“Hot” Docs and Fantasies

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• “We want to coordinate prices with competitors.”

• “Our goal is to stabilize prices.”

• “It is to the mutual benefit of both parties to have defined geographic areas within which the parties may exclusively conduct their respective businesses without competition from the other.”

• “A agrees to pay B $400,000 in exchange for B’s agreement not to submit any further bids on the Shops at the Auction…A’s obligation to make the No Bid Payment shall be expressly contingent upon A being the successful bidder…”

• “I made a point about lowering the prices of catalogs; that we are all committing suicide, if we do not stick together. Jane agreed with me but as usual, Steve cautioned me about price fixing…Ha! Ha! Ha! I warned him that by not sticking together, we would have to make 40% more volume in order to make the same figures as last year, but you know Steve, he always thinks he can get more if he acts that way.”

• “The idea is to buy up free market material to create an artificial demand.”

• “It is necessary to introduce an artificial factor to provide the momentum for an upward price adjustment.”

• “Pricing: It’s anticipated that upon introduction of the Agency relationship to Sales, that price points offered will not be as aggressive as those ultimately set when the two companies are formally integrated and the transaction is complete. Expectations should be managed accordingly.”

• “How long will it take to break them and elevate prices?”

• “The strategy is to prevent them from going ahead with the new plant, with the expectation that they might even be forced to cease operating the existing plant.”

• “I tried to tell him what else we could do if they do not sell out to us. I tried to tell him how much we could do with $1 billion. I tried to be non-threatening, but let him know we would do something aggressively.”

• “We would have a near-monopoly and the FTC/our customers probably wouldn’t like it.”

These are excerpts (with identifiers scrubbed) from actual documents that either were submitted to the Federal Trade Commission or the Department of Justice as a part of the premerger notification process, or disclosed in litigation.

The Hazards of Hot Docs

Such "hot" documents are a real threat to the smooth closing of a transaction. The FTC's report of its horizontal merger investigations during the fiscal years 1996 through 2007 indicates that it investigated a greater percentage of transactions with hot documents than similar transactions without hot documents. Even more consequentially, hot documents may be evidence of a criminal price fixing conspiracy, that may be subject to penalties for individuals of up to $1 million and 10 years' imprisonment and for corporations of up to $100 million.

The irony is that most of these documents have little connection with reality. Especially in the case of transactions, much of the problematic language are puffing by transaction proponents to gain internal support. In the case of language suggesting cartel conduct, they often reflect aggressive intent without any implementing conduct and so become primarily fodder for potential government investigations. Where the language does reflect actual cartel conduct, the document makes the prosecutors' and private plaintiffs' cases much easier. The highly dubious wisdom of cartel conduct is beyond the scope of this paper, but certainly documenting the conduct compounds the problem.

Documents containing problematic language have wreaked antitrust havoc in transactions large and small:

• The Federal Trade Commission's challenge to Whole Foods's 2007 acquisition of Wild Oats was significantly fueled by statements of Whole Foods's CEO, including claims that "By buying [Wild Oats] we will…avoid nasty price wars in Portland (both in Oregon and Maine), Boulder, Nashville, and several other cities which will harm [Whole Foods's] gross margins and profitability. By buying [Wild Oats]…we eliminate forever the possibility of Kroger, Super Value, or Safeway using their brand equity to launch a competing national natural/organic food chain to rival us…[Wild Oats] may not be able to defeat us but they can still hurt us…[Wild Oats] is the only existing company that has the brand and number of stores to be a meaningful springboard for another player to get into this space. Eliminating them means eliminating this threat forever, or almost forever." While Whole Foods did acquire Wild Oats, it was not until March 2009, after a defeat at the Court of Appeals, that it reached a settlement with the FTC permitting it to keep some of the Wild Oats locations and requiring it to divest a significant number of locations.

• The 2004 NBC – Vivendi Universal Entertainment merger was delayed for months because the FTC was perturbed by statements in documents indicating that some at NBC felt that the merged company could raise the fees cable operators pay for its programming. NBC and Vivendi had announced their merger on October 8, 2003. The FTC asked for additional information and extended the Hart-Scott-Rodino premerger waiting period into April 2004. The deal did not close until May 12, 2004. In contrast, the European Commission had quickly cleared the deal from the competition perspective, although it is often seen as more stringent in its competition merger control than U.S. enforcers.

• In a 2001 transaction, a document stating that one of the goals of the transaction was to "run a major competitor out of business" caused the FTC to investigate the deal. That investigation delayed the closing of a transaction that did not create any competitive concerns and would probably have been quickly cleared but for the "hot" document.

• The opposition to the proposed combinations in 1998 of the four major drug wholesalers into two was bolstered by statements like "the proposed merger will be positive for industry conditions in that excess capacity will be removed."

• In 1997, when Staples tried to acquire Office Depot, the parties' argument that the transaction would not hurt competition was undermined by their own documents, which discussed the "[b]enefits from pricing in [newly, as a result of consolidation] noncompetitive markets" and the "potential margin lift overall as the industry moves to 2 players." *Federal Trade Commission v. Staples, Inc.*, 970 F. Supp. 1066, 1079 (D.C. 1997). This deal was ultimately blocked at least in part as a result of the parties' own statements.

