Antitrust Update

DAVIS POLK & WARDWELL

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Recent Developments in Antitrust Law

There have been two significant antitrust law developments since our last update on March 13, 2006: a settlement of an action for alleged pre-merger "gun-jumping" activity, and a settlement of charges relating to an alleged invitation to collude. The following are some brief highlights.

DOJ Settles Action for Alleged Pre-Merger "Gun-Jumping" Violation by Imposing $1.8 Million in Civil Penalties

On April 13, 2006, the Department of Justice (the "Department") announced a settlement with QUALCOMM Incorporated and Flarion Technologies, Inc. ("Flarion") for alleged violations of the pre-merger waiting period requirements of the Hart-Scott-Rodino ("HSR") Act. During the HSR waiting period, merging companies are prohibited from consummating the proposed transaction and are required to operate independently of one another. The Department's complaint against the parties alleged that certain provisions in the merger agreement, and certain conduct by the parties during the waiting period, constituted illegal "gun-jumping" activity that effectively gave QUALCOMM control, and thus beneficial ownership, of Flarion before expiration of the waiting period. The applicable waiting period expired on December 23, 2005, and QUALCOMM completed its acquisition of Flarion on January 18, 2006.

In particular, the companies' merger agreement required Flarion to seek QUALCOMM's consent prior to undertaking certain business activities, such as: entering into IP licensing agreements with third parties; entering into agreements involving the obligation to pay or receive $75,000 or more in a year, or $200,000 or more in aggregate; entering into agreements relating to the acquisition or disposition of intellectual property rights, except for certain minor transactions; and presenting business proposals to customers.

Further, while not required by the agreement, during the waiting period Flarion also sought QUALCOMM's consent prior to undertaking numerous routine activities (such as hiring consultants and employees), providing discounts to specific customers, and pursuing certain smaller customer accounts not of interest to QUALCOMM. A senior executive at Flarion admitted that "before we sign any new contracts we seek [QUALCOMM's] consent."

According to the complaint, one reason for QUALCOMM insisting on the merger agreement provisions at issue was to prevent Flarion from commercializing one of its products in its current form, in conflict with QUALCOMM's future plans for that technology.

As part of the settlement, the parties were ordered jointly and severally to pay a $1.8 million fine. The amount of the fine was reduced from the statutory maximum of $11,000 per day of the violation for each defendant (an aggregate maximum of approximately $3.4 million) because the companies voluntarily reported the gun-jumping problems to the Department, and took measures to amend the contract and change their conduct prior to the Department's complaint.

It should be noted that, after a second request investigation of the transaction, the Department ultimately permitted the acquisition to proceed. This illustrates that the Department may challenge "gun jumping" activity even if it concludes that the underlying transaction does not raise antitrust concerns.

FTC Settles Charges of Attempted Collusion Triggered by Statements in a Quarterly Earnings Call

On March 14, 2006, the Federal Trade Commission (the "FTC") announced it had settled charges that Valassis Communications, Inc. ("Valassis") indirectly invited its sole competitor to collude during a public earnings call with analysts. The Commission's consent order bars Valassis from inviting collusion and entering into or implementing a collusive scheme.

The FTC had alleged that Valassis violated Section 5 of the Federal Trade Commission Act when the company's president and CEO opened a July 2004 earnings call by announcing Valassis would, among other things, (1) no longer seek a 50% market share, (2) aggressively maintain its current customers and market share, (3) raise bids for its competitor's customers well above market levels, and (4) monitor its competitor's response. Such announcement, in the FTC's view, amounted to an invitation to Valassis's only competitor to collude on pricing.

Valassis and News America Marketing are the only two producers of "free-standing inserts," which are booklets of coupons and other ads placed inside newspapers. For years, the two companies had held stable 50% market shares. Valassis unilaterally raised its prices in 2001, causing a substantial loss of customers to News America that Valassis has subsequently (and unsuccessfully) attempted to reverse.

The FTC's charges are significant because they result from unilateral conduct—Valassis's statement of its strategic plan, made in accordance with Securities and Exchange Commission regulations on a public earnings call—rather than from any alleged agreement to collude. However, despite the absence of such an agreement or even a response by the competitor invitee, the FTC chose to challenge Valassis's conduct because (1) the call communicated its strategic plans at a level of specificity inappropriate for a public forum; (2) it had not historically given such information to securities analysts; (3) analysts neither needed nor reported this information; and (4) it had no legitimate business reason for making such a disclosure. In the FTC's view, the only conceivable purpose for making the announcement was to convey an invitation to News America, as Valassis knew that its rival would be monitoring the call.

If you have any questions regarding the above, do not hesitate to call any of the persons listed below.

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