No. 07-5276

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA

FEDERAL TRADE COMMISSION,

Plaintiff-Appellant,

v.

WHOLE FOODS MARKET, INC., and
WILD OATS MARKETS, INC.

Defendants-Appellees.

Appeal from the United States District Court
for the District of Columbia, No. 07-cv-01021-PLF

BRIEF FOR THE AMERICAN ANTITRUST INSTITUTE AS AMICUS CURIAE IN SUPPORT OF THE FEDERAL TRADE COMMISSION

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STATEMENT OF INTEREST OF AMICUS CURIAE

The American Antitrust Institute ("AAI") is an independent non-profit education, research, and advocacy organization. Its mission is to advance the role of competition in the economy, protect consumers, and sustain the vitality of the antitrust laws. The Advisory Board of AAI, which serves in a consultative capacity, consists of prominent antitrust lawyers, law professors, economists, and business leaders. *See* http://www.antitrustinstitute.org. AAI's Board of Directors has approved the filing of this brief[1] because the issue raised by the appeal – the proper allocation of authority between the district courts and the FTC in adjudicating mergers – is critical to the effective enforcement of Section 7 of the Clayton Act by the FTC.

[1] The individual views of the members of the Advisory Board or Board of Directors may differ from the positions taken by AAI.

SUMMARY OF ARGUMENT

1. The realities of modern merger enforcement support a deferential standard for preliminary injunctions in § 13(b) merger cases. The FTC challenges only those few mergers that it predicts are likely to be anticompetitive after a thoroughgoing investigation. But while the FTC has become more judicious in bringing cases, district courts have inexplicably and wrongly become less deferential to the agency's expertise.

2. The Commission's role as the principal arbiter of the lawfulness of a merger challenged by the FTC dictates a deferential preliminary injunction standard. Without a broad power to obtain preliminary relief, the Commission could not perform its adjudicatory function in most cases because of the difficulty of unscrambling the merger after consummation. The incipiency doctrine also militates in favor of a deferential standard.

3. The "serious questions" standard is a deferential standard. It does not require the Commission even to show that it is more likely than not that the merger will violate Section 7. Yet, the district court required the Commission to prove a violation of Section 7, as evidenced by the court's statements as to the burden of proof and its rejection of the "fair and tenable" chance of success standard. Moreover, the court ignored key elements of the FTC's case, including the explosive comments of Whole

Foods' CEO as to the anticompetitive purposes of the transaction, the anticompetitive implications of the closure of numerous Wild Oats stores, and the implications for unilateral anticompetitive effects suggested by the diversion ratio in the "Project Goldmine" report.

ARGUMENT

I. THE REALITIES OF MODERN MERGER ENFORCEMENT SUPPORT A DEFERENTIAL STANDARD FOR PRELIMINARY INJUNCTIONS IN SECTION 13(b) MERGER CASES.

Any consideration of the proper standard to be applied to the FTC's request for a preliminary injunction must recognize certain realities about modern merger enforcement:

1. The Horizontal Merger Guidelines, promulgated by the Department of Justice in 1982 and subsequently revised and adopted by the FTC and the Justice Department, ushered in a new era of judicious, economically-based merger enforcement.[2]

2. Nevertheless, modern merger analysis, and market definition in particular, is not an exact science and often "involves many judgment calls and a great deal of balancing of the evidence . . . ." [3]

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[2] *See, e.g.,* David Scheffman et al., *Twenty Years of Merger Guidelines Enforcement at the FTC: An Economic Perspective*, 71 Antitrust L.J. 277, 318 (2003) ("The 1982 Merger Guidelines and the three subsequent revisions have been a very important advance in antitrust and economic analysis because they have provided an economically sound, implementable approach to merger review.").

[3] Jonathan B. Baker & Carl Shapiro, *Reinvigorating Horizontal Merger Enforcement* 6 (Oct. 2007), http://faculty.haas.berkeley.edu/shapiro/mergerpolicy.pdf. (forthcoming in *Where the Chicago School Overshot the Mark: Effect of Conservative Economic Analysis on U.S. Antitrust* (Robert Pitofsky ed., 2008)); *see* Robert Pitofksy, *New Definitions of Relevant Market and the Assault on Antitrust*, 90 Colum. L. Rev. 1805, 1812 (1990) ("the determination whether to include a product or cluster of products in the relevant market is almost always based on rough estimates" and "often depends on fact determinations that are largely speculative"); Jonathan B. Baker, *Market Definition: An Analytical Overview*, 74 Antitrust L. J. 129, 143 (2007) ("The process of market definition involves judgments

3. The FTC has earned an excellent reputation for the competence of its lawyers, economists, and Commissioners.[4] All of the Commissioners are highly-regarded, seasoned antitrust experts and leaders in the field.[5]

4. In 1996, the FTC adopted a "fast track" procedure for administrative litigation, which permits merging parties subject to a preliminary injunction to obtain a final decision from the FTC within 13 months of the injunction. *See* 16 C.F.R. § 3.11A (2007).[6]

5. Although the Commission can authorize staff to seek a preliminary injunction merely when it "has reason to believe" that a merger will violate Section 7 of the Clayton Act and that a preliminary injunction would be in the public interest, 15 U.S.C. § 53(b), the Commission only authorizes a

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as to 'matters of degree' that can at times be 'extremely difficult to measure.'") (quoting Pitofsky, *supra*, at 1807).

