

Companies Charged with Pre-Merger Transfer of Control Pay \$1.8 Million Penalty

Communications technology companies Qualcomm Inc. and Flarion Technologies, Inc. have agreed to pay a \$1.8 million penalty to resolve a complaint by the Department of Justice that Qualcomm prematurely acquired control of Flarion prior to their January 2006 merger.

Hart-Scott-Rodino Act

The Hart-Scott-Rodino Act requires companies planning acquisitions or mergers that meet certain thresholds to file notification documents prior to closing. In order to allow the antitrust authorities to investigate the proposed transaction, the parties are required to remain independent during a 30-day waiting period, which may be extended by the government. Although what may or may not occur during this waiting period is not entirely straightforward, antitrust counsel can provide guidance on how to minimize the risk of penalties.

Qualcomm's Acquisition of Flarion

Qualcomm filed the appropriate HSR filings for its \$600 million acquisition of Flarion when the parties signed a merger agreement in July 2005. The waiting period was extended until December 2005, and the merger was completed in January 2006.

Although DOJ did not challenge the underlying merger, it found evidence that Qualcomm had obtained control of Flarion prior to the expiration of the HSR waiting period. DOJ analyzed the written merger agreement as well as the parties' conduct during the waiting period.

- Flarion was prohibited from entering into new agreements involving the obligation to pay, or right to receive, \$75,000 or more per year or \$200,000 or more in the aggregate.
- Flarion was required to obtain Qualcomm's written consent prior to licensing its intellectual property to third parties.
- Flarion was required to obtain Qualcomm's written consent prior to presenting business proposals to customers or prospective customers, and Qualcomm discouraged Flarion from pursuing certain business opportunities.
- Flarion requested approval from Qualcomm before hiring employees.
- Flarion requested approval of price quotations and discounts, and on at least one occasion, Qualcomm denied Flarion's request to offer a discount.

In light of this evidence, DOJ concluded that the parties had transferred control as soon as their merger agreement was signed.

Penalties

Parties charged with an HSR violation can be liable for up to \$11,000 for each day of noncompliance, which in the Qualcomm case amounted to \$3.32 million. Because Qualcomm and Flarion were cooperative in the investigation, DOJ agreed to a \$1.8 million settlement.

Practical Guidance

During the interim period between signing a merger or purchase agreement and consummating the transaction at closing, a buyer has a legitimate interest in protecting the value of the target company. Nonetheless, the Qualcomm case reiterates that the companies should not act as though the merger or acquisition has already occurred.

- Antitrust focus is on provisions that give a buyer control over the seller's fundamental business decisions or day-to-day operations. For example, provisions giving the buyer control over pricing decisions or allocation of accounts are risky.
- To the extent possible, the seller should be allowed to operate its business in the ordinary course consistent with its past practices, and this should be made clear in the parties' written agreement. On the other hand, the government has sanctioned provisions that give the buyer certain rights in the event there is a material adverse change in the seller's business.
- During due diligence and transition planning, the exchange of sensitive information such as pricing information should be handled carefully. The parties should consider using lagged or aggregated information, or relying upon outside consultants. Another possibility is for the transition-planning personnel to be kept separate and distinct from the personnel involved in the post-merger daily business operations.
- While it is permissible to jointly market the transaction, parties should seek the advice of counsel prior to making any joint communications with customers to discuss the transaction prior to expiration of the HSR waiting period.
- Some of the restrictions in the Qualcomm case are relatively standard. For example, it is common to place restrictions on material agreements and intellectual property licensing. When those restrictions are combined with more far-reaching provisions-- such as requiring approval for customer proposals or pricing decisions--the government is likely to take a second look.
- Because transactions involving competitors will be examined with the most scrutiny, parties in this situation should be especially attentive to how they conduct themselves during the HSR waiting period.

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