NO. 07-5276

UNITED STATES COURT OF APPEALS
DISTRICT OF COLUMBIA CIRCUIT

APPEAL FROM DISTRICT OF DISTRICT OF COLUMBIA
CIVIL ACTION NO. 07-1021 (PLF)

FEDERAL TRADE COMMISSION,

Plaintiff,

v.

WHOLE FOODS MARKET, INC. and

WILD OATS MARKET, INC.

Defendants.

AMICUS BRIEF ON BEHALF OF THE AMERICAN ANTITRUST INSTITUTE, THE CONSUMER FEDERATION OF AMERICA, AND THE ORGANIZATION FOR COMPETITIVE MARKETS IN SUPPORT OF THE FEDERAL TRADE COMMISSION'S REQUEST FOR A STAY PENDING APPEAL

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Corporate Disclosure Statement and Statement of Financial Interest

Pursuant to Circuit Rule 26.1 the American Antitrust Institute, the Consumer Federation of America, and the Organization for Competitive Markets make the following disclosure:

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Dated: August 23, 2007

/s/ David A. Balto
David A. Balto

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AAI	American Antitrust Institute
CFA	Consumer Federation of America
FTC	Federal Trade Commission
OCM	Organization for Competitive Markets
OP	August 16, 2007 Opinion from the United States District Court for the District of Columbia in the matter of the Federal Trade Commission v. Whole Foods Markets, Inc. and Wild Oats Markets, Inc., Case No. 07-1021 (PLF)
PNOS	Premium Natural Organic Supermarkets

INTERESTS OF AMICI

The American Antitrust Institute ("AAI") is an independent Washington-based non-profit education, research, and advocacy organization. Its mission is to increase the role of competition, assure that competition works in the interests of consumers, and challenge abuses of concentrated economic power in the American and world economy. The AAI is particularly involved in research and advocacy on retail competition issues. It has sponsored preeminent seminars on retail competition bringing together industry participants, antitrust enforcers, and academics on important topics such as market power, buyer power, merger policy, category management and other supermarket promotion practices. It has submitted public comments on proposed supermarket merger enforcement actions, testified on merger enforcement standards and provided Congressional testimony on federal government enforcement policy.

The Consumer Federation of America ("CFA") is the nation's largest consumer-advocacy group, composed of over 280 state and local affiliates representing consumer, senior citizen, low income, labor, farm, public power and cooperative organizations, with more than 50 million individual members. CFA represents consumer interests before federal and state regulatory and legislative agencies and participates in court proceedings.

The Organization for Competitive Markets ("OCM") is a national non-profit, public policy research organization headquartered in Lincoln, Nebraska which advocates for open and competitive agriculture and retail markets. Its members are farmers and ranchers, some of whom produce natural or organic food for the natural foods industry. OCM has testified before Congress and filed amicus briefs on numerous competition issues, including supermarket mergers and merger enforcement.

The Amici support the position of the Federal Trade Commission (FTC) because this acquisition will lead to higher prices, less service, and diminished consumer choice. The decision below denying the FTC's request for an injunction is inconsistent with merger law and important antitrust principles and will ultimately harm consumers and competition. Specifically:

- First, the lower court erred in finding the relevant product market is all food supermarkets rather than premium natural foods supermarkets.

- Second, the court erred in ignoring evidence that the intent of this merger was to extinguish competition from a critical rival; intent documented in numerous deal-related documents used to justify this transaction at the highest levels of Whole Foods.

- Third, the court erred by focusing upon marginal consumers rather than core consumers.

- Finally, the court never addressed the fundamental question: "what is the real purpose of this transaction?" Instead of answering that question or grappling with the parties' documents, the court relied extensively on economic expert testimony, in a fashion inconsistent with its own guidance that "antitrust theory and speculation cannot trump facts." (Op. at 9 (citing *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109 (D.D.C. 2004)).

Because the parties presented no evidence of cognizable efficiencies from this transaction, and because it admittedly was not designed to benefit consumers or consumer welfare, the Court should grant a stay for a full briefing and argument on the merits. That this transaction generates no efficiencies is extraordinary, since in almost all of the recent litigated merger cases, the parties presented evidence of significant efficiencies. In this situation, where there is no benefit to consumers from this transaction, and the harm to the parties generated by a stay is greatly outweighed by any harm to consumers, a stay pending appeal is wholly appropriate.