[4] *See, e.g.,* Richard A. Posner, *The Federal Trade Commission: A Retrospective*, 72 Antitrust L.J. 761, 771 (2005) ("the Commission's improvements in the years since the ABA Commission's report have been considerable, and far greater than would have been achieved by simply heeding the ABA's call for better people.").

[5] The Commission is led by a former principal deputy assistant attorney general of the Antitrust Division and antitrust partner at a top national law firm, and includes a prolific antitrust scholar, a former head of the ABA Antirust Section, a former chief counsel and staff director for the U.S. Senate Antitrust Subcommittee, and a former antitrust partner at a prominent law firm and New York State Deputy Attorney General. *See Assessing Part III Administrative Litigation: Interview with Timothy J. Muris*, Antitrust, Spring 2006, at 6, 7 (former FTC chairman Muris stating, "With the recent additions of Commissioners Kovacic and Rosch, we have a Commission with a strong and expert Chairman and with spectacular antitrust strength.").

[6] *See* D. Bruce Hoffman & M. Sean Royall, *Administrative Litigation at the FTC: Past, Present, and Future*, 71 Antitrust L.J. 319, 322 (2003) ("In 1996 the FTC took aggressive steps to transform Part III litigation into procedure faster by far than virtually any federal antitrust case . . . .").

preliminary injunction proceeding when the Commissioners are confident that the merger will be anticompetitive.[7] Indeed, the Commission "generally issues second requests only when there is a strong possibility that some aspect of a transaction would violate the antitrust laws."[8]

6. Before the FTC seeks a preliminary injunction, the bureaus of competition and economics will have conducted an extensive investigation,[9] and the Commissioners themselves will have reviewed the evidence and often have spoken independently with the experts and advocates of the merging parties, and others.

7. The FTC and the Department of Justice together challenge only a tiny fraction of mergers each year. In the last two fiscal years, the two

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[7] *See, e.g.,* Federal Trade Commission, Performance and Accountability Report, Fiscal Year 2007, at 58 ("When the FTC concludes that the likelihood of [competitive] harm indicates a law violation, and no settlement is possible, the Commission authorizes its staff to litigate the matter."); Statement of Chairman Majoras, Commissioner Kovacic, and Commissioner Rosch Concerning the Closing of the Investigation Into Transactions Involving Comcast, Time Warner Cable, and Adelphia Communications, File No. 051-0151, at 2 (January 31, 2006) (explaining why merger investigation was closed, over the objection of two dissenting Commissioners: "As our colleagues … point out, Section 7 of the Clayton Act does not require the Commission 'to determine, at this stage, whether harm absolutely will occur.' But we do need facts that show that it is likely that the transactions would lessen competition in a relevant market."). This does not mean that the Commissioners will not take a fresh look at the evidence when called upon to do so in their adjudicatory capacity.

[8] Deborah Platt Majoras, Reforms to the Merger Review Process 5 (Feb. 16, 2006).

[9] The Commission's second requests for information can be burdensome to merging parties, but "are essential to the merger review process because they enable the FTC … to determine and document with facts, rather than guesswork and speculation, whether certain transactions are likely to be anticompetitive." *Id.* at 4.

agencies combined have challenged 32 mergers each year, or an average of less than 1.7% of the HSR filings during this period.[10] Very few of the challenges are litigated, and most are resolved by consent decree permitting the transaction to go forward. The fraction of mergers challenged by the FTC and the Dept. of Justice has declined in recent years.[11]

These practical realities suggest that before a generalist federal district judge rejects one of the few merger challenges that the FTC does make, he or she should be reasonably certain that the Commission has gone astray, as a proper understanding of the preliminary injunction standard implies. Yet, the court below, and several other district courts recently,[12] gave short shrift to the prosecutorial judgment of the Commission, preempted the

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[10] "Challenges" include transactions that were voluntarily abandoned or restructured in response to an FTC or DOJ investigation. Enforcement data are contained in Federal Trade Commission, Performance and Accountability Report, Fiscal Year 2007, at 52, 55 (reporting 2,108 HSR filings and 22 merger enforcement actions in FY 2007), Statement of Thomas O. Barnett, Asst. Attorney General, Antitrust Division, Before the Task Force on Antitrust and Competition, House Committee on the Judiciary 9 (Sep. 25, 2007) (reporting 10 merger challenges in FY 2007), and FTC and Dept. of Justice, Hart-Scott-Rodino Annual Report Fiscal Year 2006, at 2-3 (reporting 1,768 HSR filings in FY 2006 and that each agency challenged 16 transactions). The universe of mergers is larger than HSR filings, which are only required for transactions in excess of $50 million, as adjusted. *See id.* at 2 n.2

[11] According to data assembled by Professors Baker and Shapiro, the average rate of merger challenges for each agency from 1982 to 2000 (before the HSR thresholds were raised) was .9% of HSR filings, while the rate of challenge by the FTC in the first term of the George W. Bush administration (adjusting for the reduction in HSR filings) was .8% and dropped to .6% during the first two years of the second term. *See* Baker & Shapiro, *supra*, at 15, 17.

[12] *See FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109 (D.D.C. 2004); *FTC v. Foster*, 2007 U.S. Dist. LEXIS 47606 (D. N.M. 2007).

Commission's adjudicatory function, and fundamentally usurped the Commission's role as the expert antitrust administrative agency.

II. THE STATUTORY SCHEME AND PURPOSE OF SECTION 7 SUPPORT A DEFERENTIAL STANDARD FOR PRELIMINARY INJUNCTIONS.

"This court and others have suggested that the standard for likelihood of success on the merits is met if the FTC has raised questions going to the merits so serious, substantial, difficult and doubtful as to make them fair ground for thorough investigation, study, deliberation and determination by the FTC in the first instance and ultimately by the Court of Appeals." *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 714-15, 727 (D.C. Cir. 2001) (internal quotes omitted) (reversing denial of preliminary injunction where the "FTC has raised serious and substantial questions"). Under this standard, the FTC need not "prove . . . probable success on the merits but something less." *FTC v. Lancaster Colony Corp., Inc.*, 434 F. Supp. 1088, 1090 (S.D. N.Y. 1977); *see Washington Metro. Area Transit Comm'n v. Holiday Tours, Inc.*, 539 F.2d 841, 844 (D.C. Cir. 1977) (rejecting requirement that a private party demonstrate a "mathematical probability" of success); 2 Phillip E. Areeda et al., *Antitrust Law* ¶ 302e & n.25, at 16 (2d. ed. 2000) (FTC "must show some chance of ultimate success").

This relatively deferential standard is necessitated by the statutory scheme making the Federal Trade Commission, not the courts, the principal arbiter of an FTC merger challenge, as well as by the substantive standard under Section 7, which seeks to root out anticompetitive dangers in their "incipiency."

A. The Commission's Role as the Principal Arbiter of the Lawfulness of a Merger Challenged by the FTC Dictates a Deferential Standard.

As Judge Posner has explained, "One of the main reasons for creating the Federal Trade Commission and giving it concurrent jurisdiction to enforce the Clayton Act was that Congress distrusted judicial determination of antitrust questions. It thought the assistance of an administrative body would be helpful in resolving such questions and indeed expected the FTC to take the leading role in enforcing the Clayton Act, which was passed at the same time as the statute creating the Commission." *Hospital Corp. of America v. FTC,* 807 F.2d 1381, 1386 (7th Cir. 1986); *see also FTC v. Cement Institute*, 333 U.S. 683, 693 (1948) (abiding purpose of Congress was "to vest both the Commission and the courts with adequate powers to hit at every trade practice … which restrained competition or might lead to such restraint if not stopped in its incipient stages"). Section 5 of the Federal Trade Commission Act authorized the Commission to issue a cease and

desist order against a corporation engaged in an "unfair method of competition," 38 Stat. 717, 319 (1914), to be defined by the Commission, while Section 11 of the Clayton Act gave the Commission power to issue a similar order, or order of divestiture, for a violation of Section 7 or other provisions of the Clayton Act. *See* 38 Stat. 730, 735 (1914); *FTC v. Dean Foods Co.*, 384 U.S. 597, 606 (1966) ("[T]he Commission is a governmental agency to which Congress has entrusted, *inter alia*, the enforcement of the Clayton Act, granting it the power to order divestiture in appropriate cases.").

The Commission was intended to be an independent and non-partisan expert agency,[13] "its members … called upon to exercise the trained judgment of a body of experts appointed by law and informed by experience." *Humphrey's Ex'r v. United States*, 295 U.S. 602, 624 (1935) (internal quotes omitted); *see also Cement Institute*, 333 U.S. at 695 (intent of Congress was "to create an agency whose membership would at all times be experienced, so that its conclusions would be the result of expertness coming from experience."). Thus, in judicial review of the agency's decisions, its findings "as to the facts, if supported by evidence, shall be conclusive." 15 U.S.C. § 45(c); *see also* 15 U.S.C. § 21(c) (substantial

[13] The five commissioners are appointed for staggered 7-year terms, and no more than three may be members of the same political party. 15 U.S.C. § 41.

evidence standard under Clayton Act). "The statute forbids a court to make its own appraisal of the testimony, picking and choosing for itself among uncertainties and conflicting inferences." *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 454 (1986) (internal quotes omitted); *see also FTC v. Consolidated Foods Corp.*, 380 U.S. 592, 600 (1965) (finding by the Commission, "whose expertise the Congress trusts, should be honored, if there is substantial evidence to support it."); *id.* at 606 (Stewart, J., concurring) ("[O]ur responsibility to the Commission – to respect its findings where there is evidence to support them – requires close scrutiny of the record before its conclusions are upset.").

Indeed, in reviewing the Commission's decision to block a merger, the court's "only function," according to Judge Posner, "is to determine whether the Commission's analysis of the probable effects of these acquisitions on … competition … is so implausible, so feebly supported by the record, that it flunks even the deferential test of substantial evidence." *Hospital Corp. of America,* 807 F.2d at 1385; *see id.* at 1386 (drawing inferences of competitive consequences from facts "is a matter within the Commission's primary responsibility too"; "whether we might have come up with a different prediction on our own is irrelevant"); *accord Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 935 (7th Cir. 2000).

Without a broad power to obtain preliminary relief, the deference due to the Commission would be virtually meaningless. The Commission could not perform its adjudicatory function in most merger cases because of the difficulty of "unscrambling" the merger after consummation.[14] Thus, in *Dean Foods* the Supreme Court held that the FTC could obtain preliminary relief in the courts of appeal to enjoin a merger prior to consummation, even absent express statutory authorization:

> [W]ithout standing to secure injunctive relief, and thereby safeguard its ability to order an effective divestiture of acquired properties, the Commission's efforts would be frustrated. . . .
>
> If consummation of the merger is not restrained, the restoration of the [acquired company] as an effective and viable competitor will obviously be impossible by the time a final order is entered. This is not unusual. Administrative experience shows that the Commission's inability to unscramble merged assets frequently prevents entry of an effective order of divestiture.

384 U.S. at 606-07 n.5.

As this Court has observed, "These concerns later motivated Congress [in 1973] to grant the FTC, in 15 U.S.C. § 53(b), express statutory authority to petition the District Court for a temporary restraining order or preliminary

[14] That was certainly true in this case, where Whole Foods intended to close down 30 or more competing Wild Oats stores and sell numerous others. Whole Foods' contention that there is little left of Wild Oats at this point, *see* Whole Foods Market, Inc.'s Reply in Support of its Motion to Dismiss This Appeal as Moot at 4 n.1, only underscores the difficulty of post-consummation relief. It is nevertheless evident that *some* remedy may still be possible after the adjudicatory hearing *if* the Court grants interim relief, and hence the case is not moot.

injunction." *FTC v. Exxon Corp.*, 636 F.2d 1336, 1343 (D.C. Cir. 1980); *see also Lancaster Colony*, 434 F.Supp. at 1096 (legislative history of 13(b) "reveals congressional concern with the FTC's historic inability to effectuate a remedy once an acquisition is consummated"); *accord Heinz,* 246 at 726 ("Section 13(b) itself embodies congressional recognition of the fact that divestiture is an inadequate and unsatisfactory remedy in a merger case . . . ."). These same concerns about the ineffectiveness of post-consummation remedies led Congress to adopt the Hart-Scott-Rodino Antitrust Improvement Act of 1976, which fundamentally changed the merger review process to give the FTC and the Justice Department the practical ability to block significant mergers before consummation. *See* William J. Baer, *Reflections on Twenty Years of Enforcement Under the Hart-Scott-Rodino Act*, 65 Antitrust L.J. 825, 830-31 (1997) (discussing legislative history).

In enacting section 13(b), Congress intended that "injunctive relief be broadly available to the FTC" as demonstrated "by incorporating a unique 'public interest' standard in 15 U.S.C. § 53(b), rather than the more stringent, traditional 'equity' standard for injunctive relief." *Exxon Corp.,* 636 F.2d at 1343. This Court further explained that "Congress determined that the traditional standard was not 'appropriate for the implementation of a Federal statute by an independent regulatory agency where the standards of

the public interest measure the propriety and the need for injunctive relief.'"

Heinz, 246 F.3d at 714 (quoting H.R. Rep. No. 93-624, at 31 (1973)).[15]

The purpose of a preliminary injunction under §13(b) is not merely to quickly halt anticompetitive practices, but rather to preserve the status quo so that the Federal Trade Commission can perform its statutory function of determining whether a merger violates Section 7. Thus, as the Fourth Circuit explained:

> It is at once obvious that in a proceeding under § 13, the granting or denial of a temporary restraining order or a preliminary injunction is [not] an end unto itself. The district court is not authorized to determine whether the antitrust laws have been or are about to be violated. That adjudicatory function is vested in F.T.C. in the first instance. The only purpose of a proceeding under § 13 is to preserve the *status quo* until F.T.C. can perform its function.

FTC v. Food Town Stores, Inc., 539 F.2d 1339, 1342 (4th Cir. 1976); *accord Heinz*, 246 F.3d at 726 ("Congress enacted section 13(b) to preserve the status quo until the FTC can perform its function"); *FTC v. Warner Communications Inc.*, 742 F.2d 1156, 1162 (9th Cir. 1984) ("Our present

[15] § 13(b) of the FTCA provides: "Upon a proper showing that, weighing the equities and considering the Commission's likelihood of ultimate success, such action would be in the public interest, … a temporary restraining order or a preliminary injunction may be granted . . . ." 15 U.S.C. § 53(b). Notably, the standard expressly does not require the FTC to establish irreparable harm, *see FTC v. Weyerhaeuser Co.,* 665 F.2d 1072, 1082 (D.C. Cir. 1981), which is consistent with the congressional recognition that in merger cases, divestiture is an inadequate and unsatisfactory remedy. *Heinz*, 246 F.3d at 726.

task is not to make a final determination on whether the proposed merger violates Section 7, but rather to make only a preliminary assessment of the merger's impact on competition.").

