UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA
United States Department of Justice
Antitrust Division
450 Fifth Street, N.W., Suite 8700
Washington, D.C. 20530

Plaintiff

v.

L.B. FOSTER COMPANY
415 Holiday Drive
Pittsburgh, Pennsylvania 15220

and

PORTEC RAIL PRODUCTS, INC.
900 Old Freeport Road
Pittsburgh, Pennsylvania 15238

Defendants

Case: 1:10-cv-02115
Assigned To : Urbina, Ricardo M.
Assign. Date : 12/14/2010
Description: Antitrust

COMPLAINT

The United States of America ("United States"), acting under the direction of the Attorney General of the United States, brings this civil antitrust action against Defendants L.B. Foster Company ("Foster") and Portec Rail Products, Inc. ("Portec") to enjoin Foster's proposed acquisition of Portec and to obtain other equitable relief. The United States complains and alleges as follows:

I. NATURE OF THE ACTION

1. On February 16, 2010, Foster and Portec entered into an Agreement and Plan of Merger ("Merger Agreement"). Pursuant to the Merger Agreement, on February 26, 2010, Foster made a cash tender offer to acquire all the outstanding shares of common stock of Portec

for $11.71 per share. On August 30, 2010, Foster increased its offer to $11.80 per share. The transaction is valued at approximately $114 million.

2. In the United States, Foster's proposed acquisition of Portec likely would substantially lessen competition in two separate product markets—bonded insulated rail joints ("bonded joints") and polyurethane-coated insulated rail joints ("poly joints"). Foster and Portec are virtually the only manufacturers of bonded joints in the United States and currently supply approximately 95 percent of the market. For many customers, Foster and Portec are the only approved suppliers of these joints. In addition, Foster and Portec are two of only three suppliers of poly joints in the United States and currently supply approximately 54 percent of the market.

3. Elimination of the competition between Foster and Portec likely will result in Foster's ability to unilaterally raise prices of bonded joints and poly joints to most customers. The proposed acquisition also likely would reduce Foster's incentive to invest in innovation in bonded joints. In addition, by eliminating Portec as a supplier, the acquisition increases the likelihood of coordinated interaction between Foster and the other supplier of poly joints.

4. As a result, the proposed acquisition likely would substantially lessen competition in the development, manufacture, and sale of bonded joints and in the development, manufacture, and sale of poly joints in the United States, in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18.

II. THE DEFENDANTS

5. Foster is incorporated in Pennsylvania and has its headquarters in Pittsburgh, Pennsylvania. It manufactures and distributes numerous products and services for the rail, construction, energy, and utility industries and has approximately 30 locations throughout the United States. For the rail industry, Foster manufactures, among other products, bonded joints,

poly joints, tie plates, and rails. Foster had total revenues of approximately $512 million in 2008 and approximately $382 million in 2009.

6. Portec is incorporated in West Virginia and has its headquarters in Pittsburgh, Pennsylvania. Portec also manufactures and distributes numerous products and services for the rail industry and other industries. For the rail industry, Portec manufactures, among other things, bonded joints, poly joints, rail lubricators, end posts, and curv blocks. Portec has several locations in the United States and abroad. Portec had total revenues of approximately $109 million in 2008 and approximately $92.2 million in 2009.

III. JURISDICTION AND VENUE

7. The United States brings this action under Section 15 of the Clayton Act, 15 U.S.C. §§ 4 and 25, as amended, to prevent and restrain Defendants from violating Section 7 of the Clayton Act, 15 U.S.C. § 18.

8. Defendants develop, manufacture, and sell bonded joints, poly joints, and other products in the flow of interstate commerce. Defendants' activities in the development, manufacture, and sale of these products substantially affect interstate commerce. This Court has subject matter jurisdiction over this action pursuant to Section 15 of the Clayton Act, 15 U.S.C. § 25, and 28 U.S.C. §§ 1331, 1337(a), and 1345.

9. Defendants have consented to venue and personal jurisdiction in this judicial district.

IV. TRADE AND COMMERCE

A. Background

(1) Insulated Rail Joints

10. Railroad tracks are divided into discrete sections, called track circuits. Electricity flows through the rail in each track circuit. Each track circuit is electrically isolated from the others. As the train enters a track circuit, the circuit allows the train to signal that it is passing through that particular circuit, which leads to the operation of automatic signals at rail crossings and switches farther up the line. The track circuit also enables the railroad operator to monitor the location of the trains.

11. Railroad tracks are generally welded together, within a track circuit, forming the strongest possible bond. However, welding cannot be used to connect the pieces of rail between separate track circuits because that would allow the electric current to flow between the circuits and interfere with a train's signaling. Using an insulated rail joint is the only method available to connect the rail pieces at the ends of the track circuits and insulate the circuits from one another. Rail joints consist of steel bars that are bolted onto the ends of each of the rail pieces and are used to connect the abutting ends of the rails. Insulated rail joints are joints that are used to break the electric current flowing through the rail, using a material placed on the steel bars and between the two abutting pieces of rail.

12. The reliability of an insulated rail joint is critical to the safety and efficient operation of the railroad. It is difficult to develop and manufacture insulated rail joints that can successfully withstand railroads' usage without failing, particularly in the most demanding applications. Rail connected by a rail joint is inherently weaker than rail that has been welded together. If the joint is subjected to heavy usage—for example, because the track it is on

frequently carries heavily loaded rail cars—the joint may wear down over time and eventually break. In addition, an insulated rail joint may lose its insulating properties. If an insulated rail joint fails, the railroad operator will not know the location of the train and the signals will not operate properly. At the extreme, the failure of an insulated rail joint could cause a train derailment. At the least, failure of an insulated rail joint could cause the railroad to expend significant amounts of money determining the location of and replacing the failed joints. It could also bring the operation of the railroad to a halt while the failed joints are replaced.

13. Ensuring that the insulated rail joints will last for the expected life of the joint without failure is vital to the railroads. It is costly to replace these joints and an unscheduled replacement can disrupt the operations of the railroad. As a result, the largest U.S. railroads, called Class 1 railroads, engage in extensive, multi-year testing to ensure than any new insulated rail joint, or any insulated rail joint offered by a new supplier, will meet their reliability and quality needs. The railroads must be assured that the joints are designed to last and the supplier's manufacturing processes are sufficiently well controlled that all joints will last the requisite time without failing.

14. Railroads gain substantially from improvements in the reliability and effective life of insulated rail joints. Therefore, railroads have made research and development associated with these joints an important component of the competitive process. Manufacturers must make substantial investments in research and development to compete effectively for the business of the major railroads.

15. The two primary types of insulated rail joints are bonded joints and poly joints. Customers seek bids for either bonded joints or poly joints, based on the particular application.

(2) Bonded Joints

16. Bonded joints use epoxy in addition to bolts to bind the steel bars to the rails. With the addition of epoxy, the rails, bars, bolts, and insulating material that make up the joint are less subject to movement when a railcar passes over the joint and thus suffer less wear and tear. As a result, bonded joints are able to withstand the heaviest loads for extended periods of time. Because of their strength, certain of Foster's and Portec's bonded joints typically are guaranteed to last until 500 million gross tons have passed over the joints.

17. The strength of bonded joints makes them necessary for the freight railroads' high-usage main track lines. This is especially true for the Class 1 railroads, which handle most of the heavy rail traffic in the United States. No other insulated rail joint is strong enough to withstand the heavy loads on these lines. Bonded joints are also necessary for some heavily traveled areas on main passenger lines and regional and short line railroads.