I. THE COURT ERRED BY FAILING TO EVALUATE WHETHER TRADITIONAL SUPERMARKETS CONSTRAIN PREMIUM NATURAL AND ORGANIC FOODS SUPERMARKETS

The primary issue in this appeal is the appropriate definition of the relevant product market. In all other respects, as the court below concluded, the FTC prevails. Because the court defined the product market inaccurately, there is no basis for its conclusion that there is "no substantial likelihood that the FTC can prove its asserted product market and thus no likelihood that it can prove that the proposed merger may substantially lessen competition or tend to create a monopoly." (Op. at 92).

The court's error in this case is simple, but fatal. It relied on the fact that some customers of Premium Natural Organic Supermarkets ("PNOS") also shop elsewhere, and that PNOSs price check against traditional supermarkets. From those two facts, the court below reaches the erroneous conclusion that the relevant product market must include traditional supermarkets. But decades of antitrust jurisprudence have explained that simply because products or services are similar does not mean they are in the relevant market. Rather, only those products that can constrain price increases (or decreases in quality or service) are properly considered to be in the relevant market.

The FTC's successful challenge to the Staples-Office Depot merger demonstrates the importance of the issue of constraint to relevant market analysis. *See FTC v. Staples, Inc.*, 970 F. Supp. 1066 (D.D.C. 1997). As in this case, Staples' consumers shopped at other formats, and office supply superstores priced checked other stores. Beginning with the proposition articulated in the Supreme Court's seminal *duPont* decision that "an element for consideration as to cross-elasticity of demand between products is the

responsiveness of the sales of one product to price changes of the other," the Court concluded that even though post-its, paper pads and other products were sold at many different locations and at different types of stores, there was a degree of specialized (*i.e.*, "localized") competition between office superstores that caused each to price constrain the other in a way that other office supply retailers did not. *See Staples,* 970 F. Supp. at 1074 (internal quotations and citations omitted). The court rejected the defendants' attempt to broaden the relevant market, holding that **"the mere fact that a firm may be termed a competitor in the overall marketplace does not necessarily require that it be included in the relevant product market for antitrust purposes."** *Staples,* 970 F. Supp. at 1075 (emphasis added).

By unhinging the relevant market inquiry from the question of constraint, the decision below is inconsistent with previous decisions of this Court and effectively reverses decades of antitrust merger jurisprudence. For example, this approach would permit a merger of Coca-Cola and Dr Pepper because consumers drink water and other liquids (contrary to *FTC v. Coca Cola Co.*, 641 F. Supp. 1128, 1132 (D.D.C. 1986), *vacated mem. as moot*, 829 F.2d 191 (D.C. Cir. 1987) (enjoining merger)).

Moreover, the lower court failed to consider the traditional *Brown Shoe* factors when defining the relevant product market in this case. Of course, *Brown Shoe* stands for the proposition that a relevant market analysis requires an examination of, *inter alia*, distinct consumer characteristics, industry recognition, product characteristics, distinct product prices, specialized sellers, and unique production facilities. *Brown Shoe v. United States,* 370 U.S. 294 (1962). *See Rothery Storage & Van Co. v. Atlas Van Lines,*

Inc., 792 F.2d 210, 219 (D.C. Cir. 1986) (*Brown Shoe's* "submarket indicia are viewed as proxies for cross-elasticities [and] assist in predicting a firm's ability to restrict output and hence to harm consumers."); *see also FTC v. Swedish Match*, 131 F. Supp. 2d 151, 156 (D.D.C. 2000); *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 45 (D.D.C. 1998); *Staples*, 970 F. Supp. at 1075 ("[W]ell-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes.") (internal quotations and citations omitted). The lower court received scores of documents—which it failed to even acknowledge in its opinion—from the parties recognizing a separate and distinct PNOS relevant market. As Judge Bork has instructed, such evidence is particularly relevant: "[I]ndustry or public recognition of the submarket as a separate economic unit matters because we assume that economic actors usually have accurate perceptions of economic realities." *Rothery*, 792 F.2d at 219. The court below substituted its own judgment of the market for that of the parties who regularly compete against each other for customers, by offering lower prices and wider selection of premium and natural organic foods, and by offering a distinct shopping environment. Indeed, Whole Foods' documents were replete with suggestions that this competition from Wild Oats—which served to depress its margins—was the driving force behind the acquisition.

