepared by company personnel, financial advisors, counter parties
- If not necessary, do not discuss “markets” or “competitors” …
- … But if it is necessary, ensure you discuss all (five or more) significant competitors
- Do not inaccurately embellish market shares
- Increasing prices, obtaining “pricing synergies,” “rationalizing capacity,” margin uplift, leverage over customers etc. should not be a rationale for the transaction
- Eliminating a key competitor should not be an efficiency
- Feel free to discuss savings and synergies, comparable transactions, valuation and other deal rationales

Monitor management presentations and planning sessions for antitrust issues

Segregate all deal documents in separate, easy to find files

- Create email and document folders and segregate hard copy documents

Examples of unhelpful documents

Bankers and consultants overstating market shares as part of their teasers and offering memoranda:

“We are the only two real competitors.”

“Eliminate [counterparty], a primary competitor”

“Pricing accretion due to combination”

“Taking out only competitor”

“Eliminate the time and cost of taking [the counterparty’s] accounts”

“Market will pay a premium on us having such a dominant market position”

SPEAKER BIOGRAPHY

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Education

- University of Pennsylvania Law School, J.D., 1998
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Recognition

- Selected to *Super Lawyers* (Thomson Reuters), 2018
- Recognized as a "Future Leader" for being one of the top antitrust lawyers under the age of 45,*Global Competition Review and Who's Who Legal,* 2017
- *Legal 500 U.S.,* Antitrust – Cartel, Antitrust - Civil Litigation/Class Actions, and Antitrust – Merger Control, 2016 and 2017
- Recognized, *U.S. News & World Report* and *Best Lawyers* 2017 Practice Group of the Year for Antitrust Law (2017)

Darren Tucker is a partner in the Antitrust Group in Washington, DC. Darren has two decades of experience handling the largest, most complex merger and non-merger antitrust investigations, with a focus on the technology, energy, and pharmaceutical sectors.

Darren has played key roles in many of the most prominent antitrust cases involving the U.S. agencies, including two trials against the U.S. government (*FTC v. Arch Coal* (D.D.C) and *FTC v. CCC* (D.D.C.)) and the settlement of a leading gun jumping case (*US v. Gemstar* (D.D.C.)). He has helped obtain clearance for approximately 100 mergers and acquisitions.

Darren also has extensive experience on competition matters outside the U.S., having counseled clients on merger and non-merger antitrust matters in Europe, Canada, Japan, China, South Korea, Taiwan, Russia, and Australia.

In 2017, *Global Competition Review* recognized Darren as one of the leading antitrust lawyers under the age of 45. Other credentialing groups recognizing Darren as a leading antitrust lawyer include The *Legal 500* and *Super Lawyers*. He has been part of the leadership of the American Bar Association's Section of Antitrust Law for over a decade, where he currently serves on the section's governing Council.

Darren regularly speaks and writes on antitrust issues relevant to technology, energy, and life science companies, as well as on competition agency practice and procedure. He recently served as the editorial chair of *Antitrust Law Developments*, the leading antitrust treatise for practitioners. He previously served as the editorial chair of the ABA's *Antitrust Source* and as a member of the *Law360 Competition* editorial advisory board. He has taught an advanced antitrust seminar as an adjunct professor at Antonin Scalia Law School at George Mason University.

From 2009-2013, Darren served as an attorney advisor to Commissioners Joshua D. Wright and J. Thomas Rosch at the FTC. In that role, he advised the commissioners on staff enforcement recommendations, litigation strategy, and policy matters, including the 2010 Merger Guidelines. This experience allows Darren to provide valuable insights to clients regarding competition enforcement and policy issues.

