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Transaction Parties Pay Hefty Antitrust Fines for Unlawful Premerger Coordination

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On November 7, 2014, Flakeboard America Limited (Flakeboard), its parent companies, and SierraPine ***entered into a settlement*** with the Department of Justice (DOJ) resolving allegations that the parties engaged in illegal premerger coordination activity during the DOJ's antitrust review of Flakeboard's proposed $107 million acquisition of certain assets from SierraPine. The settlement requires each of Flakeboard and SierraPine to pay $1.9 million in civil penalties for violating the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act), and that Flakeboard disgorge $1.15 million of unlawful profits for violating Section 1 of the Sherman Act.

The HSR Act and Section 1 of the Sherman Act restrict pre-closing activities between parties who have agreed to a merger or acquisition but have not yet closed the transaction. The HSR Act bars acquisitions of voting securities or assets that exceed certain size thresholds unless the parties have filed the required premerger notification with the federal antitrust agencies and have observed the applicable statutory waiting period. The waiting period seeks to ensure that the transaction parties remain independent entities while the reviewing agency, the DOJ or the Federal Trade Commission, investigates the proposed transaction to determine if it is likely to substantially lessen competition in a relevant market. In cases where the acquiring company acts as if it has acquired control or obtained beneficial ownership of the business to be acquired prior to the completion of the HSR process, it can be charged with "jumping the gun" in violation of the HSR Act and may be subject to significant civil penalties of up to $16,000 per day.

Section 1 of the Sherman Act prohibits agreements in restraint of trade. Prior to closing, parties to a proposed transaction remain separate economic actors who are under an obligation to compete independently. Thus, until a transaction is consummated, a party that coordinates with its rival on price, output, or other competitively significant matters may violate Section 1. Section 1 applies irrespective of whether a transaction requires a filing under the HSR Act.

Flakeboard owns and operates numerous mills in North America that produce particleboard and medium density fiberboard (MDF). In January 2014, Flakeboard agreed to purchase three competing SierraPine mills. The transaction was reportable under the HSR Act. The DOJ alleges that, during the mandatory HSR waiting period, Flakeboard and SierraPine coordinated to close SierraPine's Springfield mill (which SierraPine had no plans to close prior to its transaction with Flakeboard) and move the mill's customers to Flakeboard. The mill was permanently shut down in March 2014, before the HSR waiting period expired. SierraPine gave Flakeboard competitively sensitive information about the mill's customers, including names, volume and product information, which Flakeboard shared with its sales personnel. Also, at the request of Flakeboard, SierraPine instructed its employees to inform customers that Flakeboard wanted to serve their business and would match SierraPine's prices. As a result of these actions, according to the DOJ, Flakeboard successfully secured a substantial amount of Springfield's business, including a significant number of new customers that Flakeboard had not previously served. The ***DOJ's complaint*** alleges that Flakeboard's and SierraPine's actions amounted to a per se unlawful agreement between competitors to reduce output and allocate customers in violation of Section 1 of the Sherman Act, and a premature transfer of operational control, and therefore beneficial ownership, of SierraPine's business to Flakeboard in violation of the HSR Act.

In addition to hefty civil penalties assessed for the HSR Act violations, the settlement also requires Flakeboard to disgorge its ill-gotten profits gained from the Springfield mill's customers. The DOJ noted that disgorgement has previously been found to be an appropriate remedy in cases brought under the Sherman Act.[1] It found disgorgement appropriate in this case because the injunctive relief that would most likely restore competition, that is, requiring the mill to be reopened, is impractical, since the mill has been closed for several months and the employees have either left the mill or been terminated.

The DOJ settlement bars the parties, during any pending transaction, from entering into agreements that affect price or output for competing products or that allocate customers, and from disclosing information about customers, prices, or output for competing products. Perhaps more noteworthy than the prohibited conduct is that the settlement explicitly permits certain "conduct of business" covenants that are intended to protect a transaction's value and are common in M&A agreements, as well as disclosure of competitively sensitive information in the context of customary due diligence, provided certain safeguards are put in place. The settlement also requires the companies to establish an antitrust compliance program, which includes naming an antitrust compliance officer responsible for supervising compliance with the settlement.

The Flakeboard case serves as a reminder that the antitrust agencies take gun-jumping concerns very seriously. It highlights the importance of exercising caution when transaction parties wish to coordinate their activities or exchange non-public, competitively sensitive information prior to closing, whether during pre-signing due diligence or in the period between signing and closing, e.g., for integration planning purposes. On the other hand, the case helpfully confirms the accepted view that various pre-closing conduct and information sharing is permissible so long as appropriate precautions are taken. This may involve, for example, blinding or aggregating certain competitively sensitive information, or restricting access to that information by employees of the recipient company who are responsible for marketing, pricing, or sales of competing products. This case also emphasizes the need for companies to establish and maintain an antitrust compliance program and ensure that employees are educated about these issues.

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[1] *See United States v. Keyspan Corp*., 763 F. Supp. 2d 633 (S.D.N.Y. 2011); *See also* February 17, 2011 Bracewell Update: