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FEDERAL TRADE COMMISSION

In the Matter of:)
Staples, Inc.)
a corporation)
and) Docket No.
Office Depot, Inc.,) 9367
a corporation.)

Monday, January 4, 2016

Room 532
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, D.C.

The above-entitled matter came on for
hearing, pursuant to notice, at
2:10 p.m.

1 APPEARANCES:

2

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1 PROCEEDINGS

2 (2:10 p.m.)

3 JUDGE CHAPPELL: Docket 9367, Staples and
4 Office Depot. Is everybody in the right place?
5 Okay.

6 We will take appearances of the parties
7 first. We will start with the government.

8 MS. REINHART: Good afternoon, Your
9 Honor, Tara Reinhart for Complaint counsel. With
10 me at table I have Jeff Loughlin and Stelios
11 Xenakis.

12 JUDGE CHAPPELL: And for Respondents?

13 MR. PERRY: Good afternoon, Your Honor,
14 Jeff Perry from Weil Gotshal for Respondents,
15 Staples. Here with me is my colleague Megan
16 Granger.

17 MR. REILLY: Matt Reilly from Simpson
18 Thacher.

19 JUDGE CHAPPELL: Mr. Reilly.

20 MR. REILLY: Nice to see you again, Your
21 Honor.

22 JUDGE CHAPPELL: You were usually --

23 MR. REILLY: I was usually there. They
24 kicked me out, and I ended up on this side of the
25 table.

1 JUDGE CHAPPELL: Changed teams. All
2 right.

3 MR. REILLY: Matt Reilly, Simpson Thacher
4 on behalf of Office Depot. With me is Andrew Lacy
5 from Simpson Thacher as well.

6 JUDGE CHAPPELL: Thank you.

7 MR. REILLY: Nice to see you again.

8 JUDGE CHAPPELL: Let's talk first about
9 the ancillary federal action, start with the
10 government. You can maybe update me on the status
11 of all of that.

12 MR. REILLY: Certainly, Your Honor. The
13 FTC filed a complaint on December 8th, and it has
14 been assigned to Judge Emmet Sullivan here in the
15 District of D.C., and we have a schedule set in
16 that case that contemplates the close of fact
17 discovery around the middle of February with expert
18 discovery following on and a hearing date set for
19 March 21st.

20 JUDGE CHAPPELL: Anything to add to that?

21 MR. PERRY: No, Your Honor.

22 JUDGE CHAPPELL: Any of the parties keep
23 me updated on the action, just follow up on any
24 substantive orders or rulings that come out.

25 MS. REINHART: We will do so, Your Honor.

1 JUDGE CHAPPELL: Pursuant to 3.41(f) the
2 pendency of a collateral federal court action does
3 not stay the proceedings, unless a court of
4 competent jurisdiction or the Commission for good
5 cause so directs.

6 So my question is, first of all for the
7 government, are you prepared to tell me what your
8 plans are if the injunction is not granted?

9 MS. REINHART: We would have to consider
10 our options at the time, but, of course, if there
11 is a legal issue we would take an appeal.

12 JUDGE CHAPPELL: All right. Respondents,
13 are you prepared to tell me what your clients plan
14 to do if the injunction is granted?

15 MR. PERRY: Yes, Your Honor, Jeff Perry.
16 Unfortunately if the injunction is granted, I
17 expect the transaction will be terminated, Your
18 Honor.

19 JUDGE CHAPPELL: Based on what I just
20 heard, it appears that at some point our trial may
21 become a moot point. If either party doesn't plan
22 to pursue the merger case after the Federal Court
23 proceeding, perhaps that constitutes good cause.

24 So I am wondering if we don't have a
25 ruling, and I am -- I saw where I think the judge

1 said he anticipates a ruling in May. And we're set
2 for early May.

3 And I am wondering if we don't have a
4 ruling, do the parties intend to file a joint
5 motion to stay this proceeding pursuant to rule
6 3.41?

7 MR. PERRY: Your Honor, our hope is that
8 that will not become an issue. If it does, as Your
9 Honor suggests, I believe that will be the position
10 of Respondents. Obviously I can't speak to whether
11 that motion will be joined or not.

12 JUDGE CHAPPELL: I am anticipating you
13 are going to say you not sure today.

14 MS. REINHART: Well, we're not sure
15 today, but as Mr. Perry said, he has no intention,
16 as I heard him say, if indeed the injunction is
17 granted, it is -- we would take the Court's
18 decision on how to move forward.

19 I think it is our intention to litigate
20 all the way through, so we would keep our options
21 open.

22 JUDGE CHAPPELL: Well, if a joint motion
23 is not agreed to, I see no reason why one party
24 cannot file the motion.

25 MR. PERRY: Thank you, Your Honor.

1 JUDGE CHAPPELL: Let's talk about the
2 scheduling order. I'm sure you received the draft
3 and the comments. I saw a few modifications to the
4 dates on additional provisions.

5 I wanted to note that the joint proposal
6 set two deadlines on a Saturday, April 23rd and
7 30th, and this is for exchange of expert reports
8 and proposed stipulations.

9 That's an exchange date, not a filing
10 date. Did the parties intend for those dates to be
11 Saturday? Is that fine?

12 MS. REINHART: We did, Your Honor. We
13 chose these dates just for the convenience of the
14 parties and to give everyone more time on the
15 experts and the schedule.

16 MR. PERRY: That's right, Your Honor.
17 We're comfortable with those dates. Thank you.

18 JUDGE CHAPPELL: Other than that, all the
19 modifications that were submitted are acceptable,
20 and I will incorporate them into the order that I
21 will issue shortly.

22 MR. PERRY: Thank you, Your Honor.

23 JUDGE CHAPPELL: I trust the parties have
24 attempted to settle this matter. Who would like to
25 update me on the status of settlement discussions?

1 I will start with the government.

2 MS. REINHART: Thank you, Your Honor.

3 Yes, there have been discussions between the
4 parties about settlement. And, in fact, an offer
5 and an increased offer were made by the
6 Respondents, and the Commission has expressed that
7 the offer is not acceptable for a couple of
8 reasons; one being that the -- Staples is intending
9 to divest some contracts and, in other words, there
10 is an assignment of contracts and not a true
11 divestiture of physical assets of a business.

12 And, therefore, the remedy to the extent
13 there would be one is temporary because as those
14 contracts expire, then the customers could go back
15 to the combined Staples and Office Depot. It is
16 not a structural remedy.

17 And, second, the acquiring company is not
18 at the same level of competition providing direct
19 supply to the customers the way Staples and Office
20 Depot are.

21 Having said that, Your Honor, we are
22 continuing discussions.

23 JUDGE CHAPPELL: So your position, the
24 government's position as of today would be you are
25 only going to accept a structural remedy?

1 MS. REINHART:

2 Q. That's correct, Your Honor?

3 JUDGE CHAPPELL: All right. Complainant?

4 MR. PERRY: Your Honor, it won't surprise
5 you to know that I don't agree with the
6 characterization of our offer, Your Honor. It is a
7 substantial offer. It is not limited merely to
8 contracts.

9 There are additional assets, including IT
10 assets and important HR assets, but I don't suppose
11 you want to engage in detailed debate on that, Your
12 Honor. We have made that offer. We think not only
13 does it fully replicate competition, but it is
14 consistent with and relies upon the guidance of the
15 Commission's own statement in 2013.

16 That being said, if this case can be
17 settled on reasonable terms, we will do it, Your
18 Honor. Our discussions are ongoing.

19 JUDGE CHAPPELL: All right. Thank you.

20 MR. PERRY: Thank you, Your Honor.

21 JUDGE CHAPPELL: At this time I am going
22 to hear the overview of the case. I will allow
23 each side to make a presentation limited to 15
24 minutes. That time will be extended if time is
25 used based on my questions I may ask during your

1 presentation. We will start with the government.

2 MS. REINHART: Thank you, Your Honor. I
3 have very brief slides as well as hard copies to
4 hand out. May I approach?

5 JUDGE CHAPPELL: I don't need the slides
6 if the screens work. If you have a copy of the
7 slides, a member of my staff would like a copy.
8 Thank you.

9 MR. PERRY: May I pass one up as well?

10 JUDGE CHAPPELL: Yes. Thank you.

11 MS. REINHART: May it please the Court,
12 Your Honor, the parties to this transaction are the
13 two largest suppliers of consumable office supplies
14 in the United States.

15 And they are the two most significant
16 suppliers to the very important segment of their
17 own customers, which are the large businesses that
18 buy these consumable office supplies for their own
19 use. We call them business-to-business or B-to-B
20 customers because they purchase not for resale but
21 for use in their own offices.

22 Before I move off this slide, let me give
23 you a quick overview. It is companies that are the
24 purchasers we're concerned about today, include
25 household names that have branch offices and retail

1 outlets that we all see walking around this
2 neighborhood. Staples and Office Depot are these
3 large businesses' top two choices for vendors and
4 many of these companies consider Staples and Office
5 Depot to be the only two viable choices.

6 The evidence will show that any third
7 option is a distant third option. And these large
8 business customers play Staples and Office Depot
9 off each other in lengthy bidding situations, and
10 that results for the customers in the best prices
11 and the most optimal services, things that they
12 require to keep their costs down.

13 If this deal were to be consummated,
14 there would be only one best option left and any
15 second viable option would be a distant second. So
16 these large business customers that count on
17 competition between Staples and Office Depot would
18 be harmed, and this is why the deal must be
19 stopped.

20 Consumable office supplies, that's what
21 we're concerned with here. And relevant product
22 market is consumable office supplies sold or
23 distributed to large B-to-B customers. These kinds
24 of supplies provide the daily sustenance for basic
25 office functions. You think of envelopes for a

1 bank, you think of pens for a retail store.

2 The companies use these supplies, they
3 discard them, and then they reorder more on a
4 constant basis. This is a cluster market. The
5 envelopes and pens that I just mentioned are not
6 themselves interchangeable with each other, but it
7 is appropriate to combine into a single market a
8 number of different products like these; where that
9 combination reflects the commercial reality. And
10 the commercial reality being that the customers buy
11 these consumable office supplies together.

12 The relevant market excludes adjacent
13 categories of things that are used in offices but
14 they are subject to different competitive
15 conditions and they are supplied by different sets
16 of vendors.

17 The one example is ink and toner. The
18 manufacturers of copiers in recent years have done
19 a good job of moving business away from Staples and
20 Office Depot to themselves, so they supply these
21 big customers not only the copiers and the
22 maintenance services but also the ink and the
23 toner, the consumable supplies that are necessary
24 to keep those copiers running.

25 That is just one example of an adjacent

1 category that is not included in the relevant
2 market.

3 Now, the evidence will show that the
4 needs of these large B-to-B customers are different
5 from others' needs. First of all, they buy on
6 behalf of all of their branch offices or outlets
7 across the country with the resulting large volumes
8 that allow them to negotiate the best prices.

9 And Staples and Office Depot are able to
10 provide those low prices because, as the largest
11 purchasers of office supplies from the
12 manufacturers and the wholesalers themselves, they
13 get the lowest costs.

14 These large B-to-B customers have
15 thousands of employees who purchase and use
16 supplies on a daily basis. And so control over the
17 purchasing and the delivery and the reordering is
18 essential to keeping costs down and to allow
19 employees to focus on doing their jobs without
20 having to worry about where they are going to get
21 their binders.

22 So these companies consistently require
23 significant value-added services. I will just name
24 a few. For example, desktop delivery. The
25 products come from Staples or Office Depot directly

1 to the employee who ordered them, so that employee
2 doesn't have to go down to a local centralized
3 supply location and figure out which of the things
4 that he or she ordered.

5 The customers also require customized
6 electronic catalogues. These are electronic
7 systems that are very sophisticated and are tied in
8 to the company's IT systems.

9 And this allows employees to order
10 directly what they need but only within the
11 confines of the products that are within the
12 contract. So it is not Staples or Office Depot's
13 entire catalogue on-line. It is just the products
14 that the company has designated may be purchased.

15 And another example of a required service
16 is detailed utilization reporting. Staples and
17 Office Depot allow the companies to monitor their
18 purchasing so that they can spot trends, they can
19 tell if they are buying more or less of a certain
20 product than they had expected, and they can make
21 cost saving adjustments so that employees are
22 steered away from expensive products to cheaper
23 ones or they can negotiate more discounts with
24 Staples or Office Depot because the company finds
25 it is buying more than it had planned to.

1 JUDGE CHAPPELL: Let me go back a second.
2 It says here next-day delivery on your slide. Are
3 you saying that these companies' employees actually
4 provide delivery or do they use someone like Fed Ex
5 or UPS?