If the district court had followed the instruction of this Court to evaluate those factors, it would have found a relevant market including only PNOS stores, like the parties. The FTC demonstrated Whole Foods' and Wild Oats' marketing philosophy centers on health and sustainability-oriented "lifestyle" retailing. This approach is built around service, superior quality, amenities, knowledgeable personnel, trustworthiness (*e.g.*, in actually implementing natural, organic, and sustainable strategies in product

offerings) and a store "environment" (*e.g.*, ambience and experience) that is very different from conventional supermarket shopping. Moreover, the documents unambiguously reflected the parties' belief that PNOS stores were distinctly different from—and did not compete directly against—traditional supermarkets with natural/organic selections because such traditional supermarkets could not match the breadth and depth of selection offered by PNOS-focused chains like Whole Foods and Wild Oats.

II. THE COURT ERRED IN ELEVATING THEORY OVER FACT BY IGNORING CONTEMPORANEOUS BUSINESS DOCUMENTS DEMONSTRATING THE ANTICOMPETITIVE PURPOSE OF THE MERGER

Documents are the crucible of antitrust litigation. The reasons are obvious: the parties' internal documents relate their contemporaneous beliefs on the nature of competition and reveal the motivations behind the strategies they adopt. As Judge Gesell explained a generation ago these types of documents expose the "business realit[ies]" critical to the workings of the market -- "how the market is perceived by those who strive to profit in it." *Coca-Cola Co.*, 641 F. Supp. at 1132.

The parties' documents in this case are compelling and crystal clear about the purpose of this acquisition. It is rare that there is explicit evidence of an intent to merge to extinguish competition – but this is that case. Whole Foods' CEO explained to his Board of Directors the primary reasons to acquire Wild Oats:

> By buying them we will . . . avoid nasty price wars in Portland (both Oregon and Maine), Boulder, Nashville, and several other cities which will harm our gross margins and profitability. OATS may not be able to defeat us but they can still hurt us. Furthermore, we eliminate forever the possibility of Kroger, Super Value, or Safeway using their brand equity to launch a competing national natural/organic food chain to rival us. . . . [Wild Oats] is the only

> existing company that has the brand and number of stores to be a meaningful springboard for another player to get into this space. Eliminating them means eliminating that threat forever, or almost forever. (FTC Complaint at 15)

Whole Foods explained that the reason it wanted to acquire Wild Oats was to avoid price erosion and to forestall competitive entry. There were no pro-competitive reasons articulated by Whole Foods for the acquisition and inexplicably, the court below never addresses this admission of anticompetitive intent.

The simple question never addressed by the court below is "what is the purpose of this acquisition?" Why is Whole Foods willing to pay over $500 million for a rival that it decries as high cost and inefficient? Why does this merger make sense if the parties agree there are no cost savings and efficiencies to be derived from the merger? Mr. Mackey's statements and other documents answer the question unequivocally: the purpose is to eliminate rivalry. *Compare United States v. Franklin Elec. Co.*, 130 F. Supp. 2d 1025, 1034 (W.D. Wis. 2000) ("[I]t's hard to imagine any reason other than the achievement of a dominant position in the market that would explain why Franklin Electric was willing to pay over $65 million" for a declining business.). Although a good motive will not justify a merger once it has been shown to be substantially anticompetitive, *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586, 607 (1957), "knowledge of intent may help the court to interpret facts and predict consequences." *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918). As the leading antitrust treatise observes: evidence of intent in a merger case may be particularly probative in helping determine whether the market "has been too broadly defined," or that "the acquired firm, though having a relatively small share, is a particularly disruptive force. . . ." Areeda, Antitrust Law ¶ 964c at 20 (2006). That is

why courts have relied on this type of evidence in enjoining potentially anticompetitive mergers.