(3) Poly Joints

18. Poly joints can be used to electrically isolate track circuits from one another. In contrast to bonded joints, poly joint components are not bound together by epoxy. Instead, electrical insulation in poly joints is provided by a polyurethane-covered bar that is bolted to the rail. No mechanism is added to provide additional strength, and nothing binds the joint to the rails except the bolts. Poly joints are not as strong and long lasting as bonded joints. They are significantly less expensive than bonded joints.

19. Poly joints are generally used by Class 1 railroads to create track circuits in areas with lesser loads and traffic than on the main tracks, or on other less-heavily used sections of track. Poly joints also may be used as temporary replacements for bonded joints, but only until

bonded joints can be installed. In addition, poly joints are used by some passenger railroads or other smaller railroads, which carry less weight on their tracks.

B. Relevant Markets

(1) Bonded Joints

20. The development, manufacture, and sale of bonded joints in the United States is a line of commerce and relevant market within the meaning of Section 7 of the Clayton Act.

21. Bonded joints have specific applications, for which other types of joints can rarely, if ever, be employed. Bonded joints are typically used on the main tracks of the freight railroads. Other types of joints, such as poly joints, cannot handle over time the heavy loads on these tracks because they are not strong enough.

22. The vast majority of Foster's and Portec's sales of bonded joints are made to large customers located in the United States. Major U.S. customers consider only those suppliers of bonded joints located in the United States because of these suppliers' proximity to their rail lines. A supplier's proximity to customers' rail lines reduces both freight costs, which are a significant factor in the final cost of a bonded joint, and delivery times, and allows better customer service.

23. A small but significant increase in the price of bonded joints would not cause U.S. customers of bonded joints to substitute a different joint or other product, reduce purchases of bonded joints, or turn to suppliers outside the United States, in volumes sufficient to make such a price increase unprofitable.

(2) Poly Joints

24. The development, manufacture, and sale of poly joints in the United States is a line of commerce and relevant market within the meaning of Section 7 of the Clayton Act.

25. A customer whose requirements will be satisfied by a poly joint would rarely, if ever, substitute a bonded joint, even if the price of poly joints were to rise.

26. The three primary suppliers of poly joints in the United States ship poly joints to customers located throughout the United States. Because all three suppliers are located within approximately 200 miles of one another, customers pay only minimal differences in freight costs. U.S. customers of poly joints consider only those suppliers located in the United States to avoid higher freight costs, reduce delivery times, and allow better customer service.

27. A small but significant increase in the price of poly joints would not cause U.S. customers of poly joints to substitute a different joint or other product, reduce purchases of poly joints, or turn to suppliers outside the United States, in volumes sufficient to make such a price increase unprofitable.

C. Market Participants

(1) Bonded Joints

28. Foster and Portec are the only significant competitors in the U.S. market for bonded joints. Currently, Foster and Portec sell approximately 51 and 44 percent, respectively, of U.S. bonded joints. One other company accounts for the remaining five percent of this market. In addition, this third competitor does not have the same commitment to research and development as Foster and Portec. As a result, the combination of Foster and Portec will create a virtual monopoly in the U.S. market for bonded joints.

(2) Poly Joints

29. Foster, Portec, and one other company are the only competitors in the U.S. market for poly joints. Currently, Foster and Portec sell approximately 21 and 33 percent, respectively, of U.S. poly joints. The third competitor accounts for the remaining sales in this market.

V. COMPETITIVE EFFECTS

A. Bonded Joints

30. Foster's proposed acquisition of Portec likely would substantially lessen competition in the U.S. market for bonded joints. Foster and Portec are the two primary suppliers of bonded joints to most U.S. customers. If the acquisition is not enjoined, the combined firm would supply approximately 95 percent of the bonded joints in the United States. Using a measure called the Herfindahl-Hirschman Index ("HHI") (explained in Appendix A), the HHI would increase by approximately 4,500 points, resulting in a post-acquisition HHI of more than 9,000 points.

31. Foster's and Portec's bidding behavior often has been constrained by the possibility of losing sales of bonded joints to the other. For many customers of bonded joints, Foster and Portec are either the only sources, or the two best sources.