B. Congress's Intent to Arrest Anticompetitive Tendencies in Their "Incipiency" Militates in Favor of a Deferential Standard.

A restrictive standard for granting preliminary relief not only usurps the FTC's statutory role in adjudicating mergers, it also undermines Congress's intent to restrict mergers with uncertain but possibly substantial anticompetitive effects. From its enactment in 1914, Section 7 of the Clayton Act barred acquisitions whose effect "*may be* to substantially lessen competition." 38 Stat. 730, 731-32 (1914) (emphasis added).[16] This language reflected that Congress intended to "arrest in its incipiency … the substantial lessening of competition" from an acquisition. *United States v. E.I. duPont de Nemours & Co.*, 353 U.S. 586, 589 (1957). In 1950, when Congress substantially strengthened Section 7, it reiterated its intent to "arrest[] mergers at a time when the trend to a lessening competition in a

[16] The language was a compromise between the House, which advocated a standard that would bar acquisitions where the effect "*is* to eliminate or substantially lessen competition," and the Senate, which had adopted the less restrictive "may be to lessen competition" standard. 51 Cong. Rec. 16001-02 (1914), *reprinted in* 3 *The Legislative History of the Antitrust Laws & Related Statutes* 2628-29 (Earl W. Kintner ed., 1978); *Brown Shoe*, 370 U.S. at 318 n.32 ("That § 7 of the Clayton Act was intended to reach incipient monopolies and trade restraints outside the scope of the Sherman Act was explicitly in the Senate Report on the original Act.").

line of commerce was still in its incipiency." *Brown Shoe Co. v. United States*, 370 U.S. 294, 317 (1962).[17] "Congress saw the process of concentration in American business as a dynamic force; it sought to assure the Federal Trade Commission and the courts the power to brake this force at its outset and before it gathered momentum." *Id.*

The incipiency doctrine means that "the statute requires a prediction, and doubts are to be resolved against the transaction." *FTC v. Elders Grain, Inc.*, 868 F.2d 901, 906 (7th Cir. 1989) (Posner, J.). "All that is necessary is that the merger create an appreciable danger of [higher prices] in the future. A predictive judgment, necessarily probabilistic and judgmental rather than demonstrable … is called for." *Hospital Corp. of America,* 807 F.2d at 1389 (Posner, J.); *accord Heinz*, 246 F.3d at 719. Because of the uncertainty of predicting the effects of a merger on competition, notwithstanding the increased economic sophistication of modern merger analysis, courts and enforcers inevitably make some errors in these judgments. The incipiency doctrine reflects the congressional judgment that the cost of erroneously

[17] Congress amended Section 7 in the Celler-Kefauver Act of 1950 because the "asset loophole" had rendered Section 7 "largely a dead letter," and the Supreme Court's 1948 decision in *Columbia Steel* had made it clear that the Sherman Act was unable to deal with the problem of corporate concentration. *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 339-40, 342 n.20 (1963); *see also* Richard A. Posner, *Antitrust Law* 122 (2d ed. 2001) ("[T]here is no doubt that Congress wanted to stiffen the vague and loose legal standard of *Columbia Steel*, in much the same way as the original Clayton Act had been intended to harden the vague 'Rule of Reason' laid down by the *Standard Oil* decision.").

permitting an anticompetitive merger is higher than the cost of erroneously blocking a merger that is competitively benign.[18] Indeed, from a decision-theoretic point of view, where, as here, the parties' claimed efficiencies are weak,[19] the prospect or potential for increased prices need not be high to warrant blocking the merger.

If congressional intent to arrest anticompetitive tendencies in their incipiency is to be respected, then the courts must apply a deferential standard for determining whether the FTC should be granted a preliminary injunction to protect its ability to adjudicate merger challenges, particularly since "[t]he determination of a likelihood of success must be made under time pressure and on incomplete evidence," so that "[t]he risk of an erroneous assessment is … higher than it is after a full evidentiary

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[18] *See generally* Robert H. Lande, *Resurrecting Incipiency: From* Von's Grocery *to Consumer Choice*, 68 Antitrust L.J. 875, 881 (2001) (incipiency mandate may be understood as directing decisionmakers to err more on the side of making Type I errors than Type II errors). Lande suggests that modern enforcers and many courts seem to have forgotten the incipiency doctrine. *See id.* at 888. However, the doctrine is recognized in the Horizontal Merger Guidelines. *See* U.S. Dept. of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 0.1 (1997) ("[T]he Guidelines reflect the congressional intent that merger enforcement should interdict competitive problems in their incipiency."). And it continues to be invoked by many courts. *See, e.g., Midwestern Machinery Co., Inc. v. Northwest Airlines, Inc.*, 392 F.3d 265, 269 (8th Cir. 2004) ("Section 7 exists primarily to arrest, at their incipiency, mergers that could produce anti-competitive results."); *United States v. Dairy Farmers of America, Inc.*, 426 F.3d 850, 858 (6th Cir. 2005); *FTC v. University Health, Inc.*, 938 F.2d 1206, 1218 (11th Cir. 1991). Indeed, the court below cited the *Brown Shoe* incipiency language, *see* 502 F.Supp. 2d at 9, but plainly failed to give it effect.