6 MS. REINHART: So they, if they -- to the
7 extent they do not deliver themselves, they use
8 third-party distributors. The point is that the
9 products are coming overnight from the order, where
10 they have been ordered from -- to the companies.

11 JUDGE CHAPPELL: And are you aware if
12 both companies do this identically?

13 MS. REINHART: I am not aware if they do
14 it identically, Your Honor.

15 The final example I wanted to point out
16 from this slide is that the companies require
17 dedicated customer service. And in the industry,
18 this means there is one throat to choke, that's
19 what they say.

20 A manager at any location, whether it is
21 a company's branch office in New York or one in
22 Idaho can pick up the phone and call to report a
23 problem. And they get the same voice on the phone,
24 the same responsive person who will fix whatever
25 problem that is.

1 The large B-to-B customers will testify
2 that Staples and Office Depot are by far their two
3 best options to provide the lowest pricing as well
4 as these required services.

5 JUDGE CHAPPELL: Did you say froke to
6 choke?

7 MS. REINHART: Throat as in --

8 JUDGE CHAPPELL: Throat, all right.
9 Makes more sense. I don't know what a froke is.

10 MS. REINHART: I need to enunciate
11 better, perhaps, Your Honor. Okay.

12 Unlike small business customers, which
13 buy on a purchase order by purchase order basis,
14 large business customers go through a lengthy
15 multi-step RFP process with their potential
16 suppliers' vendors. They negotiate price. They
17 negotiate the range of services. And they
18 negotiate additional monetary incentives to give
19 the vendor the business.

20 And they get the best price and the best
21 terms because they have Staples and Office Depot
22 bid against each other; usually through multiple
23 rounds of negotiation.

24 These customers employ procurement
25 specialists whose job it is to ensure they get what

1 they bargained for. Not so with small businesses.
2 Small businesses do not receive monetary incentives
3 or even significant discounts.

4 For all the reasons I have just stated,
5 the sale and distribution of consumable office
6 supplies to large B-to-B customers is the relevant
7 product market.

8 Because of their nationwide footprint,
9 Staples and Office Depot are able to serve these
10 large customers that have locations scattered from
11 shore to shore or at least across multiple regions.

12 They provide uniform pricing to these
13 customers regardless of the location of the office
14 that is actually receiving and using the supplies.
15 The large business customers and other supply
16 vendors will testify that large B-to-B customers
17 prefer a single national supplier over the multiple
18 regional or local vendors.

19 It goes back to the one throat-to-choke
20 concept as well as just the ability to manage the
21 number of locations that are ordering receivable
22 supplies.

23 JUDGE CHAPPELL: Let me talk about this
24 uniform pricing you referred to.

25 If I understood your point, if a customer

1 is located in all 50 states, that customer will get
2 the same price in Hawaii as in Idaho?

3 MS. REINHART: That is my understanding,
4 Your Honor.

5 JUDGE CHAPPELL: But what about not the
6 same company, is your position that a customer in
7 Idaho pays the same as a customer in Hawaii for the
8 same product?

9 MS. REINHART: So we're talking two
10 unrelated customers, Your Honor?

11 JUDGE CHAPPELL: Yes.

12 MS. REINHART: They do not necessarily
13 get the same pricing. There are a whole host of
14 factors that go into what prices are ultimately
15 negotiated.

16 JUDGE CHAPPELL: Your position is on the
17 nationwide company with headquarters in Atlanta, my
18 people all over the country will pay the same
19 regardless of where the product is delivered to?

20 MS. REINHART: Yes, Your Honor, that is
21 one of the services that Staples and Office Depot
22 provide to these large customers.

23 So the company's own documents state that
24 they are the only two real choices for services
25 across the country for these companies that have

1 this nationwide footprint. And the testimony of
2 the customers and other supply vendors will confirm
3 that as well.

4 And so, Your Honor, the relevant
5 geographic market is the United States.

6 Many large B-to-B customers are expected
7 to testify that they are concerned that they will
8 be harmed by this deal. The proposed merger would
9 take away one of their two top choices of vendors,
10 and it would leave these large businesses with a
11 supplier, single supplier with an overwhelming
12 percentage of sales in the market, at least
13 70 percent or more.

14 This combined firm would dwarf its next
15 largest competitor. That would result in higher
16 prices and would prevail absent a merger. The
17 evidence will show it is unlikely that other viable
18 vendors would replace the competition lost from
19 this proposed merger.

20 JUDGE CHAPPELL: Is this next largest
21 competitor you referred to a nationwide competitor?

22 MS. REINHART: I'm sorry, Your Honor, I
23 didn't hear you.

24 JUDGE CHAPPELL: You said the next
25 largest competitor would have 5 percent of the

1 market. Is that a nationwide competitor?

2 MS. REINHART: It is not. It is a
3 regional competitor, Your Honor.

4 As I mentioned at the outset, Your Honor,
5 the parties have proposed a fix. They originally
6 proposed selling 500 million dollars in customer
7 contracts to an acquiring company and then they
8 recently announced they would go as high as 1.25
9 billion in sales as a means of addressing the FTC's
10 concerns, but the problem, as I said earlier, are
11 two problems, actually.

12 JUDGE CHAPPELL: I don't want to get into
13 anything that is proprietary.

14 MS. REINHART: I agree, Your Honor.

15 JUDGE CHAPPELL: I am just wondering if
16 the acquiring company that was slotted in to take
17 the proposed contracts, that's an existing company,
18 correct, not a new company?

19 MS. REINHART: It is an existing company,
20 Your Honor. And just without getting into
21 confidentiality concerns, I can tell you that a
22 concern about the acquiring company is just that
23 they do not compete at the same level of commerce
24 as Staples and Office Depot.

25 In other words, they do not currently

1 supply directly to these big customers.

2 It is speculative as to whether they
3 would be able to provide the same level of
4 necessary services at the same level of pricing.

5 JUDGE CHAPPELL: Let me ask you about
6 your market analysis. I hear you talking a lot
7 about apparently on-line ordering, on-line
8 business.

9 Are you including the people in the
10 office, three or four of them take a half a day, go
11 get some coffee and go to Office Depot and Staples
12 and buy office supplies? Are they included in your
13 market?

14 MS. REINHART: The consumers in our market
15 are the large business entities themselves, and, of
16 course, all of the thousands of their employees are
17 the ones who are actually doing the ordering, like
18 you say.