32. Customers have benefitted from the competition between Foster and Portec for sales of bonded joints by receiving lower prices. In addition, Foster and Portec have competed vigorously by providing innovations that have resulted in higher-quality and longer-lasting joints. The combination of Foster and Portec would eliminate this competition and its future benefits to customers. Post-acquisition, Foster likely would have the incentive and gain the ability profitably to increase prices, reduce quality, reduce innovation, and provide less customer service compared to these aspects of competition absent the acquisition. The small remaining

competitor has limited customer acceptance and would not have the ability to make additional sales sufficient to discipline post-acquisition anticompetitive effects.

33. The proposed acquisition, therefore, likely would substantially lessen competition in the United States for the development, manufacture, and sale of bonded joints. This likely would lead to higher prices, lower quality, less customer service, and less innovation in violation of Section 7 of the Clayton Act.

B. Poly Joints

34. Foster's proposed acquisition of Portec likely would substantially lessen competition in the U.S. market for poly joints. If the acquisition is not enjoined, the combined firm would supply approximately 54 percent of the poly joints in the United States. The HHI would increase by more than 1,300 points, resulting in a post-acquisition HHI of more than 5,000 points.

35. Foster's and Portec's bidding behavior often has been constrained by the possibility of losing sales of poly joints to the other.

36. Customers have benefitted from competition between Foster, Portec, and the other competitor by receiving lower prices. The products of the three firms are to some degree different, and the elimination of Portec likely would allow the two remaining competitors to increase prices. The combination of Foster and Portec would eliminate the significant competition between Foster and Portec and its future benefits to customers. Post-acquisition, Foster likely would have the incentive and gain the ability to profitably increase prices and provide less customer service compared to these aspects of competition absent the acquisition.

37. In addition, by reducing the number of competitors in the U.S. market for poly joints from three to two, Foster and its only remaining competitor likely would gain the incentive

and ability to raise prices through coordinated interaction by directly increasing prices, allocating customers, or restricting output or capacity. Coordination would be more likely or more effective because, with two significant competitors in the market, both could be reasonably certain of the identity of the other's customers, likely making cheating, such as discounting, easier to detect and discipline.

38. The proposed acquisition, therefore, likely would substantially lessen competition in the United States for the development, manufacture, and sale of poly joints. This likely would lead to higher prices and less customer service in violation of Section 7 of the Clayton Act.

VI. DIFFICULTY OF ENTRY

A. Bonded Joints

39. Sufficient, timely entry of additional competitors into the U.S. market for bonded joints is unlikely. Therefore, entry or the threat of entry into this market is not likely to prevent the harm to competition caused by the elimination of Portec as a supplier.

40. Firms attempting to enter the U.S. market for the development, manufacture, and sale of bonded joints face several significant impediments to rapid, successful, and profitable entry. The new supplier of bonded joints must develop and successfully operate a production process that consistently produces a large number of high-quality bonded joints that meet the rigorous specifications set by the railroads. In addition, a new entrant must be committed to investing in research and development to meet the railroads' ongoing desire for innovation. The design for bonded joints is continually evaluated in order to improve the strength and longevity of the joints. The technical know-how and expertise necessary to consistently manufacture a large number of high-quality bonded joints and to design improvements that pass customers' qualification tests are difficult to obtain and learned only after years of direct experience.

41. Further, a new supplier's bonded joint must pass potential customers' approval processes by demonstrating that the joints can meet rigorous quality and performance standards and perform well over time with heavy freight loads. For example, many railroads, especially the Class 1 railroads, insist that new bonded joints undergo laboratory testing plus several years of in-track testing. Railroads want to observe that the joints perform well over time before installing a significant number on their tracks. Moreover, attempts for approval are not guaranteed to be successful, and the approval process can take several years, especially if the first few attempts for approval are not successful. Because each customer's specifications may be unique, approval by one customer does not guarantee approval by any other customer.