[19] The district court rejected Whole Foods' efficiency arguments as insufficient under the Horizontal Merger Guidelines. *See* 502 F.Supp. 2d at 48-49.

presentation." *FTC v. Weyerhaeuser Co.*, 665 F.2d 1072, 1083 (D.C. Cir. 1981).

III. THE DISTRICT COURT DID NOT APPLY THE APPROPRIATE STANDARD.

The district court recited the "serious questions" standard, *FTC v. Whole Foods Market, Inc.*, 502 F.Supp. 2d 1, 6, 49 (D.D.C. 2007), but did not apply it. Rather, the court effectively required the FTC to prove a Section 7 violation. This legal error is illustrated by several points.

A. The District Court Cited the Wrong Standard Throughout its Opinion.

First, there are many instances in the court's opinion where the court expressly stated that the FTC was required to prove, or had failed to prove, certain elements of a Section 7 violation. *See* 502 F.Supp 2d at 7 ("To determine whether the FTC has met its burden of establishing a prima facie case . . . ."); *id.* at 8 ("The government also has the burden of proving the relevant geographic market.");[20] *id.* at 36 ("The Court therefore concludes

[20] As the FTC notes in its brief at pp. 34-35, the district court relied on Eighth Circuit case law that refuses to apply the "serious questions" standard to market definition. The leading case, *FTC v. Freeman Hospital*, 69 F.3d 260, 268 n.12 (8th Cir. 1995), reasoned that "[w]ithout a well-defined relevant market, a particular transaction's effect on competition cannot be evaluated [and] no *National Tea* 'question' exists to be answered." This makes no sense, especially in a unilateral effects case such as this where the definition of the relevant market and the anticompetitive effects are intertwined. *See* FTC & U.S. Dept. of Justice, Commentary on the Horizontal Merger Guidelines 10 (2006) ("Evidence pertaining more directly to a merger's actual or likely competitive effects also may be useful in determining the relevant market in which effects are likely.").

that the FTC has not met its burden to prove that 'premium natural and organic supermarkets' is the relevant product market in this case for antitrust purposes."); *id.* at 38 ("[S]ince the FTC has not met its burden with respect to the relevant product market, the Court need not closely examine the alleged relevant geographic market."); *id.* at 49 ("[T]he Court concludes that the FTC has not proven that it is likely to prevail on the merits at an administrative proceeding and subsequent appeal to the court of appeals.").[21]

The court failed to recognize that the language of the statute itself does not require the FTC to prove anything, merely that the court "consider[] the Commission's likelihood of ultimate success," 15 U.S.C. § 53(b), and that "likelihood of success" under §13(b) does not mean that the FTC must establish that it is more likely than not to succeed, any more than a private plaintiff in equity must make such a showing.[22]

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[21] Indeed, the district court also applied the wrong standard to the "equities," stating that "The FTC also has the burden of showing that the balance of the equities warrants entry of the injunction." 502 F. Supp. 2d at 49. There is no such requirement in the statute or the case law. On the contrary, if the Commission establishes a likelihood of success on the merits (under the serious, substantial questions standard), it is presumed that the public will be served by interim relief. *See Weyerhaeuser*, 665 F.2d at 1082, 1085; *Warner Communications*, 742 F.2d at 1165.

[22] The "serious questions" standard comes from traditional equity practice in many jurisdictions, including this one, that adopt a "sliding scale" principle under which a plaintiff need not prove probable success on the merits when the other traditional equitable factors favor preliminary relief. *See Washington Metro. Area Transit Comm'n v. Holiday Tours, Inc.*, 539 F.2d 841, 844 (D.C. Cir. 1977) (quoting *Hamilton Watch Co. v. Benrus Watch Co.*, 206 F.2d 738, 740 (2d Cir. 1953), a private action to enjoin a merger); Charles A. Wright et al., 11A *Fed. Prac. & Proc. Civ. 2d* § 2948.3, at 195 (2d ed. 1995). Congress intended to hold the FTC to a lower, not higher, standard under

