MERGER ANTITRUST LAW

Unit 11: Sysco/U.S. Foods

Class 17

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merger. However, rival firms may provide relevant facts, and even their overall views may be instructive, especially in cases where the Agencies are concerned that the merged entity may engage in exclusionary conduct.

> *Example 2:* Merging Firms A and B operate in a market in which network effects are significant, implying that any firm's product is significantly more valuable if it commands a large market share or if it is interconnected with others that in aggregate command such a share. Prior to the merger, they and their rivals voluntarily interconnect with one another. The merger would create an entity with a large enough share that a strategy of ending voluntary interconnection would have a dangerous probability of creating monopoly power in this market. The interests of rivals and of consumers would be broadly aligned in preventing such a merger.

3. Targeted Customers and Price Discrimination

When examining possible adverse competitive effects from a merger, the Agencies consider whether those effects vary significantly for different customers purchasing the same or similar products. Such differential impacts are possible when sellers can discriminate, e.g., by profitably raising price to certain targeted customers but not to others. The possibility of price discrimination influences market definition (see Section 4), the measurement of market shares (see Section 5), and the evaluation of competitive effects (see Sections 6 and 7).

When price discrimination is feasible, adverse competitive effects on targeted customers can arise, even if such effects will not arise for other customers. A price increase for targeted customers may be profitable even if a price increase for all customers would not be profitable because too many other customers would substitute away. When discrimination is reasonably likely, the Agencies may evaluate competitive effects separately by type of customer. The Agencies may have access to information unavailable to customers that is relevant to evaluating whether discrimination is reasonably likely.

For price discrimination to be feasible, two conditions typically must be met: differential pricing and limited arbitrage.

First, the suppliers engaging in price discrimination must be able to price differently to targeted customers than to other customers. This may involve identification of individual customers to which different prices are offered or offering different prices to different types of customers based on observable characteristics.

> *Example 3:* Suppliers can distinguish large buyers from small buyers. Large buyers are more likely than small buyers to self-supply in response to a significant price increase. The merger may lead to price discrimination against small buyers, harming them, even if large buyers are not harmed. Such discrimination can occur even if there is no discrete gap in size between the classes of large and small buyers.

In other cases, suppliers may be unable to distinguish among different types of customers but can offer multiple products that sort customers based on their purchase decisions.

Second, the targeted customers must not be able to defeat the price increase of concern by arbitrage, e.g., by purchasing indirectly from or through other customers. Arbitrage may be difficult if it would void warranties or make service more difficult or costly for customers. Arbitrage is inherently impossible for many services. Arbitrage between customers at different geographic locations may be

impractical due to transportation costs. Arbitrage on a modest scale may be possible but sufficiently costly or limited that it would not deter or defeat a discriminatory pricing strategy.

4. Market Definition

When the Agencies identify a potential competitive concern with a horizontal merger, market definition plays two roles. First, market definition helps specify the line of commerce and section of the country in which the competitive concern arises. In any merger enforcement action, the Agencies will normally identify one or more relevant markets in which the merger may substantially lessen competition. Second, market definition allows the Agencies to identify market participants and measure market shares and market concentration. See Section 5. The measurement of market shares and market concentration is not an end in itself, but is useful to the extent it illuminates the merger's likely competitive effects.

The Agencies' analysis need not start with market definition. Some of the analytical tools used by the Agencies to assess competitive effects do not rely on market definition, although evaluation of competitive alternatives available to customers is always necessary at some point in the analysis.

Evidence of competitive effects can inform market definition, just as market definition can be informative regarding competitive effects. For example, evidence that a reduction in the number of significant rivals offering a group of products causes prices for those products to rise significantly can itself establish that those products form a relevant market. Such evidence also may more directly predict the competitive effects of a merger, reducing the role of inferences from market definition and market shares.

Where analysis suggests alternative and reasonably plausible candidate markets, and where the resulting market shares lead to very different inferences regarding competitive effects, it is particularly valuable to examine more direct forms of evidence concerning those effects.

Market definition focuses solely on demand substitution factors, i.e., on customers' ability and willingness to substitute away from one product to another in response to a price increase or a corresponding non-price change such as a reduction in product quality or service. The responsive actions of suppliers are also important in competitive analysis. They are considered in these Guidelines in the sections addressing the identification of market participants, the measurement of market shares, the analysis of competitive effects, and entry.

Customers often confront a range of possible substitutes for the products of the merging firms. Some substitutes may be closer, and others more distant, either geographically or in terms of product attributes and perceptions. Additionally, customers may assess the proximity of different products differently. When products or suppliers in different geographic areas are substitutes for one another to varying degrees, defining a market to include some substitutes and exclude others is inevitably a simplification that cannot capture the full variation in the extent to which different products compete against each other. The principles of market definition outlined below seek to make this inevitable simplification as useful and informative as is practically possible. Relevant markets need not have precise metes and bounds.

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- legal or regulatory requirements; and
- the influence of downstream competition faced by customers in their output markets.

When the necessary data are available, the Agencies also may consider a "critical loss analysis" to assess the extent to which it corroborates inferences drawn from the evidence noted above. Critical loss analysis asks whether imposing at least a SSNIP on one or more products in a candidate market would raise or lower the hypothetical monopolist's profits. While this "breakeven" analysis differs from the profit-maximizing analysis called for by the hypothetical monopolist test in Section 4.1.1, merging parties sometimes present this type of analysis to the Agencies. A price increase raises profits on sales made at the higher price, but this will be offset to the extent customers substitute away from products in the candidate market. Critical loss analysis compares the magnitude of these two offsetting effects resulting from the price increase. The "critical loss" is defined as the number of lost unit sales that would leave profits unchanged. The "predicted loss" is defined as the number of unit sales that the hypothetical monopolist is predicted to lose due to the price increase. The price increase raises the hypothetical monopolist's profits if the predicted loss is less than the critical loss.

The Agencies consider all of the evidence of customer substitution noted above in assessing the predicted loss. The Agencies require that estimates of the predicted loss be consistent with that evidence, including the pre-merger margins of products in the candidate market used to calculate the critical loss. Unless the firms are engaging in coordinated interaction (see Section 7), high pre-merger margins normally indicate that each firm's product individually faces demand that is not highly sensitive to price.[6] Higher pre-merger margins thus indicate a smaller predicted loss as well as a smaller critical loss. The higher the pre-merger margin, the smaller the recapture percentage necessary for the candidate market to satisfy the hypothetical monopolist test.

Even when the evidence necessary to perform the hypothetical monopolist test quantitatively is not available, the conceptual framework of the test provides a useful methodological tool for gathering and analyzing evidence pertinent to customer substitution and to market definition. The Agencies follow the hypothetical monopolist test to the extent possible given the available evidence, bearing in mind that the ultimate goal of market definition is to help determine whether the merger may substantially lessen competition.

4.1.4 Product Market Definition with Targeted Customers

If a hypothetical monopolist could profitably target a subset of customers for price increases, the Agencies may identify relevant markets defined around those targeted customers, to whom a hypothetical monopolist would profitably and separately impose at least a SSNIP. Markets to serve targeted customers are also known as price discrimination markets. In practice, the Agencies identify price discrimination markets only where they believe there is a realistic prospect of an adverse competitive effect on a group of targeted customers.

> *Example 11:* Glass containers have many uses. In response to a price increase for glass containers, some users would substitute substantially to plastic or metal containers, but baby food manufacturers would not. If a

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[6] While margins are important for implementing the hypothetical monopolist test, high margins are not in themselves of antitrust concern.

hypothetical monopolist could price separately and limit arbitrage, baby food manufacturers would be vulnerable to a targeted increase in the price of glass containers. The Agencies could define a distinct market for glass containers used to package baby food.

The Agencies also often consider markets for targeted customers when prices are individually negotiated and suppliers have information about customers that would allow a hypothetical monopolist to identify customers that are likely to pay a higher price for the relevant product. If prices are negotiated individually with customers, the hypothetical monopolist test may suggest relevant markets that are as narrow as individual customers (see also Section 6.2 on bargaining and auctions). Nonetheless, the Agencies often define markets for groups of targeted customers, i.e., by type of customer, rather than by individual customer. By so doing, the Agencies are able to rely on aggregated market shares that can be more helpful in predicting the competitive effects of the merger.

4.2 Geographic Market Definition

The arena of competition affected by the merger may be geographically bounded if geography limits some customers' willingness or ability to substitute to some products, or some suppliers' willingness or ability to serve some customers. Both supplier and customer locations can affect this. The Agencies apply the principles of market definition described here and in Section 4.1 to define a relevant market with a geographic dimension as well as a product dimension.

The scope of geographic markets often depends on transportation costs. Other factors such as language, regulation, tariff and non-tariff trade barriers, custom and familiarity, reputation, and service availability may impede long-distance or international transactions. The competitive significance of foreign firms may be assessed at various exchange rates, especially if exchange rates have fluctuated in the recent past.

In the absence of price discrimination based on customer location, the Agencies normally define geographic markets based on the locations of suppliers, as explained in subsection 4.2.1. In other cases, notably if price discrimination based on customer location is feasible as is often the case when delivered pricing is commonly used in the industry, the Agencies may define geographic markets based on the locations of customers, as explained in subsection 4.2.2.

4.2.1 Geographic Markets Based on the Locations of Suppliers

Geographic markets based on the locations of suppliers encompass the region from which sales are made. Geographic markets of this type often apply when customers receive goods or services at suppliers' locations. Competitors in the market are firms with relevant production, sales, or service facilities in that region. Some customers who buy from these firms may be located outside the boundaries of the geographic market.

The hypothetical monopolist test requires that a hypothetical profit-maximizing firm that was the only present or future producer of the relevant product(s) located in the region would impose at least a SSNIP from at least one location, including at least one location of one of the merging firms. In this exercise the terms of sale for all products produced elsewhere are held constant. A single firm may operate in a number of different geographic markets, even for a single product.

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critical loss. While this "breakeven" analysis differs somewhat from the profit-maximizing analysis called for by the HMT, it can sometimes be informative.

The Agencies require that estimates of the predicted loss be consistent with other evidence, including the pre-merger margins of products in the candidate market used to calculate the critical loss. Unless the firms are engaging in coordinated interaction, high pre-merger margins normally indicate that each firm's product individually faces demand that is not highly sensitive to price. Higher pre-merger margins thus indicate a smaller predicted loss as well as a smaller critical loss. The higher the pre-merger margin, the smaller the recapture rate[85] necessary for the candidate market to satisfy the hypothetical monopolist test. Similar considerations inform other analyses of the profitability of a price increase.

4.3.D. Market Definition in Certain Specific Settings

This Section provides details on market definition in several specific common settings. In much of this section, concepts are presented for the scenario where the merger involves sellers. In some cases, clarifications are provided as to how the concepts apply to merging buyers; in general, the concepts apply in an analogous way.

4.3.D.1. Targeted Trading Partners

If the merged firm could profitably target a subset of customers for changes in prices or other terms, the Agencies may identify relevant markets defined around those targeted customers. The Agencies may do so even if firms are not currently targeting specific customer groups but could do so after the merger.

For targeting to be feasible, two conditions typically must be met. First, the suppliers engaging in targeting must be able to set different terms for targeted customers than other customers. This may involve identification of individual customers to which different terms are offered or offering different terms to different types of customers based on observable characteristics.[86] Markets for targeted customers need not have precise metes and bounds. In particular, defining a relevant market for targeted customers sometimes requires a line-drawing exercise on observable characteristics. There can be many places to draw that line and properly define a relevant market. Second, the targeted customers must not be likely to defeat a targeted worsening of terms by arbitrage (e.g., by purchasing indirectly from or through other customers). Arbitrage may be difficult if it would void warranties or make service more difficult or costly for customers, and it is inherently impossible for many services. Arbitrage on a modest scale may be possible but sufficiently costly or limited, for example due to transaction costs or search costs, that it would not deter or defeat a discriminatory pricing strategy.

If prices are negotiated or otherwise set individually, for example through a procurement auction, there may be relevant markets that are as narrow as an individual customer. Nonetheless, for analytic convenience, the Agencies may define cluster markets for groups of targeted customers for whom the

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[85] The recapture rate is sometimes referred to as the aggregate diversion ratio, defined in Section 4.2.B.

[86] In some cases, firms offer one or more versions of products or services defined by their characteristics (where brand might be a characteristic). When customers can select among these products and terms do not vary by customer, the Agencies will typically define markets based on products rather than the targeted customers. In such cases, relevant antitrust markets may include only some of the differentiated products, for example products with only "basic" features, or products with "premium features." The tools described in Section 4.2 can be used to assess competition among differentiated products.

conditions of competition are reasonably similar. (See Section 4.3.D.4 for further discussion of cluster markets.)

Analogous considerations arise for a merger involving one or more buyers or employers. In this case, the analysis considers whether buyers target suppliers, for example by paying targeted suppliers or workers less, or by degrading the terms of supply contracts for targeted suppliers. Arbitrage would involve a targeted supplier selling to the buyer indirectly, through a different supplier who could obtain more favorable terms from the buyer.

If the HMT is applied in a setting where targeting of customers is feasible, it requires that a hypothetical profit-maximizing firm that was the only present or future seller of the relevant product(s) to customers in the targeted group would undertake at least a SSNIPT on some, though not necessarily all, customers in that group. The products sold to those customers form a relevant market if the hypothetical monopolist likely would undertake at least a SSNIPT despite the potential for customers to substitute away from the product or to take advantage of arbitrage. In this exercise, the terms of sale for products sold to all customers outside the region are held constant.

4.3.D.2. Geographic Markets

A relevant antitrust market is an area of effective competition, comprising both product (or service) and geographic elements. A market's geography depends on the limits that distance puts on some customers' willingness or ability to substitute to some products, or some suppliers' willingness or ability to serve some customers. Factors that may limit the geographic scope of the market include transportation costs, language, regulation, tariff and non-tariff trade barriers, custom and familiarity, reputation, and local service availability.

4.3.D.2.a. Geographic Markets Based on the Locations of Suppliers

The Agencies sometimes define geographic markets as regions encompassing a group of supplier locations. When they do, the geographic market's scope is determined by customers' willingness to switch between suppliers. Geographic markets of this type often apply when customers receive goods or services at suppliers' facilities, for example when customers buy in-person from retail stores. A single firm may offer the same product in a number of locations, both within a single geographic market or across geographic markets; customers' willingness to substitute between products may depend on the location of the supplier. When calculating market shares, sales made from supplier locations in the geographic market are included, regardless of whether the customer making the purchase travelled from outside the boundaries of the geographic market (see Section 4.4 for more detail about calculating market shares).

If the HMT is used to evaluate the geographic scope of the market, it requires that a hypothetical profit-maximizing firm that was the only present or future supplier of the relevant product(s) at supplier locations in the region likely would undertake at least a SSNIPT in at least one location. In this exercise, the terms of sale for products sold to all customers at facilities outside the region are typically held constant.[87]

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[87] In some circumstances, as when the merging parties operate in multiple geographies, if applying the HMT, the Agencies may apply a "Hypothetical Cartel" framework for market definition, following the approach outlined in Section 4.3.A, n.81.

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Buyer characteristics and the nature of the procurement process can affect coordination. For example, sellers may have the incentive to bid aggressively for a large contract even if they expect strong responses by rivals. This is especially the case for sellers with small market shares, if they can realistically win such large contracts. In some cases, a large buyer may be able to strategically undermine coordinated conduct, at least as it pertains to that buyer's needs, by choosing to put up for bid a few large contracts rather than many smaller ones, and by making its procurement decisions opaque to suppliers.

8. Powerful Buyers

Powerful buyers are often able to negotiate favorable terms with their suppliers. Such terms may reflect the lower costs of serving these buyers, but they also can reflect price discrimination in their favor.

The Agencies consider the possibility that powerful buyers may constrain the ability of the merging parties to raise prices. This can occur, for example, if powerful buyers have the ability and incentive to vertically integrate upstream or sponsor entry, or if the conduct or presence of large buyers undermines coordinated effects. However, the Agencies do not presume that the presence of powerful buyers alone forestalls adverse competitive effects flowing from the merger. Even buyers that can negotiate favorable terms may be harmed by an increase in market power. The Agencies examine the choices available to powerful buyers and how those choices likely would change due to the merger. Normally, a merger that eliminates a supplier whose presence contributed significantly to a buyer's negotiating leverage will harm that buyer.

> *Example 22:* Customer C has been able to negotiate lower pre-merger prices than other customers by threatening to shift its large volume of purchases from one merging firm to the other. No other suppliers are as well placed to meet Customer C's needs for volume and reliability. The merger is likely to harm Customer C. In this situation, the Agencies could identify a price discrimination market consisting of Customer C and similarly placed customers. The merger threatens to end previous price discrimination in their favor.

Furthermore, even if some powerful buyers could protect themselves, the Agencies also consider whether market power can be exercised against other buyers.

> *Example 23:* In Example 22, if Customer C instead obtained the lower pre-merger prices based on a credible threat to supply its own needs, or to sponsor new entry, Customer C might not be harmed. However, even in this case, other customers may still be harmed.

9. Entry

The analysis of competitive effects in Sections 6 and 7 focuses on current participants in the relevant market. That analysis may also include some forms of entry. Firms that would rapidly and easily enter the market in response to a SSNIP are market participants and may be assigned market shares. See Sections 5.1 and 5.2. Firms that have, prior to the merger, committed to entering the market also will normally be treated as market participants. See Section 5.1. This section concerns entry or adjustments to pre-existing entry plans that are induced by the merger.

Sysco/US Foods

Press Releases

Sysco and US Foods Agree to Merge, Creating a World-Class Foodservice Company

12/09/2013

Combination brings together the best of both companies to do more for our customers and invest in accelerating the transformation of Sysco and the industry

Total enterprise value of $8.2 billion, representing 9.9x US Foods' trailing 12-month adjusted EBITDA of $826 million before synergies

Expect to achieve annual synergies of at least $600 million

More information on the transaction, including video material, can be found at **www.bestofbothinfood.com**

HOUSTON and ROSEMONT, Ill, Dec, 9, 2013 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) and US Foods today announced an agreement to merge, creating a world-class foodservice company. The total enterprise value of the transaction is approximately $8.2 billion and the combination has been approved by the Board of Directors of each company.

Bill DeLaney, Sysco president and chief executive officer, will lead the combined company, which will continue to be named Sysco and headquartered in Houston, Texas. At closing, Sysco will have estimated annual sales of approximately $65 billion.

Sysco will pay approximately $3.5 billion for the equity of US Foods, comprising $3 billion of Sysco common stock and $500 million of cash. As part of the transaction, Sysco will also assume or refinance US Foods' net debt, which is currently approximately $4.7 billion, bringing the total enterprise value to $8.2 billion. Sysco has secured fully committed bridge financing and expects to issue permanent financing prior to closing.

After completion of the transaction, the equity holders of US Foods will own approximately 87 million shares, or roughly 13% of Sysco. A representative of each of US Foods' majority shareholders, affiliates of Clayton, Dubilier & Rice LLC and Kohlberg Kravis Roberts & Co. L.P., will join Sysco's Board of Directors upon closing.

Bill DeLaney, Sysco president and chief executive officer, said, "As we continue on our transformational journey at Sysco, this transaction will position us to significantly accelerate our progress in achieving the vision we have for our company: to be our customers' most valued and trusted business partner. Sysco and US Foods have highly complementary core strengths including a broad product portfolio and passionate food people deeply committed to customer service, quality-assured products and safety. In particular we look forward to welcoming US Foods' talented employees and continuing to invest in the development of all of our people. Together we will strive to enhance shareholder value by providing our customers with highly differentiated products and services."

John Lederer, president and chief executive officer of US Foods, said, "Combining and maximizing the significant strengths of two outstanding companies is certain to be of tremendous advantage in supporting our customers as they tackle the challenges of today's demanding environment."

Compelling Strategic Rationale

This transaction will bring together Sysco and US Foods' complementary strengths including talented and dedicated associates, a broad product portfolio, supply chain excellence and a commitment to continuous improvement. Going forward, Sysco will continue to create value for customers through insights-driven product innovation and expanded services that go beyond food. Increased geographic coverage and scale will enhance our flexibility and responsiveness as we provide unique, on-trend food products that save customers time and improve performance.

Financial Details

At closing, the combined companies are expected to have annualized sales of approximately $65 billion and generate operating cash flows of approximately $2 billion. Sysco will purchase the outstanding equity of US Foods and assume or refinance its net debt in a transaction with an enterprise value of $8.2 billion. This represents a 9.9x multiple of US Foods' trailing 12-month (as of September 28, 2013) adjusted EBITDA of $826 million. Additionally, the transaction is expected to generate significant strategic benefits and cost synergies, achieving annual synergies of at least $600 million after three to four years, primarily stemming from supply chain efficiencies, merchandising activities, and overlapping general and administrative functions. The transaction is expected to be immediately accretive to earnings after adjusting for transaction-related costs and amortization of intangibles.

Sysco expects to maintain a strong investment grade rating. Additionally, Sysco is committed to continuing to invest in its dividend and returning value to shareholders. Sysco has paid a dividend every quarter since 1970 and has increased its dividend 45 times since becoming a public company.

Commitment to Investment

Sysco remains committed to investing in its businesses and its people to accelerate the transformation of the industry, including customer-friendly technology, robust category management, food safety and quality assurance and sustainable business practices.

Integration

Sysco will establish a team comprising members of both companies to prepare for and oversee a comprehensive integration for employees, customers and suppliers.

Additional Information

The transaction, which is expected to close in the third quarter of calendar year 2014, is subject to customary closing conditions and regulatory approvals, including antitrust approval.

Goldman, Sachs & Co. is serving as financial advisor to Sysco and Wachtell, Lipton, Rosen & Katz and Arnall, Golden & Gregory LLP are serving as its legal advisors. Simpson Thacher & Bartlett LLP and Debevoise & Plimpton LLP are serving as US Foods' legal advisors.

Additional Information for US Foods Stockholders

In connection with the proposed transaction, Sysco currently intends to file a Registration Statement on Form S-4 that will include a consent solicitation statement of US Foods. Sysco also plans to file other relevant materials with the SEC. Stockholders of US Foods are urged to read the consent solicitation statement/prospectus contained in the Registration Statement and other relevant materials because these materials will contain important information about the proposed transaction. These materials will be made available to the stockholders of US Foods at no expense to them. The consent solicitation statement/prospectus, Registration Statement and other relevant materials, including any documents incorporated by reference therein, may be obtained free of charge at the SEC's website at **www.sec.gov** or for free from Sysco at **www.sysco.com/investors** or by emailing **investor_relations@corp.sysco.com**. Such documents are not currently available. You may also read and copy any reports, statements and other information filed by Sysco with the SEC at the SEC public reference room at 100 F Street N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at (800) 732-0330 or visit the SEC's website for further information on its public reference room.

This document shall not constitute an offer to sell or the solicitation of an offer to buy any securities, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to the registration or qualification under the securities laws of any such jurisdiction. No offering of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

Conference Call Details

Sysco will host a conference call at 9:30am Eastern time today to discuss the announcement. Domestic and international participants may access the conference call toll-free by dialing (888) 256-9128 (US/Canada Toll Free) and (913) 312-1480 (International Toll) respectively, and using the passcode 8730765. This conference call, along with webcast presentation materials, can also be accessed live on Sysco's Investor Relations website at **www.sysco.com/investors**. To access a replay of the conference call, please dial (888) 203-1112 (US/Canada Toll Free) or (719) 457-0820 (International Toll), passcode 8730765.

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 193 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2013 that ended June 29, 2013, the company generated record sales of more than $44 billion. Connect with Sysco on Facebook at **www.facebook.com/SyscoCorporation** or Twitter at **www.twitter.com/Sysco**.

About US Foods

As one of America's great food companies and leading distributors, US Foods is Keeping Kitchens Cooking and making life easier for customers, including independent and multi-unit restaurants, healthcare and hospitality entities, government and educational institutions.

With approximately $22 billion in annual revenue, the company offers more than 350,000 products, including high-quality, exclusive brands such as the innovative Chef's Line, a time-saving, chef-inspired line of scratch-quality products, and Rykoff Sexton, a premium line of specialty ingredients sourced from around the world. The company proudly employs approximately 25,000 people in more than 60 locations nationwide. US Foods is headquartered in Rosemont, Ill., and jointly owned by affiliates of Clayton, Dubilier & Rice LLC and Kohlberg Kravis Roberts & Co. L.P.