19 Having the on-line catalogues allows them
20 to do so without leaving their desks, but one of
21 the other services that the companies provide to
22 the customer is the ability of those employees to
23 walk down the street if they need to and buy from
24 either a Staples or Office Depot outlet.

25 JUDGE CHAPPELL: So walk-in traffic is

1 included in your market?

2 MS. REINHART: I think that services that
3 are provided are intended to avoid the walk-in
4 traffic, Your Honor. That's one reason why --

5 JUDGE CHAPPELL: Why do they have all
6 those stores, though, if they don't want people to
7 walk in?

8 MS. REINHART: Why do they have all the
9 stores? Well, Your Honor, it is, it is the
10 employee's ability to walk down the street if they
11 need to, in other words, for an emergency. They
12 can buy on the contract that way.

13 But the bulk of the sales that are done
14 under these contracts are done through the on-line
15 portal.

16 JUDGE CHAPPELL: I am just trying to
17 drill down into exactly what market the government
18 is proposing here. Sounds like you are focused on
19 on-line contracts. It doesn't sound like to me you
20 are talking about these people that go in and buy
21 their supplies maybe once a month without a
22 contract.

23 MS. REINHART: I apologize, Your Honor.
24 I do understand your question at this point.

25 We are not alleging harm in the retail

1 sector. We are alleging the harm is through the
2 business consumers, specifically the large
3 businesses that buy for their own use.

4 To the extent that the employees of those
5 large businesses buy on-line or walk down the
6 street to buy from Staples or Office Depot, they
7 are included in the market.

8 But what is excluded are people who are
9 employees of the small businesses who regularly
10 just go to Staples and Office Depot or any other
11 provider like Walmart to get their suppliers.

12 JUDGE CHAPPELL: Would the Department of
13 Defense be considered a customer in your eyes?

14 MS. REINHART: Government entities have a
15 lot of similarities to these big customers, big
16 business customers that are the market. A lot of
17 the government entities that we have seen actually
18 have local preferences. They buy from local
19 suppliers, small business preferences required by
20 law.

21 JUDGE CHAPPELL: How about the government
22 entity you are standing in the middle of?

23 MS. REINHART: Exactly. The FTC buys
24 from a small supplier. And so while there are a
25 number of government entities that we have seen

1 that have the indicia of the big B-to-B businesses,
2 not all of them do, and they are not considered
3 part of the market.

4 JUDGE CHAPPELL: All right. Thank you.

5 MS. REINHART: Okay. Your Honor, I think
6 I already addressed the fix in my opening remarks
7 before I started this. So that concludes my
8 presentation, unless you have further questions.

9 JUDGE CHAPPELL: Nope. Thank you.

10 For Respondent, are we going to have one
11 or two Respondents?

12 MR. PERRY: Just one, Your Honor, Jeff
13 Perry. I will be giving remarks on behalf of both
14 Respondents. Mr. Reilly won't be shy if he has
15 anything to add, I'm sure.

16 JUDGE CHAPPELL: You need to clear the
17 screen.

18 MR. PERRY: Thank you, Your Honor.
19 Success.

20 May I begin, Your Honor?

21 JUDGE CHAPPELL: Go ahead.

22 MR. PERRY: Your Honor, there isn't time
23 to address every area of disagreement, you won't be
24 surprised to know, with Complaint counsel. So I
25 want to focus on four areas I would like to

1 address.

2 The first area is the motivation --

3 JUDGE CHAPPELL: You said I won't be
4 surprised, correct?

5 MR. PERRY: Correct. I figured you knew
6 that already, Your Honor.

7 The first point is where this transaction
8 began. Your Honor, this transaction is motivated
9 by efficiencies that will benefit customers. And
10 this transaction is further supported by the FTC's
11 own admissions in 2013, and that wasn't mentioned
12 by Complaint counsel, but I want to talk about
13 public statement and public guidance this agency
14 put out in 2013 when it closed its investigation of
15 the Office Depot and OfficeMax transaction.

16 Second point, Your Honor, Complaint
17 counsel's relevant market. Your Honor, this
18 relevant market is a fairy tale. It has been
19 created for purposes of this litigation. It is not
20 consistent with the commercial reality and how
21 competition takes place in this industry. And it
22 focuses on a tiny fraction of Respondents'
23 customers.

24 JUDGE CHAPPELL: You are not saying that
25 they created a market; you are saying the

1 boundaries of the so-called market are a fairy
2 tale; is that what your position is?

3 MR. PERRY: Yes, Your Honor, this
4 collection of customers and this collection of
5 products is a product market made for this
6 litigation. It does not comport with how these
7 companies do business or how suppliers and
8 customers buy and sell these services. That's my
9 point, Your Honor.

10 JUDGE CHAPPELL: So you are saying that
11 the problem with the government's market is more of
12 a problem from the company's angle or from the
13 consumers' stand?

14 MR. PERRY: It is both, Your Honor. It
15 is both. It doesn't fit how these companies sell
16 these services. And it doesn't fit from a customer
17 side of that negotiating table how they think about
18 the contract and pricing and delivery to their
19 offices.

20 And, Your Honor, I will talk about that
21 more in detail, but I hope that gives you a brief
22 answer to your question.

23 Your Honor, in addition to the market, I
24 want to talk about the options that customers have
25 for the delivery of consumable office supplies.

1 And on top of that, the additional tools that these
2 large customers have to ensure competitive pricing.

3 And those two points, Your Honor, were
4 admitted by the FTC in 2013. And we will show you
5 that language, Your Honor.

6 Your Honor, to start at the beginning,
7 the purpose and effect of this acquisition, Your
8 Honor, is to reduce costs but not to just reduce
9 costs, to reduce costs and reinvest those savings,
10 Your Honor, in lower pricing, better service, and
11 greater value for our customers.

12 And when Staples and Office Depot, not
13 for purposes of this litigation, but back in 2014,
14 when they were evaluating this transaction and
15 advising their respective boards, they did their
16 own analysis. Staples estimated at least 1 billion
17 dollars a year in savings from this deal. That's a
18 huge number, Your Honor.

19 Office Depot, having benefited from the
20 learnings of integrating the Depot Max merger in
21 2013 and the cost savings that that produced,
22 Office Depot estimated 1.5 billion in synergies,
23 Your Honor.