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Education

- George Washington University Law Center, J.D., 1990
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Select Recognition

- *Chambers USA,* Antitrust (District of Columbia), 2010–2018
- Selected to the Washington, DC *Super Lawyers* list, Super Lawyers (Thomson Reuters), 2012–2017
- *Legal 500 U.S.,* Antitrust: Merger Control, 2017 and 2018; M&A Antitrust, 2012–2014
- American Lawyer Media, *Washington DC & Baltimore's Top Rated Lawyers*, 2012–2013

William (Billy) Vigdor came to Vinson & Elkins from the Federal Trade Commission (FTC) in 2003. He assists clients in identifying and managing the antitrust and national security risk of global mergers and joint ventures.

Billy provides substantive and strategic antitrust risk assessments in a wide array of industries and transaction structures (mergers, acquisitions, and joint ventures) and represents clients before the FTC, Department of Justice, and states attorneys general. He assists private equity, hedge funds, portfolio and public companies in addressing global merger control issues and in assessing risks. Billy also represents clients before the Committee on Foreign Investment in the United States (CFIUS).

Billy represents clients in some of the most complex mergers and acquisitions, joint ventures, partial ownerships, and government investigations involving price-fixing and monopolistic practices, as well as multijurisdictional merger control. He works with a wide range of clients, including hedge funds, master limited partnerships, and private equity firms. His antitrust work covers most of the economy, including energy (from well to burner tip or gas tank), petrochemicals, health care, technology, aerospace, telecommunications equipment, auto parts, retailing, food manufacturing, and pharmaceuticals. Billy has experience seeking agencies' approval not to challenge mergers and not to issue second requests.

Since 1995, Billy has represented clients—buyers, sellers, and privately and government-owned—in multibillion dollar transactions before CFIUS, including companies involved in energy, technology, telecommunications, petrochemicals, satellites, real estate, and other industries. He has assisted clients in negotiating FOCI mitigation agreements with CFIUS agencies.

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- *Chambers USA*, Antitrust Litigation (District of Columbia), 2011–2018
- *The Best Lawyers in America*, Antitrust Law, Litigation – Antitrust 2016–2018
- *Legal 500 U.S.*, Antitrust - Cartel, Civil Litigation/Class Actions, and Merger Control 2017

Hill Wellford is a partner at Vinson & Elkins, LLP in the Washington, D.C. office. He advises clients on antitrust matters, especially where U.S. Department of Justice (DOJ), Federal Trade Commission, and foreign agency enforcement intersects with energy, telecom, media, technology, standard-setting, pharmaceuticals, or patents. His practice includes matters in the Americas, Asia, and Europe, and his experience includes mergers and acquisitions, criminal investigations, civil conduct challenges, and jury, bench, and administrative trials. He also counsels agency-appointed trustees overseeing merger divestitures.

Hill previously served as Chief of Staff at the DOJ's Antitrust Division in Washington, DC, where he oversaw cartel, merger, civil conduct, and international work by the Antitrust Division's 400-plus lawyers and economists. Before becoming chief of staff, he served at DOJ as counsel to the Assistant Attorney General, as an investigator and a trial lawyer, and as counsel in the Antitrust Division's Legal Policy Section. He worked extensively with other components of the broader DOJ—including the DOJ Intellectual Property Task Force—and with the Federal Trade Commission, Federal Communications Commission, Department of Transportation, Federal Energy Regulatory Commission, Office of the United States Trade Representative, and other U.S. and foreign agencies.

Hill is a longtime leader in the American Bar Association's Section of Antitrust, where he currently serves as co-chair of the Dominance Divergence Task Force, after just concluding a three-year term on the section's governing Council. He is recognized for antitrust by *Chambers USA* (2017), which describes him as a "very strong" partner who is "one to watch," and recently was profiled in *Competition Law360*.

Hill writes, teaches, and lectures widely on antitrust and technology issues, both in the U.S. and abroad. Past work has included antitrust seminars to businesses, lawyers at the DOJ, U.S. agencies, and foreign officials. He also taught a formal antitrust course at Vanderbilt University Law School and frequently contributes to courses, events, and student competitions at the George Mason University School of Law and the University of Virginia.

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