Cautionary Statement Regarding Forward-Looking Statements

Information included in this document (including information included or incorporated by reference in this document) that look forward in time or that express beliefs, expectations, or hopes are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are all statements other than statements of historical facts. The words "anticipates," "may," "can," "plans," "believes," "estimates," "expects," "projects," "intends," "likely," "will," "should," "to be" and any similar expressions or other words of similar meaning are intended to identify those assertions as forward-looking statements. Such forward-looking statements reflect the views of management at the time such statements are made and are subject to a number of risks, uncertainties, estimates, and assumptions that may cause actual results to differ materially from current expectations, including but not limited to the ability of the parties to satisfy the conditions precedent and consummate the proposed merger, the timing of consummation of the proposed merger, the ability of the parties to secure stockholder and regulatory approvals in a timely manner or on the terms desired or anticipated, the ability of Sysco to integrate the acquired operations, the ability to implement the anticipated business plans of the combined company following closing and achieve anticipated benefits and savings, risks related to disruption of management's attention from ongoing business operations due to the pending merger, the effect of the announcement of the proposed merger on either party's relationships with their respective customers, vendors, lenders, operating results and businesses generally, the outcome of any legal proceedings related to the proposed merger, the general risks associated with the respective businesses of Sysco and US Foods, including the risk of interruption of supplies due to lack of long-term contracts, intense competition, severe weather, crop conditions, work stoppages, inflation risks, the impact of fuel prices, adverse publicity, labor issues, and risks impacting the economy generally, including the risks that the current general economic conditions will deteriorate, or that consumer confidence in the economy may not increase and decreases in consumer spending, particularly on food-away-from-home, may not reverse. For a discussion of additional factors impacting Sysco's business, see Sysco's Annual Report on Form 10-K for the year ended June 29, 2013, as filed with the Securities and Exchange Commission and the Company's subsequent filings with the SEC. For a discussion of additional factors impacting US Foods' business, see US Foods' filings with the SEC. Neither Sysco nor US Foods undertakes to update or revise any forward-looking statements, based on new information or otherwise.

CONTACT: Investor Inquiries

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Source: Sysco Corporation

Sysco's Merger with US Foods

December 9, 2013

Good things come from Sysco®

Forward-Looking Statements

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Additional Information for US Foods Stockholders

In connection with the proposed transaction, Sysco currently intends to file a Registration Statement on Form S-4 that will include a consent solicitation statement of US Foods. Sysco also plans to file other relevant materials with the SEC. Stockholders of US Foods are urged to read the consent solicitation statement/prospectus contained in the Registration Statement and other relevant materials because these materials will contain important information about the proposed transaction. These materials will be made available to the stockholders of US Foods at no expense to them. The consent solicitation statement/prospectus, Registration Statement and other relevant materials, including any documents incorporated by reference therein, may be obtained free of charge at the SEC's website at www.sec.gov or for free from Sysco at www.sysco.com/investors or by emailing investor_relations@corp.sysco.com. Such documents are not currently available. You may also read and copy any reports, statements and other information filed by Sysco with the SEC at the SEC public reference room at 100 F Street N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at (800) 732-0330 or visit the SEC's website for further information on its public reference room.

This document shall not constitute an offer to sell or the solicitation of an offer to buy any securities, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to the registration or qualification under the securities laws of any such jurisdiction. No offering of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

Two Great Companies

Bringing Together the Best of Both

Consistent with Sysco's Strategic Focus

Sustainable Profitable Growth

- Leverage customer insights
- Enhance and expand channels
- Increase customer retention
- Execute fold-in and regional acquisitions
- Build human capital

Expand international growth

Operating Margin

- Reduce operating costs
- Lower product costs
- Continue to develop Sysco Ventures
- Further develop enterprise structure
- Integrate higher margin products

Asset Optimization and Free Cash Flow

- Invest prudently in the core
- Increase working capital efficiency
- Increase capital efficiency
- Use our capital structure as a competitive advantage

26

A Transformational Acquisition

Benefits all stakeholders

Customers

- ❑ Combined strengths deliver greater value, more services and innovation for customers
- ❑ Strengthen our role as our customers' most valued and trusted business partner

Suppliers

- ❑ Achieve shared efficiencies with suppliers
- ❑ Platform for enhanced innovation and development of exclusive products

Employees

- ❑ Greater opportunities for career development
- ❑ Enhanced financial stability drives benefits to employees

Shareholders

- ❑ Leverage revenue growth through best-in-class operating efficiencies and lowest-cost to serve
- ❑ Strong EPS growth and substantial cash flow

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A World Class Foodservice Company

Complementary core strengths
Sysco operations and service fit nicely with US Foods food and innovation focus

Scale advantages
More leverage to lower cost of goods, accelerate innovation, and improve overall service

Improved offerings
New ability to create a compelling product portfolio and differentiated solutions by segment

Enhanced productivity
Streamlined operations will enhance productivity and lower cost to serve

Multi-channel approach
US Foods' mobile app and "Cash & Carry" stores complement Sysco's ISR and MA strength

Transaction Financing Structure

Approximate Total Transaction Value:

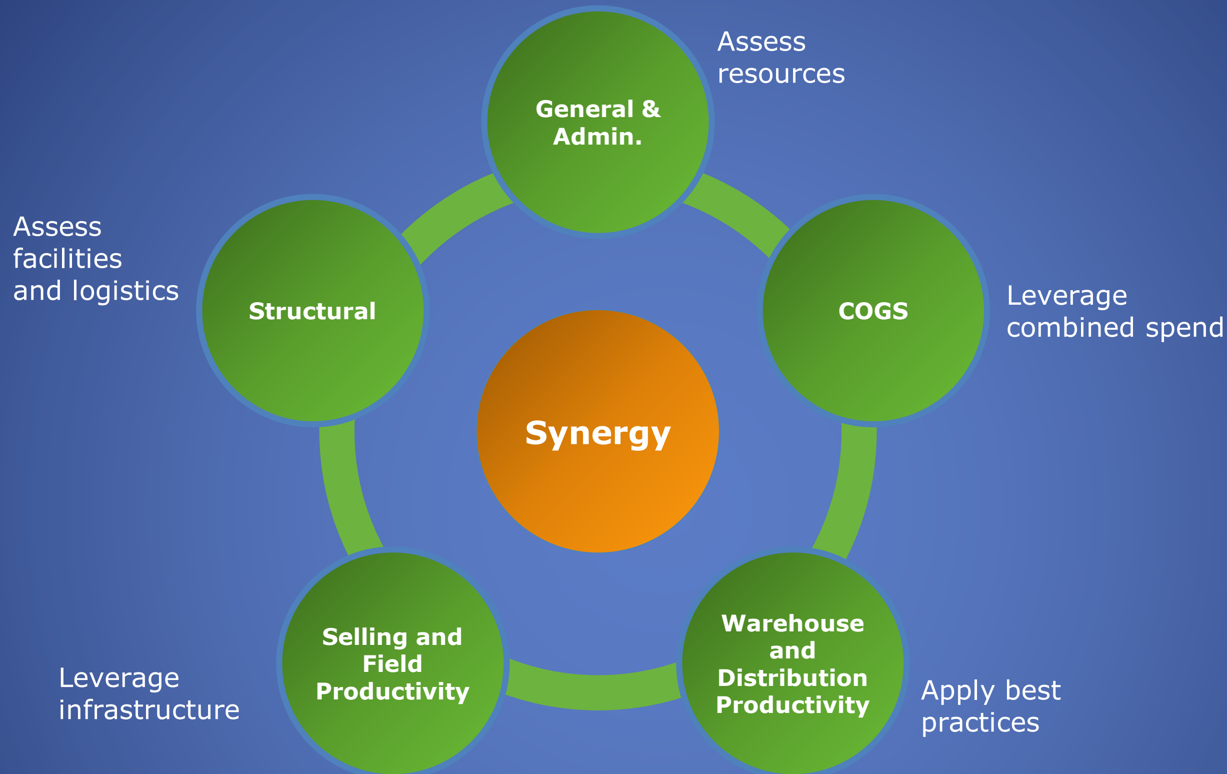
Equity	3.0B	❑ Equity holders of US Foods will own approx. 87 million shares or, 13%, of combined company at closing, and ❑ A representative of each of US Foods' majority shareholders will join Sysco's Board of Directors
Cash	0.5B	
US Foods Net Debt	$4.7B	Sysco to assume or refinance
Total Enterprise Value	$8.2B	

Represents 9.9x US Foods LTM adjusted EBITDA of $826 million[1]

Good things come from Sysco

[1] US Foods LTM adjusted EBITDA of $826 million is as of September 28, 2013

At Least $600 Million in Estimated Annual Synergies[1]



We Will Continue To Move Forward With Our Business Transformation Initiatives

[1] To be achieved after three to four years

Combination Creates Significant Shareholder Value

Earnings	Immediately accretive to earnings after adjusting for transaction-related costs and amortization of intangibles
Synergies	Annual synergies of at least $600 million realized after three to four years
Cash Flow	Approximate sales of $65 billion Approximate cash flows of $2 billion
Balance Sheet	Balance sheet flexibility retained Commitment to maintaining a strong investment grade credit rating

Good things
come from
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Good things
come from
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Addition Reading

N.Y. Times Editorial Bd., *A Potentially Harmful Merger*, N.Y. Times.com, Jan. 20, 2014.

William McConnell, *Sysco-US Foods Merger Under Fire From Teamsters*, TheStreet.com, Aug. 29, 2014.

Brent Kendall & Annie Gasparro, *FTC Considers Challenge to Food Merger*, Wall St. J., Sept. 22, 2014.

Diane Bartz, *Sysco Looks to Divestitures to Nail Down US Foods Deal*, Reuters.com, Oct. 17, 2014.

PaRR, *Sysco/US Foods Divestitures Not Clear Solution, Industry Sources* Say (Oct. 28, 2014).

Annie Gasparro, *Sysco Doesn't Expect US Foods Deal to Close This Yea*r, Wall St. J., Nov. 3, 2014.

Diane Bartz & Greg Roumeliotis, *Sysco May Face about $1 Billion in Costs If US Foods Merger Dies*, Reuters.com, May 15, 2015 ($300 million breakup fee to U.S. Foods, $25 million breakup fee to divestiture buyer Performance Food Group, $265 million to redeem financing, $258 million on integration planning and advisers, $100 million in historical financing costs, and $53 million in computer systems integration).

The Hale Group, Foodservice Distributors of the Future: The Evolution of the Foodservice Distributor Sector

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food&water watch

Ms. Deborah L. Feinstein
Director, Bureau of Competition
Office of Policy and Coordination
Room 7117
Federal Trade Commission
601 New Jersey Avenue NW
Washington, DC 20580

January 8, 2014

BY POST AND ELECTRONIC MAIL: antitrust@ftc.gov

Dear Director Feinstein:

The non-profit consumer advocacy organization Food & Water Watch respectfully requests that the U.S. Federal Trade Commission and/or the U.S. Department of Justice oppose the early termination of the antitrust examination and undertake a second review of the proposed merger between Sysco Corp. (Sysco) and US Foods Holding Corp, parent of US Foods, Inc. (US Foods). The U.S. Federal Trade Commission must conduct a complete investigation of the proposed merger to assess the negative impact on competition in the foodservice industry for manufacturers, foodservice operators and consumers. The proposed merger creates a considerably more concentrated marketplace for foodservice distribution in the broadline segment, which warrants the request for additional information needed for a more thorough and comprehensive analysis.[1]

Sysco and US Foods have aggressively pursued a string of mergers in recent years, but the proposed merger would create a significantly larger amalgamation of foodservice distribution market power at the national level. The increase in concentrated market power is especially acute at the regional and local level. Although both firms have purchased many smaller, local distribution firms, this is the first merger between foodservice distribution firms that each serve the national market and in many regions, states and metropolitan areas, they are the primary rivals for this market.

Rapid consolidation in the food and agriculture sectors has been of rising concern to farmers, consumers and federal regulators. In 2010, the U.S. Department of Agriculture and the U.S. Department of Justice held a series of five workshops exploring the impact of consolidation in the food and agriculture sectors, and a May 2012 Department of Justice report "stressed the importance of vigorous antitrust enforcement" and detailed the ways that anticompetitive mergers and conduct can harm producers, consumers, and others.[2]

The proposed merger between Sysco and US Foods, announced on December 9, 2013, represents just such an anticompetitive merger. It joins the two largest foodservice distribution companies,

[1] U.S. Department of Justice and the Federal Trade Commission (DoJ/FTC). "Horizontal Merger Guidelines." August 19, 2010 at 19; Sysco and US Foods are broadline foodservice distributors, which provide an extensive line of products to a variety of foodservice operations. Other foodservice segments include system distributors that supply a narrow range of products to specific larger-scale foodservice networks and specialty foodservice distributors that supply a narrow range of products (like produce or seafood) to many foodservice outlets.
[2] U.S. Department of Justice. "Competition and Agriculture: Voices from the Workshops on Agriculture and Antitrust Enforcement in our 21st Century Economy." May 2012 at 2.

which deliver food products to restaurants, hotels, schools, hospitals and other institutional foodservice providers.[3] The merger is valued at $8.2 billion, including $3 billion in Sysco stock, $500 million in cash and the assumption of $4.7 billion in U.S. Food debt.[4] It is the largest food wholesaling transaction since Albertson's wholesaling line was sold for $16.1 billion in 2006.[5]

Both Sysco and US Foods operate in virtually every market and have distribution centers and sales staff in many of the same regions, states and metropolitan areas.[6] Food & Water Watch estimates that in the United States, Sysco has 151 distribution centers and delivers to 44 states and US Foods has 72 distribution centers and delivers in 36 states.[7]

The proposed merger represents "a lot of size and scale and force within the sector," according to an Edward Jones & Co. analyst.[8] The combined firms would have revenue of $65 billion in North America's $235 billion food distribution market.[9] Sysco is already considered the "dominant industry player."[10] The proposed merger cements Sysco as "the reigning giant in an already consolidated industry," according to the *New York Times*.[11]

The Clayton Antitrust Act bars mergers that could substantially reduce competition in any business line in any part of the country.[12] The post-merger Sysco threatens to reduce competition in the foodservice industry. It could have detrimental impacts on foodservice operations like restaurants and cafeterias (including schools and hospitals) and food manufacturing and potentially reduce consumer welfare.

The combination substantially increases Sysco's market power, allowing it to unilaterally impose small but significant price hikes on foodservice operations with few other options (monopoly power) and could leverage price concessions from manufacturers that would be forced to accept price cuts in order to get on Sysco's trucks (monopsony power). Consumers could see higher prices for food they eat away from home in foodservice establishments when these higher prices are passed on to consumers. A proposed merger of this size and scope warrants close scrutiny by antitrust regulators.

These unilateral anticompetitive effects are already occurring. Mega-distributors like Sysco can utilize their scale and buy up rivals to leverage their market power.[13] Sysco is "one of the most aggressive on pricing," according to foodservice industry *F&D Reports* because it can "easily

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[3] Mulvaney, Erin. "Sysco finds purchase of top rival appetizing." *Houston Chronicle*. December 10, 2013.
[4] Hirst, Ellen Jean. "Sysco plans to buy US Foods for $3.5B." *Chicago Tribune*. December 10, 2013.
[5] *Ibid*.
[6] Mirabella, Lorraine. "Sysco to buy US Foods." *Baltimore Sun*. December 10, 2013.
[7] Food & Water Watch analysis of Information Clearinghouse. "Foodservice Sector Special Analysis: Foodservice Distribution Channel." *F&D Reports*. December 13, 2013 at 2; US Foods. "US Foods Locations." Available at http://www.usfoods.com/about-us/contact-us/USFLocations.html, accessed January 2014; Sysco Corporation. U.S. Securities and Exchange Commission. 10-K filing. August 27, 2013 at 12.
[8] Mulvaney (2013).
[9] Cavale, Siddharth. "Sysco to buy US Foods to create distribution giant." *Washington Post*. December 10, 2013.
[10] Information Clearinghouse (2013) at 4.
[11] Gelles, David and Micheal J. De La Merced. "Sysco to buy rival US Foods in deal valued at $3.5 billion." *New York Times*. December 9, 2013.
[12] 15 U.S.C. §18.
[13] Blissett, Guy, Robin Hahn and Maureen Stancik Boyce. IBM Global Business Services. "Break Out or Get Boxed In." June 2008 at 1.

absorb short-term margin pressures" and disadvantage its smaller competitors.[14] Sysco reports that it may undercut prices and erode margins "to attract and retain customers."[15]

These effects could be magnified in many parts of the country where the merger would eliminate Sysco's main rival. Mergers that increase local or regional market power by reducing competition can facilitate price increases to consumers (restaurants and their patrons) or reduce prices paid to suppliers (foodservice manufacturers) because there are few other geographically practical options.[16] The merger dramatically increases regional concentration in many areas where there often are few practical alternative competitors by eliminating a significant rivalry in the foodservice industry. One Citigroup analyst noted that the merger would eliminate "a volatile – at times aggressive – competitor."[17]

Merger significantly accelerates consolidation in foodservice distribution

The foodservice distribution market is fragmented, with many small local firms, but the biggest firms have a dominant position in the marketplace and the merger of the two largest firms would significantly diminish competition. Concentrated markets create barriers to entry for new competitors, allow economies of scale to drive out innovation, and allow oligopolies to raise prices on captive consumers. Mergers between rivals can distort markets sufficiently to deter new market entrants from restoring competition.[18]

There are thousands of smaller distributers, but their size pales in comparison to the size of Sysco.[19] While one Morningstar analyst estimated that there were 16,000 food distributors,[20] mega-distributors have cemented their dominant position in the fragmented industry and are increasing consolidation in the industry through mergers and acquisitions.[21] The ten largest broadline foodservice distributors captured all of the segment's growth between 2003 and 2010 and Sysco alone captured one third of the growth.[22]

Consolidation has been "a key feature of the [foodservice distribution] landscape."[23] Over the past decade, larger chains have purchased more than 100 independent food distributors.[24] Foodservice financial specialists Keiter Stephens Advisors predicted that 2012 would mark the beginning of a very active foodservice distribution merger period comparable to "the big roll-up years" in the late 1980s.[25] As predicted, in 2012, nine of the biggest 60 foodservice distributors with total revenue of about $3 billion were absorbed by mergers.[26]

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[14] Information Clearinghouse (2013) at 1.
[15] Sysco Corporation (2013) at 6.
[16] Baye, Michael R. and Graeme Hunter. NERA Economic Consulting. "Going beyond the conventional wisdom on whether merger-related cost savings will benefit consumers." *Antitrust Insights*. Spring 2010 at 7.
[17] Gelles and De La Merced (2013).
[18] Ross, Douglas. "Antitrust enforcement and agriculture." Address before the American Farm Bureau Policy Development Meeting. Kansas City, Missouri. August 20, 2002 at 16.
[19] Gelles and De La Merced (2013).
[20] Hirst (2013).
[21] Blissett, Hahn and Boyce (2008) at 5.
[22] The Hale Group. "Foodservice Distributors of the Future – The Evolution of the Foodservice Distributor Sector." 2013 at 3.
[23] Information Clearinghouse (2013) at 1.
[24] Daly, Pete. "Gordon Food Service not surprised by Sysco merger." *Grand Rapids Business Journal*. December 13, 2013.
[25] Keiter Stephens Advisors. "KSA foodservice update: Merger & acquisition trends." February 2013.
[26] Information Clearinghouse (2013) at 6; Keiter Stephens Advisors (February 2013).

The largest distributors have purchased large, mid-sized and smaller companies to grow their businesses and revenues.[27] Between 2008 and 2013, the five largest foodservice distributors (Sysco, US Foods, Performance Food Group, Reinhart and Gordon) purchased about three-quarters of the 86 independent foodservice distributors that were sold.[28] Sysco has acquired more than 150 smaller companies in the past forty years.[29] In 2013 alone, Sysco purchased 14 companies with total revenue of more than $1 billion, representing about half of Sysco's revenue growth in 2013.[30]

Broadline Foodservice Distribution Market

Sysco and US Foods are two of the three broadline foodservice distributors with national operations, although the rest of the top 10 are super regional competitors with national reach.[31] Foodservice represents about one-fifth of wholesale food and related product sales and broadliners distribute a full range of food, equipment and supplies for foodservice outlets.[32] Although there are other food distribution firms that provide wholesale supply services to retail food establishments, Sysco is the largest foodservice distributor serving the away-from-home food market (restaurants, cafeterias, hospitality, schools, hospitals and catering services).[33] Sysco also provides foodservice distribution to the U.S. military.[34]

The appropriate market for analysis is the broadline foodservice distribution market, not the entire wholesale food distribution market or the entire foodservice distribution market. Broadline firms provide one-stop distribution from a single truck shipment but they are increasingly servicing chain restaurants and other multi-unit institutions and operations.[35] Broadline foodservice distributors control about three-fifths of the foodservice market, with the remainder of the foodservice market supplied by specialty products distributors and those firms distributing solely to multi-unit foodservice operations.[36]

The distinction between foodservice distribution and broadline foodservice distribution is significant. The entire foodservice market is estimated at about $235 billion in total sales in 2013,[37] but foodservice analyst the Hale Group and International Foodservice Manufacturers estimate the broadline foodservice market at $185 billion in 2013.[38] Sysco estimates its own market share at 18 percent, which represents its share of the total foodservice market. But more accurately, its share of the broadline market was about 24 percent in 2013. Food & Water Watch

[27] Keiter Stephens Advisors. "KSA foodservice update: Financial and operational trends in distribution." October 2011 at 1.
[28] Keiter Stephens Advisors (February 2013).
[29] Hirst (2013).
[30] Sysco Corporation (2013) at 17.
[31] Information Clearinghouse (2013) at 2; The Hale Group. "Focus on Foodservice Distribution." April 11, 2013 at 5 and 6; The Hale Group (2013) at 8.
[32] Harris, Michael et al. U.S. Department of Agriculture. Economic Research Service. "U.S. Food Marketing System, 2002." Agricultural Economic Report No. AER-811. August 2002 at 14.
[33] Sysco Corporation (2013) at 1.
[34] Gelles and De La Merced (2013).
[35] The Hale Group (2013) at 4.
[36] The Hale Group (April 2013) at 5.
[37] Sysco Corporation (2013) at 3; Information Clearinghouse (2013) at 4.
[38] The Hale Group/International Foodservice Manufacturing Association (IFMA). "What the Sysco/US Foods merger means for foodservice manufacturers." December 11, 2013.

believes Sysco's competitors are solely the broadline foodservice distributors and that the appropriate antitrust consideration should look at those firms that are competing for the same customers and using the same suppliers.

Geographic Market

Foodservice distribution firms operate in both national and local markets. They buy from national and large regional suppliers and sell to customers that are national, regional and local. Food & Water Watch believes that the proposed merger will significantly harm competition on the national, regional and local level.

National Level: On the national level, larger distribution firms deploy distribution centers that can supply and deliver to multiple population centers in regional markets rather than serving any single market.[39] Foodservice distribution is inherently a business that relies on warehouses, trucks and logistical systems and it remains an asset-intensive industry that is built on a network of physical assets like distribution centers.[40] The advantages of large foodservice distribution firms are their efficient storage and transportation capacity.[41]

The distribution industry is presently investing in larger warehouses that are capable of providing better market coverage.[42] In 2013, Sysco had more than 150 distribution facilities with 150,000 square feet of average capacity in the United States.[43] Larger facilities allow distribution firms to serve broader market areas,[44] as the average freight shipment of prepared food and meat products travels about 250 miles, according to the U.S. Department of Transportation.[45] Historically, distribution facilities were located primarily to serve large population centers or metropolitan markets, but distribution firms are increasingly locating their facilities near transportation routes that serve many markets.[46] The largest foodservice distribution firms like Sysco and US Foods coordinate shipments of inbound supplies – making larger pick-ups from manufacturers – and then distribute the supplies throughout their distribution networks.[47]

Regional and Local: Sysco reports competing "primarily with local and regional distributors, a few organizations compete with us on a national basis,"[48] and Sysco's distribution capacity far exceeds that of its mostly regional and local competitors. Foodservice markets are regional and obviously cross state lines, especially to serve densely populated areas. Firms with more distribution facilities are closer and better positioned to deliver goods and satisfy customers.[49] Sysco "believes that in most instances our local operations are among the leading distributors of

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[39] Andreoli, Derik, Anne Goodchild and Kate Vitasek. "The rise of mega distribution centers and the impact on logistical uncertainty." *International Journal of Transportation Research*. Vol. 2. 2010 at 75.
[40] Blissett, Hahn and Boyce (2008) at 13.
[41] *Ibid*. at 1.
[42] Andreoli, Goodchild and Vitasek (2010) at 77.
[43] Food & Water Watch analysis. Sysco Corporation (2013) at 12.
[44] Andreoli, Goodchild and Vitasek (2010) at 80.
[45] U.S. Department of Transportation. Bureau of Transportation Statistics. *National Transportation Statistics*. 2013 at Table 1-59.
[46] Andreoli, Goodchild and Vitasek (2010) at 76.
[47] Franklin Foodservice Solutions. "Foodservice Supply Chain Study." February 2009 at 3 to 4.
[48] Sysco Corporation (2013) at 3.
[49] Ribaudo, Frank, Drew Satherlie and Mike Younkin. FedEx. "Best-in-Class in Wholesale Distribution Series." January 2006 at 6.

food and related non-food products to foodservice customers in their respective trading areas."[50] Sysco identifies this "wide geographic" footprint as one of its key competitive advantages.[51]

National Broadline Foodservice Distribution Concentration Levels

In 2013, the top 10 national and regional broadline foodservice firms controlled more than half (56 percent) of the sector's national sales.[52] Food & Water Watch found that the top four firms controlled nearly half of the broadline foodservice distribution market (48.0 percent) in 2013 – almost all of the top 10 market share (*see* Table 1).[53] The four-firm concentration has been rising rapidly. Between 2010 and 2013, the top four-firm market share rose 17.5 percent from 40.9% in 2010 to 48.0 percent in 2013.[54]

Table 1. National Market Concentration of Top Four Broadline Foodservice Distribution Firms

Firm	2003	2010	2013	Post-Merger
Sysco	19.2%	20.4%	23.9%	35.8%
US Foods	12.4%	10.8%	11.9%	
Performance Food Group	3.2%	5.5%	6.9%	6.9%
Gordon	2.3%	4.1%	5.2%	5.2%
Reinhart	1.1%	2.4%	3.0%	3.0%
CR4	37.1%	40.9%	48.0%	51.0%
HHI	536	580	789	1369

Sources: Food & Water Watch analysis. The Hale Group/International Foodservice Manufacturing Association 2013; *F&D Reports* 2013; *ID Report* 2004 and 2011.