24 And every third-party --

25 JUDGE CHAPPELL: How many -- but now you

1 have actual numbers. They estimated 1.5 billion.

2 What was the reality?

3 MR. PERRY: I'm sorry, Your Honor. What
4 I meant to say is informed by the experience from
5 2013, that 1.5 billion is an estimate for this
6 transaction.

7 Mr. Reilly can speak to the Depot Max
8 synergies. I think the public guidance is annual
9 synergies in the range of 700 million dollars.

10 MR. REILLY: That's correct, Your Honor.
11 And Office Depot has shown, if you look at this on
12 a regular basis, that their efficiencies estimates
13 from the Office Depot/OfficeMax transaction, the
14 efficiencies have been exceeded, gone up further.
15 And they are in a more quicker manner as well.

16 So that's why they are a higher estimate
17 of efficiencies here. And from the past
18 transaction from two years ago, Office Depot has
19 realized a large number of efficiencies that have
20 been passed on to consumers.

21 JUDGE CHAPPELL: So the estimate of the
22 previous merger, the estimates were not just borne
23 out but they were exceeded?

24 MR. REILLY: They were exceeded and
25 obtained more quickly than they expected, Your

1 Honor. And that guidance allowed them to estimate
2 the proposed efficiencies and synergies in this
3 transaction.

4 JUDGE CHAPPELL: Thank you.

5 MR. PERRY: Thank you, Your Honor. And
6 it is not just Staples and Office Depot. Every
7 third-party analyst who has looked at this, as I
8 said, across the board has estimated similar or in
9 many cases higher savings. We have a couple
10 examples here, but I could have given you 10 or 15,
11 Your Honor.

12 Examples are Credit Suisse and KeyBanc,
13 1.44 billion could be as high as 2 billion. These
14 savings are real, Your Honor.

15 Your Honor, efficiencies are critically
16 important in this industry because this is an
17 industry where demand is declining. We all use
18 pens and pencils and papers less, and we use iPads
19 and e-mail more.

20 And on top of the declining demand, Your
21 Honor, there is intense competition and growing
22 competition in this industry, as the FTC itself
23 admitted in 2013. And in an industry like that, of
24 declining demand and intense competition, the name
25 of the game is to cut costs and offer more value

1 and lower pricing to your customers. Again, that
2 is what this deal is about, Your Honor.

3 So let's look, Your Honor, if we could at
4 the FTC 2013 statement. This wasn't mentioned by
5 Complaint counsel. Your Honor, this is the most
6 on-point merger precedent in the history of a
7 merger case.

8 In 2013 the FTC investigated this market,
9 these products, these customers for seven months.
10 And when it closed that investigation concluding
11 that it would not result in competitive harm, it
12 put out public guidance to the business community.

13 And, Your Honor, these companies, Staples
14 and Office Depot, relied upon that guidance. And
15 on top of that, Your Honor, there are factual
16 findings in the Commission's statement that were
17 true in 2013, they are more true today, and they
18 undermine any theory of competitive harm.

19 So here is what the Commission said, Your
20 Honor, in 2013. It admitted that a host of non-OSS
21 competitors, and what that means, Your Honor, OSS
22 competitors are Staples, Office Depot, OfficeMax,
23 that stands for office supply super stores, it
24 relates more to the retail side of the business,
25 but the Commission in talking about this B-to-B

1 side of the business said that other competitors, a
2 host of them, provide strong competition for
3 multi-regional and national customers. Those are
4 the large customers.

5 So I understand Ms. Reinhart suggested
6 that the third largest competitor has a tiny market
7 share, and it is regional. The FTC said there are
8 --

9 JUDGE CHAPPELL: But at the time one of
10 those competitors was Staples, correct?

11 MR. PERRY: Yes, Your Honor, Staples
12 certainly was another competitor at the time, but
13 none of these statements relate to Staples.
14 Because they all say a host of non-OSS competitors.
15 And Staples is an OSS competitor.

16 So this statement says a host of other
17 firms provide strong competition for these
18 customers, the same ones at issue. The FTC
19 admitted in 2013 that these non-OSS competitors are
20 growing in number and strength and have
21 demonstrated the ability to win large accounts.
22 This is the same accounts we're talking about here,
23 Your Honor.

24 The FTC admitted as well in 2013 that
25 these non-OSS competitors win business in a

1 substantial number of contracting opportunities.
2 And on top of that, the large customers, the same
3 customers at issue today, have a variety of tools
4 to ensure that they receive competitive pricing.

5 JUDGE CHAPPELL: I understand we're
6 talking about non-office supply super stores, but
7 in this same statement you are talking about, did
8 they identify who the remaining office supply super
9 stores were?

10 MR. PERRY: The OSS term refers generally
11 to Staples, Office Depot, and OfficeMax. And that
12 is a relative, as you may know, of the 1997 case
13 where there was a merger.

14 And the question before the court at that
15 time was the retail stores, consumers.

16 These statements all relate to the
17 Commission's 2013 investigation on the B-to-B side,
18 selling to businesses as Ms. Reinhart said. The
19 same product, the same product market at issue
20 here. And these statements are all talking about
21 other competitors, so OSS is a shorthand, but what
22 all of this means is if you put aside Staples and
23 Office Depot and OfficeMax, there are a host of
24 other competitors who provide strong competition,
25 growing in number and strength, with a demonstrated

1 ability to win these accounts. These are the same
2 issues before the court here, Your Honor.

3 And, Your Honor, I want to talk if I
4 could about the customers because I mentioned when
5 I first began that this case relates to a small
6 fraction of Staples and Office Depot's customers.
7 And I wanted to give a little context.

8 This chart shows that Staples and Office
9 Depot have about 405,000 B-to-B customers. These
10 are all businesses. This is not Joe Schmow going
11 to buy for his home. These are businesses.

12 Now, if you look at business customers
13 who purchase more than a million dollars a year, it
14 comes down to 1374 customers. And if you look at
15 the FTC's market, as we understand it, and we have
16 run the numbers, there are 454 customers,
17 businesses in the FTC's alleged market. That
18 is .1 percent of Staples' and Office Depot's
19 business customers.

20 And what that means, Your Honor, is that
21 even before we start the trial, we know
22 unquestionably that all the individual consumers
23 who shopped in stores and on-line and 99.9 percent
24 of business customers will be better off as a
25 result of this acquisition or, at worst, not

1 impacted. That's where we start.

