The Do's and Don'ts of Premerger Coordination between Buyers and Sellers

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For companies pursuing a potential merger or acquisition, it is extremely important to remember that just because the companies are pursuing a potential combination, their conduct prior to closing is *not* insulated from the antitrust laws. Indeed, since the federal antitrust authorities (either the Federal Trade Commission or Department of Justice) will likely be scrutinizing closely any deal through their review under the Hart-Scott-Rodino Antitrust Improvements Act (the "HSR Act"), it is especially important to be mindful of what type of premerger coordination is permissible and what type is not.[1] Certain pre-closing cooperative activities may catch the agencies' eye and delay or interfere with the completion of their HSR review. Or, if the deal ultimately falls through as is often the case (e.g., General Electric/Honeywell), such conduct may trigger an investigation of potential violations of Section 1 of the Sherman Act.

So, merging companies must be very careful that their pre-closing coordination efforts fall within the normal course of premerger cooperation and due diligence, and do not unwittingly extend into the area of two competitors sharing information or cooperating in a manner that might be construed as potentially anticompetitive. Below, I have briefly distinguished permissible premerger coordination from that which should be avoided.

Distinguishing Permissible Activites

The two types of premerger activity about which the agencies are most concerned are: (i) that the parties not "jump the gun" by transferring some or all of the incidents of beneficial ownership from the seller to the buyer prior to the expiration or termination of the applicable HSR waiting period; and (ii) that the parties not coordinate competitive activities or exchange competitively sensitive information, potentially reducing competition between them.

"Jumping the Gun"

The agencies' concern with "jumping the gun" is fairly straightforward. The primary purpose behind the premerger notification process under the HSR Act is to allow the agencies to seek a preliminary injunction to prevent mergers they believe to be anticompetitive. Thus, the premerger review process attempts to avoid the problem of "unscrambling" the assets after an anticompetitive transaction has taken place. Any action taken by the parties to transfer beneficial ownership prior to agency approval of the deal undermines the prophylactic purpose the HSR Act is intended to serve. For HSR purposes, beneficial ownership is generally determined by whether a party enjoys the benefits and assumes the risks of ownership. This would include the right to obtain the benefit of any increase in value of the assets or stock, the right to collect dividends, the risk of a loss of value of the assets or stock, the right to vote or to determine who may vote on the company's operations and direction, and investment discretion.

Premerger Coordination

The agencies' concern with premerger coordination and information exchange is a little more tricky. While the agencies recognize that the parties need to undertake due diligence and engage in a certain degree of advance planning, they are concerned about the sharing between competitors of competitively sensitive information such as prices and costs. Generally, the government will be guided by a reasonableness standard and will evaluate premerger activity based on whether it is reasonably necessary for the parties' evaluation and negotiation of the deal.

The following is a listing of some basic pointers to guide merging companies in their premerger cooperative activities.

- Do not enter into any agreement which allows the buyer to exercise influence or control over the seller's business in any way prior to closing. However, agreements which protect the buyer's interest in the seller are permissible (e.g., agreements that the seller will operate in the ordinary and normal course of business, will not assume significant additional debt or engage in certain other forms of financing, will not dispose of assets, will not enter into or terminate material contracts, will not make any material changes in its business prior to closing, *etc.*).

- Do not enter into any agreements governing premerger cooperation which are inherently anticompetitive, such as allocating customers or regions, fixing prices, restricting

marketing, or otherwise interfering with or influencing the seller's business operations.

Limit meetings between employees of the two companies to those necessary for purposes of the buyer's due diligence review, evaluation, and negotiation of the transaction.

Do not provide the seller with information about the buyer and its subsidiaries (unless the seller will be acquiring an ownership interest in the buyer as part of the deal). The only information exchanged between the parties should be a one-way exchange from seller to buyer to facilitate the buyer's evaluation of the proposed deal. It is also best if the exchange is a one-time exchange rather than one that continues on an on-going basis.

- Only review material provided by the seller that is reasonably necessary to the buyer's due diligence review. In this regard, the agencies have been sensitive to exchanges of information about current customers, current and future costs and prices, and future marketing plans. They have also generally been more sensitive to information provided *after* a final agreement and price is reached.

- As the completion of the transaction draws near, the agencies are more amenable to cooperative efforts relating to planning the post-merger entity. However, this justification is typically not as compelling as that related to due diligence review. So, it is important to limit the cooperation in this regard to information which is absolutely necessary for post-merger planning, and to those individuals who will be directly involved.
- Enter into a confidentiality agreement which limits the buyer's use of the information the seller provides to evaluating the proposed transaction and which prohibits the buyer's use of the information in the ordinary course of business. You may also want to limit the number of employees of the buyer who have access to the materials the seller provides.

Conclusion

There is obviously a great deal of grey area here. So, it is important to keep your antitrust counsel apprised of all pre-closing coordination activities between the merging parties. The most important thing to keep in mind is that the key to all of this is reasonableness: as long as the premerger cooperative activities are reasonably necessary to making the deal happen, the agencies will likely find them unobjectionable. ❧

[1] Under the HSR Act, 15 U.S.C. §18a as amended, the FTC or DOJ will review all mergers or acquisition resulting in the buyer acquiring at least $50 million worth of assets or voting securities (assuming certain thresholds for the size of the parties are reached). A transaction that is reportable under the HSR Act may not close until the FTC or DOJ have "cleared" the transaction.

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