In 2013, the national Herfindahl-Hirschman Index ("HHI") for the broadline foodservice distribution sector was 789, considered un-concentrated under the 2010 Horizontal Merger Guidelines.[55] But the proposed merger would significantly increase the market power and market concentration on the national level. The post-merger Sysco would control more than a third (35.8 percent) of the market, increasing the firm's market share by 50.0 percent (*see* Table 2).

Although the four-firm market share concentration level would rise only slightly (by 3.0 percent), the HHI concentration index would rise significantly. The post-merger HHI would increase by 580, a 73.5 percent increase and rapidly approach the 1,500 level of moderate concentration. The size of the increase in the national HHI warrants close examination by the Federal Trade Commission because such a dramatic increase in market concentration suggests that the post-merger Sysco would have significantly enhanced market power.

Table 2. Change in Market Share and Concentration Post Sysco-US Food Merger

	Absolute	Percentage
Sysco Market Share Change	11.9%	50.0%
HHI Change	580	73.5%
CR-4 Change	3.0%	6.2%

Although the sector includes many smaller firms, the largest firms maintain a significant edge over their rivals. In 2013, Sysco had twice the revenue of US Foods, the merger target and second largest firm, three-and-a-half times the revenue of the third largest firm and four-and-a-half times the revenue of the fourth largest firm. Firms smaller than the tenth largest foodservice distributor have less than one half of one percent of total national sales.

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[50] Sysco Corporation (2013) at 4.
[51] *Ibid*. at 19.
[52] The Hale Group/IFMA (2013).
[53] Food & Water Watch analysis of 2013 market. Firm sales from Information Clearinghouse (2013); National broadline total sales from The Hale Group/IFMA (2013).
[54] Food & Water Watch calculation from Information Clearinghouse (2013); The Hale Group/IFMA (2013); *ID Report.* 2011 Top 50 Roster. The concentration levels are lower for the entire foodservice distribution industry, which would include firms that do not compete directly with Sysco or US Foods. In 2013, the top four broadliners controlled 37.9 percent of all foodservice distribution and the merger would increase that four-firm figure to 40.3 percent.
[55] DoJ/FTC at 19. The comparable HHI for the entire foodservice distribution industry would be 493 for the four largest broadline foodservice distributors and the merger would increase the HHI by 362 to 856. Even using a larger market, which artificially dilutes the industry concentration, the increase in HHI by nearly four times the level that could trigger regulatory interest.

The proposed merger exacerbates the gap between the post-merger Sysco and its closest rivals on the national level. Sysco would have $50 billion more in sales than its largest rival after the merger.[56] Sysco would be more than five times larger than the second largest firm, nearly seven times larger than the number three firm and twelve times larger than the fourth largest firm. The gap is larger for smaller but still major market participants. The post-merger Sysco would be more than 20 times larger than the fifth-place firm and sixty times larger than the ninth largest firm.

The significant size of the gap between the post-merger Sysco and the rest of the marketplace suggests that the remaining market participants will be unable to provide sufficient competition.[57] The foodservice trade publication *F&D Reports* noted "the gap between number one and two will widen significantly and will certainly limit choice – particularly on the national level."[58] Post-merger, smaller firms would be unable to replace the competition provided by former rival US Foods.

Estimating Regional and State Concentration Levels

The proposed merger will have greater impacts on regional and local markets. The bigger post-merger Sysco with its dominant market share and strong geographic footprint will significantly reduce competition in supplying foodservice outlets. In some regions and markets, the merger will significantly increase Sysco's market power and reduce the number and strength of its rivals. The director of BB&T Capital Markets noted "In certain regions, the combined market share is going to raise some red flags" that could warrant divestitures.[59]

Assessing the regional and local markets is difficult as there is limited information about the market shares of foodservice distribution. Sysco admits that "adequate industry statistics are not available" to assess the local foodservice distribution marketplace.[60] Moreover, there is little academic literature on the spatial dispersion and geography of distribution warehouse networks.[61]

Food & Water Watch analyzed the regional and state locations of the top 50 foodservice distribution firms and developed a model to estimate the market share of these warehouses in every state and every U.S. Census Bureau region.[62] The model calculates a company's distribution center or warehouse market share by comparing the number of top 50 broadline foodservice distribution firms' warehouses, by state, to an estimate for the total number of foodservice wholesale distribution establishments (by region or state) based on the number of wholesale grocery distributors from the 2007 Economic Census.[63] This approximates the market share of distributional capacity.

[56] Information Clearinghouse (2013) at 4.
[57] DoJ/FTC at 18.
[58] Information Clearinghouse (2013) at 1.
[59] Gelles and De La Merced (2013).
[60] Sysco Corporation (2013) at 3.
[61] Andreoli, Goodchild and Vitasek (2010) at 76.
[62] Food & Water Watch analyzed the state locations of the top 50 away-from-home foodservice distribution firms compiled in the Information Clearinghouse (2013). The U.S. state locations were determined from company disclosures on their websites or in Securities and Exchange Commission filings.
[63] Food & Water Watch approximated foodservice distribution market shares by comparing the number of top 50 broadline foodservice distribution establishments to the number of wholesale food distribution establishments from the 2007 Economic Census. The U.S. Department of Agriculture determined that the foodservice share of wholesale grocery distribution was 22 percent in 2007 (U.S. Department of Agriculture. Economic Research Service. "Retailing & Wholesaling: Wholesaling." February 2013. Available online at http://www.ers.usda.gov/topics/food-markets-prices/retailing-

The share of distribution facilities is a reasonably good proxy for local market share and market concentration. The 2010 Horizontal Merger Guidelines recognize that capacity may reflect the market power of suppliers and can be considered an appropriate substitute for market share of revenues under some circumstances.[64] The top 50 firms represent nearly two-thirds (63.3 percent) of the national foodservice distribution revenues and likely are an even larger share of warehouse capacity.[65] Most of the remainder of the market is comprised of smaller, single facility firms and these warehouses generally have smaller square footage storage capacity. Given the limitations of the local level market share data, this analysis presents an appropriate substitute for market shares based on local or regional sales revenue.

Table 3. Regional Foodservice Distribution Center Concentration

Census Region	New England	Mid-Atlantic	South Atlantic	East North Central	East South Central	West North Central	West South Central	Mountain	Pacific
States	CT, MA, ME, NH, RI, VT	NJ, NY, PA	DE, DC, FL, GA, MD, NC, SC, WV	IL, IN, MI, OH, WI	AL, KY, MS, TN	IA, KS, MN, MO, NE, ND, SD	AR, LA, OK, TX	AZ, CO, ID, MT, NV, NM, WY	AK, CA, HI, OR, WA
Population	14.6M	41.3M	61.8M	46.7M	4.8M	20.9M	37.9M	22.3M	51.4M
Pre-Merger Firms	18	23	22	16	15	11	15	16	14
Top 50 Distribution Centers	19	48	83	52	33	39	63	39	71
Est. Total Foodservice Wholesale Establishments	24	60	104	65	41	49	79	49	89
2013 Sysco % Distrib. Centers	29.5%	20.0%	31.8%	29.2%	21.8%	18.5%	33.0%	28.7%	24.8%
2013 USF % Distrib. Centers	12.6%	16.7%	14.5%	10.8%	12.1%	22.6%	10.2%	16.4%	6.8%
Post-Merger % Distrib. Centers	42.1%	36.7%	46.3%	40.0%	33.9%	41.0%	43.2%	45.1%	31.5%
HHI 4-firm Distribution Pre-Merger	1116	739	1268	1074	756	980	1274	1182	759
HHI 4-firm Distribution Post-Merger	1932	1417	2203	1742	1291	1851	1971	2162	1126
Increase in Distrib HHI	816	678	935	667	535	1361	1,088	980	573

Source: Food & Water Watch analysis of Information Clearinghouse, U.S. Census Bureau data.

Proposed merger would significantly increase concentration in many regions

Food & Water Watch found that the proposed merger would significantly increase Sysco's regional market share and increase the regional market concentration to the levels that should warrant antitrust scrutiny. Food & Water Watch examined the effects of the proposed merger on the market share and HHI concentration levels in the nine U.S. Census Bureau regions. These

wholesaling/wholesaling.aspx#.UssdiyQrPPY). The top 50 broadline foodservice distributors represented 17.5 percent of the 2007 wholesale grocery distributors, meaning that the top broadline foodservice distributors represented about 80 percent of the foodservice distributors. Food & Water Watch estimated the total number of foodservice distributors as 125 percent of the top 50 broadliners in each Census Bureau region and state. Warehouse capacity market share, four-firm concentration and HHI values were calculated based on the share of this estimated total foodservice establishments. This necessarily underestimates the actual market shares. The total number of establishments has likely declined since 2007; the number of grocery wholesalers declined by about 15 percent between 2002 and 2007 and may have declined more or less since 2007. Additionally, USDA did not distinguish between broadline foodservice distributors and other types, such as system distributors or specialty distributors. Thus, in this instance, Food & Water Watch is estimating the market share of all foodservice distributors.

[64] DoJ/FTC at 17.

[65] Food & Water Watch analysis of Information Clearinghouse (2013) data.

regional breakdowns approximate the delivery routes and service areas of the national and regional foodservice distribution firms. These definitions do not perfectly match the foodservice companies' markets, but most firms are regional and not national, and the Census Bureau regional divisions provide a good benchmark to account for differences in the service areas of regionally based foodservice distributors. By looking at the top 50 broadline foodservice distribution firms, the top-four firm concentration levels can capture the largest firms in any region or state.

Food & Water Watch found that Sysco's post-merger regional market share increased by an average of 55.7 percent (from an average 26.4 percent before the merger to 40.0 percent) and increased the HHI concentration level by an average 848 – four times the 200 point increase that suggests an increase in market power (*see* Table 3). In six regions (South Atlantic, Mountain, West South Central, West North Central, New England and East North Central), the regional concentration increased from un-concentrated to moderately concentrated, with an average increase in concentration of 974 points. These regions exhibit post-merger concentration increases that "potentially raise significant concentration concerns and often warrant scrutiny."[66]

Table 4. Foodservice Distribution Center Concentration in Selected States

	Post-Merger Concentration Level	Top 50 Distribution Centers	Est. Total Foodservice Wholesale Establishments	# Top 50 Companies Serving the State	Sysco % Distrib	USF % Distrib Sites	Post-Merger % Distrib Sites	HHI Pre-Merger	HHI Post-Merger	Increase in HHI
Alabama	Moderately	6	8	10	26.7%	13.3%	40.0%	1093	1982	889
Arizona	Moderately	8	10	6	20.0%	20.0%	40.0%	940	1840	900
Arkansas	Highly	5	6	8	32.0%	16.0%	48.0%	1568	2592	1024
Florida	Highly	32	40	9	37.5%	12.5%	50.0%	1644	2638	994
Georgia	Moderately	15	19	9	26.7%	10.7%	37.3%	896	1579	683
Illinois	Moderately	15	19	11	32.0%	10.7%	42.7%	1284	2080	796
Indiana	Highly	3	4	9	26.7%	26.7%	53.3%	1476	2898	1422
Iowa	Moderately	4	5	7	20.0%	20.0%	40.0%	1240	2040	800
Kansas	Highly	3	4	9	26.7%	26.7%	53.3%	1476	2898	1422
Massachusetts	Moderately	8	10	12	20.0%	20.0%	40.0%	1220	2120	900
Michigan	Moderately	10	13	9	24.0%	8.0%	32.0%	912	1552	640
Minnesota	Moderately	13	16	9	18.5%	24.6%	43.1%	1123	2183	1060
Mississippi	Moderately	4	5	7	20.0%	20.0%	40.0%	1240	2040	800
Missouri	Moderately	8	10	7	20.0%	20.0%	40.0%	1240	2040	800
Nebraska	Moderately	5	6	7	16.0%	16.0%	32.0%	1568	2080	512
Nevada	Highly	7	9	8	34.3%	34.3%	68.6%	2374	4725	2351
New Jersey	Moderately	13	16	17	24.6%	18.5%	43.1%	1046	1955	909
New Mexico	Moderately	5	6	8	16.0%	16.0%	32.0%	800	1568	768
North Carolina	Highly	11	14	8	43.6%	14.5%	58.2%	2198	3467	1269
North Dakota	Moderately	5	6	5	16.0%	32.0%	48.0%	1344	2368	1024
Oklahoma	Highly	7	9	5	45.7%	22.9%	68.6%	2743	4833	2090
Pennsylvania	Moderately	17	21	17	18.8%	18.8%	37.6%	816	1547	731
Tennessee	Moderately	16	20	12	25.0%	15.0%	40.0%	990	1765	775
Texas	Moderately	44	55	11	34.5%	9.1%	43.6%	1354	2035	681
Utah	Highly	3	4	5	26.7%	26.7%	53.3%	1476	2898	1422
Virginia	Moderately	9	11	12	26.7%	17.8%	44.4%	1379	2327	948
Washington	Moderately	7	9	4	11.4%	22.9%	34.3%	1851	2374	522
Wisconsin	Highly	6	8	6	40.0%	13.3%	53.3%	1804	2871	1067

Proposed merger would enhance Sysco market power in 28 states

Food & Water Watch found that the proposed merger would substantially increase Sysco's market share and concentration in most (28) states. States are imperfect market geographies but do reflect the markets where independent foodservice establishments purchase their supplies. Because average food deliveries may travel about 250 miles, some establishments may be served by

[66] DoJ/FTC at 19.

distribution centers across state lines. Nonetheless, the state concentration levels are instructive and demonstrate the proposed merger's impact on local markets.

The merger would increase the concentration in eight already highly concentrated states (Florida, Indiana, Kansas, Nevada, North Carolina, Oklahoma, Utah and Wisconsin) and increase the concentration level from moderately concentrated to highly concentrated in Arkansas (*see* Table 4).[67] The merger would increase Sysco's market share from about one-third (34.8 percent) to more than half (56.3 percent); in four of the states, the merger would double Sysco's market share. In all nine of these states, the merger would result in highly concentrated state markets where the HHI concentration level increased by more than 200 points, a level of concentration that is "presumed to be likely to enhance market power."[68] In fact, the average increase in concentration in these nine states was not 200 but 1,451 – seven times higher than the presumption of enhanced market power.

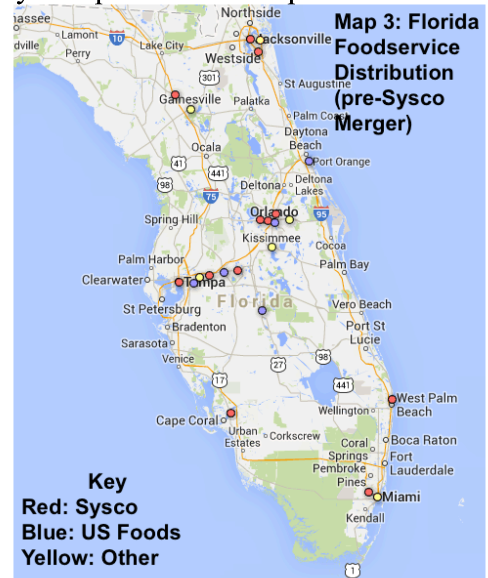
In another 19 states, the merger would result in moderately concentrated markets.[69] In eleven of these states, the merger would double Sysco's market share. Sysco would have an average 44.9 percent market share in these moderately concentrated states after the merger. In twelve of these states, the merger would transform un-concentrated state markets into moderately concentrated state markets; in all nineteen states, the increase in the HHI concentration levels exceeded 100 points (averaging a 797 point increase). These moderately concentrated states with substantial increases in concentration levels "potentially raise significant competition concerns and often warrant scrutiny."[70]

Proposed merger significantly increases concentration in local and metropolitan markets

The proposed merger would significantly increase Sysco's dominant local footprint in key markets and would enhance Sysco's market power in many metropolitan and local areas across the country

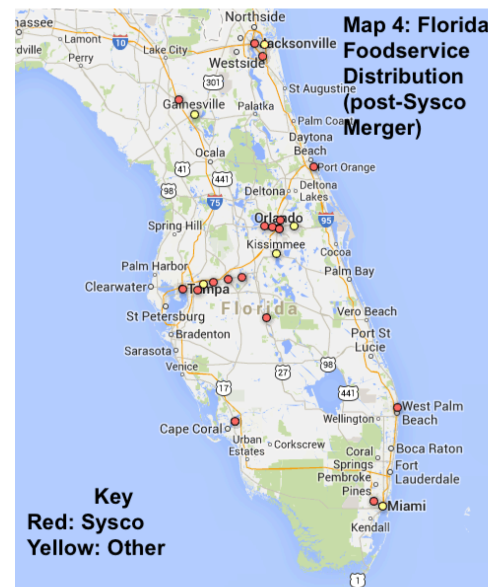
[67] The U.S. Department of Justice and U.S. Federal Trade Commission consider markets with HHI concentration levels over 2,500 to be highly concentrated.
[68] DoJ/FTC at 19.
[69] The U.S. Department of Justice and U.S. Federal Trade Commission consider markets with HHI concentration levels between 1,500 and 2,500 to be moderately concentrated.
[70] DoJ/FTC at 19.

(see maps 5 and 6 at Appendix for examples). Food & Water Watch believes that the increased consolidation raises antitrust concerns in many markets that warrant divestitures to ensure that local foodservice customers can secure supplies in a sufficiently competitive marketplace. Food & Water Watch plotted the locations of the distribution centers of the top five broadline foodservice distribution firms before and after the proposed merger and found that the merger clearly erodes competition on the local level. Southern California and Central Florida are illustrative of the deleterious effect the proposed merger would have on many parts of the country.



Southern California: Prior to the merger, in the area around Los Angeles and San Diego, Sysco had seven distribution centers and US Foods had three, with two other facilities operated by much smaller third-place competitor Performance Food Group (*see* Map 1). In both Los Angeles and San Diego, US Foods and Sysco directly compete. However, after the merger, Sysco would essentially have complete control over the entire region. In San Diego the only local option would be Sysco, and in Los Angeles, Performance Food Group with its two facilities must compete for restaurant business with the eight Sysco distribution centers in the area surrounding Los Angeles, for which Performance Food Group could not possibly provide equivalent capacity. (*see* Map 2).

Central and Southern Florida: In Florida, the pre-merger landscape had 12 Sysco Facilities, five US Foods locations, and six other facilities run by smaller competitors (*see* Map 3). After the proposed merger, Sysco would dominate the region. Sysco would have eleven distribution centers along the Interstate Route 4 corridor – in the Tampa Bay region one top four competitor has a single facility compared to five operated by Sysco (*see* Map 4). Around the hospitality hub of Orlando, Sysco would have four facilities with two other top-four distribution facilities. Prior to the merger, there were three Sysco facilities, one US Foods facility and two other rival distribution facilities. The merger effectively makes Sysco the dominant player in South Florida and probably the only single company that could supply to restaurants and food service institutions with multiple locations around the state.



Proposed Sysco-US Foods merger creates anticompetitive selling power over foodservice operators and ultimately consumers

The proposed merger will significantly disadvantage independent foodservice operations such as restaurants that will have fewer options from which to source their supplies. Foodservice

distributors provide foodservice operators with supplies, product information and credit to purchase their supplies.[71] Consolidation in foodservice distribution makes schools, hospitals, restaurants and other cafeterias more dependent on the remaining large suppliers and makes them vulnerable to unilateral price hikes. This kind of monopoly power allows sellers to keep prices higher than they would be under more competitive conditions.[72] As the foodservice segment has consolidated, revenues have risen as firms impose price hikes on their customers.[73]

Foodservice distribution customers like national restaurant chains would have significantly fewer options to source their supplies after the merger.[74] The giant hospitality and foodservice firm Aramark believes it is Sysco's biggest customer and purchases 60 percent of its food supplies from Sysco.[75] Many customers use both Sysco and US Foods, one as a primary supplier and the other as a backup supplier, and the elimination of the primary rivalry in foodservice distribution forces restaurants to either find another backup supplier or rely solely on the post-merger Sysco.[76] Some restaurants contend that the competition between Sysco and US Foods has been the sole leverage to prevent the distributors' power to impose price increases.[77]

The consolidated foodservice distribution market power is especially disadvantageous to independent restaurants. Foodservice distribution to independent restaurants and other independent foodservice operators has declined significantly. Sysco is rapidly shifting its business to larger regional and national customers.[78] Smaller, independent foodservice operators have difficulty getting supplied by larger distributors that are increasingly requiring minimum purchases for each delivery.[79] Average shipment and order size have been rising four percent annually in recent years.[80]

The merger of the two largest foodservice distributors will make it considerably harder and more expensive for smaller and independent foodservice outlets to secure supplies. Already, foodservice establishments face price markups that average 25 percent above manufacturers' prices and smaller, independent operations are more vulnerable to markup price gouging – including several alleged cases of fraudulent price padding.[81] This will be especially true in local markets where the merger considerably lessens competition, as noted above.

Proposed Sysco-US Foods merger exacerbates anticompetitive monopsony buyer power over suppliers

Foodservice distributors buy goods from food manufacturers and market their products to restaurants, cafeterias and other hospitality operations. Foodservice distributors (beyond the

[71] The Hale Group (April 2013) at 10.
[72] United States v. Cargill, Incorporated, and Continental Grain Company. United States District Court for the District of Columbia. Civil Action No. 99-1875 (GK). "United States Response to Public Comments." February 11, 2000 at 18.
[73] Grocery Manufacturers Association. "The GMA 2010 Logistics Benchmark Report." March 2010 at 5.
[74] Information Clearinghouse (2013) at 1.
[75] Aramark Corporation. U.S. Securities and Exchange Commission. 10-K filing. September 28, 2012 at 4.
[76] Gelles and De La Merced (2013).
[77] Gasparro, Annie and Jesse Newman. "Restaurants Fear New Food Giant's Clout," *Wall Street Journal*. January 7, 2014.
[78] Sysco Corporation (2013) at 8.
[79] The Hale Group (2013) at 11.
[80] Grocery Manufacturers Association (2010) at 5.
[81] Gasparro and Newman (2014).

obvious distributional value to manufacturers) historically helped determine the product mix offered by manufacturers, provided additional promotional services and set prices for sales to foodservice establishments, providing some integrated marketing services to manufacturers.[82] Bigger distributors are less likely to deal with smaller suppliers. Sysco's buyers are focused on large volume, high profit items, and their income is based on commission from this volume and profit. The company has thousands of products to sell to foodservice vendors all over the country, and it has little incentive to focus on buying from smaller and startup suppliers with lower volume food items.[83]

Larger distributors continue to collaborate and coordinate promotions and product launches with their manufacturer suppliers.[84] Mega-distributors have "distinct advantages" over manufacturers because their sheer size gives them the market power to leverage price concessions over their suppliers.[85] These bigger firms seek detailed cost information from their manufacturing suppliers purportedly to maximize their distributional efficiency,[86] but the market power of these larger distributors combined with the detailed information and integration with the manufacturers also gives them tremendous leverage over their suppliers. Manufacturers that become entangled with information sharing and integrated supply chain management with the largest foodservice distributors may be less able to switch to smaller, regional distributors.[87]

Sysco is shifting both its supplies and sales to increased use of contracts.[88] Sysco reports that the use of long-term contracts with suppliers is increasing to improve category management.[89] The use of contracts can exacerbate market power because buyers have more difficulty switching to alternate suppliers.[90] Manufacturers without extensive ties to Sysco or US Foods or those that want to avoid over reliance on a single distributor would have to develop relationships with distributors beyond Sysco and US Foods to provide "broad customer access" to their products.[91]

Although buyer power is similar to seller power, buyers can extract greater leverage over suppliers with lower market shares than are typically necessary to capitalize on monopoly seller power. Sellers may need to control more than half of the consumer market to exercise single-firm monopoly power, but buyers can potentially exert dominance over suppliers with less than ten percent of the purchasing market share.[92] The market pressure that encourages competitors to undercut price-gouging monopolist sellers to capture consumer markets does not work as well on

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[82] The Hale Group (April 2013) at 9.
[83] Ennis, Jim. "Characterizing Optimal Business Conditions for Commerce Between Farmers and SYSCO - Phase Two." Final Report to the Value Chain Partnerships for a Sustainable Agriculture project (VCPSA) and the Regional Food Systems Working Group (RFSWG). July 2006 at 15.
[84] Blissett, Hahn and Boyce (2008) at12.
[85] *Ibid*. at 5.
[86] Franklin Foodservice Solutions (2009) at 2.
[87] *Ibid*. at 6.
[88] The Hale Group (2013) at 9.
[89] Sysco Corporation (2013) at 7.
[90] DoJ/FTC at 17.
[91] The Hale Group/IFMA (2013).
[92] Foer, Albert A. American Antitrust Institute. "Mr. Magoo Visits Wal-Mart: Finding the Right Lens for Antitrust." Working Paper No. 06-07. November 30, 2006 at 5.

the buyer side. Because all buyers benefit when purchase prices are low, there is little incentive in a concentrated market for competitors to bid up input prices. [93]

This monopsony power is especially damaging to innovative and emerging food companies that have difficulty getting to consumers because of the intense consolidation in the distribution and retail market. The owners of the organic beverage manufacturer Honest Tea sold the company to Coca-Cola to access its distributional network.[94] Foodservice operators like schools and hospitals have had difficulty meeting the demand – and sometimes mandate – to offer local foods because the largest foodservice distributors have been unwilling to serve this small but growing demand.[95]

Although Sysco has an aggressive public relations promotion of a more diverse food supply, including "sustainable" food products, Sysco mainly distributes "nationally-branded merchandise" primarily from large food manufacturers and processors.[96] The merger between Sysco and US Foods will make it harder for innovative new companies to get into the foodservice marketplace and contribute further to an already over consolidated food manufacturing and processing sector.

* * *

The proposed merger significantly increases concentration in foodservice distribution and raises several relevant questions for the Federal Trade Commission:

1) Has the Federal Trade Commission adequately assessed the national, regional, state and local markets for foodservice distribution? The proposed merger will have a markedly more significant impact on many areas of the country and many local or metropolitan markets are likely to be more acutely affected. The Federal Trade Commission must fully analyze the impact of the merger on local, state and regional customers with an especial focus on the impact of the elimination of Sysco's main and most aggressive rival.

2) Has the Federal Trade Commission assessed the impact the proposed merger will have on consumers? Consumers spend nearly half their food dollars away-from-home and consumer away-from-home food prices rose nearly 50 percent faster than wages between 2010 and 2012.[97] The proposed merger is likely to increase costs for foodservice establishments, which will in turn likely pass these costs onto consumers. To date, Sysco has been "one of the most aggressive on pricing," according to foodservice industry F&D Reports because it can "easily absorb short-term margin pressures" and disadvantage its smaller competitors.[98] Sysco reports that it may undercut prices and erode margins "to attract and retain customers."[99] The proposed merger will potentially give Sysco enough

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[93] Carstensen, Peter C. University of Wisconsin Law School. Statement Prepared for the Workshop on Merger Enforcement. February 17, 2004 at 3.
[94] Cohen, Deborah L. "Honest Tea founder on being owned by Coke: 'It's a dual identity.'" *Reuters*. May 20, 2011.
[95] Field, Jay. "Distributors slow to embrace local food movement." *National Public Radio*. May 3, 2010.
[96] Sysco Corporation (2013) at 2.
[97] U.S. Bureau of Labor Statistics. Monthly average consumer price index for food away from home (CUSR0000SEFV) and average hourly earnings of private sector production workers and non-supervisory employees (CES0500000008).
[98] Information Clearinghouse (2013) at 1.
[99] Sysco Corporation (2013) at 6.

market power to abandon its aggressive pricing since the merger eliminates its chief rival. Consumers will end up paying the price for this enhanced market power.

3) Has the Federal Trade Commission considered the impact the merger will have on the hundreds of thousands of independent restaurants, which are small businesses? Nearly 700,000 restaurants are single-unit operations according to National Restaurant Association statistics.[100] The proposed merger will enhance the market power of the primary supplier to this crucial segment of the small business sector and potentially undermine the economic viability of this industry for family-owned, independent small businesses.

4) Has the Federal Trade Commission considered the impact the merger will have on the many foodservice establishments that are public or non-profit entities – like schools and hospitals and government cafeterias? These cafeteria operations would be substantially harmed by the exercise of unilateral market power that would increase their costs (potentially increasing costs to taxpayers) and force them to raise their prices. Since many of these facilities serve lower- and moderate-income customers who are often nearly captive markets (in the case of school cafeterias and military PX customers), these potential price impacts would have deleterious effects on the income of these households.

5) Has the Federal Trade Commission taken into account the pending legal actions against foodservice distributors alleging fraudulent billing practices and the extent to which the consolidation in the industry and concomitant pricing power is enabling potentially anticompetitive and fraudulent practices that disadvantage small, independent foodservice establishments?

6) Has the Federal Trade Commission factored in the impact this merger will have on food manufacturers that supply to the food service industry, and whether Sysco's absorption of the only other major national buyer will allow Sysco to unilaterally reduce the prices it pays to manufacturers that would have significantly reduced options for buyers?

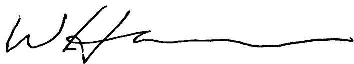
7) Has the Federal Trade Commission analyzed the impact this merger will have on new and innovative market entrants, including organic, natural, and sustainable food manufacturers, which as smaller companies, may not be able to provide the scale and production capacity that a national foodservice distributor would require before purchasing any of those products?

The food industry is already excessively concentrated. Food & Water Watch believes that this proposed merger would reduce competition in the foodservice industry and harm foodservice establishments, manufacturers and consumers. We request that no early termination of the antitrust evaluation be granted and that the investigation be extended.[101] The FTC must extend the merger-waiting period and make a second request to solicit further information from the parties and give

[100] National Restaurant Association. "2013 Restaurant Industry Pocket Factbook." 2013. More than 70 percent of the 980,000 restaurants are single-unit operations. http://www.restaurant.org/News-Research/Research/Facts-at-a-Glance.
[101] 15 USC§18(b)(1).

the agencies more time to review the complexities of the proposed merger.[102] Food & Water Watch would appreciate the opportunity to study these issues more closely and share our findings with the appropriate federal regulators.

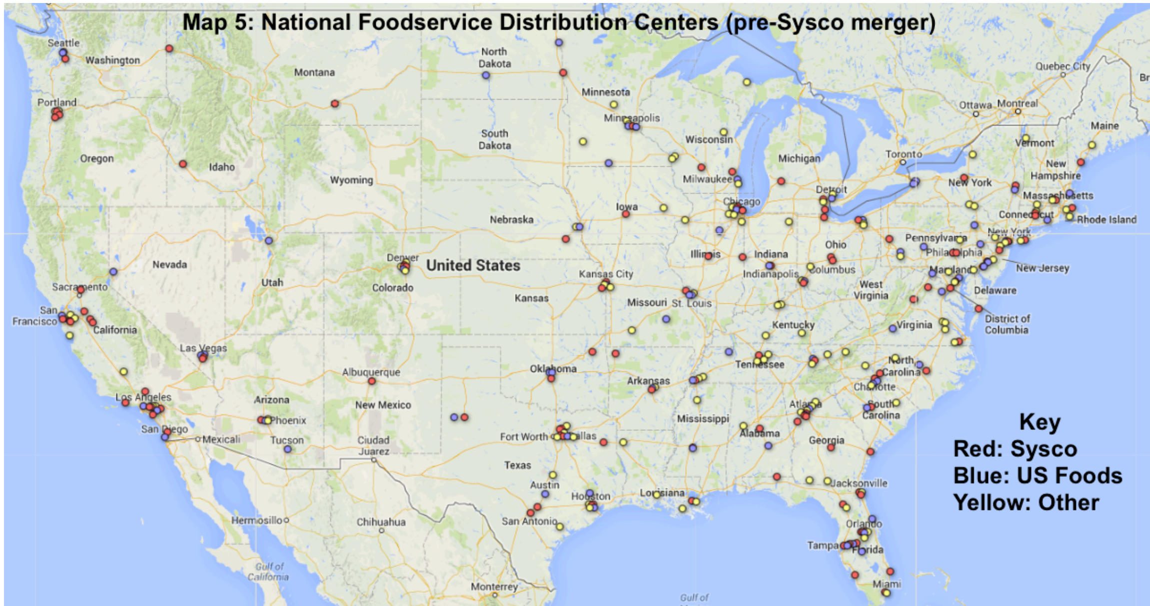
Sincerely,

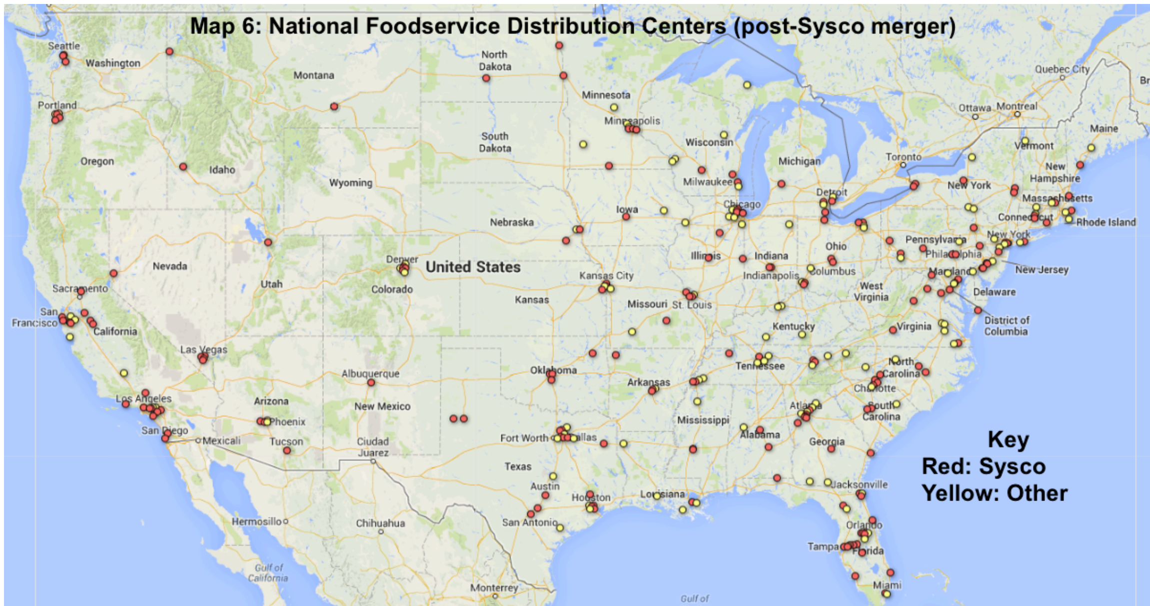


Wenonah Hauter
Executive Director

[102] 15 USC§18(e)(1).

Appendix: National Map of Top 5 Broadline Foodservice Distribution Facilities Pre- and Post Sysco-US Foods Merger





The American Antitrust Institute

February 25, 2014

The Honorable Edith Ramirez, Chairwoman
Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, D.C. 20580

Via Electronic Delivery Re: Proposed Merger of Sysco and US Foods

Dear Chairwoman Ramirez:

I. Introduction

The American Antitrust Institute (AAI) has been active in supporting a strong response to impediments to competition in all segments of the U.S. agricultural supply chain. This includes mergers, exclusionary conduct, and collusion that potentially harm competition and consumers in production, processing, food manufacturing, distribution, and retail grocery markets.[1] Major themes raised by industry participants in the joint U.S. Department of Justice (DOJ)/U.S. Department of Agriculture workshops held in 2010 coalesced around concerns over market concentration, merger enforcement, and monopsony.[2]

The proposed merger of Sysco and US Foods comes on the heels of a series of large mergers in the U.S. agriculture and food industries – transactions that extend and exacerbate the concerns raised in the 2010 joint workshops. The combination would enhance Sysco-US Foods' market power in the increasingly important broadline foodservice distribution market and create a monopoly in the national broadline foodservice market. The merger would likely result in higher prices; lower quality, reliability, and food safety; and less innovation – to the detriment of foodservice outlets and consumers of food that is prepared away from the home. The proposed merger also raises the specter of enhanced buyer market power and higher entry barriers for smaller, innovative or alternative food producers and systems.

For the reasons discussed in this letter, the proposed merger of Sysco and US Foods should be carefully scrutinized, not only in the context of the relevant markets identified, but also in terms of how it will alter the competitive dynamics between different segments of our increasingly concentrated food supply chain. The AAI urges the Federal Trade Commission (FTC) and state attorneys general investigating the proposed merger of Sysco and US Foods to collaborate with the DOJ. Both agencies have reviewed the mergers that have created the extraordinary levels of concentration and incentives for strategic competitive conduct in inter-related segments of the food supply chain. This letter frames out what the AAI believes are the key competitive issues raised by

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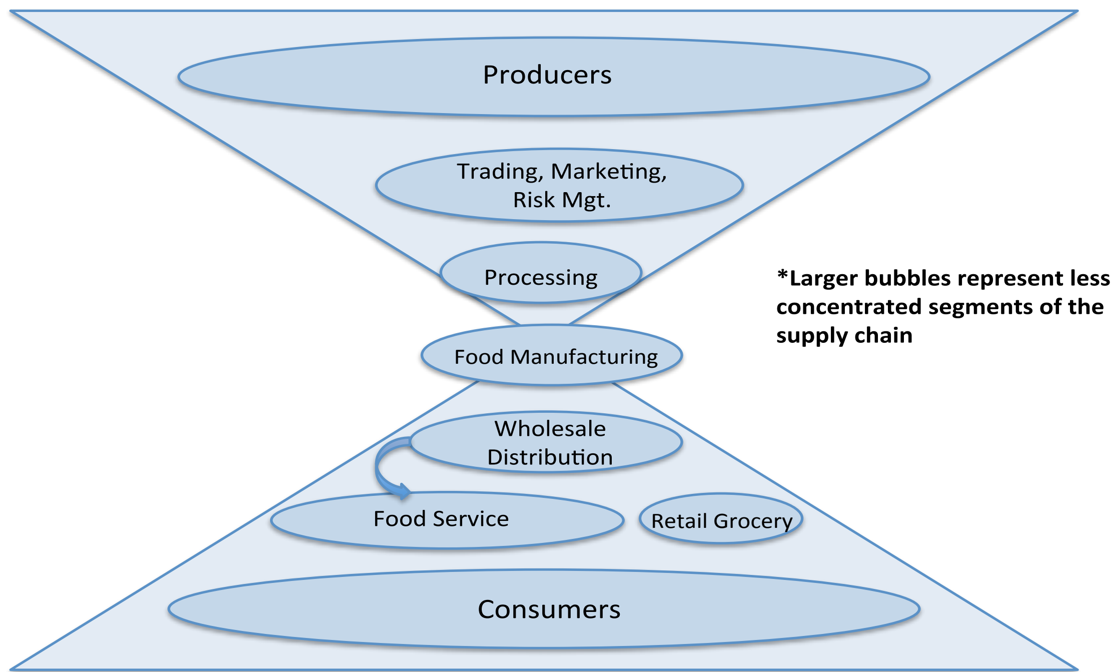
[1] The AAI is an independent non-profit education, research, and advocacy organization. Its mission is to advance the role of competition in the economy, protect consumers, and sustain the vitality of the antitrust laws. AAI is managed by its Board of Directors, which alone has approved this letter. For more information, see www.antitrustinstitute.org.
[2] U.S. Department of Justice, COMPETITION AND AGRICULTURE: VOICES FROM THE WORKSHOPS ON AGRICULTURE AND ANTITRUST ENFORCEMENT IN OUR 21ST CENTURY ECONOMY AND THOUGHTS ON THE WAY FORWARD (May 2012), at 4. Available http://www.justice.gov/atr/public/reports/283291.pdf.

the proposed merger, as well as important context and background that the agencies might consider in reviewing it.

II. Consolidation of the U.S. Agricultural and Food Supply Chains

In evaluating the proposed Sysco-US Foods merger, it is important to consider the broader picture of consolidation involving the U.S. agricultural and food supply chains. The weakened competitive health of the overall supply chain is depicted in the figure below. The upstream production segment is relatively atomistic and competitive. We note, however, that many of the antitrust immunities and exemptions in agriculture (e.g., the Capper-Volstead Act and Agricultural Agreement Marketing Act) that were originally intended to give producers bargaining power against powerful "middlemen" are now outdated. Many immunized cooperatives and associations have grown into large vertically and horizontally integrated entities that wield significant market power, exacerbating the plight of the independent, nonmember producer.

The upstream segment narrows significantly to a competition "bottleneck" in midstream food processing and manufacturing, both of which have become more concentrated over the last several years. The downstream food distribution and grocery segments have also experienced significant consolidation. The DOJ Antitrust Division has typically evaluated competitive issues involving the upper to middle portions of the agricultural supply chain while the FTC has handled some midstream industries, such as food manufacturing, and the downstream segments, including retail grocery mergers.



A brief look at merger enforcement statistics in agriculture and food provides important context for evaluating the Sysco-US Foods merger.[3] Almost 400 transactions in agriculture and food were reported under the Hart Scott Rodino (HSR) Premerger Notification Program over the last ten years (2003-2012). These transactions fall into three major categories: crop and animal production, food processing and manufacturing, and supermarkets and grocery stores. Crop and animal production account for only about six percent of food and agriculture-related merger transactions reported under the HSR program from 2003-2012, for which there were no second requests. At the downstream end of the supply chain, mergers of grocery stores account for about 13 percent of total HSR transactions reported, with a sporadic record of second requests over the period.

Consolidation in the grocery segment has continued relatively unabated over the several decades. Consumer food advocate Food & Water Watch (F&WW) explains that the "rise of the big-box food retailers like WalMart precipitated a wave of supermarket mergers starting in the 1990s that created a network of national supermarket chains."[4] WalMart's share of the national retail grocery market has increased from virtually nothing in the 1980s to 28 to 32 percent today.[5] Even in the absence of backward vertical integration, the presence of a dominant firm like WalMart is felt in virtually all segments of the supply chain through contracts and practices that affect prices, non-price terms and conditions, and even how food products are processed and manufactured.

About 81 percent of total reported HSR transactions from 2003-2012 involve food processing and manufacturing. Mergers in food production show a large increase in the mid-2000s (2006-2007), with a fall off until 2009, followed by a sharp rise in 2010. The rate of second requests involving food manufacturing mergers has trended downward since 2009, despite the uptick in merger activity in the same year. Food company consolidation continues, with predictions that merger activity will eventually reach the pre-2008 recession rate of 100 transactions annually.[6]

Beef packers, poultry processors, and food manufacturers have all responded to consolidation in the downstream portions of the supply chain by bulking up. Significant buyer and seller market power at the processing, food manufacturing, and grocery levels have induced a surge of consolidation to gain bargaining power in negotiating with input suppliers and customers. Examples of these deals – including some transactions that were challenged by the antitrust agencies – are: ConAgra-Ralcorp, ConAgra-Cargill-CHS Horizon Milling, U.S. v. George's Foods, LLC, George's Family Farms, LLC and George's, Inc., U.S. et al. v. Dean Foods Company, and U.S. et al. v. JBS S.A. and National Beef Packing Company, LLC.

ConAgra recently summed up the motivation for consolidation in the midstream and downstream segments of the food supply chain. In explaining its recent proposal to create Ardent Mills, a joint venture with Cargill/CHS Horizon Milling that would control over one-third of the U.S. wheat milling market, ConAgra stated: "Ardent Mills will set the new industry standard by addressing…the

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[3] Federal Trade Commission and U.S. Department of Justice, ANNUAL REPORTS TO CONGRESS PURSUANT TO THE HART-SCOTT-RODINO ANTITRUST IMPROVEMENTS ACT OF 1976, years 2003-2012. Available http://www.ftc.gov/policy/reports/policy-reports/annual-competition-reports.

[4] Food & Water Watch (F&WW), GROCERY GOLAITHS, December 5, 2013, at 3-4. Available http://www.foodandwaterwatch.org/reports/grocery-goliaths-how-food-monopolies-impact-consumers/.

[5] Grant Gerlock, *What Does Walmart Have To Do With Conagra's Move Into Store Brand Food?* April 10, 2013, NET News/Harvest Public Media, http://netnebraska.org/article/news/what-does-walmart-have-do-conagras-move-store-brand-food.

[6] F&WW, GROCERY GOLIATHS, *supra* note 4, at 5.

need for more cost-effective supply."[7] Another spokesman added: "The future of flour milling is tied to serving the innovation and supply chain management challenges of food producers."[8]

Much of the "domino effect" consolidation in midstream processing, food manufacturing, and retail grocery has adversely affected producers, who are squeezed by powerful processors and food manufacturers, who are in turn squeezed by powerful grocers. United Food & Commercial Worker Union data reveals that while the packers have actually defended or even increased their margins, the farmer's share of the food dollar has plummeted. For example, the rancher received $.59 of the beef dollar in 1990 but only $.42 in 2009. The pig farmer received $.45 of the pork dollar in 1990, but only $.25 in 2009.[9] At the other end of the supply chain, the consumer has higher prices, potentially greater food safety problems, and less choice to show for consolidation. Between 2010 and 2012, for example, grocery food prices rose twice as quickly as average wages.[10]

III. The Sysco-US Foods Merger in Context of Broader Supply-Chain Consolidation

Food distributors now appear to be joining ranks with powerful processors, food manufacturers, and grocers in order to exploit and respond to shifts in the balance of economic power in the midstream to downstream segments of the supply chain. To date, retail grocery consumers have battled rising prices, quality issues, and lack of choice. Now restaurants, schools, colleges, universities, healthcare facilities, the government and military, hotels, and business/industry will fall increasing victim to the ongoing parlay of countervailing market power between the midstream and downstream segments.

The proposed Sysco-US Foods merger extends consolidation in distribution with the largest deal to date. For example, F&WW estimates that in 2012, nine of the biggest 60 foodservice distributors with total revenue of about $3 billion were absorbed by mergers. Between 2008 and 2013, the five largest foodservice distributors purchased about three-quarters of the 86 independent foodservice distributors. In 2013 alone, Sysco purchased 14 companies with total revenue of more than $1 billion, representing about half of Sysco's revenue growth in 2013.[11]

Sysco is the largest U.S. firm in the sale, marketing, and distribution of food products to restaurants, healthcare and educational facilities, the hospitality industry, and other customers that specialize in meals away from home. Sysco also sells equipment and supplies for the foodservice and hospitality industries. The company operates 193 distribution facilities and has about $44 billion in revenue for fiscal year 2013.[12] US Foods is the second largest U.S. foodservice distributor to restaurants,

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[7] Carey Gillam, *Flour power: ConAgra, Cargill, CHS to create mega-miller*, newsandinsight.thomsonreuters.com, March 5, 2013, http://newsandinsight.thomsonreuters.com/Legal/News/2013/03_-_March/Flour_power_ConAgra,_Cargill,_CHS_to_create_mega-miller/ and *ConAgra Foods, Cargill and CHS announce agreement to form joint venture combining flour milling businesses into new company, Ardent Mills*, cargill.com, March 15, 2013, http://www.cargill.com/news/releases/2013/NA3071787.jsp.

[8] *Id.*

[9] The meat packer's share of the beef dollar increased from $.08 in 1990 to $.09 in 2009. The pork packer's share of the pork dollar increased from $.10 in 1990 to $.14 in 2009. *See,* United Food and Commercial Workers, ENDING WALMART'S RURAL STRANGLEHOLD (2010), at 3-4. Available http://grist.files.wordpress.com/2010/09/ag_consolidation_white_paper2.pdf?CFID=10082208&CFTOKEN=55376804.

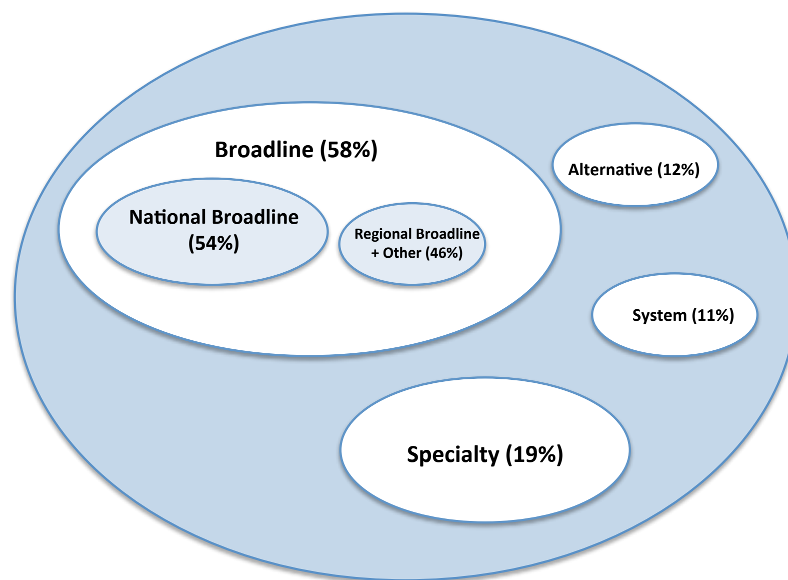
[10] F&WW, GROCERY GOLIATHS, *supra* note 4, at 2.

[11] Food & Water Watch, letter to Deborah L. Feinstein, Director, Bureau of Competition Office of Policy and Coordination, Federal Trade Commission, January 8, 2014, at 3-4.

[12] The Sysco Story, http://sysco.com/about-sysco.html.

healthcare and hospitality facilities, government operations and educational institutions. In 2013, US Foods had $22 billion in annual revenue with more than 60 locations nation-wide.[13]

As shown in the figure below, there are a number of important distinctions regarding the foodservice distribution market that are relevant to the proposed Sysco-US Foods combination. Foodservice is a subset of the wholesale food distribution market, with a value of about $175 billion in the U.S. in 2010.[14] Industry experts generally include four different types of distributors in the foodservice market: broadline distributors, system distributors, specialty distributors (e.g., dairy, produce, etc.), and alternative distributors (e.g., Costco, etc.).[15] Based on 2010 data, Sysco had about a 20 percent share of the total foodservice market, followed by US Foods with 11 percent. They are followed by Performance Food Group (PFG), with about a 6 percent share, and Gordon Food Service, with about 4 percent of the market.[16] Notably, Sysco accounted for about 36 percent of the growth in the foodservice industry from 2003-2010.[17]



[13] US Foods, *About Us: First in Food*, http://www.usfoods.com/about-us.html.
[14] In 2007 foodservice was estimated to account for just over 20 percent of total wholesale food sales. *See* U.S. Department of Agriculture (USDA), Economic Research Service (ERS), *Retailing and Wholesale*, http://www.ers.usda.gov/topics/food-markets-prices/retailing-wholesaling/wholesaling.aspx#.Uwwm9Ci2pD4. *See also* FOODSERVICE DISTRIBUTORS OF THE FUTURE – THE EVOLUTION OF THE FOODSERVICE DISTRIBUTOR SECTOR, IFMA's Foodservice 2020 Strategic Issues Series, The Hale Group (no date), at 1-2, http://www.halegroup.com/~halegrou/wp-content/uploads/2013/01/Distributor-of-the-Future.pdf. *See also Focus on Foodservice Distribution*, The Hale Group (April 11, 2013), http://enterprisectr.org/wp-content/uploads/2013/04/MacPhail-Distribution-Ent-Cent-Program-10-April.pdf. Estimated sales by the foodservice industry in the U.S. in 2012 are $226 billion. *See* http://www.ifdaonline.org/About-IFDA/Who-Are-Foodservice-Distributors.
[15] USDA-ERS, *supra* note 14, and The Hale Group, *supra* note 14, at 2.
[16] *Id. See also* Sysco: INVESTOR DAY 2010, December 2, 2010, http://files.shareholder.com/downloads/SYY/1124004662x0x425013/e7a21c77-2b2e-4cf6-b6c0-9b059aa02865/Investor_Day_2010_FInal_8-K.pdf.
[17] The Hale Group, *supra* note 14, at 3.

Broadliners (national and regional) comprise almost 60 percent of the total foodservice market. They distribute food and paper and plastic products to schools and universities, hospitals, military bases, chain and independent restaurants, catering services, and hospitality outlets. Broadliners display economies of scale in distribution with the ability to buy an array of foods in large volumes, with well-developed distribution networks of sales and delivery personal, and the ability to deliver products to multiple types of outlets. Likewise, foodservice consumers rely on broadliners for economies of purchasing, their vast distribution networks, and one-stop-shop procurement.

Broadline foodservice distribution has grown in importance over time. For example, in 1995, broadline distribution (national and regional) accounted for 45 percent of total foodservice sales. By 2010, this share had risen to 58 percent.[18] As shown in the table below, Sysco accounts for about 35 percent of the broadline foodservice market, while US Foods accounts for about 19 percent. Together, Sysco and US Foods would control about 54 percent of the broadline market – a significantly higher market share than they possess in all foodservice (31 percent).[19] The merger would increase concentration by 1,307 HHI points, resulting in a highly concentrated market (3,169 HHI). In a broadline foodservice market, the proposed merger far exceeds the tolerance limits for changes in concentration and post-merger concentration that are set forth in the DOJ/FTC 2010 HORIZONTAL MERGER GUIDELINES.

In the national broadline foodservice market, the merger of Sysco and US Foods is a merger to monopoly, with an increase in market concentration (as measured by the HHI) of 4,515 points, and post-merger concentration of 10,000 HHI.[20] From the perspective of consumers that rely on national broadliners to satisfy their demand for products, the market is far from "highly fragmented," as Sysco attests.[21]

Table: Market Shares of Sysco and US Foods in Foodservice Markets

	Market Shares of Sysco and US Foods (2010)		
Firm	**All Foodservice Market[22]**	**Broadline Foodservice Market**	**National Broadline Foodservice Market**
Sysco	20%	35%	66%
US Foods	11%	19%	34%
Merged Firm	31%	54%	100%
Change in HHI	-	1,307	4,515
Post-merger HHI	-	3,169	10,000

IV. A Sysco-US Foods Combination Raises a Number of Competitive Issues

The dynamics in the broader food supply chain bring the proposed merger of Sysco and US Foods into sharper focus. As shown in the figure, foodservice distribution – particularly broadline distribution – is a major input to foodservice. The merger of Sysco and US Foods will combine two

[18] *Id.,* at 2.
[19] Gordon Foodservice is the largest regional broadliner. *See* Sysco INVESTOR DAY 2010, *supra* note 16.
[20] Sysco appears to consider Performance Food Group to be a national broadliner. See, e.g., *supra* note 16, at 6. However, we note that PFG is one-fifth the size of Sysco and one-fourth the size of US Foods in terms of number of distribution centers. *See, e.g.,* http://www.foodservice.com/foodshow/foodservice_distributors.cfm.
[21] Sysco INVESTOR DAY 2010, *supra* note 16, at 6.
[22] Based on 2013 data, Sysco and US Foods would have a combined share of 35 percent. *See What the Sysco/US Foods merger means for foodservice manufacturers,* The Hale Group, December 11, 2013, http://www.ifmaworld.com/articles/what-the-sysco-us-foods-merger-means-to-foodservice-manufacturers/.

largest broadline distributors and only two national broadliners. The proposed merger raises at least four competitive issues, by: (1) perpetuating domino-like consolidation in the supply chain, leading to instability, safety and reliability problems, and lack of choice, (2) eliminating head-to-head competition between major rivals, (3) increasing concentration in local and regional geographic markets, and (4) enhancing buyer market power and barriers to entry for smaller or alternative food systems.

A. The proposed merger perpetuates "domino-like" consolidation in the supply chain

As noted earlier, the proposed merger of Sysco and US Foods is likely motivated by the acquisition of bargaining market power in dealing with major food manufacturers and processors. By amassing dominance in the distribution segment, Sysco and US Foods will enhance their buyer power vis-à-vis these midstream entities. A Sysco-US Foods merger will perpetuate the cycle of consolidation in the midstream segment. If approved, there is no logical end to this kind of "domino effect" consolidation, which would erect enormous barriers to entry for smaller and innovative food producers, promote a lack of redundancy and diversity of suppliers, eliminate consumer choice, and potentially increase food safety and reliability problems.

The merger will therefore exchange price determination through market forces for bargaining between powerful suppliers and customers. This is an inferior outcome from the perspective of foodservice outlets that feed a major part of the consuming public when they eat away from home. Vigorous enforcement of the U.S. merger law is a key tool for preventing a bad situation from getting worse. At the same time, however, the government must also begin a process of decentralization up and down the supply chain through advocacy of legislative reform.

B. Sysco and US Foods are likely each other's closest rivals for foodservice outlets that require national broadline distribution

Large chain restaurants, healthcare facilities, schools, and other large foodservice customers require the economies of purchasing associated with one-stop shopping and large distribution networks. Sysco and US Foods are the only two national broadline suppliers with the scale and scope to meet these needs. Together, they will command 54 percent of the broadline foodservice market and 100 percent of the national broadline foodservice market. In light of this dominance, the AAI encourages the FTC to explore the unilateral effects of the proposed merger, for several reasons.

First, if a relevant product market is defined to be broadline foodservice distribution, Sysco and US Foods are very likely to be each other's closest competitors. The proposed merger would eliminate this vital head-to-head competition. For example, in the event of a price increase by either Sysco or US Foods, a high proportion of sales to foodservice customers that require broadline services would be diverted to the merging partner. The fact that the merging partners would capture the bulk of each other's sales in the event of a price increase means that a post-merger price increase would likely be profitable. Upward pricing pressure should therefore a significant concern. In national broadline foodservice, the merger of Sysco and US Foods is a merger to monopoly. The diversion of sales from one merging partner to the other would be so significant as to guarantee upward pricing pressure.

Second, it is unlikely that regional broadliners could have the capacity or ability to respond to a price increase by expanding their business. There is no other truly national broadliner. PFG is one-fifth

the size of Sysco and one-fourth the size of US Foods in terms of number of distribution centers.[23] PFG and regional broadliners may have neither the existing scale, nor ability to expand on a national scale in response to a post-merger price increase. They may also be non-viable alternatives from the consumer perspective. Larger foodservice outlets utilize national broadliners to exploit purchasing economies, extensive distribution networks, and lower transactions costs, as opposed to patching sourcing together from regional or local distributors. And even if regional broadliners could absorb the demand from Sysco-US Foods customers, switching costs associated with shifting purchases are likely to be high.

C. The proposed merger will likely have a significant adverse effect on regional and local geographic markets

The proposed merger also raises concerns about its effect on smaller chains and independent restaurants, catering firms, and hotels as well as schools, hospitals, and other foodservice outlets in local and regional geographic markets. In these markets, Sysco and US Foods may compete to some extent with regional broadline distributors, other regional distributors, and local distributors. While these markets may appear to contain a significant range and number of competitors, it is clear that many of them are likely to be concentrated. Publicly available information indicates that there are overlaps between Sysco and US Foods distribution centers in an estimated 30 U.S. cities. F&WW has analyzed regional foodservice distribution center concentration for nine regions of the U.S. and found that the proposed merger will increase concentration in some regions beyond the tolerance limits set forth in the DOJ/FTC 2010 HORIZONTAL MERGER GUIDELINES.[24]

The AAI encourages the FTC to look closely at geographic market overlaps involving regional and local distribution and consider a number of issues that bear on competition in regional and local food distribution markets. First, larger foodservice outlets are unlikely to satisfy their purchasing needs from smaller local distributors. For example, local competition may not offer the same breadth of products or distribution networks that Sysco or US Foods can provide.

Second, the AAI would caution against overreliance on the role of distributors of locally sourced ingredients such as meat and produce as a constraint on the pricing of larger distributors. Sysco acknowledges this industry trend in its most recent Form 10-K: "Non-traditional competitors are becoming more of a factor in terms of competition within our industry, and consumer spending trends are gradually shifting more to fresh, natural and sustainably-produced products."[25] This observation should be interpreted as a signal that Sysco needs to enhance efforts to obtain locally-sourced ingredients, as opposed to concern over the impact of local distribution on tempering its significant market power. While the effects of the locally sourced ingredient movement may be felt on the margin, it is likely that only a small proportion of foodservice customers focus on consumer demand in this niche market. Local providers do not have the ability to impose pricing restraint on national or regional foodservice distributors, or other types of food distributors.

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[23] Foodservice.com, *supra* note 20.
[24] F&WW letter to the FTC, *supra* note 11.
[25] Sysco Form 10-K (period ending August 29, 2013) at 18, August 27, 2013, http://sysco.q4cdn.com/960c5a82-89cd-4828-9d4b-be722a91725b.pdf.

D. The proposed merger is likely to enhance buyer power and raise barriers to entry for alternative food producers and systems

As noted earlier, the proposed merger of Sysco and US Foods is likely motivated by the acquisition of bargaining power in dealing with major food manufacturers and processors. By amassing dominance in the distribution segment, Sysco and US Foods will enhance their buyer power vis-à-vis these midstream entities. For those smaller food processors and producers, there is a real chance that a merged Sysco-US Foods could exercise its enhanced monopsony power in distribution to depress the prices paid for their products.

The effects of enhanced buyer power exercised by Sysco and US Foods would be felt by food processers and producers in directly adjacent markets, and also further upstream. For example, as processors and producers are squeezed, they respond by squeezing their own input suppliers – especially those who are powerless. Hence, the response to buyer pressure is often to drive further down the prices paid for inputs from those providers who cannot resist effectively, i.e., those with high switching costs, high sunk costs, or no viable alternative outlets.

A Sysco-US Foods merger also opens a "Pandora's box" of potential incentives to impose or pressure foodservice customers into exclusive or sole source contracts and complex, potentially exclusionary bundling of foodservice products. As we have observed in the healthcare industry (e.g., Group Purchasing Organizations), this type of concentration in aggregation and distribution has led to the exclusion of smaller drug and medical device manufacturers, thus hampering innovation, reducing redundancy in the supply chain, and reducing benefits to consumers. To the extent that alternative food systems are attempting to gain a foothold in the market, the prospect of dealing with a merged Sysco-US Foods that would deal only with large food processors and manufacturers is likely to make entry and expansion of those systems more difficult.

V. Conclusion

The AAI strongly encourages the FTC to consider the issues raised in this letter when evaluating the potential competitive effects of a Sysco-US Foods merger. Adverse effects could be felt at any number of stages in the food supply chain, raising concerns about prices, food quality and safety, innovation, and choice. We appreciate your attention to this matter. If the AAI can be of further assistance, please feel free to contact us.

Sincerely,

Diana Moss
Vice-President, American Antitrust Institute

cc:
The Honorable William J. Baer, Assistant Attorney General, U.S. Department of Justice Antitrust Division
The Honorable Julie Brill, Commissioner, Federal Trade Commission
The Honorable Maureen K. Ohlhausen, Commissioner, Federal Trade Commission
The Honorable Joshua D. Wright, Commissioner, Federal Trade Commission
Deborah Feinstein, Director, Bureau of Competition, Federal Trade Commission

Press Releases

Sysco Corporation Receives Request for Additional Information From FTC Regarding Proposed US Foods Merger

HOUSTON, Feb. 18, 2014 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) announced today that it received a request for additional information and documentary materials from the Federal Trade Commission (FTC) in connection with Sysco's pending merger with US Foods. The request was issued under notification requirements of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act).

Frequently referred to as a "second request," this is a standard part of the FTC review process and was anticipated by Sysco. Sysco will continue to work closely and cooperatively with the FTC as it conducts its review of the proposed merger.

Completion of the transaction remains subject to regulatory review, including the expiration or termination of the waiting period under the HSR Act, and other customary closing conditions. Sysco's outlook on the transaction, and the likely timing for closing in the third quarter of calendar 2014, remains unchanged.

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 193 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2013 that ended June 29, 2013, the company generated record sales of more than $44 billion. Connect with Sysco on Facebook at **www.facebook.com/SyscoCorporation** or Twitter at **www.twitter.com/Sysco**.

Additional Information for US Foods Stockholders

In connection with the proposed transaction, Sysco currently intends to file a Registration Statement on Form S-4 that will include a consent solicitation statement of US Foods. Sysco also plans to file other relevant materials with the SEC. Stockholders of US Foods are urged to read the consent solicitation statement/prospectus contained in the Registration Statement and other relevant materials because these materials will contain important information about the proposed transaction. These materials will be made available to the stockholders of US Foods at no expense to them. The consent solicitation statement/prospectus, Registration Statement and other relevant materials, including any documents incorporated by reference therein, may be obtained free of charge at the SEC's website at **www.sec.gov** or for free from Sysco at **www.sysco.com/investors** or by emailing **investor_relations@corp.sysco.com**. Such documents are not currently available. You may also read and copy any reports, statements and other information filed by Sysco with the SEC at the SEC public reference room at 100 F Street N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at (800) 732-0330 or visit the SEC's website for further information on its public reference room.

This document shall not constitute an offer to sell or the solicitation of an offer to buy any securities, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to the registration or qualification under the securities laws of any such jurisdiction. No offering of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

Cautionary Statement Regarding Forward-Looking Statements

Information included in this document (including information included or incorporated by reference in this document) that look forward in time or that express beliefs, expectations, or hopes are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are all statements other than statements of historical facts. The words "anticipates," "may," "can," "plans," "believes," "estimates," "expects," "projects," "intends," "likely," "will," "should," "to be" and any similar expressions or other words of similar meaning are intended to identify those assertions as forward-looking statements. Such forward-looking statements reflect the views of management at the time such statements are made and are subject to a number of risks, uncertainties, estimates, and assumptions that may cause actual results to differ materially from current expectations, including but not limited to the ability of the parties to satisfy the conditions precedent and consummate the proposed merger, the timing of consummation of the proposed merger, and the ability of the parties to secure stockholder and regulatory approvals in a timely manner or on the terms desired or anticipated. For a discussion of additional factors impacting Sysco's business, see Sysco's Annual Report on Form 10-K for the year ended June 29, 2013, as filed with the Securities and Exchange Commission and the Company's subsequent filings with the SEC. For a discussion of additional factors impacting US Foods' business, see US Foods' filings with the SEC. Neither Sysco nor US Foods undertakes to update or revise any forward-looking statements, based on new information or otherwise.


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Sysco Corporation

Source: Sysco Corporation

Press Releases

Sysco-US Foods Merger Regulatory Review Remains on Track

HOUSTON, June 16, 2014 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) issued the following statement in response to a recent report containing unfounded, inaccurate and irresponsible rumors regarding the status of the Federal Trade Commission's review of the proposed Sysco-US Foods merger.

Bill DeLaney, Sysco president and chief executive officer, said: "In light of this recent misleading report, it's important to convey that Sysco continues to cooperate closely with the Federal Trade Commission in its review of the proposed merger of Sysco and US Foods. We are engaged in a productive dialogue with the FTC, and the review is proceeding as expected. We continue to believe that the Commission, once it finishes its investigation, will conclude that our industry is -- and will continue to be -- fiercely competitive. Our proposed merger will benefit customers and help us become more efficient in this rapidly evolving marketplace."

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 193 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2013 that ended June 29, 2013, the company generated sales of more than $44 billion. For more information, visit www.sysco.com or connect with Sysco on Facebook at www.facebook.com/SyscoCorporation or Twitter at www.twitter.com/Sysco. For important news regarding Sysco, visit the Investor Relations portion of the company's Internet home page at www.sysco.com/investors, follow us at www.twitter.com/SyscoStock and download the Sysco IR App, available on the iTunes App Store and the Google Play Market. In addition, investors should also continue to review our press releases and filings with the Securities and Exchange Commission. It is possible that the information we disclose through any of these channels of distribution could be deemed to be material information.

Cautionary Statement Regarding Forward-Looking Statements

Information included in this press release (including information included or incorporated by reference in this press release) that look forward in time or that express beliefs, expectations, or hopes are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are all statements other than statements of historical facts. The words "anticipates," "may," "can," "plans," "believes," "estimates," "expects," "projects," "intends," "likely," "will," "should," "to be" and any similar expressions or other words of similar meaning are intended to identify those assertions as forward-looking statements. Such forward-looking statements reflect the views of management at the time such statements are made and are subject to a number of risks, uncertainties, estimates, and assumptions that may cause actual results to differ materially from current expectations, including but not limited to the ability of the parties to satisfy the conditions precedent and consummate the proposed merger, the timing of consummation of the proposed merger, and the ability of the parties to secure stockholder and regulatory approvals in a timely manner or on the terms desired or anticipated. For a discussion of additional factors impacting Sysco's business, see Sysco's Annual Report on Form 10-K for the year ended June 29, 2013, as filed with the Securities and Exchange Commission, and the Company's subsequent filings with the SEC. For a discussion of additional factors impacting US Foods' business, see US Foods' filings with the SEC. Neither Sysco nor US Foods undertakes to update or revise any forward-looking statements, based on new information or otherwise.

Additional Information for USF Stockholders

In connection with the proposed transaction, Sysco has filed with the Securities and Exchange Commission ("SEC") a Registration Statement on Form S-4 that includes a preliminary consent solicitation statement of USF that also constitutes a prospectus of Sysco. The Registration Statement has not yet become effective. Sysco also plans to file other relevant materials with the SEC. Stockholders of USF are urged to read the preliminary consent solicitation statement/prospectus contained in the Registration Statement and other relevant materials that will be filed with the SEC carefully and in their entirety when they become available, because these materials will contain important information. The preliminary consent solicitation statement/prospectus, Registration Statement and other relevant materials, including any documents incorporated by reference therein, may be obtained free of charge at the SEC's website at www.sec.gov or for free from Sysco at www.sysco.com/investors or by emailing investor_relations@corp.sysco.com. Such documents are not currently available. You may also read and copy any reports, statements and other information filed by Sysco with the SEC at the SEC public reference room at 100 F Street N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at (800) 732-0330 or visit the SEC's website for further information on its public reference room.

This document shall not constitute an offer to sell or the solicitation of an offer to buy any securities, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to the registration or qualification under the securities laws of any such jurisdiction. No offering of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

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Charley Wilson
Vice President, Corporate Communications
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Sysco Corporation

Source: Sysco Corporation

Press Releases

Sysco Reaches Agreement to Sell 11 US Foods Distribution Centers to Performance Food Group Contingent on Consummation of Sysco-US Foods Merger

Package of Locations With $4.6 Billion in Annual Revenue Designed to Allay Federal Trade Commission Concerns

HOUSTON, Feb. 2, 2015 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) today announced that it has reached a definitive agreement to sell Performance Food Group 11 US Foods facilities related to its pending merger with US Foods. The divestiture package is contingent on consummation of the proposed merger of Sysco and US Foods announced in December 2013.

"Over the past 12 months, we have worked in good faith with the FTC to help them better understand the highly competitive U.S. foodservice distribution industry and the significant customer benefits that will result from the merger of Sysco and US Foods," said Sysco President and Chief Executive Officer Bill DeLaney. "Unfortunately, the FTC has taken a different view of the potential competitive impacts of the merger. While we respectfully but vigorously disagree with the FTC's analysis, we believe this divestiture package fully addresses its concerns."

Sysco will now present its position, including this proposed remedy, to the five FTC commissioners and seek to obtain their approval.

The agreement calls for Sysco to sell Performance Food Group the following US Foods facilities at the completion of the US Foods transaction: Corona, Calif.; Denver, Col.; Kansas City, Kan.; Phoenix, Ariz.; Salt Lake City, Utah; San Diego, Calif.; San Francisco, Calif.; Seattle, Wash.; Cleveland, Ohio; Las Vegas, Nev.; and Minneapolis, Minn.

In US Foods' most recent fiscal year, these distribution centers generated $4.6 billion in annual revenue. Sysco and Performance Food Group have also have agreed on a comprehensive multi-year transition services agreement to ensure a smooth transfer of assets from US Foods to Performance Food Group by providing various support services and personnel to help Performance Food Group succeed as the new business owner in these locations.

"The collection of distribution centers and other assets that Performance Food Group will acquire along with related support services agreements will enable us to compete effectively for national broadline foodservice customers," said George Holm, Performance Food Group Chief Executive Officer and President. "We are excited by the opportunities for growth presented by this transaction and are confident that we will effectively execute our plans to become one of the country's premier broadline distributors serving customers coast to coast."

After selling these facilities, Sysco estimates it still will be able to achieve net annual synergies of at least $600 million in four years. This estimate reflects additional synergies identified during the company's integration planning efforts.

"Our analysis shows that our projected synergies will remain as substantial as we had previously outlined, even after reflecting the impact of divestitures," DeLaney said. "This is a testament to the strength of our ongoing integration planning work and reaffirms the major efficiencies we can achieve by bringing Sysco and US Foods together. These savings will position Sysco to deliver significant new value to our customers, including lower costs."

Conference Call & Webcast

Sysco will discuss these matters with analysts and investors on its second quarter fiscal 2015 earnings conference call on Monday, February 2, 2015, at 10:00 a.m. Eastern. A live webcast of the call, a copy of this press release and a slide presentation will be available online at www.sysco.com in the Investors section.

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 194 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2014 that ended June 28, 2014, the company generated sales of more than $46 billion. For more information, visit www.sysco.com or connect with Sysco on Facebook at www.facebook.com/SyscoCorporation or Twitter at https://twitter.com/Sysco.

About US Foods

As one of America's great food companies and leading distributors, US Foods is Keeping Kitchens Cooking™ and making life easier for customers, including independent and multi-unit restaurants, healthcare and hospitality entities, government and educational institutions. With approximately $22 billion in annual revenue, the company offers more than 350,000 products, including high-quality, exclusive brands such as the innovative Chef's Line®, a time-saving, chef-inspired line of scratch-quality products, and Rykoff Sexton®, a premium line of specialty ingredients sourced from around the world. The company proudly employs approximately 25,000 people in more than 60 locations nationwide. US Foods is headquartered in Rosemont, Ill., and jointly owned by affiliates of Clayton, Dubilier & Rice LLC and Kohlberg Kravis Roberts & Co. L.P. Discover more at www.usfoods.com.

About Performance Food Group

Through its leading family of foodservice distributors – Performance Foodservice, Vistar and PFG Customized Distribution, Performance Food Group, Inc. (PFG) delivers over 150,000 national and proprietary-branded food and food-related products to more than 150,000 independent and national chain restaurants, quick-service eateries, pizzerias, theaters, schools, hotels, health care facilities and other institutions. PFG operates one of the nation's largest private truck fleets, as well as 67 distribution centers and 11 Merchant's Mart locations across the United States. The company currently employs more than 12,000 people nationwide. For more information, visit www.pfgc.com.

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Sysco Corporation

Source: Sysco Corporation

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 8-K

CURRENT REPORT PURSUANT TO
SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Date of Report (date of earliest event reported): February 2, 2015

SYSCO CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	1-06544	74-1648137
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification No.)

1390 Enclave Parkway, Houston, TX	77077-2099
(Address of principal executive office)	(Zip Code)

Registrant's telephone number, including area code: (281) 584-1390

N/A
(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 1.01. Entry into a Material Definitive Agreement.

Asset Purchase Agreement

On February 2, 2015, Sysco Corporation ("Sysco"), US Foods, Inc. ("US Foods"), a number of US Foods' subsidiaries (together with US Foods, the "Sellers"), and the parent of US Foods, USF Holding Corp. ("USF") entered into an asset purchase agreement (the "Purchase Agreement") with Performance Food Group, Inc. ("PFG"), through which PFG has agreed to purchase, subject to the terms and conditions of the Purchase Agreement, eleven US Foods distribution centers in the Cleveland, Ohio; Corona, California; Denver, Colorado; Kansas City, Kansas; Las Vegas, Nevada; Minneapolis, Minnesota; Phoenix, Arizona (including the Phoenix Stock Yards business); Salt Lake City, Utah; San Diego, California (including the San Diego Stock Yards business); San Francisco, California and Seattle, Washington markets, and related assets and liabilities (the "Transaction") from the Sellers in connection with (and subject to) the closing of Sysco's previously announced pending acquisition of USF (the "Merger"), as described below. The purchase price for the Transaction is $850 million, in cash, subject to certain adjustments.

The Purchase Agreement generally requires each party to use its reasonable best efforts to resolve objections to the Transaction under any antitrust law, provided that Sysco and USF are not required by the Purchase Agreement to take any such actions with respect to the Merger.

The Purchase Agreement also contemplates the entry by the parties into a Transition Services Agreement as of the closing of the Transaction, pursuant to which the Sellers and Sysco will provide certain support services to PFG to facilitate its operation of the divested distribution centers and their integration into PFG's operating systems. The support services include information technology, supply chain, merchandising, certain administrative services pertaining to accounting, vendor and customer contract administration and personnel management. PFG will also provide a continuation of certain support services to the Sellers. These services to be provided by the Sellers and PFG under the Transition Services Agreement will generally be provided at cost for periods ranging up to 36 months from the closing of the Transaction. The parties also agreed to enter into certain other agreements at closing, including agreements relating to employee matters and the transfer of purchased real estate.

The parties to the Purchase Agreement have made customary representations, warranties and covenants in the Purchase Agreement, including that, subject to certain exceptions, the Sellers will conduct the business at the distribution centers in the ordinary course consistent with past practice during the period between the execution of the Purchase Agreement and the date on which the closing of the Transaction occurs.

In addition, the parties agreed on certain post-closing restrictions on solicitations by Sysco, US Foods and their respective affiliates (the "Restricted Parties") of certain customers of the distribution centers being acquired by PFG. None of these restrictions prohibit the Restricted Parties from seeking or making sales to any customer not under contract, fulfilling existing contractual arrangements, responding to requests for proposals for contracts that will commence after the expiration of the restrictions or making sales on a "cash and carry" basis or sales through US Foods' Culinary Equipment & Supplies or directly through US Foods' Stock Yards businesses. Moreover, PFG, on the one hand, and Sysco and US Foods, on the other hand, agreed that they would refrain from soliciting or hiring certain employees, principally those engaged in key functions providing transition services after the closing of the Transaction, for specified periods of time following the closing of the Transaction, subject to certain exceptions.

The closing of the Transaction is not subject to PFG's receipt of financing or approval by the shareholders of any party to the Purchase Agreement. The obligations of each of the parties to close the Transaction are subject to the fulfillment of certain conditions, including: (1) the approval of the Transaction by the Federal Trade Commission or the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Act; (2) that there be no law or governmental order enacted that would prohibit the consummation of the Transaction; (3) the absence of any injunction or other judgment prohibiting the consummation of the Transaction; (4) subject to materiality qualifications, the accuracy of representations and warranties of the other party (or parties); (5) the delivery of specified ancillary documents and (6) material compliance of the other party (or parties) with its (or their) covenants. Additionally, PFG's obligation to consummate the Transaction is conditioned on the non-occurrence of a material adverse effect (as defined in the Purchase Agreement) on the divested distribution centers, taken as a whole. Additionally, Sellers' obligations to consummate the transaction are conditioned on the consummation of the Merger.

The Purchase Agreement contains certain termination rights, including the right for PFG to terminate if the Transaction has not closed by the earlier of September 9, 2015 and the termination date of the Merger pursuant to the merger agreement (subject to PFG's right to extend such date under certain circumstances), and automatically terminates in the event that such merger agreement terminates. The Purchase Agreement provides that, upon termination of the Purchase Agreement under certain circumstances, PFG will be entitled to receive an aggregate termination fee of $25 million if the Purchase Agreement is terminated after May 2, 2015 and on or prior to July 6, 2015 and $50 million if the Purchase Agreement is terminated after July 6, 2015, with each of Sysco and US Foods responsible for one half of such aggregate fee.

US Foods agreed to indemnify PFG and its affiliates after the closing of the Transaction against losses arising from, among other things: (1) breaches of certain representations or warranties; (2) breaches of any agreement or covenant on the part of the Sellers or Sysco contained in the Purchase Agreement; (3) all excluded assets that will not be transferred to PFG and (4) all liabilities that will be retained by the Sellers. The obligations of US Foods to indemnify Purchaser and its affiliates are

subject to certain limitations. Sysco agreed to irrevocably guarantee to PFG and its affiliates the prompt and complete performance of the Sellers' obligations under the Purchase Agreement and other transaction documents, in each case following the closing of the Transaction, including US Foods' obligations to indemnify PFG and its affiliates.

The foregoing description of the Purchase Agreement and the Transaction does not purport to be complete and is qualified in its entirety by reference to the Purchase Agreement which is filed as Exhibit 2.1 hereto and is incorporated herein by reference. The Purchase Agreement has been included as an exhibit hereto solely to provide investors and security holders with information regarding its terms. It is not intended to be a source of financial, business or operational information about Sysco, US Foods, PFG or their respective subsidiaries or affiliates. The representations, warranties and covenants contained in the Purchase Agreement are made only for purposes of the Purchase Agreement and are made as of specific dates; are solely for the benefit of the parties; may be subject to qualifications and limitations agreed upon by the parties in connection with negotiating the terms of the Purchase Agreement, including being qualified by confidential disclosures made for the purpose of allocating contractual risk between the parties rather than establishing matters as facts; and may be subject to standards of materiality applicable to the contracting parties that differ from those applicable to investors or security holders. Investors and security holders should not rely on the representations, warranties and covenants or any description thereof as characterizations of the actual state of facts or conditions of Sysco, USF or their respective subsidiaries or affiliates. Moreover, information concerning the subject matter of the representations, warranties and covenants may change after the date of the Purchase Agreement, which subsequent information may or may not be fully reflected in public disclosures.

Forward-Looking Statements

Information included in this Current Report (including information included or incorporated by reference in this Current Report) that look forward in time or that express beliefs, expectations, or hopes are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are all statements other than statements of historical facts. The words "anticipates," "may," "can," "plans," "believes," "estimates," "expects," "projects," "intends," "likely," "will," "should," "to be" and any similar expressions or other words of similar meaning are intended to identify those assertions as forward-looking statements. Such forward-looking statements reflect the views of management at the time such statements are made and are subject to a number of risks, uncertainties, estimates, and assumptions that may cause actual results to differ materially from current expectations. For a discussion of additional factors impacting Sysco's business, see Sysco's Annual Report on Form 10-K for the year ended June 28, 2014, as filed with the Securities and Exchange Commission and Sysco's subsequent filings with the SEC. For a discussion of additional factors impacting USF's business, see USF's filings with the SEC. None of Sysco, US Foods or PFG undertakes to update or revise any forward-looking statements, based on new information or otherwise, except as required by applicable law.

Item 8.01. Other Events.

On February 2, 2015, Sysco and USF issued a joint press release announcing the execution of the Purchase Agreement. The joint press release is attached hereto as Exhibit 99.1 and is incorporated by reference herein.

Item 9.01. Financial Statements and Exhibits.

(d) Exhibits

Exhibit	Description
2.1*	Asset Purchase Agreement by and among Performance Food Group, Inc., E&H Distributing LLC, RS Funding, Inc., USF Propco, I, LLC, USF Propco II LLC, Trans-Porte, Inc., US Foods, Inc., USF Holding Corp. and Sysco Corporation, dated February 2, 2015
99.1	Press Release, dated February 2, 2015

* Schedules and exhibits have been omitted pursuant to Item 601(b)(2) of Regulation S-K. A copy of any omitted schedule or exhibit will be furnished supplementally to the Securities and Exchange Commission upon request.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, Sysco Corporation has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

Sysco Corporation

Date: February 5, 2015

By: /s/ Russell T. Libby
Russell T. Libby
Executive Vice President-Corporate Affairs,
Chief Legal Officer and Corporate Secretary

EXHIBIT INDEX

Exhibit	Description
2.1*	Asset Purchase Agreement by and among Performance Food Group, Inc., E&H Distributing LLC, RS Funding, Inc., USF Propco, I, LLC, USF Propco II LLC, Trans-Porte, Inc., US Foods, Inc., USF Holding Corp. and Sysco Corporation, dated February 2, 2015
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* Schedules and exhibits have been omitted pursuant to Item 601(b)(2) of Regulation S-K. A copy of any omitted schedule or exhibit will be furnished supplementally to the Securities and Exchange Commission upon request.

Exhibits omitted

FTC Challenges Proposed Merger of Sysco and US Foods

Agency Charges Merger Would Create a National Broadline Foodservice Distributor With 75 Percent Market Share, And Harm Customers in Numerous Local Markets

FOR RELEASE

February 19, 2015

TAGS: Bureau of Competition | Competition

The Federal Trade Commission today filed an administrative complaint charging that the proposed merger of Sysco and US Foods would violate the antitrust laws by significantly reducing competition nationwide and in 32 local markets for broadline foodservice distribution services. The FTC alleges that if the merger goes forward as proposed, foodservice customers, including restaurants, hospitals, hotels, and schools, would likely face higher prices and diminished service than would be the case but for the merger.

The FTC also authorized staff to seek in federal court a temporary restraining order and a preliminary injunction to prevent the parties from consummating the merger, and to maintain the status quo pending the administrative proceeding.

"This proposed merger would eliminate significant competition in the marketplace and create a dominant national broadline foodservice distributor," said Debbie Feinstein, the Director of the FTC's Bureau of Competition. "Consumers across the country, and the businesses that serve them, benefit from the healthy competition between Sysco and US Foods, whether they eat at a restaurant, hotel, or a hospital."

Sysco and US Foods are – by far – the largest broadline foodservice distributors in the United States. Broadline distributors offer extensive product lines, including national-brand and private-label food products, and provide frequent and flexible delivery, high levels of customer service, and other value-added services such as order tracking, menu planning, and nutritional information.

According to the FTC complaint, a combined Sysco/US Foods would account for 75% of the national market for broadline distribution services. In addition, the parties would also hold high shares in a number of local markets.

As detailed in the complaint, the merger presents a significant risk of competitive harm for two sets of customers who rely on broadline foodservice distribution:

- **National customers** – Sysco and US Foods are the only broadline distributors with a truly national footprint, and compete vigorously with each other to meet the needs of customers with foodservice locations dispersed nationwide or across multiple regions of the country. Sysco and US Foods are the only broadline distributors with numerous distribution centers spread throughout the country. Many hotel chains, foodservice management companies, and group purchasing organizations, for example, consider Sysco and US Foods to be each other's closest competitor, and in

- **Local customers** – Sysco and US Foods also compete aggressively for the broadline business of independent restaurants and other local customers that operate in a local area or region. The merger is likely to harm competition in 32 local markets, according to the agency's complaint.

The Commission also charges that the proposed sale of 11 US Foods distribution centers to Performance Food Group would neither enable PFG to replace US Foods as a competitor nor counteract the significant competitive harm caused by the merger. According to the FTC, even with the addition of 11 distribution centers, PFG would not approach the scale or competitiveness of US Foods today, and therefore would not restore the competition eliminated by this merger.

The following state attorneys general have joined the FTC's complaint for a preliminary injunction to be filed in federal district court: California, Illinois, Iowa, Maryland, Minnesota, Nebraska, Ohio, Virginia, Pennsylvania, Tennessee, and the District of Columbia.

The Commission vote to issue the administrative complaint and to authorize staff to seek a temporary restraining order and preliminary injunction in federal court was 3-2, with Commissioners Maureen K. Ohlhausen and Joshua D. Wright voting no. The administrative trial is scheduled to begin on July 21, 2015.

NOTE: The Commission files a complaint when it has "reason to believe" that the law has been or is being violated and it appears to the Commission that a proceeding is in the public interest. The issuance of the administrative complaint marks the beginning of a proceeding in which the allegations will be tried in a formal hearing before an administrative law judge.

The FTC's Bureau of Competition works with the Bureau of Economics to investigate alleged anticompetitive business practices and, when appropriate, recommends that the Commission take law enforcement action. To inform the Bureau about particular business practices, call 202-326-3300, send an e-mail to antitrust{at}ftc{dot}gov, or write to the Office of Policy and Coordination, Bureau of Competition, Federal Trade Commission, 600 Pennsylvania Ave., NW, Room CC-5422, Washington, DC 20580. To learn more about the Bureau of Competition, read Competition Counts. Like the FTC on Facebook, follow us on Twitter, and subscribe to press releases for the latest FTC news and resources.

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ftc.gov

Press Releases

Sysco to Contest Federal Trade Commission's Attempt to Block Proposed US Foods Merger

Company Says Facts Support Procompetitive Benefits of Merger
HOUSTON, Feb. 19, 2015 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) today announced that it will contest the U.S. Federal Trade Commission's (FTC) attempt to block its proposed merger with US Foods. The company said it is looking forward to a full judicial review of the significant competitive benefits of the merger.

The five FTC Commissioners voted by a slim margin of 3-2 to seek a preliminary injunction in the U.S. District Court for the District of Columbia to prevent the parties from closing the transaction. The narrow vote demonstrates a lack of consensus within the Commission that the proposed merger could be viewed as harmful to competition under the law.

Sysco believes that the FTC's decision is based on an erroneous view of the competitive dynamics of the foodservice distribution industry.

"The facts are strongly in our favor and we look forward to making our case in court," said Bill DeLaney, Sysco's president and chief executive officer. "Those of us who work in this industry every day know it is fiercely competitive. Customers of all types have access to food distribution services from a wide variety of companies and any number of channels. In fact, the overwhelming majority of restaurants and food operators choose their foodservice distributor locally, where they have choices among many excellent companies."

"For example, the FTC claims that Sysco and US Foods combined have a 75 percent market share in an ill-defined 'national broadline market,' ignoring the fact that the vast majority of 'national customers' use multiple regional or local distributors. Additionally, the FTC claims the merger would harm competition in 32 local markets, ignoring the existence of myriad local suppliers, including broadline companies, specialty companies, cash-and-carry, and club stores with whom Sysco and US Foods compete on a daily basis."

Despite its fundamental disagreement with the FTC's position, Sysco listened closely to the agency's concerns and delivered a substantial divestiture package to enable Performance Food Group (PFG) to compete more effectively for customers coast to coast.

"This merger has always been about serving customers better and driving costs out of the system," DeLaney said. "By unlocking at least $600 million in annualized cost synergies, the merger will allow Sysco to lower costs for customers, deliver better service and improve selection across all product segments, all of which will increase competition across the entire foodservice distribution industry to the benefit of customers."

Sysco believes that its merger with US Foods is in the best interest of all stakeholders for the following reasons:

1. Customer Focus

The merger of Sysco and US Foods will benefit customers and help the business become more efficient in an evolving and competitive marketplace. It will increase efficiency and innovation to the benefit of small and large customers across the country. This includes providing the highest quality service, great brands and competitive pricing. The combined company will continue to create value for customers through insights-driven product innovation and expanded services that go beyond food. The merger will enhance the company's flexibility and responsiveness to provide unique, on-trend food products that save customers time and improve performance. The foodservice industry is a collection of local and fiercely competitive markets where customers of all sizes continue to enjoy a wide range of choice among broadline, specialty and other distribution channels.

2. Substantial Efficiencies

The proposed merger creates supply chain efficiencies through the optimization of inbound and outbound freight and the opportunity to partner more closely with suppliers and brokers to address customer needs and help them grow their businesses. Sysco estimates it will be able to achieve net annual synergies of at least $600 million in four years even after its announced divestiture to Performance Food Group (PFG).

3. Enhanced Employee Opportunities

Sysco remains committed to investing in its businesses and its people to accelerate the transformation of the industry, including customer-friendly technology, robust category management, food safety and quality assurance, and sustainable business practices. The combined business will continue to be a significant national and local employer. By combining the strengths of the two companies, Sysco will provide employees even more opportunities to grow and develop their careers.

4. Substantial Divestiture Package

As previously announced, the definitive divestiture agreement includes selling US Foods facilities in 11 markets to PFG upon consummation of the merger. These facilities, representing approximately $4.6 billion in annual sales, will expand PFG's geographic footprint in the U.S. and enable PFG to compete more effectively for customers coast to coast.

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 194 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2014 that ended June 28, 2014, the company generated sales of more than $46 billion. For more information, visit **www.sysco.com** or connect with Sysco on Facebook at **www.facebook.com/SyscoCorporation** or Twitter at **https://twitter.com/Sysco**.

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Sysco Corporation

Source: Sysco Corporation

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

FEDERAL TRADE COMMISSION, *et al.*, Plaintiffs, v. **SYSCO CORPORATION**, And **USF HOLDING CORP.**, and **US FOODS, INC.**, Defendants.	Civil Action No. 15-cv-00256 (APM)

STIPULATION AND ~~[PROPOSED]~~ ORDER

WHEREAS, Plaintiff, the Federal Trade Commission (the "Commission"), filed its Complaint on February 19, 2015, seeking, among other relief, a temporary restraining order and preliminary injunction enjoining Defendants Sysco Corporation ("Sysco") and USF Holding Corp. ("US Foods") from merging; and

WHEREAS, absent this Stipulation, Defendants would be free to consummate the proposed merger after 11:59 p.m. on March 2, 2015; and

WHEREAS, the parties have agreed that Defendants will not consummate the proposed merger until three calendar days after the Court rules on the Commission's motion for a preliminary injunction to enjoin the merger.

NOW, THEREFORE, IT IS HEREBY STIPULATED AND AGREED AMONG THE PARTIES:

1. Defendants shall not consummate the proposed merger, or otherwise effect a combination of Defendants until three calendar days after the Court rules on the Commission's motion for a preliminary injunction, pursuant to Section 13(b) of the Federal Trade Commission Act.

2. Defendants shall take any and all necessary steps to prevent any of their officers, directors, domestic or foreign agents, divisions, subsidiaries, affiliates, partnerships, or joint ventures from consummating, directly or indirectly, any such merger, or otherwise effecting any combination between Defendants Sysco and US Foods.

3. This Stipulation and Order is without prejudice to any rights or defenses that any Defendants may have.

4. Any Party may seek to amend this Stipulation and Order at any time upon proper notice.

Dated: February 24, 2015

Respectfully submitted,

By: /s/ Stephen Weissman

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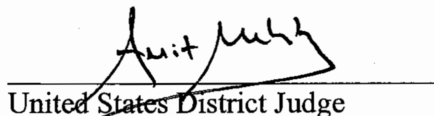
ISSUED this 27th day of February, 2015, at 12:30 a.m./p.m.

ORDERED:



United States District Judge

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Federal Trade Commission, *et al.*, **Plaintiffs,** **v.** **Sysco Corporation, *et al.*,** **Defendants.**	**Civil No. 1:15-cv-00256 (APM)**

ORDER

This matter comes before the court on lead Plaintiff Federal Trade Commission's ("FTC") motion to enjoin the proposed merger of Defendant Sysco Corp. ("Sysco") with Defendants USF Holding Corp. and US Foods, Inc. (together, "US Foods"), under Section 13(b) of the Federal Trade Commission Act, 15 U.S.C. § 53(b). After considering the extensive record in this matter and the parties' legal arguments, the court finds that the FTC has carried its burden of showing that a preliminary injunction of the proposed merger between Sysco and US Foods is in the public interest. The FTC has shown that there is a reasonable probability that the proposed merger will substantially impair competition in the national customer and local broadline markets and that the equities weigh in favor of injunctive relief. The court's reasoning is set forth in the accompanying Memorandum Opinion.[1]

[1] Because the Memorandum Opinion likely contains "competitively sensitive information" of Defendants and third parties, Protective Order Governing Confidential Material, ECF No. 87 ¶ 1, the court has issued the Memorandum Opinion under seal to allow the parties to propose redactions of competitively sensitive information. The parties shall meet and confer and present to the court proposed redactions to the Memorandum Opinion no later than 5:00 p.m. on June 25, 2015. After considering the proposed redactions, the court will issue a public version of the Memorandum Opinion on June 26, 2015.

Accordingly, it is hereby ordered that:

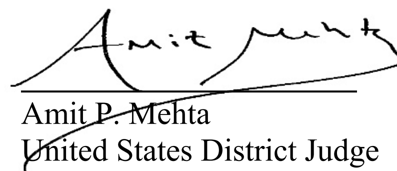
1. The FTC's motion for a preliminary injunction enjoining the merger between Sysco and US Foods is granted;

2. Sysco and US Foods are hereby enjoined and restrained, under Section 13(b) of the Federal Trade Commission Act, 15 U.S.C. § 53(b), from completing the proposed merger, or otherwise effecting a combination of Sysco and US Foods, until the completion of the administrative proceedings evaluating the proposed transaction now pending before the FTC;

3. Defendants shall take any and all necessary steps to prevent any of their officers, directors, domestic or foreign agents, divisions, subsidiaries, affiliates, partnerships, or joint ventures from consummating, directly or indirectly, any such merger, or otherwise effecting any combination between Defendant Sysco and Defendant US Foods;

4. Defendants are directed to maintain the status quo until either: (1) the completion of all legal proceedings by the FTC challenging the transaction, including all appeals, or (2) further order of the court, including upon the request of the FTC, before completion of such legal proceedings;

5. This court shall retain jurisdiction of this matter for all purposes and for the full duration of this Order, as provided in the previous paragraph.



Dated: June 23, 2015

Amit P. Mehta
United States District Judge

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Federal Trade Commission, ***et al.*****,**	)	
Plaintiffs,	)	
v.	)	**Civil No. 1:15-cv-00256 (APM)**
Sysco Corporation, ***et al.*****,**	)	
Defendants.	)	

MEMORANDUM OPINION

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INTRODUCTION

Americans eat outside of their homes with incredible frequency. The U.S. Department of Commerce, for instance, recently reported, for the first time since it began tracking such data, that Americans spent more money per month at restaurants and bars than in grocery stores.[1] Of course, Americans eat out at many other places, too—sports arenas, school and workplace cafeterias, hotels and resorts, hospitals, and nursing homes, just to name a few. The foodservice distribution industry supplies food and related products to all of these locations. Foodservice distribution is big business. In 2013, the market grew to $231 billion. By some estimates, there are over 16,000 companies that compete in the foodservice distribution marketplace.

The two largest foodservice distribution companies in the country are Defendants Sysco Corporation ("Sysco") and US Foods, Inc. ("USF"). Both are primarily "broadline" foodservice distributors. As the name implies, a broadline foodservice distributor sells and delivers a "broad" array of food and related products to just about anywhere food is consumed outside the home. In 2013, Sysco's broadline sales were over $█ billion and USF's were over $█ billion.

In December 2013, Sysco and USF announced that they had entered into an agreement to merge the companies. Fourteen months later, in February 2015, Sysco and USF announced that they intended to divest 11 USF distribution facilities to the third largest broadline foodservice distributor, Performance Food Group, Inc., if the merger received regulatory approval.

On February 20, 2015, the Federal Trade Commission ("FTC") and a group of states filed suit in this court seeking an injunction to prevent the proposed merger. Specifically, under Section 13(b) of the Federal Trade Commission Act, the FTC asked this court to halt the proposed merger

[1] Michelle Jamrisko, *Americans' Spending on Dining Out Just Overtook Grocery Sales for the First Time Ever*, Bloomberg Business (Apr. 14, 2015), http://www.bloomberg.com/news/articles/2015-04-14/americans-spending-on-dining-out-just-overtook-grocery-sales-for-the-first-time-ever.

until the FTC completes an administrative hearing—scheduled to begin on July 21, 2015—to determine whether the proposed combination would violate Section 7 of the Clayton Act.

The precise question presented by this case is whether the court should enjoin Sysco and USF from merging until the proposed combination is reviewed by an FTC Administrative Law Judge. The real-world impact of the case, however, is more consequential. Sysco and USF have announced that they will not proceed with the merger if the court grants the requested injunction.

The proceedings in this case have been extraordinary. The FTC investigated the proposed merger for more than a year before filing suit. Then, within a two-month period, the parties worked tirelessly to exchange millions of documents, depose dozens of witnesses, and secure over a hundred declarations. The court heard live testimony for eight days in early May 2015. Counsel for the parties have done all of this work while exhibiting the highest degree of skill and professionalism.

Congress passed the Clayton Act to enable the federal government to halt mergers in their incipiency that likely would result in high market concentrations. Congress was especially concerned with large combinations that would impact everyday consumers across the country. The court has considered all of the evidence in this case and has reached the following conclusion: The proposed merger of the country's first and second largest broadline foodservice distributors is likely to cause the type of industry concentration that Congress sought to curb at the outset before it harmed competition. The court finds that the FTC has met its burden under Section 13(b) of the Federal Trade Commission Act of showing that the requested injunction is in the public interest. The court, therefore, grants the FTC's motion for preliminary injunctive relief.

BACKGROUND

I. THE FOODSERVICE DISTRIBUTION INDUSTRY

A. Overview

Defendants operate in a $231 billion foodservice distribution industry, where over 16,000 companies battle daily to sell food and related products to restaurants, resorts, hotels, hospitals, schools, company cafeterias, and so on—everywhere food is served outside the home. Hr'g Tr. 1324; DX-00329 at 17. The types of customers served by the foodservice distribution industry come in all shapes and sizes. They range from independent restaurants, to well-known quick-service and casual dining chains (*e.g.*, Five Guys, Subway, and Applebee's), to hospitality procurement companies and hotel chains (*e.g.*, Avendra, Hilton Supply Management, and Starwood Hotels and Resorts), to government agencies (*e.g.*, the U.S. Department of Veterans Affairs), to foodservice management companies (*e.g.*, Aramark, Sodexo, and Compass Group), to healthcare group purchasing organizations (*e.g.*, Premier, Novation, and Navigator).

The industry recognizes four general categories of foodservice distribution companies: (i) broadline distributors, (ii) systems distributors, (iii) specialty distributors, and (iv) cash-and-carry and club stores. Customers commonly purchase from foodservice distributors in one or more of these different categories, or "channels," mixing and matching to suit their needs. For example, customers may purchase products directly from a broadline distributor; they may contract with a brand-named food manufacturer (*e.g.*, Tyson Foods for chicken or Kellogg's for cereal) and use a broadline or systems distributor for warehousing and delivery; they may use specialty distributors for select items such as produce or seafood; or they may make their purchases at a cash-and-carry or club store (*e.g.*, Restaurant Depot or Costco).

Understanding these different channels of distribution and the different customers they serve is central to the antitrust analysis that this case demands. The court, therefore, describes below the sellers and buyers of foodservice distribution in the United States.

B. Channels of Foodservice Distribution

1. Broadline Distributors

Broadline distribution is characterized by several key features, including: (i) product breadth and depth; (ii) availability of private-label products; (iii) frequent and flexible delivery, including next-day service; and (iv) "value-added" services, such as menu and nutrition planning.

Broadline distributors offer thousands of distinct items for sale—known as "stock keeping units" ("SKUs") for inventory management purposes—in a wide array of product categories, including canned and dry goods, dairy, meat, poultry, produce, seafood, frozen foods, beverages, and even janitorial supplies such as chemicals, cleaning equipment, and paper goods. Broadliners also sell "private label" goods, which are akin to "Trader Joe's" or "Safeway" brand products found in those grocery stores. "Private label" products are often comparable in quality to their name-brand counterparts, but are cheaper in price. Because they are able to offer such a diverse array of products, broadline distributors market themselves to customers as a "one-stop shop," by virtue of their ability to supply most—if not all—food and related products needed by their customers. Customers value the breadth of product offerings and the opportunity to aggregate a substantial portion of their purchases with one distributor, allowing them to save costs. They also appreciate broadliners' high level of customer service, which usually includes next-day and emergency deliveries. Focusing heavily on individualized customer service, broadline distributors employ much larger salesforces than the other channels.

Broadline distributors come in different sizes. The largest, by any measure, are Sysco and USF. In 2013, Sysco and USF made $[redacted] billion and $[redacted] billion in broadline sales, respectively. PX09350-236, Table 44. The next largest broadliner made less than $6 billion. *Id.* Sysco and USF are also the only two broadliners with true nationwide service capability. Sysco and USF have 72 and 61 distribution centers, respectively—each with more than twice the number of distribution centers operated by the next-largest broadliners. Because of their nationwide footprint, Sysco and USF are often referred to as "national" broadliners. Combined, Defendants employ over 14,000 sales representatives. No other broadliner employs more than 1,600. Defendants together operate over 13,000 trucks. The next largest broadliners have just over 1,600.

The next tier of companies are "regional broadliners," so called because their distribution capabilities are concentrated in discrete regions of the United States. The largest regional broadliner, Performance Food Group ("PFG"), is the country's third-largest broadliner in terms of sales. PFG operates 24 broadline distribution facilities, mainly in the eastern and southern parts of the country and, in 2013, earned $6 billion in broadline revenue. The next five largest regional broadline distributors, in order of 2013 revenues, are: (i) Gordon Food Service, which has 10 distribution centers mainly in the Midwest, Florida, and Texas; (ii) Reinhart Foodservice, which has 24 distribution centers, primarily in the East and Midwest; (iii) Ben E. Keith Company, which has seven distribution centers in Texas and bordering states; (iv) Food Services of America, which has 10 distribution centers, concentrated in the Northwest; and (v) Shamrock Foods, which has four distribution centers in the Southwest and southern California. These regional broadliners had 2013 revenues ranging from approximately $[redacted] billion to $[redacted] billion.

The last tier of broadliners have five or fewer distribution centers and 2013 revenues of less than $1.1 billion. Many of these operate in a single locality or region, like Shetakis Wholesalers, which has one distribution center in Las Vegas, Nevada.

Regional broadline distributors have formed consortiums to compete for customers with multi-regional distribution needs. The largest consortium is Distribution Market Advantage ("DMA"). DMA is a supply chain sales and marketing cooperative owned by nine independent regional distributors, which are also its members, including Gordon Food Service, Ben E. Keith, and Reinhart Foodservice. DMA does not own any trucks or distribution facilities; rather, its purpose is to coordinate the bidding, contracting, and operational processes of its members to meet the needs of large customers that require a distributor with extensive geographic coverage. Another consortium is Multi-Unit Group ("MUG"), an alliance of 19 broadline distributors who are part of UniPro Foodservice, a larger consortium that includes distributors in different channels. As explained later, these regional consortia have had mixed results in competing for large, geographically dispersed customers.

2. Systems Distributors

Systems distributors, also referred to as "custom" or "customized" distributors, primarily serve fast food, quick service, fast casual, and casual chain restaurants (*e.g.*, Burger King, Wendy's, and Applebee's), which have fixed or limited menus. Unlike broadliners, systems distributors do not carry a large, diverse number of SKUs. Rather, their inventory profile is a small number of proprietary SKUs, which are manufactured specifically for the customer. For instance, the systems distributor for Wendy's carries and delivers the food products needed for Wendy's' menu and does not make those products available to others. As a result, systems distributors typically provide only warehousing and transport services. They do not offer private label products

or value-added services such as menu planning, and they have very small salesforces, if any. Systems distributors make large, limited-SKU deliveries on a fixed, limited schedule, and typically do not offer next-day or emergency deliveries.

Some foodservice distribution companies operate both systems and broadline divisions. For instance, Sysco operates SYGMA, a systems distribution division. SYGMA is run by a different set of executives and, for the most part, operated out of separate distribution centers. PFG offers systems distribution through PFG Customized, which is run separately from its broadline division.

3. Specialty Distributors

Specialty distributors offer a limited and focused grouping of products within one or more product categories—typically fresh produce, meat, seafood, dairy or baked goods. Other specialty distributors focus on a specific type of cuisine, such as Italian fare. Many customers, especially independent restaurants, use specialty distributors to supplement their purchases from broadline distributors because the specialty distributor offers higher quality or fresher products than the broadline distributor or provides unique products that the broadline distributor does not carry, such as products from local farmers. Both in terms of number of SKUs and geographic coverage, specialty distributors are typically smaller than broadline distributors.

To compete with specialty distributors, some broadliners operate specialty divisions. Sysco, for instance, operates several specialty divisions separately from its broadline division. So, too, does PFG, which operates Roma, a specialty division for Italian food products.

4. Cash-and-Carry and Club Stores

Cash-and-carry stores offer a "self-service" model of food distribution, in which customers make purchases at the store and transport the purchased goods themselves. Club stores like Costco

and Sam's Club also fall within this distribution channel. With limited exceptions, cash-and-carry stores do not deliver. They also offer fewer products than broadline distributors. For example, the largest cash-and-carry store, Restaurant Depot, only carries up to ███ SKUs. Additionally, cash-and-carry stores do not have sales personnel dedicated to individual customers. Because of these features, the prices offered by cash-and-carry stores are significantly lower than those offered by broadliners. The typical cash-and-carry customer is an independent restaurant that either does not meet broadline distributors' minimum purchase requirements or needs to supplement its broadline deliveries.

C. Foodservice Distribution Customers

Foodservice distribution customers are a heterogeneous group. The largest customers, such as group purchasing organizations and foodservice management companies, buy hundreds of millions of dollars of product a year, whereas a single independent restaurant buys a small fraction of that amount. Some customers choose to buy from a single line of distribution; others mix distribution channels. Some customers demand fixed pricing, whereas others buy based on daily market rates. Generally speaking, however, customers can be grouped into several categories.

1. Group Purchasing Organizations

Group purchasing organizations, or GPOs, are entities that, through the collective buying power of their members, obtain lower prices for foodservice products. GPOs negotiate direct contracts with food manufacturers and thereby secure lower prices than a member could individually.

GPOs do not have their own distribution capabilities. Rather, they contract with broadline distributors for warehousing, delivery, and operational services. When a member purchases a GPO-contracted good, the member pays the broadliner on a "cost-plus" basis: it pays for the "cost"

of the product based on the GPO's contract with the manufacturer, "plus" the distributor's markup, which is negotiated between the GPO and distributor. GPOs also contract with broadliners to allow their members to purchase products from broadline distributors (rather than from manufacturers), in which case they pay the broadline distributor both the distribution margin (markup) and the cost for the product set by the distributor. GPO members also buy from specialty distributors.

GPOs are prominent in the healthcare and hospitality industries. The largest healthcare GPOs include Premier, Novation, and Navigator. One of the largest hospitality GPOs is Avendra. These companies annually spend hundreds of millions of dollars on broadline distribution.

2. *Foodservice Management Companies*

Foodservice management companies operate cafeterias or other dining facilities at educational institutions, sports venues, and workplaces. Like GPOs, foodservice management companies negotiate contracts with food manufacturers and rely on broadliners for storage and delivery; they also purchase directly from broadliners and specialty distributors. Sodexo, Compass Group, and Aramark are among the country's largest foodservice management companies. Those three companies each spend approximately $█ billion annually on broadline distribution.

3. *Hospitality Chains*

Hospitality chains are also large purchasers. Hilton Hotels, for example, uses a system similar to a GPO. It has a subsidiary, Hilton Supply Management LLC, which negotiates contracts on behalf of over 4,000 members to obtain food and related items at a discounted price. Other hospitality companies, such as Hyatt Hotels, purchase most of their foodservice products through Avendra, the largest hospitality GPO. Starwood Hotels and Interstate Hotels & Resorts, on the other hand, directly manage food procurement and distribution contracts for their properties.

Regardless of the food purchasing model, hospitality chains also buy food directly from broadliners and rely on them for their storage and delivery needs. These companies spend hundreds of millions of dollars annually on broadline distribution. Individual hotels and resorts also buy directly from specialty distributors, as needed.

4. Restaurant Chains

Restaurant chains come in many sizes with a wide variety of characteristics. This customer category includes nationwide fast food or quick service restaurants such as Burger King and Subway, each with thousands of locations in all regions of the country. It also includes regional fast casual restaurant chains such as Culver's (primarily in the Midwest) and Zaxby's (primarily in the Southeast), as well as nationwide sit-down restaurant chains, such as Applebee's and Cheesecake Factory. The channel of distribution a chain restaurant uses depends, in part, on the number of locations and menu variety. The greater the number of locations and the fewer the menu items, the more amenable the chain restaurant is to systems distribution.

5. Government Agencies

Some government agencies, notably the Defense Logistics Agency and the U.S. Department of Veterans Affairs, are large buyers of broadline distribution services. Those agencies, for instance, spend hundreds of millions of dollars each year on broadline foodservice.

6. "Street" Customers

Customers with only one location, or a handful of locations, are referred to in the industry as "street," "local," or "independent" customers. Examples of this type of customer include independent restaurants and resorts. Unlike the types of customers identified above, street customers usually do not have written contracts with broadliners; instead, they negotiate prices on a weekly or other short term basis. They also tend to diversify their purchases among multiple

distribution channels. Indeed, according to a study conducted by an industry trade group, the International Foodservice Distributors Association, the typical independent customer uses up to twelve different supply sources. DX-00293 at 29.

II. CASE HISTORY

A. Sysco and USF

Defendant Sysco is a publicly-traded corporation headquartered in Houston, Texas. As the largest North American foodservice distributor, Sysco distributes food to approximately 425,000 customers in the United States, generating sales of about $46.5 billion in fiscal year 2014. Compl. for TRO and Prelim. Inj. Pursuant to Section 13(b) of the FTC Act, ECF No. 3 at ¶ 24 [hereinafter Compl.]. Sysco's business is divided into three divisions: (i) Broadline (81 percent of revenue); (ii) SYGMA, which provides systems distribution (13 percent of revenue); and (iii) "Other," which provides, among other things, specialty produce distribution (6 percent of revenue). *Id.* ¶ 25. Sysco's broadline division operates out of 72 distribution centers located across the United States. *Id.*

Defendant US Foods, Inc., is a privately-held corporation based in Rosemont, Illinois, and is a wholly owned subsidiary of Defendant USF Holding Corp. USF is controlled by the investment funds of Clayton, Dubilier & Rice, Inc., and KKR & Co., L.P. The second-largest foodservice distributor in the United States, USF operates 61 broadline distribution centers across the country and serves over 200,000 customers nationwide. *Id.* ¶ 27. In fiscal year 2013, USF generated approximately $22 billion in revenue. *Id.*

B. History of the Merger

On December 8, 2013, Sysco and USF signed a definitive merger agreement, whereby Sysco agreed to acquire all shares of USF for $500 million in cash and $3 billion in newly issued

Sysco equity. Sysco also agreed to assume $4.7 billion in USF's existing debt, for a total transaction value of $8.2 billion. The merger agreement expires on September 8, 2015.

After announcing the merger, Defendants filed a notification regarding the merger as required by the Hart-Scott-Rodino Antitrust Improvements Act, 15 U.S.C. § 18a. As a result of this filing, the FTC commenced an investigation to determine the effects of the proposed combination. The FTC is an administrative agency of the United States federal government that derives its authority from the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. §§ 41 *et seq.* Among other duties, the FTC is vested with authority and responsibility for enforcing Section 7 of the Clayton Act, 15 U.S.C. § 18, and Section 5 of the FTC Act, 15 U.S.C. § 45.

During the FTC's investigation, and with the hope of gaining regulatory approval, on February 2, 2015, Sysco and USF announced an asset purchase agreement with regional broadline distributor Performance Food Group, Inc. ("PFG"), to sell 11 of USF's 61 distribution centers to PFG, contingent upon the successful completion of the merger. The 11 USF distribution centers—intended to increase PFG's geographic footprint—are, for the most part, located within the western half of the country, where PFG at present has only one distribution center. Currently, the 11 distribution centers account for approximately $4.5 billion in broadline sales. PX09250-011. The parties also executed a Transition Services Agreement. Under the two agreements, PFG would acquire all assets and employees at the 11 distribution centers, all customers under those contracts (assuming the customers consent), and the right to use USF private label products at those facilities for up to three years.

C. History of these Proceedings

On February 19, 2015, the Commissioners of the FTC voted 3-2 to authorize the filing of an administrative complaint in the FTC's Article I court to block the proposed merger, based on a

finding that there was reason to believe that the merger would violate Section 7 of the Clayton Act, 15 U.S.C. § 18, and Section 5 of the FTC Act, 15 U.S.C. § 45. Trial before an Administrative Law Judge is scheduled to begin on July 21, 2015.

Also, on February 19, 2015, the Commission authorized the FTC staff to seek a preliminary injunction in federal court under Section 13(b) of the FTC Act in order to prevent Defendants from completing the merger. The FTC filed this action on February 20, 2015, seeking a temporary restraining order ("TRO") and preliminary injunction to maintain the status quo until the conclusion of the administrative trial. The FTC is joined in this action by the District of Columbia and the following states: California, Illinois, Iowa, Maryland, Minnesota, Nebraska, North Carolina, Ohio, Tennessee, Pennsylvania, and Virginia (collectively, the "Plaintiff States"). By and through their respective Attorneys General, the Plaintiff States have joined with the FTC in this action pursuant to Section 16 of the Clayton Act, 15 U.S.C. § 26, in their sovereign or quasi-sovereign capacities as *parens patriae* on behalf of the citizens, general welfare, and economy of each of their states.

On February 24, 2015, Defendants stipulated to a TRO, agreeing not to merge until three calendar days after this court rules on the FTC's Motion for Preliminary Injunction. The court entered the stipulated TRO on February 27, 2015. Defendants have since represented that they will abandon the transaction if this court grants the preliminary injunction.

On March 4, 2015, the court scheduled a preliminary injunction hearing to start on May 5, 2015. The parties' counsel accomplished an extraordinary amount of work in the two months leading up to the evidentiary hearing. They exchanged approximately 14.8 million documents and took 72 depositions. Moreover, in addition to the more than 90 industry participant declarations that accompanied the FTC's motion for preliminary injunction, Defendants obtained 65 new

declarations or counter declarations, while the FTC obtained an additional 25 new or counter declarations. During the eight-day evidentiary hearing, the court heard testimony from 20 witnesses, either live or via video deposition. The parties submitted a total of 185 declarations into evidence, as well as over 3,500 exhibits and excerpts of over 70 depositions. The court heard closing arguments on May 28, 2015.

LEGAL STANDARD

I. SECTION 7 OF THE CLAYTON ACT

Section 7 of the Clayton Act prohibits mergers or acquisitions "the effect of [which] may be substantially to lessen competition, or to tend to create a monopoly" in "any line of commerce or in any activity affecting commerce in any section of the country." 15 U.S.C. § 18. When the FTC has "reason to believe that a corporation is violating, or is about to violate, Section 7 of the Clayton Act," it may seek a preliminary injunction under Section 13(b) of the FTC Act to "prevent a merger pending the Commission's administrative adjudication of the merger's legality." *FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1070 (D.D.C. 1997) (citing 15 U.S.C. § 53(b)). "Section 13(b) provides for the grant of a preliminary injunction where such action would be in the public interest—as determined by a weighing of the equities and a consideration of the Commission's likelihood of success on the merits." *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 714 (D.C. Cir. 2001) (citing 15 U.S.C. § 53(b)).

II. SECTION 13(B) STANDARD FOR PRELIMINARY INJUNCTIONS

The Section 13(b) standard for preliminary injunctions differs from the familiar equity standard applied in other contexts. As the Court of Appeals explained in *Heinz*: "Congress intended this standard to depart from what it regarded as the then-traditional equity standard, which it characterized as requiring the plaintiff to show: (1) irreparable damage, (2) probability of

success on the merits and (3) a balance of equities favoring the plaintiff." 246 F.3d at 714 (internal citation omitted). The court continued: "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.'" *Id.* (quoting H.R. Rep. No. 93-624 at 31 (1971)); *see also FTC v. Exxon Corp.*, 636 F.2d 1336, 1343 (D.C. Cir. 1980) ("In enacting [Section 13(b)], Congress further demonstrated its concern that injunctive relief be broadly available to the FTC 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.").

Under Section 13(b)'s "public interest" standard, "[t]he FTC is not required to *establish* that the proposed merger would in fact violate section 7 of the Clayton Act." *Heinz*, 246 F.3d at 714. Rather, to demonstrate the likelihood of success on the merits, "the government need only show that there is a reasonable probability that the challenged transaction will substantially impair competition." *Staples*, 970 F. Supp. at 1072 (citation omitted) (internal quotation marks omitted).

A trial court evaluating a demand for injunctive relief therefore must "measure the probability that, after an administrative hearing on the merits, the Commission will succeed in proving that the effect of the [proposed] merger 'may be substantially to lessen competition, or to tend to create a monopoly' in violation of section 7 of the Clayton Act.'" *Heinz*, 246 F.3d at 714 (quoting 15 U.S.C. § 18). The FTC satisfies this standard if it "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." *Id.* at 714-15 (citations omitted) (internal quotation marks omitted). This standard reflects Congress' use of the words "*may* be substantially to lessen competition" in

Section 7, as Congress' concern "was with probabilities, not certainties" of decreased competition. *Id.* at 713 (citing *Brown Shoe Co. v. United States*, 370 U.S. 294, 323 (1962)) (other citations omitted).

Though more relaxed than the traditional equity injunction standard, Section 13(b)'s public interest standard nevertheless demands rigorous proof to block a proposed merger or acquisition. "[T]he issuance of a preliminary injunction prior to a full trial on the merits is an extraordinary and drastic remedy." *Exxon*, 636 F.2d at 1343 (citations omitted) (internal quotation marks omitted). That is because "the issuance of a preliminary injunction blocking an acquisition or merger may prevent the transaction from ever being consummated." *Id.* "Given the stakes, the FTC's burden is not insubstantial . . . ." *FTC v. Arch Coal*, 329 F. Supp. 2d 109, 123 (D.D.C. 2004), *case dismissed*, No. 04-5291, 2004 WL 2066879 (D.C. Cir. Sept. 15, 2004). "[A] showing of a fair or tenable chance of success on the merits will not suffice for injunctive relief." *Id.* (citation omitted) (internal quotation marks omitted).

III. *BAKER HUGHES* BURDEN-SHIFTING FRAMEWORK

In *United States v. Baker Hughes, Inc.*, 908 F.2d 981, 982-83 (D.C. Cir. 1990), the Court of Appeals established a burden-shifting framework for evaluating the FTC's likelihood of success on the merits. *See Heinz*, 246 F.3d at 715 (applying *Baker Hughes* "to the preliminary injunctive relief stage"). Under the *Baker Hughes* framework, the FTC bears the initial burden of showing that the merger would lead to "undue concentration in the market for a particular product in a particular geographic area." *Baker Hughes*, 908 F.2d at 982; *see also Heinz*, 246 F.3d at 715 (quoting *United States v. Phila. Nat'l Bank*, 374 U.S. 321, 363 (1963)) ("[T]he government must show that the merger would produce 'a firm controlling an undue percentage share of the relevant market, and [would] result[ ] in a significant increase in the concentration of firms in that

market.'"). Such a showing establishes a "presumption" that the merger will substantially lessen competition. *Baker Hughes*, 908 F.2d at 982.