By ignoring Mr. Mackey's pre-litigation statements, the court has permitted theory to trump fact, saying, in effect that the testimony of a retained economic expert is of greater probative value than that of the CEO who has successfully run the business for years. Economic testimony is relevant but it can not trump marketplace realities.

III. THE COURT ERRED BY CONSIDERING THE IMPACT OF THE MERGER SOLELY ON "MARGINAL CONSUMERS"

Section 7 of the Clayton Act prevents mergers that will result in a substantial lessening of competition "in any line of commerce or . . . in any section of the country." 15 U.S.C. § 18. The purpose of the statue is expansive: to protect competition in any line of commerce and protect any set of consumers. *See FTC v. H.J. Heinz Co.*, 246 F.3d 708, 718 (D.C. Cir. 2001) (reversing district court for failing to recognize impact on wholesale competition of baby food, even if there was no effect on retail competition). The district court erred in ignoring the "core customers" in its analysis. Instead, the decision narrowly focused upon a smaller subset of "marginal consumers" who already rely on numerous alternatives to the stores operated by the parties to the transaction.

The District Court's misguided marginal customer analysis resulted in the conclusion that the merger is not problematic - because for that set of marginal consumers, there are other alternatives. However, that is simply a tautology, one wholly inconsistent with the purpose of Section 7 to protect competition for *any* set of consumers.

In any merger different groups of consumers will be impacted in different fashions. In this case, the court below focuses on the effect of the merger on "marginal

consumers" arguing that "the effect of the proposed merger on marginal consumers is more important than the effect on . . . core customers, as it is the marginal consumers for whom the stores must and do compete most vigorously." (Op. at 38).[1] On the other hand, the FTC persuasively argues that the key set of consumers are "core consumers" that "have decided that natural and organic is important."

Section 7 of the Clayton Act protects competition in any line of commerce in any product or geographic market. Clearly, that also means that any group of consumers are protected from the anticompetitive effects of a merger. For example, in *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 47 (D.D.C. 1998) the court examined the impact of two mergers of drug wholesalers on various consumers, including chain drugstores, hospitals, buying groups and independent drug stores. Since some chain drug stores could self-distribute they were clearly "marginal" since they had other alternatives. Yet the court enjoined the merger because the other sets of consumers were inframarginal. The legal standard adopted by the court below would have permitted the drug wholesaler merger solely because some consumers had alternatives. Indeed, this standard would justify virtually every merger because it is almost impossible to contemplate a situation in which no marginal group of consumers has an element of choice. Even a 100% monopolist sets a price that takes into account the possible exit of a marginal consumer.

IV. THE BENEFITS OF A STAY FAR OUTWEIGH ANY THEORETICAL HARM FROM DELAYING THIS MERGER

Fundamentally, the question before this Court is an equitable one – whether the

[1] The sole support for this argument is the defendants' expert's testimony. There is no legal or economic support for the proposition. (Op. at 27, citing Dr. Scheffman).

public interest supports a stay pending appeal so that the legal errors below can be assessed by this Court. However, this case is unlike other recent merger cases because of the lack of any proposed or cognizable efficiencies. For example, in *Heinz* the equitable question was more complex because of the significant proposed efficiencies stemming from the acquisition of Beech-Nut by Heinz. But even with these articulated potential efficiencies, this Court enjoined the merger observing that permitting the merger would eliminate a rival forever, whereas an injunction was not too great a burden because if "the merger makes economic sense now, the appellees have offered no reason why it would not do so later." *FTC v. H.J. Heinz Co.*, No. 00-5362, 2000 WL 1741320, at *2 (D.C. Cir. Nov. 8, 2000). Of course, in *Heinz*, this Court was discussing the delay caused by an administrative trial that might have taken several years; in this case the delay to hear an appeal might just be a matter of months. Thus, as in *Heinz*, an injunction pending appeal is necessary because "[t]he public interest in enforcement of the antitrust laws is strong; any injury to competition from going forward with the merger would plainly be irreversible, while the same cannot be said for any loss to competition from its delay." *Id.*

V. CONCLUSION

The Amici consumer groups respectfully urge this Court to grant the FTC's request for a stay pending appeal.

Dated: August 23, 2007

Respectfully submitted,

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