FTC Warns Parties on Information Exchanges During M&A Due Diligence

In Short

The Situation: The Federal Trade Commission ("FTC") recently published a blog post reminding merging parties to avoid creating antitrust liability through the exchange of competitively sensitive information during merger negotiations and due diligence.

The Risk: Information-sharing violations between competitors in the merger context are rare, but when the FTC and Department of Justice ("DOJ") uncover violations, they will aggressively pursue them.

The Solution: To avoid violations, merging parties should share competitively sensitive information only as necessary to advance negotiations and due diligence, and then only subject to procedural safeguards. Parties also should rely on antitrust counsel to advise on other measures to avoid liability.

Parties to a merger, acquisition, or joint venture routinely share substantial information during due diligence. The buyer needs to know what it is buying; the seller wants to get the deal done. When the transaction involves competitors, sharing competitively sensitive information can raise antitrust concerns, as highlighted again in a recent FTC online blog post. Parties to a transaction should avoid any activity that could risk delaying close of their transaction or raising antitrust liability.

Antitrust Restrictions on Merging Parties

The federal antitrust laws require that parties to a transaction continue to act as separate and independent companies until the transaction closes. Parties may engage in legitimate due diligence information exchanges and other information exchanges to assist in transaction planning, but this "legitimate due diligence" does not give competitors free rein to open their books to one another.

Antitrust laws impose two practical restrictions on merging parties. First, under the Hart-Scott-Rodino ("HSR") Act, parties must remain separate companies prior to closing. Until the HSR investigation is closed, they cannot combine their operations or hold themselves out as a single company, and the buyer cannot begin to control the business activities of the seller. No "gun jumping" is permitted. Unlike certain other federal antitrust laws, an HSR Act violation does not require an anticompetitive effect; this procedural violation can result in fines of up to $41,484 per day of the violation, without proving any impact on competition. Investigations to determine whether gun jumping has occurred can delay closing of the transaction.

Second, parties must be careful not to share competitively sensitive information during due diligence in a way that might lessen competition between them either pre-closing or if the transaction does not close. Section 1 of the Sherman Act, which also prohibits collusive activity such as price fixing and market allocation, applies prior to closing, including during pre-signing diligence, throughout post-signing integration planning, and during the period after an HSR investigation is closed but before consummation. Exchanging competitively sensitive information, such as current or future prices, strategic plans, individual customer or supplier details, or sensitive cost information, may implicate Section 1 if it allows the competing parties to raise prices or otherwise lessen competition.

Representative Enforcement Actions

While information-sharing enforcement actions are rare, the FTC and DOJ will aggressively pursue violations if they are uncovered, either during mandatory HSR review of notifiable transactions or in a separate investigation. Past enforcement activities serve as benchmarks for future agency actions. The recent FTC posting highlighted several gun-jumping enforcement actions:

In one action, the FTC charged aluminum tube manufacturers with violating the FTC Act after they exchanged competitively sensitive information during due diligence. According to the agency's blog post, the sharing of non-aggregated, customer-specific information, including current and future pricing plans, was "particularly harmful to competition because the two companies competed against each other in two highly concentrated markets." The FTC also challenged the merger itself, concluding that the transaction was anticompetitive. As a condition of closing, the agency required the buyer to divest two mills.

In another action, the DOJ challenged as gun jumping the pre-closing agreement between a software developer and the rival it proposed to acquire, under which the seller would obtain the buyer's agreement before offering customer discounts exceeding 20 percent off list price.

The DOJ also challenged merging providers of television programming that allegedly agreed to stop competing for customers, fixed prices and terms to be offered to customers, and jointly managed their interactive program guide business prior to obtaining clearance under the HSR Act and before closing.

Enforcement activity and the FTC's recent posting reaffirm the agency's long-held position that, while merging parties may have a legitimate need for due diligence, exchanging competitively sensitive information without proper protections can violate the federal antitrust laws.

FTC's Recent Guidance and Implications

The FTC's posting provides practical guidance that is consistent with sound advice often delivered by antitrust counsel.

- Most due diligence information exchanges are appropriate in the context of negotiating and planning a transaction.

- Merging parties should consider sharing the least amount of competitively sensitive information possible. For example, parties could redact customer identities or aggregate sensitive information to minimize the risk that the information exchange could be used to lessen competition.

- If parties need to exchange competitively sensitive information, they should only do so through third-party consultants or internal "clean teams" to minimize the risk of the exchange. Third-party consultants offer significant protection by ensuring no sensitive information of one party is reviewed by the competitor counterparty, but can result in substantial expense to the parties. A less-costly alternative is to use internal "clean teams" of employees whose responsibilities do not cover competitive activities like pricing and marketing. Or the parties may consider retired or former employees who will have no ongoing business responsibilities with the company.

Nondisclosure agreements or other agreements not to share information should be used to prevent "clean team" employees from sharing competitive information more broadly within their organization.

- Parties should rely on antitrust counsel to police the procedures and information flow and to ensure adherence with the established protocols. They can advise parties about employees who should and should not participate on clean teams, work with consultants and clean team members to review (and redact, as necessary) summary reports that will be disseminated to the business more broadly, and review and redact ordinary-course documents that might be shared through a data room in connection with due diligence.

Two Key Takeaways

1. Merging parties must remain vigilant on pre-closing information-sharing practices. Most due diligence information exchanges are appropriate, but parties should exercise caution where there may be risk.

2. The FTC's posting reaffirms best practices for exchanges of competitively sensitive information before and during merger negotiations and transaction planning, and it demonstrates the agency's commitment to enforcing improper pre-closing information sharing and coordination.

Lawyer Contacts

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