2 And when we look at this one-tenth of
3 1 percent of our business customers, that's the
4 relevant market, and I know Ms. Reinhart mentioned
5 that many customers consider Staples and Office
6 Depot is their best options, but those allegations,
7 Your Honor, are based largely on 21 customer
8 declarations; seven Staples customers and 14 Office
9 Depot customers who have submitted declarations
10 either supporting Complaint counsel's case or
11 expressing concern about the merger.

12 Now, those small numbers, Your Honor, can
13 hardly be representative of even this .1 percent,
14 let alone business customers more generally.

15 Now, Your Honor, if you look at
16 the .1 percent, these are the largest, most
17 powerful customers we have. In many cases these
18 are the largest, most powerful companies in the
19 country. These are the Fortune 100-type companies.

20 These customers today on average pay the
21 lowest prices. They have numerous alternatives, as
22 the FTC admitted, and they already multi-source
23 today. Your Honor gave one example of people at a
24 business going across the street. That's true on a
25 much grander scale even because none of these

1 businesses buy all of these consumable office
2 supplies from Staples or Office Depot.

3 They send people to the store. They have
4 the Topeka office order from the local supplier or
5 they order paper directly from a paper
6 manufacturer. Because they are a Fortune 100
7 company and they can do that today. And, of
8 course, if we raise prices, they can do that even
9 more.

10 Your Honor, the evidence will show in
11 this case that these Fortune 100 companies, these
12 top 454 customers are fully capable of defending
13 against higher prices for the delivery of these
14 basic supplies like paper clips.

15 Now, Your Honor, I want to talk about the
16 definition of the relevant market. And
17 Ms. Reinhart discussed this. And she talked about
18 paper and ink and toner. And that is an example I
19 want to highlight for a second because one of the
20 reasons -- and Your Honor asked about this -- that
21 this market doesn't align with how competition
22 takes place is because the market excludes a huge
23 range of products, in many cases half or more than
24 half of what the customers are actually buying from
25 Staples or Office Depot.

1 So what does that mean? So their market,
2 consumable office supplies, has paper in the
3 market, ink and toner out of the market. Now,
4 those products are negotiated together as part of
5 the same contract. The pricing for those products
6 is not determined independently. It is determined
7 as part of everything else that goes into the
8 contract.

9 And those products are literally
10 delivered on the same trucks to the same customers
11 to the same loading docks. Splitting them up
12 doesn't make sense here, Your Honor. And the
13 impact of that is that it ignores significant
14 competition from the likes of HP and others for our
15 most significant product, ink and toners,
16 20 percent in many cases of what these large
17 customers buy from us.

18 And it pushes that competition to the
19 side but, Your Honor, that is part of how these
20 contracts are made. That's part of how competition
21 works.

22 The other point on relevant market, Your
23 Honor, the market has changed.

24 JUDGE CHAPPELL: Do I understand you to
25 say that ink and toner is still a big part of your

1 business?

2 MR. PERRY: It is, Your Honor. It is
3 about 20 percent.

4 Your Honor, the other point I want to
5 make about the relevant market is it changed. And
6 I don't know why. But in 2013 the Commission in
7 its public guidance was very clear, it said that
8 consumable office supplies, the same market here,
9 includes these products and it gives examples. And
10 it specifically says ink and toner.

11 In 1997 the case involving not B-to-B
12 business but retail stores, again, ink and toner is
13 out of the market. And Complaint counsel's own
14 witnesses, Your Honor, we expect, based on what we
15 have seen, many of them will not agree with this
16 product grouping that says papers in and ink and
17 toners out.

18 JUDGE CHAPPELL: So what is your bottom
19 line, though, if you include ink and toner in the
20 market, how does that change the numbers?

21 MR. PERRY: The market shares go down
22 significantly, Your Honor. It is very hard for us
23 to gather market share information because the
24 truth of the matter is we don't know who our
25 customers are buying other products from in a

1 systematic way.

2 I will show you the best sources we have
3 for that information, but we know unquestionably
4 that this carving out of the market drives up the
5 shares.

6 So, Your Honor, the .1 percent at issue,
7 this is a sampling of the kinds of competition they
8 have and suppliers they have available to them.
9 They have independent office products dealers.
10 And, Your Honor, I will show you the web sites of
11 these companies.

12 They are not regional. They say they can
13 deliver nationally. And the FTC in 2013
14 specifically said that a host of them can deliver
15 to multi-regional and national customers. That's
16 the FTC's admission.

17 Eighteen of these others dealers, not
18 Staples and Office Depot, today -- these are just
19 the ones we're aware of -- today are serving these
20 large customers with the same products, 18 other
21 firms that won this business, Your Honor, and they
22 work in conjunction with wholesalers. And
23 wholesalers are an important part of this industry.

24 Because these established wholesalers
25 give every competitor geographic access to the

1 entire country because they use their warehouses.

2 And we rely upon them as well, Your Honor.

3 So every dealer can deliver everywhere in
4 the country next day. Every dealer can deliver
5 every product that Staples and Depot have next day
6 because we rely on the wholesalers for delivery and
7 for products.

8 You asked about whether Staples and
9 Office Depot are doing that career delivery
10 internally to the customers? We at Staples
11 out-source about 95 percent of that, Your Honor.
12 It is not a unique special sauce that Staples has.
13 Office Depot out-sources about 90 percent of it.
14 These are third parties, like Fed Ex and UPS and
15 couriers that anyone can use. We don't own them.
16 We don't own them.

17 JUDGE CHAPPELL: So did I understand you
18 to say that there are simply located wholesalers,
19 and if someone buys a case of extra fine black
20 Sharpies, you buy from the wholesaler and have it
21 delivered to your customer?

22 MR. PERRY: It is a mix, Your Honor. So
23 to answer your question directly, there are some
24 products that Staples --

25 JUDGE CHAPPELL: I understand it is not

1 100 percent, but is that a significant portion of
2 your business that you are going to a third-party
3 wholesaler that another company may be using also?

4 MR. PERRY: It is a meaningful part. It
5 is not the majority of Staples' or Office Depot's
6 business. The very, very high volume SKUs, we buy
7 directly from vendors and stock in our warehouses.

8 But there is a huge long tail of SKUs.
9 So we may stock at Staples 50,000 or so products,
10 but we may -- we are able to deliver something
11 closer to a million products. The reason we do
12 that is in reliance and partnership with
13 wholesalers, just as an understanding.