B. The District Court Improperly Rejected the "Fair and Tenable" Standard.

That the district court placed too high a burden on the Commission is also clear from its express rejection of a characterization of the standard as merely requiring the FTC to show a "fair and tenable" chance of success, stating: "The FTC's burden is not insubstantial, and a showing of fair or tenable chance of success on the merits will not suffice for injunctive relief." 502 F.Supp. 2d at 6 (quoting *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 116 (D.D.C. 2004) and *FTC v. Tenet Health Care Corp.*, 186 F.3d 1045, 1051 (8th Cir. 1999)) (internal quotes omitted). Judge Hogan of this district has also rejected the "fair and tenable" language. *See FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1072 (D.D.C. 1997); *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 156 (D.D.C. 2000).[23]

However, there is another line of cases that follows the "fair and tenable" standard, which was first articulated in *Lancaster Colony,* 434 F. Supp. at 1090. *See* 2 Phillip E. Areeda et al., *Antitrust Law* ¶ 302e n.25, at

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§13(b), and tipped the scale in the FTC's favor by eliminating any requirement that the FTC show irreparable harm. *See supra*.

[23] The Eighth Circuit rejected the "fair and tenable" formulation on the ground that such a standard "reduces the judicial function to a rubber stamp procedure." *FTC v. National Tea Co.*, 603 F.2d 694, 698 (8th Cir. 1979). This does not follow. Whatever the standard for the likelihood of success may be, the court exercises its independent judgment in determining whether the evidence presented meets that standard. To be sure, a lower standard means that courts will more often grant the FTC's motion, but that is the design of the statutory scheme.

16 (citing *Lancaster Colony* for "fair and tenable" standard, but noting that the standard is in dispute); *cf.* 42 *Am. Jur. 2d* Injunctions § 16 ("The granting of preliminary injunctive relief can even be based on a 'fair chance' for success on the merits or the existence of questions serious enough to require litigation."). A motions panel of this court adopted the "fair and tenable" formulation, as reported in *FTC v. Beatrice Foods Co.*, 587 F.2d 1225, 1229 (D.C. Cir. 1978) (Appendix to Statement of McKinnon & Robb, JJ.) ,[24] and other district courts have followed it, citing *Beatrice Foods*. *See, e.g., FTC v. Southland Corp.*, 471 F. Supp. 1, 3 (D.D.C. 1979). Other decisions that follow the "fair and tenable" formulation include *FTC v. Verity Intern., Ltd.*, 194 F.Supp. 2d 270, 281 (S.D.N.Y. 2002), *FTC v. Ameridebt, Inc.*, 373 F. Supp. 2d 558, 563-64 (D. Md. 2005), and *United States v. Sun & Sand Imports, Ltd., Inc.*, 725 F.2d 184, 188 & n.5 (2d Cir. 1984) (noting that standard under FTCA was the "fair and tenable chance of ultimate success" articulated by *Lancaster Colony*, but stating, "We do not believe that there is any significant difference between the 'serious question' standard and the 'fair and tenable chance' standard."); *see also Warner Communications,* 742 F.2d at 1164 (reversing denial of preliminary injunction where court was

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[24] In *Heinz*, the court quoted *Beatrice Foods* for the "serious questions" standard, but did not address the "fair and tenable" language. *See* 246 F.3d at 715.

satisfied that the Commission "has made a tenable showing" of violation); *FTC v. Libbey, Inc.*, 211 F. Supp.2d 34, 39-40 (D.D.C. 2002) ("The Court is not convinced that the acquisition as presented will in fact violate the antitrust laws; however, the facts as presented to the Court makes the FTC's concerns plausible and therefore sufficient to establish its prima facie case that the acquisition may have an anti-competitive effect on the market.").

Whether the "fair and tenable" language sets a lower standard, or is merely a gloss on the "serious questions" standard, it appropriately suggests that the Commission need not establish that it is more likely than not that it will prove a Section 7 violation, but "something less." *Lancaster Colony Corp.,* 434 F. Supp. at 1090. The district court's rejection of the language, along with its other statements, shows that the court required something more.

C. The District Court Ignored Key Elements of the FTC's Case.

Had the district court followed the appropriate standard, it would have carefully examined the FTC's case and the evidence it presented to see whether it "raised serious questions," and then considered Whole Foods' responses, as this Court did in *Heinz*. It would not have resolved conflicts in the evidence, but would have left such conflicts for the Commission to resolve. *See Warner Communications,* 742 F.2d at 1164 ("Because the issue

in this action for preliminary relief is a narrow one, we do not resolve the conflicts in the evidence . . . ."); *Heinz*, 246 F.3d at 725 ("we recognize that, post-hearing, the FTC might accept the rebuttal arguments proffered by the appellees").

Instead, as the FTC demonstrates in its brief, the district court ignored key elements of the Commission's case, including the explosive comments of the CEO of Whole Foods as to the anticompetitive purpose of the transaction, and most of the Commission's expert's econometric studies, and accepted Whole Foods' claims even when they conflicted with the evidence in the record.