42. For these reasons, entry by new firms or the threat of entry by new firms into the U.S. market for the development, manufacture, and sale of bonded joints would not defeat the substantial lessening of competition that likely would result if Foster acquires Portec.

B. Poly Joints

43. Sufficient, timely entry into the U.S. market for poly joints is also unlikely. Therefore, entry or the threat of entry into this market is not likely to prevent the harm to competition caused by the elimination of Portec as a supplier.

44. The expertise to design and implement a process to manufacture a large number of high-quality poly joints on a consistent basis is difficult to obtain and takes years of experience to develop. In addition, a new poly joint supplier must obtain approvals from the railroads by demonstrating that its joints can meet the railroads' rigorous quality and performance standards. This rigorous approval process can take eighteen months or more. Further, attempts for approval are not guaranteed to be successful and can take several years, especially if the first few attempts for approval are unsuccessful.

45. For these reasons, entry by new firms or the threat of entry by new firms into the U.S. market for the development, manufacture, and sale of poly joints would not defeat the substantial lessening of competition that would likely result if Foster acquires Portec.

VII. THE PROPOSED ACQUISITION VIOLATES SECTION 7 OF THE CLAYTON ACT.

46. Foster's proposed acquisition of Portec likely would substantially lessen competition in the development, manufacture, and sale of bonded joints and the development, manufacture, and sale of poly joints in the United States in violation of Section 7 of the Clayton Act, 15 U.S.C. § 18.

47. Unless enjoined, the proposed acquisition likely would have the following anticompetitive effects, among others:

(a) actual and potential competition between Foster and Portec in the markets for the development, manufacture, and sale of bonded joints and the development, manufacture, and sale of poly joints in the United States would be eliminated;

(b) competition in the markets for the development, manufacture, and sale of bonded joints and the development, manufacture, and sale of poly joints in the United States likely would be substantially lessened;

(c) for bonded joints in the United States, prices likely would increase and quality, customer service, and innovation likely would decrease; and

(d) for poly joints in the United States, prices likely would increase and customer service likely would decrease.

VIII. REQUESTED RELIEF

48. The United States requests that this Court:

(a) adjudge and decree that Foster's acquisition of Portec would be unlawful and violate Section 7 of the Clayton Act, 15 U.S.C. § 18;

(b) preliminarily and permanently enjoin and restrain Defendants and all persons acting on their behalf from consummating the proposed acquisition of Portec by Foster, or from entering into or carrying out any other contract, agreement, plan, or understanding, the effect of which would be to combine Foster with Portec;

(c) award the United States its costs for this action; and

(d) award the United States such other and further relief as the Court deems just and proper.

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APPENDIX A
DEFINITION OF HHI

The term "HHI" means the Herfindahl-Hirschman Index, a commonly accepted measure of market concentration. The HHI is calculated by squaring the market share of each firm competing in the market and then summing the resulting numbers. For example, for a market consisting of four firms with shares of 30, 30, 20, and 20 percent, the HHI is 2,600 ($30^2 + 30^2 + 20^2 + 20^2 = 2{,}600$). The HHI takes into account the relative size distribution of the firms in a market. It approaches zero when a market is occupied by a large number of firms of relatively equal size and reaches its maximum of 10,000 points when a market is controlled by a single firm. The HHI increases both as the number of firms in the market decreases and as the disparity in size between those firms increases.

Markets in which the HHI is between 1,500 and 2,500 points are considered to be moderately concentrated, and markets in which the HHI is in excess of 2,500 points are considered to be highly concentrated. *See Horizontal Merger Guidelines* § 5.3 (issued by the U.S. Department of Justice and the Federal Trade Commission on Aug. 19, 2010). Transactions that increase the HHI by more than 200 points in highly concentrated markets will be presumed likely to enhance market power. *Id.*