14 In addition to wholesalers, Your Honor,
15 these large customers, in addition to going to
16 dealers, go directly to manufacturers. So if we
17 call up a Fortune 100 company after this
18 transaction and say we're going to raise your price
19 of paper, they are going to call the paper company,
20 Your Honor. They are just going to call the paper
21 company and get it delivered directly.

22 We are an intermediary. We don't make
23 the paper. We don't have the monopoly on the
24 paper. They will get it from another dealer or
25 they will go to the paper company.

1 There are also, Your Honor, cooperatives
2 of independent dealers. And some of these have
3 been born and developed even after the 2013
4 investigation. And the sole purpose and motivation
5 of these cooperatives is to achieve economies of
6 scale and serve large multi-regional, national
7 customers. That's another option.

8 Competitors in adjacent categories, Your
9 Honor, so the way this market is so carved up, Your
10 Honor, with consumables, you get down to about half
11 or less than half of what we sell as part of the
12 market, part of the alleged market, and all of that
13 other stuff the FTC seems to acknowledge that these
14 customers can get somewhere else.

15 But those other competitors like Granger
16 is a large company that delivers, for example,
17 kitchen and break-room products and cleaning
18 supplies, those companies also sell paper clips and
19 paper and pens.

20 So if we raise prices to these customers
21 and you are a Fortune 100 company, you step down
22 one bay in your loading dock and you tell the next
23 company making a delivery, next time throw in paper
24 clips and pencils and pens. It is cost-effective
25 because they are already delivering to you. They

1 are already in your procurement system and doing
2 your utilization reporting and all these things
3 that Ms. Reinhart mentioned.

4 The other thing I will say for just a
5 couple minutes, Your Honor, is Amazon Business.
6 And Amazon is a significant competitive threat, as
7 we will talk about.

8 The next two slides, Your Honor, I won't
9 spend any time on them other than to say that this
10 is a sampling of competitors that they say can
11 serve large accounts and have customers in all 50
12 states.

13 And, Your Honor, to discredit these
14 competitors and not take them seriously, you have
15 to both believe that the FTC was flat wrong in 2013
16 and you have to believe that false advertising is
17 just rampant in this industry. I'm sure we would
18 hear from the FTC if that were the case.

19 But it isn't, Your Honor. These
20 competitors are legit. They will show up in
21 Staples' and Office Depot's internal documents.
22 And they are winning these customers today.

23 Briefly, Your Honor, Amazon. I wanted to
24 take a step back just for a minute and remind
25 ourselves that this is a delivery business. This

1 is a logistics business. This is about delivering
2 pens and pencils and paper clips to large
3 companies. There is no company in the world, with
4 all due respect to our clients, more sophisticated
5 or more capable than Amazon when it comes to
6 delivery logistics.

7 In office products, in particular, Amazon
8 has 6.9 million SKUs under their office products.
9 They have 65,000 roller ball pens. I misspeak a
10 lot, but I didn't misspeak there. They have 65,000
11 roller ball pens.

12 JUDGE CHAPPELL: You mean 65,000
13 different varieties?

14 MR. PERRY: Different varieties,
15 different SKUs of roller ball pens. Staples
16 doesn't have 65,000 products of anything. They
17 have more products, more distribution centers.
18 They have next-day delivery, which Ms. Reinhart
19 talked about, and they have also same-day delivery
20 in 14 markets and same-hour delivery in seven and
21 growing markets. And they have highly competitive
22 pricing.

23 And now, Your Honor, on the point of
24 Amazon's market share, and you talked about or the
25 FTC crediting not just sales that go through the

1 contract but sales that might be through other
2 sources, three guys on their coffee break go across
3 the street or someone goes on-line, third parties
4 have looked at that, Your Honor.

5 And in a survey in 2014, they looked at
6 Amazon's share of all of that for core office
7 products and they found that it was 45 percent,
8 that 60 percent, as many as 60 percent of
9 Respondents to the survey -- and not Respondents
10 us -- have purchased from Amazon in the last 12
11 months with usage growing the fastest in larger
12 companies.

13 And they asked those companies: What
14 percentage of you could envision buying all of your
15 office products from Amazon? And 46 percent said
16 definitely or probably. Definitely or probably.

17 Now you fast forward after that survey to
18 April of this year. And this year, Amazon launched
19 Amazon Business. This is a major new initiative,
20 you can tell by its name, specifically targeting
21 business customers; adding capabilities, adding
22 services, the very same things Ms. Reinhart was
23 giving a litany of that are unique to Staples and
24 Depot, they are either not unique any more or by
25 the week they are being crossed off the list, Your

1 Honor, and Amazon is specifically targeting
2 Staples.

3 And we have been called out by business
4 journals. You see one here on the left side of
5 slide 17, this is about Amazon entering the real
6 B2B market, "the E-marketplace gorilla is now
7 officially loose." You will see at the end of
8 this, "buckle your seatbelt, especially if you are
9 an incumbent distributor like Staples."

10 If there is any question about whether
11 they are coming after us, Your Honor, they are also
12 trying to steal our people. Amazon and its
13 recruiters are calling high-level marketing and
14 sales execs at Staples and Office Depot and trying
15 to steal them away to support this effort.

16 And you see their quotes to one of our
17 people saying that Amazon's goal is to take over
18 the B2B world.

19 And at a recent major conference, Your
20 Honor, this was in October, the director of sales
21 for Amazon Business gets on stage and talks about
22 the analysis they have been doing to analyze their
23 own presence with business customers.

24 And one of the key points he made is that
25 they are already serving the Fortune 100-type

1 customer.

2 And they say they are doing it in every
3 industry, Your Honor. Those are the same customers
4 at issue here.

5 Your Honor, the last point I want to make
6 on slide 20 relates to competition and market
7 share. I don't know the basis, frankly, for the
8 70 percent market share, but it doesn't reflect the
9 way competition really plays out. And it doesn't
10 reflect the type of contracts that these companies
11 have. Here is what I mean by that.

12 The customers when they come to us to
13 discuss a contract make it clear upfront that they
14 are under no obligation to buy anything, anything.
15 The contracts literally do not require the
16 customers to purchase any products. They can go
17 enter as many additional contracts as they want.
18 They can go on-line. They can go to other dealers.
19 They can go to stores. And they can go direct to
20 manufacturers.