The failure of the court to consider the inculpatory statements by senior management as to the purposes of the transaction and nature of the market is clear error, as such statements are highly probative of the likely effect of the merger. *See* 4A Phillip E. Areeda et al., *Antitrust Law* ¶ 964a, at 18 (2d ed. 2006) ("evidence of anticompetitive intent cannot be disregarded");[25] *Brown Shoe*, 370 U.S at 329 n.48 ("Although it is

[25] Areeda uses an example apropos of this case to illustrate the relevance of "intent" evidence: "Imagine … a case in which the aggregate market share appears to be below [the] threshold [for presumptive illegality] but where an internal document of the acquiring firm states explicitly that the acquisition would 'remove our most troublesome competitor from the scene' and 'reduce price competition.' Such evidence, as an admission against interest, … may suggest that the market has been too broadly defined in the geographic or product dimension." 4A Areeda et al., *Antitrust Law* ¶ 964c, at 19-20.

unnecessary for the Government to speculate as to what is in the back of the minds of those who promote a merger … evidence indicating the purpose of the merging parties, where available, is an aid in predicting the probable future conduct of the parties and thus the probable effects of the merger.") (internal quotes omitted).

In considering other evidence, the district court failed to acknowledge the arguments made by the FTC as to their import. For example, an important element of the FTC's case was the fact that Whole Foods was planning to close 30 or more Wild Oats stores. The FTC's expert pointed out that these store closings would unambiguously harm consumers because consumers that preferred Wild Oats would be forced to shop at a less preferred option (perhaps further away from home), and all consumers would have less choice. *See* PX02878 at 3-4, 39. This loss of an alternative place to shop is a real cost and certainly cognizable under the Clayton Act. *See generally* Neil W. Averitt & Robert H. Lande, *Using the "Consumer Choice" Approach to Antitrust Law*, 74 Antitrust L.J. 175 (2007). However, while the district court recognized that Whole Foods intended to close a

number of stores, it did not address the anticompetitive implications of the closings.[26] *See* 502 F.Supp. 2d at 11, 34.

The store closings were significant in another respect not appreciated by the district court. They provided a solid basis for estimating the "diversion ratio" for purposes of critical loss analysis, because Whole Foods' "Project Goldmine" report had calculated how much of the revenue it would recapture from each Wild Oats store that it closed.[27] As the FTC points out, Dr. Scheffman's critical loss estimates simply ignored this crucial evidence. FTC Br. 19-20. The district court discounted the "Project Goldmine" estimates not because they were unreliable, as Whole Foods had argued, but because it was unimpressed by their magnitude. The court said, "As defendant Whole Foods' counsel put it, 'this is a strange monopoly if it results in a transfer of say less than a third of the store's volume . . . . [I]f

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[26] To be sure, in theory, closing a store (perhaps if unprofitable) might generate efficiencies. But any such efficiencies would not necessarily benefit consumers, and, in any event, the district court appropriately rejected Whole Foods' efficiency arguments.

[27] The diversion ratio asks, "'If you raise your price, what fraction of your lost customers will turn to your rival (now merger partner)?'" Carl Shapiro, *Mergers With Differentiated Products*, Antitrust, Spring, 1996, at 23, 24. The "aggregate diversion ratio" includes sales lost to all other products in the candidate market. *See* Michael L. Katz & Carl Shapiro, *Critical Loss: Let's Tell the Whole Story*, Antitrust, Spring, 2003, at 49, 56 n.23. The "recapture" of lost sales that would have gone to the merger partner is what ordinarily provides the incentive for the merged firm to raise prices unilaterally. *See* U.S. Dept. of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 2.21 (1997) ("Some of the sales loss due to the price rise merely will be diverted to the product of the merger partner and, depending on relative margins, capturing such sales loss through merger may make the price increase profitable even though it would not have been profitable premerger.").

two-thirds of the volume is going elsewhere in a market that is contended to be a monopoly, what kind of a monopoly is this?'" 502 F.Supp. 2d at 34 (citation omitted). In fact, however, a diversion ratio of 33% (or lower) may be quite significant, and it is hardly strange that a relevant market for differentiated products might exist (a "monopoly") even though most of the lost customers would switch to products outside the market.[28] Indeed, the court ignored Professor Murphy's calculation that the diversion ratios indicated by the "Project Goldmine" estimates would in fact make a SSNIP profitable. *See* FTC Br. at 21.

[28] *See* FTC and U.S. Dept. of Justice, Commentary on the Horizontal Merger Guidelines 27 (2006) ("A merger may produce significant unilateral effects even though a large majority of the substitution away from each merging product goes to non-merging products."); *see also* Katz & Shapiro, *supra*, at 54 ("An aggregate diversion ratio greater than the critical loss creates an economic presumption that the products under consideration constitute a relevant market.").

CONCLUSION

Any unilateral effects case involving differentiated products encounters the skeptical reaction that because the merging parties do compete in a broader market, the merger cannot "really" be anticompetitive. However, the evidence marshaled by the FTC showed just that; at a minimum it raised substantial questions that are appropriately resolved by the FTC, not the federal district court in the context of a preliminary injunction hearing. Only by misapplying the deferential standard for granting a preliminary injunction could the court have reached a contrary conclusion. Accordingly, the Court should reverse the decision below.

Respectfully submitted,

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