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$900,000 DOJ Antitrust Settlement Highlights "Gun-Jumping" Risk

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Last week's $900,000 settlement between Smithfield Foods and the Antitrust Division of the U.S. Department of Justice (the "DOJ") is a harsh reminder of the significant penalties parties to a merger may face for engaging in joint activities prior to clearing the pre-transaction notification process under the Hart Scott Rodino Antitrust Improvements Act of 1976 (the "HSR Act"). Under the HSR Act, parties to a covered transaction are prohibited from transferring a "beneficial interest" or any "operational control" from the seller to the buyer prior to receiving HSR Act clearance -- a violation known as "gun-jumping," that carries a maximum fine of $16,000 per day. While this area of the law unfortunately remains murky, the Smithfield Foods settlement is clearly a government message that merger parties should be wary of testing the limits. Below is further detail on the Smithfield Foods settlement, and some general guidelines for merger parties to follow.

In 2006, Smithfield Foods entered into a merger agreement to acquire Premium Standard, a competitor in the pork processing business. In the case filed against Smithfield Foods, the DOJ alleged that, after executing the merger agreement and prior to receiving HSR clearance, Premium Standard sought Smithfield Foods' consent prior to executing certain hog procurement contracts that were necessary to Premium Standard's ongoing business and were typically entered into in the ordinary course of business. Each time Premium Standard sought consent, it provided Smithfield with the proposed contract terms, including the price to be paid, quantity to be purchased, and length of the contract. The DOJ complained that such conduct was tantamount to Premium Standard surrendering to Smithfield Foods operational control over a significant segment of Premium Standard's business prior to the expiration of the waiting period required by the HSR Act. By controlling a significant segment of Premium Standard's business operations through the consent process, Smithfield Foods was alleged to have prematurely acquired a "beneficial ownership" of that portion of Premium Standard's assets. Rather than engage in costly litigation, with the final outcome being uncertain, Smithfield Foods settled the DOJ's complaint by agreeing to a $900,000 settlement.

Notably, the Smithfield Foods case involved a transaction that had been reviewed and cleared by the DOJ as not anticompetitive, yet the DOJ took enforcement action against the parties for conduct engaged in prior to receiving HSR Act clearance. In context the DOJ may have placed heightened concern on the gun-jumping conduct because the parties to the deal were competitors in this area.

While the Smithfield Foods settlement focused on gun-jumping, it is equally important to remember that information exchanges between parties prior to HSR Act clearance often go hand in hand with preclearance integration efforts of the parties, and raise similar antitrust concerns. Parties to a potential deal among competitors should put in place antitrust safeguards around the disclosure or exchange of nonpublic, competitively sensitive information (*e.g.*, due diligence and valuation) during the course of a transaction or when planning the integration of the companies.

In light of the Smithfield Foods settlement, it is important for all parties to a potential strategic transaction to consult antitrust counsel about any preclearance conduct or the sharing of information that does not fall clearly within these guidelines.

- *Prohibited Conduct*. The buyer should ***NOT*** take operational control of the seller and should particularly refrain from doing any of the following:
  - Direct or participate in day-to-day decision-making of the seller;
  - Take possession or control of any assets or businesses of the seller; and
  - Integrate the operations of the seller with its own operations.
- *Customer and Public Perception*. The parties should ***NOT*** act as if the transaction has already closed prior to actual consummation. Specifically, the parties should ***NOT*** take any of the following actions:
  - Make joint calls on customers to sell products or services;
  - Hold out employees of one party as working for the other;
  - Use new business cards with the other party's name;
  - Answer telephones by reference to the other party;
  - Use one party's logo with the other party's products or literature; and
  - Relocate employees of one party to space in the other party's facilities.
- *Competitively Sensitive Information*. The parties should ***NOT*** accept or provide information that is not reasonably necessary for legitimate due diligence or integration planning purposes. Generally speaking, the parties should never share marketing or strategic plans. Finally, the parties should ensure that there are appropriate safeguards in place to the extent it is necessary to review price, cost, contract and customer information or other potentially competitive information.

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