21 And they do that. And the reason we know
22 they do that, Your Honor, is that they continue to
23 price-shop throughout the life of the so-called
24 contract.

25 And as they find lower prices, they come

1 back to Staples and Office Depot and force us to
2 match or they take their business elsewhere.

3 This is the essence of competition. And
4 this is what is completely missed if you try to
5 calculate market shares or assess this market by
6 tallying up contract wins and losses. That is just
7 not how this contract, how this market, excuse me,
8 works, Your Honor.

9 JUDGE CHAPPELL: If this is all correct
10 regarding the contracts, why would you enter into
11 contracts?

12 MR. PERRY: Your Honor, because it
13 establishes a relationship with the customer.

14 JUDGE CHAPPELL: Sounds like it is no
15 more than a business account?

16 MR. PERRY: It is a hunting license. It
17 is a business account. They get -- we get tied
18 into their system. And we hope that if we give
19 them good service and great pricing, that they will
20 buy from us.

21 JUDGE CHAPPELL: Does it guarantee a
22 price for the customer?

23 MR. PERRY: It locks in a price for the
24 customer. And then what happens, unfortunately,
25 for our bottom line is that throughout the life of

1 that contract, we are forced by those customers to
2 lower prices thousands of times per week, millions
3 of dollars in price cuts. That's competition.

4 If you just tally up who won and pretend
5 that competition began and ended with that RFP, you
6 missed that. But that's what these companies deal
7 with right there.

8 Now those lost sales, Your Honor, under
9 the contract are what these companies call leakage.
10 And you talk about the three guys going to the
11 coffee shop. But as I mentioned leakage in many
12 cases is 20, 30, 40, 50 percent or higher of a
13 customer's purchase.

14 The FTC may call it a win and say we own
15 that customer but the reality is often they are
16 buying more office products from other suppliers
17 than they are from us. And we have to compete
18 against them.

19 And, Your Honor, let me just conclude by
20 saying that the purpose and effectiveness of this
21 acquisition is not to raise prices. This
22 acquisition will lead to lower prices for the
23 individuals who shop in our stores and on-line and
24 mom-and-pop businesses and businesses of every
25 size, including the .1 percent that are at issue

1 here.

2 This competitive analysis was undertaken
3 by the Commission in 2013, and they admitted the
4 market was competitive then and it is even more
5 competitive today, Your Honor.

6 Thank you. Your Honor, that's all I
7 have, unless you have additional questions.

8 JUDGE CHAPPELL: I have nothing further.
9 Thank you.

10 MR. PERRY: Thank you, Your Honor.

11 JUDGE CHAPPELL: I will ask you to
12 respond to his claim that only .1 percent of
13 customers are affected. I let him go over time, so
14 I will give you some time.

15 MS. REINHART: Thank you, Your Honor.

16 JUDGE CHAPPELL: I am not asking for
17 rebuttal of everything, just the question I asked
18 you.

19 MS. REINHART: Just that one question. I
20 understand, Your Honor.

21 I think that the percentage of Staples'
22 and Office Depot's business that is in our market
23 is much larger than that. I believe that the
24 number that Mr. Perry is referring to, whether it
25 is accurate or not, something to be seen, but is

1 the actual number of companies.

2 Staples and Office Depot sell to lots of
3 business companies. I think he had the number on
4 his slide. It is a small portion of those business
5 companies that account for a large portion of the
6 revenues on the B-to-B side.

7 And so our market is not .1 percent, it
8 is -- I would hesitate to give you a percentage
9 today, but it is something in the neighborhood of
10 between 20 or 20 plus percent.

11 JUDGE CHAPPELL: Of their revenues?

12 MS. REINHART: Of their B-to-B revenues,
13 putting aside the retail, Your Honor. And I should
14 also add that --

15 JUDGE CHAPPELL: Go ahead. Go ahead.

16 MS. REINHART: Pardon me, Your Honor. It
17 is a significant business as seen in their ordinary
18 course documents and the words of their own
19 executives. In other words, they track the large
20 B-to-B customers. They sell to them specifically.

21 And one of the large reasons for that is
22 as the retail business is migrating away from
23 Staples and Office Depot to other providers, like
24 Walmart, the large B-to-B customers are not
25 migrating away. They need the services. They need

1 the pricing.

2 JUDGE CHAPPELL: And what about the
3 apparent claim that Respondents are using the FTC's
4 own words from the OfficeMax merger as a template
5 for how to complete a legal merger?

6 MS. REINHART: Your Honor, your questions
7 from the bench were spot on regarding Staples.
8 Staples was in the market, was not part of that
9 deal. And, in fact, the evidence will show that
10 back then, as today, Staples is the closest
11 competitor to Office Depot. It was true back then.
12 In other words, Office Depot and OfficeMax were not
13 each others' closest competitors.

14 JUDGE CHAPPELL: But the non-super store,
15 are there more of those today than there were in
16 2013 or less or about the same?

17 MS. REINHART: As it pertains to the large
18 B-to-B customers, Your Honor, I believe it is fair
19 to say that the predictions were not borne out. In
20 other words, companies that looked to be growing
21 have not grown. We will be able to show that the
22 third best supplier, the distant third, only has a
23 small portion of the large B-to-B business. That
24 has not changed.

25 JUDGE CHAPPELL: All right. Thank you.

1 Any quick reply to what she just said?

2 MR. PERRY: No, Your Honor. If there is
3 anything you want to hear, I am happy to say it.
4 The only thing I would add to what I mentioned is
5 it is not fair to say that the Commission's 2013
6 statement, the words were that these competitors,
7 not Staples, put them to the side because the
8 Commission had, already provide strong competition
9 for these customers and have demonstrated the
10 ability -- demonstrated, past tense -- the ability
11 to win these accounts. Those aren't predictions.
12 That is a fact that was put out by the Commission
13 and it remains true today, Your Honor.

14 JUDGE CHAPPELL: Well, I'm sure that's
15 going to be aired out in the District Court and, if
16 necessary, here as well.

17 MR. PERRY: I am sure you are right, Your
18 Honor.

19 Thank you.

20 JUDGE CHAPPELL: Anything further?

21 MR. PERRY: Nothing for Respondents, Your
22 Honor.

23 MR. REILLY: Nothing more, Your Honor.

24 JUDGE CHAPPELL: Hearing nothing further
25 until we meet again, we are adjourned.

1 (Whereupon, at 3:07 p.m., the hearing
2 adjourned.)

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