• In 1995, when Microsoft, owner of Money, was trying to convince the government that it should be permitted to acquire Intuit, the owner of Quicken, if it concurrently divested Money to Novell, that position was substantially undercut by a document which said that "[i]f it was known that we were buying [Quicken and had to sell Money], then I can't imagine anyone would be stupid enough [to buy Money from us...they would] be way, way far behind competitively." The situation was only compounded when Intuit gave Microsoft the code name "Godzilla" during the negotiations. The parties' documents described how the transaction would give customers "one clear option," or, in other words, no choice, thus "eliminating a bloody share war," which will in turn "enrich the terms of trade we can negotiate with customers." They concluded that, "as a combination, we would be dominant." Microsoft abandoned this transaction in the face of opposition from the agencies brought on in part by these documents.

• In another 1995 transaction, an investigation was triggered by documents which contained language such as "[a]fter the merger, there will only be one other competitor left, and two nonpeople should meet and arrange prices where they should be" and "[a]mong the effects of the acquisition will be a major positive impact on product pricing, since both parties' product prices will rise with the combined market power of both companies behind it." As a result, a deal that was eventually cleared in unaltered form without challenge, was delayed for almost six months while tens of thousands of documents were reviewed and produced, dozens of interrogatory responses and affidavits were drafted, and witnesses were examined.

Avoiding the pitfalls of "hot" documents generally and for transactions particularly is not difficult. Here are some tips, as well as a checklist for avoiding the creation of documents that can fan the antitrust flames.

The Term "Market" is Loaded

One easy tip is to use the word "market" sparingly, since it is a loaded term. Overuse of the term "market" has caused antitrust problems.

• In the TCI-QVC acquisition, which combined the only two national television shopping networks, Home Shopping Network and QVC, the parties' documents discussed the relevant market as television shopping. In part because of that record, the transaction was investigated at length by the FTC staff, and it was not until appeals were made to the commissioners that a broader view of the relevant market prevailed and the transaction cleared.

• The parties in the failed Staples-Office Depot deal characterized as a "noncompetitive market," geographic areas that did not have office superstores but did have warehouse-club, consumer electronics or mass merchandiser stores. It might have been equally accurate to say simply that there were no other office superstores in the particular geographic areas.

Indeed, businesses continuously re-evaluate their views of the market place, so the characterization of one area as a "market" when drafting a document may no longer reflect the reality or their view of the market place when, perhaps only months later, the government, or opposing counsel, is challenging a transaction or some course of conduct.

In many instances, when business people refer to a market, they in fact mean "demand," "sales," or "business." For example, the suppliers of parts to the big automakers probably do not compete in a "Ford market," they are instead trying to compete for Ford business. When the phrases "total market" or "market size" are used, the writer usually means "total sales" of a particular product or service, whether or not there are substitutes for that product or service. "Market growth" may really mean "sales growth." And, similarly, "the market is strong" or "the market is soft" is probably more accurately conveyed by "demand is strong" or "demand is weak."

Business persons may be tempted to characterize their particular products as a market. For example, a business person may write that he or she is competing in the "nylon yarn market" when the business is facing stiff competition from rayon yarn. Even though nylon and rayon yarn compete, if the documents show that the business accounts for a substantial portion of the "nylon yarn market" without any reference to rayon, it may be difficult to prove the more accurate nylon-rayon yarn market. Dropping the term "market" is a simple solution. The business person should be able to discuss the subject adequately by speaking of "nylon yarn" and not the "nylon yarn market" and can accurately report the business's strong position relative to other nylon yarn makers by discussing its position in nylon yarn sales, not in the nylon yarn "market."

A significant motivation for the overuse of the word "market" may be the desire to claim "market share." However it may be more accurate, for example, to claim that the business accounts for a large "percentage of sales" of nylon yarn in North America, not that it controls a large "market share" in the North American nylon yarn market.

"Fighting Words" are Dangerous

Also, drafters may be carried away by the competitive spirit, and use what might be characterized as "fighting words." They may want to "dominate," "own," "monopolize," or "control" a "market," rather than "be a major competitor in the business." They may want to "eliminate an aggressive or disruptive competitor," rather than "compete vigorously against an aggressive competitor" or "acquire a vigorous business." They want to "eliminate the only competition" and not only "acquire a substantial competitor." They feel there is "ruinous" or "excessive" competition, rather than "vigorous" competition. Limit hyperbole.

Other Characterizations to be Avoided

In the face of competition, business people may feel that the appropriate response is to "stabilize industry dynamics," do a deal which "will let us raise prices" or otherwise try to "stabilize, support or maintain prices." It may be equally accurate, and less legally sensitive, to say that the industry is restructuring and that the business wants to increase or at least maintain profitability. Rather than try to effect a "market segment consolidation," it may be more accurate to say that the business wants to "increase its market presence."

Strategic planning documents may analyze a menu of potential transactions, including their competitive implications. A strategic plan may speculate that a positive result of a potential transaction will be that "competition will be reduced" or that a "legal monopoly" will be created. It may have been more than sufficient, and perhaps more accurate and relevant, to say that profits could rise and market presence could increase following such a deal.

Checklist

Even the most well-meaning business person can create antitrust risk by doing nothing more than describing a business acquisition or transaction plan a little too aggressively. What can business people do to avoid the possibility of inviting trouble?

• First and foremost, make sure that the staff are aware and understand the parameters of the company's guidelines for document retention and drafting; if such guidelines do not exist, have counsel develop them.

• Next, some specific drafting tips:
- Don't overuse the word "market" in describing "demand," "sales," or "business," or a product;
- Stay away from fighting words such as "dominate," "own," "monopolize," or "control"; and
- Avoid loaded terms like "stabilize prices," "consolidate a market," and "noncompetitive market."