

DOJ Announces \$900,000 Settlement with Smithfield Foods and Premium Standard Farms For Gun-Jumping

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On January 21, 2010, the United States Department of Justice (DOJ) Antitrust Division announced that it had settled charges against pork packing and processing companies Smithfield Foods and Premium Standard Farms for in effect acting as a single entity prior to the expiration of the Hart-Scott-Rodino Antitrust Improvements Act (HSR Act) waiting period. Under the proposed settlement filed with the United States District Court for the District of Columbia, the companies will pay \$900,000 in total civil penalties.

The Settlement

The DOJ alleges that after entering into a merger agreement in September 2006 and before the expiration of the waiting period in March 2007, Premium Standard Farms asked for Smithfield Foods' consent for each Premium Standard Farms hog procurement contract negotiated during the waiting period, thereby ceasing to exercise independent business judgment concerning those contracts. Premium Standard Farms provided Smithfield Foods with the contracts' terms, including price and quantity. According to DOJ's complaint, in all there were three multi-year contracts requiring Premium Standard Farms to purchase between 400,000 to 475,000 hogs per year for a total cost of roughly \$57 million to \$67 million, thus acquiring assets valued at more than \$56.7 million, the operative threshold at the time. The DOJ alleged that since the contracts were a vital part of Smithfield Foods' ongoing business and were entered in the ordinary course of business, the parties prematurely transferred operational control, in violation of the requirement that parties wait for expiration of the waiting period before consummating the transaction.

Implications

It is important that for transactions reportable under the HSR Act, parties maintain independent operations until after the expiration of the waiting period. Parties should recognize that gun-jumping can happen whether or not there is a contract in place. While in the Smithfield Foods case the DOJ does not allege that the merger agreement's provisions were problematic, the DOJ claims that the parties' interdependent decision making behavior was anticompetitive. In other cases, antitrust regulators have obtained settlements of charges that contract provisions were anticompetitive because they granted the right to control the target prior to expiration of the waiting period.

Certain types of contract provisions do not pose antitrust risk. For example, parties may safely employ a provision that requires the target to continue operating its business in the ordinary course,

and in general may agree to any provision that is a legitimate means for the buyer to protect the value of the target company without acquiring control over it. Other types of provisions may create the potential for gun-jumping and thus raise antitrust risk. Thus, antitrust counsel should be consulted before an agreement is in place, and consulted during the pendency of the HSR review process.

Kelley Drye & Warren LLP

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