The burden then shifts to the defendant to rebut the presumption by offering proof that "the market-share statistics [give] an inaccurate account of the [merger's] probable effects on competition in the relevant market." *Heinz*, 246 F.3d at 715 (quoting *United States v. Citizens & S. Nat'l Bank*, 422 U.S. 86, 120 (1975)) (internal quotation marks omitted); *see also Baker Hughes*, 908 F.2d at 991 ("[A] defendant seeking to rebut a presumption of anticompetitive effect must show that the prima facie case inaccurately predicts the relevant transaction's probable effect on future competition."). "The more compelling the prima facie case, the more evidence the defendant must present to rebut it successfully." *Baker Hughes*, 908 F.2d at 991. "A defendant can make the required showing by affirmatively showing why a given transaction is unlikely to substantially lessen competition, or by discrediting the data underlying the initial presumption in the government's favor." *Id.*

"If the defendant successfully rebuts the presumption, the burden of producing additional evidence of anticompetitive effect shifts to the government, and merges with the ultimate burden of persuasion, which remains with the government at all times." *Id.* at 983. "[A] failure of proof in any respect will mean the transaction should not be enjoined." *Arch Coal*, 329 F. Supp. 2d at 116. The court must also weigh the equities, but if the FTC is unable to demonstrate a likelihood of success, the equities alone cannot justify an injunction. *Id.*

DISCUSSION

I. THE RELEVANT MARKET

Merger analysis starts with defining the relevant market. *United States v. Marine Bancorp.*, 418 U.S. 602, 618 (1974) (Market definition is "'a necessary predicate' to deciding whether a

merger contravenes the Clayton Act.") (quoting *United States v. E.I. Du Pont De Nemours & Co.*, 353 U.S. 586, 593 (1957)); *see also FTC v. Swedish Match*, 131 F. Supp. 2d 151, 156 (D.D.C. 2000). The relevant market has two component parts. "First, the 'relevant product market' identifies the product and services with which the defendants' products compete. Second, the 'relevant geographic market' identifies the geographic area in which the defendant competes in marketing its products or service." *Arch Coal, Inc.*, 329 F. Supp. 2d at 119; *see also FTC v. CCC Holdings Inc.*, 605 F. Supp. 2d 26, 37 (D.D.C. 2009) (same). "Defining the relevant market is critical in an antitrust case because the legality of the proposed merger[ ] in question almost always depends upon the market power of the parties involved." *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 45 (D.D.C. 1998).

Market definition has been the parties' primary battlefield in this case. According to the FTC, the relevant product market is broadline foodservice distribution. Compl. ¶ 40. Because broadline distribution is defined by a number of distinct attributes—such as a vast array of product offerings, private label offerings, next-day delivery, and value-added services—the FTC contends that the other modes of distribution are not reasonable substitutes for broadline distribution and thus must be excluded from the product market.

The FTC further contends that, within the product market for broadline distribution, there is another product market for foodservice distribution sold to "national" customers. *Id.* ¶ 44. These customers, the FTC asserts, are distinct from "local" or "street" customers in multiple respects. National customers have a nationwide or multi-regional footprint and, because of that footprint, typically contract with a broadliner that has geographically dispersed distribution centers; they usually make purchases under a single contract that offers price, product, and service consistency across all facilities; and they award contracts through a request for proposal or bilateral

negotiations. National customers include, among others, GPOs, foodservice management companies, hospitality chains, and national chain restaurants. By contrast, the FTC says, the typical "local" or "street" customer is an independent restaurant, which does not require multiple, geographically dispersed distribution centers; purchases in smaller quantities; and ordinarily does not have a contract with its foodservice distributor(s) as it negotiates purchases on a weekly or other short-term basis. The FTC contends that for national customers the geographic market is nationwide. For local customers, it argues that the geographic market is localized near Defendants' distribution centers.

Defendants counter that the foodservice distribution market cannot be sliced and diced as advocated by the FTC. According to Defendants, the relevant market is the entire $231 billion foodservice distribution industry, consisting not only of broadline food distributors, but also specialty distributors, systems distributors, and cash-and-carry stores. All of these modes of distribution, Defendants argue, compete for foodservice distribution customer spending. Based on this market definition, Defendants assert that together, they make up approximately 25 percent of total foodservice distribution sales. They also dispute that there is a product market for "national customers," asserting that such a market has been created by the FTC out of whole cloth to artificially inflate Defendants' market shares. According to the FTC, Defendants combined have, at least, a 59 percent share of the national customer product market.

A. Broadline Distribution as a Relevant Product Market

1. Legal Principles Affecting the Definition of the Relevant Product Market

The Supreme Court in *Brown Shoe* set forth the general rule for defining a product market: "The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Brown*

Shoe, 370 U.S. at 325. Stated another way, a product market includes all goods that are reasonable substitutes, even though the products themselves are not entirely the same. *Cardinal Health*, 12 F. Supp. 2d at 46; *Staples, Inc.*, 970 F. Supp. at 1074 (stating the question as "whether two products can be used for the same purpose, and if so, whether and to what extent purchasers are willing to substitute one for the other").

Whether goods are "reasonable substitutes" depends on two factors: functional interchangeability and cross-elasticity of demand. "Functional interchangeability" refers to whether buyers view similar products as substitutes. *See id.* ("Whether there are other products available to consumers which are similar in character or use to the products in question may be termed 'functional interchangeability.'"). "If consumers can substitute the use of one for the other, then the products in question will be deemed 'functionally interchangeable.'" *Arch Coal*, 329 F. Supp. 2d at 119; *see also United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 393 (1956)) ("Determination of the competitive market for commodities depends on how different from one another are the offered commodities in character or use, how far buyers will go to substitute one commodity for another."). "Courts will generally include functionally interchangeable products in the same product market unless factors *other than* use indicate that they are not actually part of the same market." *Arch Coal*, 329 F. Supp. 2d at 119.

As for cross-elasticity of demand, there the question turns in part on price. *E.I. Du Pont De Nemours*, 351 U.S. at 400 ("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."). If an increase in the price for product A causes a substantial number of customers to switch to product B, the products compete in the same market. *See id.* ("If a slight decrease in the price of cellophane causes a considerable number of customers of other flexible wrappings to switch to

cellophane, it would be an indication . . . that the products compete in the same market."); *Arch Coal*, 329 F. Supp. 2d at 120. Price is not, however, the only variable in determining the cross-elasticity of demand between products. Cross-elasticity of demand also depends on the "ease and speed with which customers can substitute [the product] and the desirability of doing so." *FTC v. Whole Foods Market, Inc.*, 548 F.3d 1028, 1037 (D.C. Cir. 2008) (Brown, J.). Thus, substitution based on a reduction in price will not correlate to a high cross-elasticity of demand unless the switch can be accomplished without the consumer incurring undue expense or inconvenience. *See Phila. Nat'l Bank*, 374 U.S. at 358 (observing that "[t]he factor of inconvenience localizes banking competition as effectively as high transportation costs in other industries").

Three other established principles are critical to defining the relevant product market in this case. The first is that the "product" that comprises the market need not be a discrete good for sale. As the Supreme Court has made clear: "We see no barrier to combining in a single market a number of different products or services where that combination reflects commercial realities." *United States v. Grinnell Corp.*, 384 U.S. 563, 572 (1966); *Phila. Nat'l Bank*, 374 U.S. at 356 (citation omitted) (finding that "the cluster of products . . . and services . . . denoted by the term 'commercial banking'. . . composes a distinct line of commerce"). Thus, what is relevant for consideration here is not any particular food item sold or delivered by Defendants, but the full panoply of products and services offered by them that customers recognize as "broadline distribution."

Second, "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; *Cardinal Health*, 12 F. Supp. 2d at 47 (same). That is because market definition hinges on whether consumers view the products as "reasonable

substitutes." *Cardinal Health*, 12 F. Supp. 2d at 46. So, for example, fruit can be bought from both a grocery store and a fruit stand, but no one would reasonably assert that buying all of one's groceries from a fruit stand is a reasonable substitute for buying from a grocery store. *See Whole Foods*, 548 F.3d at 1040 (Brown, J.) ("The fact that a customer might buy a stick of gum at a supermarket or at a convenience store does not mean there is no definable groceries market."). Thus, as applicable here, the fact that buyers may cross-shop between modes of food distribution does not necessarily make them part of the same market for the purpose of merger analysis.

Third, market definition is guided by the "narrowest market" principle. *Arch Coal*, 329 F. Supp. 2d at 120. That is, "a relevant market cannot meaningfully encompass [an] infinite range [of products]. The circle must be drawn narrowly to exclude any other product to which, within reasonable variations in price, only a limited number of buyers will turn." *Times-Picayune Publ'g Co. v. United States*, 345 U.S. 594, 612 n.31 (1953). Judge Bates in *Arch Coal* succinctly described the "narrowest market" principle in practice as follows:

> The analysis begins by examining the most narrowly-defined product or group of products sold by the merging firms to ascertain if the evidence and data support the conclusion that this product or group of products constitutes a relevant market. If not, the analysis shifts to the next broadest product grouping to test whether that is a relevant market. This process continues until a relevant market is identified.

Arch Coal, 329 F. Supp. 2d at 120; *see also United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36, 58-60 (D.D.C. 2011) (explaining "the principle that the relevant product market should ordinarily be defined as the smallest product market that will satisfy the hypothetical monopolist test").

The critical question here, therefore, is whether broadline food distribution qualifies as the relevant product market, or whether the product market should be expanded to include other modes of distribution.

2. *The Brown Shoe "Practical Indicia"*

Courts look to two main types of evidence in defining the relevant product market: the "practical indicia" set forth by the Supreme Court in *Brown Shoe* and testimony from experts in the field of economics. The court turns first to the *Brown Shoe* factors.

According to *Brown Shoe*, "[t]he boundaries of [a product market] may be determined by examining such practical indicia as industry or public recognition . . . , the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors." *Brown Shoe*, 370 U.S. at 325. "These indicia seem to be evidentiary proxies for direct proof of substitutability." *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 218 (D.C. Cir. 1986); *H&R Block*, 833 F. Supp. 2d at 51. Courts have relied on the *Brown Shoe* factors in a number of cases to define the relevant product market.[2] *See, e.g.*, *Staples*, 970 F. Supp. at 1075-80; *Cardinal Health*, 12 F. Supp. 2d at 46-48; *Swedish Match*, 131 F. Supp. 2d at 159-64; *CCC Holdings*, 605 F. Supp. 2d at 39-44; *H&R Block*, 833 F. Supp. 2d at 51-60.

The court finds that the *Brown Shoe* factors support the FTC's position that broadline foodservice distribution is the relevant product market for evaluating the proposed merger. As discussed below, an analysis of those factors demonstrates that other modes of foodservice distribution are not functionally interchangeable with broadline foodservice distribution.

a. Product breadth and diversity

The most distinguishing feature of broadline distribution is its product breadth and diversity. Broadliners stock thousands of SKUs across every major food and food-related category

[2] The *Brown Shoe* practical indicia may indeed be "old school," as Sysco's counsel asserted at oral argument, Closing Arg. Hr'g Tr. 44, and its analytical framework relegated "to the jurisprudential sidelines," *see Whole Foods*, 548 F.3d at 1059 (Kavanaugh, J., dissenting). But *Brown Shoe* remains the law, and this court cannot ignore its dictates.

in their distribution centers. *See Staples*, 970 F. Supp. at 1078 (comparing SKU selections among different sales outlets). The average Sysco or USF distribution center carries over [REDACTED] SKUs. Regional broadliners carry fewer SKUs than Defendants, but still maintain between 6,000 to 19,000 SKUs in their distribution centers. PX09350-215, Table 22. Broadliners also offer "private label" products, which are a broadliner's branded products. Sysco has over [REDACTED] private-label SKUs, and USF has over [REDACTED]. PX09350-219, Table 32. This product breadth and diversity enables broadliners to serve a wide variety of customers and to be a one-stop shop, if the customer wishes. As USF's Executive Vice President of Strategy David Schreibman testified at the FTC's Investigational Hearing: "[W]e have such a broad selection of SKUs because that is a key consideration of our customer base, you have to have what they want." Investig'l Hr'g Tr., PX00590-006 at 24.

The other distribution channels pale in comparison to broadline in terms of product breadth and diversity. Systems distributors carry a limited number of SKUs—usually only a few thousand—in their distribution centers. PX09350-215, Table 22. These SKUs are ordinarily proprietary in nature and used only by the customers for which they were developed, meaning that systems products are not readily sellable to other customers. Specialty distributors also carry a limited number of SKUs, usually for niche products—such as fresh produce, meat, seafood, dairy, or bakery items—which tend to complement broadline offerings. As Sysco's CEO William DeLaney explained: "We own [specialty] to create great traction with our customers, . . . we felt we had some gaps in our [broadline] product offerings, whether it was special produce, special cut steaks . . . ." Investig'l Hr'g Tr., PX00580-010 at 38. Cash-and-carry stores likewise do not have the same breadth and diversity of products as broadline distributors. One of the largest cash-and-carry stores, Restaurant Depot, carries [REDACTED] SKUs. USF's CHEF'STORE carries less than 4,000.

PX09350-216, Table 26. A number of customer declarants stated that cash-and-carry store products tended to be less uniform and inferior in quality to products carried by broadliners.

b. Distinct facilities and operations

No one entering a systems, specialty, or cash-and-carry outlet would mistake it for a broadline distribution facility. *See Staples*, 970 F. Supp. at 1079 ("No one entering a Wal-Mart would mistake it for an office superstore . . . . You certainly know an office superstore when you see one."). Broadline distribution centers are massive. The average size of a Sysco distribution center is over 380,000 square feet; for USF, it is over 270,000 square feet. Some regional distributors also have distribution centers ranging from 200,000 to 400,000 square feet. PX09350-215, Table 25. Non-broadline facilities are generally smaller in size and cannot readily be converted into a broadline facility or accommodate broadline customers.

Broadline facilities also have large salesforces attached to them. Broadline facilities typically have dozens of sales representatives, while systems distributors have few sales representatives at their facilities. PX09350-215, Table 23. Cash-and-carry stores generally do not have dedicated account representatives at all. Because the model of distribution is self-service, cash-and-carry sales representatives do not learn the individualized needs of their customers in a systematic manner.

Additional proof that broadline foodservice distribution is a separate product market comes from the corporate structure of large foodservice distributors. Major foodservice distributors offer distribution in other channels besides broadline, but they run those businesses separately from their broadline businesses. *See, e.g.*, *H&R Block*, 833 F. Supp. 2d at 56 (observing that digital do-it-yourself tax preparation was a distinct product market from assisted tax preparation because H&R Block ran them as "separate business units"). Sysco runs its systems distribution business,

SYGMA, as a separate division. So, too, does PFG, which runs a systems business known as PFG Customized. Sysco also runs separate specialty divisions, such as Fresh Point, a fresh produce supplier. So, too, does PFG, which has its own specialty division, Roma, which supplies Italian restaurants and pizza parlors. And USF runs a separate cash-and-carry operation, CHEF'STORE. This type of corporate structuring shows that those who run and manage foodservice companies view broadline as distinct from other modes of distribution.

c. Delivery

Timely and reliable delivery is critical in the food distribution industry. Unless customers can get the food they want when they need it, their businesses are at risk of losing clients and money. Broadliners have the capacity—due in large part to their extensive fleet of service vehicles, PX09350-217, Table 29—to offer frequent and flexible delivery schedules to meet customer needs, including next-day delivery. Ample evidence shows that, for a wide array of broadline customers—from large GPOs to individually-owned restaurants—next-day delivery is crucial to meeting their needs.

Neither systems distributors nor cash-and-carry stores offer the same degree of frequency and flexibility of delivery as broadliners.[3] Systems distributors tend to make large, limited-SKU deliveries on a fixed schedule. Also, systems fleets, on average, travel longer distances than broadline fleets to make deliveries. Carry-and-carry stores, for the most part, do not deliver. Rather, their primary model is self-service—that is, the customer transports the merchandise on her own. Some cash-and-carry outlets do offer delivery options. Costco, for example, offers limited-mileage delivery from some of its stores, and Restaurant Depot leases refrigerated trucks

[3] There was little evidence presented about the delivery capabilities of specialty distributors, aside from the fact that they have a limited geographic range of delivery. *See* PX00427-002 (Sodexo declarant indicating that specialty distributors covered a limited geographic range); PX00594-012 at 45 (MedAssets stating the same); PX00407-002 (Amerinet stating the same).

to its best customers. But those programs are quite limited and cannot substitute for the comprehensive and flexible delivery networks offered by broadliners to all of their customers.

d. Customer service and value-added services

Another distinguishing feature of broadline distributors is their high degree of customer service and value-added service offerings. For example, broadliners offer menu and nutritional-meal planning services to, among others, healthcare, hospitality, and restaurant customers. They also offer value-added services at their distribution facilities, such as food safety training and new product updates. Other modes of delivery do not generally offer comparable value-added services.

e. Distinct customers

Due in large part to the breadth of their product and service offerings, broadliners are capable of serving a wide range of customers, including classes of customers that the other channels cannot reach. Systems is a more efficient and cost-effective mode of distribution for fast food and quick service restaurants. Specialty distributors can provide higher quality and fresher products in certain categories, but have limited product offerings and charge higher prices than broadliners. Cash-and-carry stores are less expensive and more accessible for buyers such as independent restaurants, but their lack of delivery service makes them unsuitable for the large majority of foodservice customers.

These other channels, therefore, simply cannot and do not serve as wide an array of customers as broadliners do. The largest broadline customers, such as GPOs, foodservice management companies, and hospitality providers, cannot use systems or cash-and-carry for their needs. They purchase only modest quantities of product from specialty distributors. Even most independent restaurants cannot use cash-and-carry stores as a reasonable substitute for their broadliner, even though such stores offer lower prices.

f. Distinct pricing

Broadliners generally compete only against other broadliners on pricing. PFG's President and CEO, George Holm, who has over 37 years of industry experience, testified that systems and specialty distributors do not significantly affect the pricing and services that PFG offers to its customers. Hr'g Tr. 575-76, 643. And, although broadliners recognize that cash-and-carry stores provide lower prices, the record does not show broadliners benchmarking their prices against cash-and-carry stores or lowering prices to compete with them. To the contrary, as USF's Executive Vice President of Strategy David Schreibman succinctly stated in an email comparing pricing between USF as a broadliner and its own cash-and-carry division, CHEF'STORE: "In the store, we will be competitive with [REDACTED] on a similar cost model. On the truck, we will be competitive with broadline distributors on a similar cost model." PX03114-003.

g. Industry or public recognition

Overwhelmingly, the evidence shows that players in the foodservice distribution industry—both its suppliers and customers—recognize broadline, systems, specialty, and cash-and-carry to be distinct modes of distribution. *See Rothery Storage*, 792 F.2d at 219 n.4 ("The 'industry 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."). The court received both live and out-of-court sworn testimony from Defendants' executives; executives from other broadline distributors; officers of non-broadline companies; and customers, large and small. They uniformly observed that these modes of distribution are distinct in the variety of ways described above. In short, the industry widely recognizes that broadline distributors offer a unique cluster of products and services that is not functionally interchangeable with other modes of distribution.

h. Defendants' response to *Brown Shoe* "practical indicia"

Defendants do not, for the most part, contest the above-described distinctions between broadline and other channels of distribution. Instead, Defendants contend that defining the relevant market to include only broadliners "misunderstands consumer behavior." Memo of Defs. Sysco Corp., USF Holding Corp. and US Foods, Inc., in Opp'n to Pls.' Mot. for A Prelim. Inj., ECF No. 130 at 19 [hereinafter Defs.' Opp'n Br.]. They argue "customers simultaneously can, and routinely do, choose to patronize competitors of all stripes offering fungible goods through different but overlapping distribution channels." *Id.* What matters, Defendants claim, is that non-broadliners are able to constrain a broadliner's pricing by competing for customers who are able to move their entire purchasing, or portions of their purchasing, between channels. *Id.* at 19 ("Whether a substitute channel is a 'comprehensive' substitute is irrelevant to that question."). Defendants offer as one compelling example the burger chain Five Guys, which recently re-allocated over $300 million in annual business from USF to a collection of regional broadliners and systems distributors.

Defendants are indisputably correct that customers buy across channels, especially independent restaurants. They are also unquestionably correct that some customers, particularly quick service and fast food restaurant chains, are capable of moving large segments of business from broadline to systems. But the fact that Defendants sometimes compete against other channels of distribution in the larger marketplace does not mean that those alternative channels belong in the relevant product market for purposes of merger analysis. *See Staples*, 970 F. Supp. at 1075 ("[T]he 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."); *see also* Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law: An Analysis of Antitrust Principles*

and Their Application ¶ 565b (4th ed. 2014) ("[I]t would be improper to group complementary goods into the same relevant market just because they occasionally substitute for one another. Substitution must be effective to hold the primary good to a price near its costs[.]").

Two key decisions from this jurisdiction, *Whole Foods* and *Staples*, support this conclusion. In *Whole Foods*, the question was whether there existed a product market for premium natural and organic supermarkets ("PNOS") separate from ordinary supermarkets. The Court of Appeals' ultimate decision was fractured—each judge issued a separate opinion, leaving no controlling opinion from the Court. Two judges, however, concluded that PNOS is a separate product market from ordinary supermarkets, even though there was evidence that customers "cross-shopp[ed]" between the two. 548 F.3d at 1040 (Brown, J.); *id.* ("But the fact that PNOS and ordinary supermarkets 'are direct competitors in some submarkets . . . is not the end of the inquiry.'") (quoting *United States v. Conn. Nat. Bank*, 418 U.S. 656, 664 n.3 (1974)); *id.* at 1048 (Tatel, J.) ("That Whole Foods and Wild Oats have attracted many customers away from conventional grocery stores by offering extensive selections of natural and organic products thus tells us nothing about whether [they] should be treated as operating in the same market as conventional grocery stores."). Both judges agreed that just because customers were able to buy some categories of grocery products from both outlets—similar to how broadline customers are able to purchase some products from other modes of distribution—did not mean that PNOS was in the same product market as grocery stores. *See id.* at 1040 (Brown, J.) (citing testimony that "Whole Foods competes actively with conventional supermarkets for dry groceries sales, even though it ignores their prices for high-quality perishables"); *id.* at 1049 (Tatel, J.) ("As Judge Brown's opinion explains, this suggests that any competition between Whole Foods and

conventional retailers may be limited to a narrow range of products that play a minor role in Whole Food's profitability.").

The court in *Staples* held much the same. There, the question was whether consumable office supplies sold by office superstores constituted a separate product market from office supplies sold elsewhere. *See Staples, Inc.*, 970 F. Supp. at 1073. The court acknowledged that no matter who sells them, office supply products—to some extent, like food products—are "undeniably the same." *Id.* at 1075. The court nevertheless held that the sale of office supplies through superstores constituted the relevant product market. "[T]he unique combination of size, selection, depth and breadth of inventory offered by the superstores distinguishes them from other retailers." *Id.* at 1079. Those words apply with equal force to broadline distributors relative to other food distribution channels. *See also Cardinal Health*, 12 F. Supp. 2d at 47 (concluding that the wholesale drug industry "provide[s] customers with an efficient way to obtain prescription drugs through centralized warehousing, delivery, and billing services that enable the customers to avoid carrying large inventories, dealing with large number of vendors, and negotiating numerous transactions").

Defendants have not convincingly distinguished *Whole Foods* or *Staples*.[4] Instead, they urge the court to look to *United States v. Sungard Data Sys., Inc.*, 172 F. Supp. 2d 172 (D.D.C.

[4] In neither their opposition to the FTC's motion for preliminary injunction nor their proposed findings of fact and conclusions of law do Defendants attempt to distinguish *Whole Foods* or *Staples*. At oral argument, Defendants distinguished *Staples* based on the fact that in *Staples* the FTC had pricing data to show that prices were lower in markets where both merging firms were present. Closing Arg. Hr'g Tr. at 38-40. Defendants also sought to distinguish *Whole Foods* on the facts, arguing that in *Whole Foods* the defendants could not show that in the event of a price increase consumers of PNOS could go to a standard grocery store. *Id.* at 40-41. But the court finds these efforts to distinguish *Staples* and *Whole Foods* unconvincing. It is true that there was stronger pricing data in *Staples*, but pricing data alone did not lead to the court's conclusion. The factual similarities between this case and *Staples*, particularly the *Brown Shoe* practical indicia, are otherwise strong. As for *Whole Foods*, it is even more factually analogous to this case than is *Staples*. If anything, the proof that other channels of distribution are not reasonable substitutes for broadline is more compelling in this case than the evidence in *Whole Foods* that ordinary grocery stores are not a reasonable substitute for PNOS.

2001), as an analogous case. There, the question was whether different types of disaster recovery services for computer data comprised the same product market. *Id.* at 183. The court rejected the government's product market definition as limited only to shared hotsite services because "the government's market contains an extremely heterogeneous group of customers," *id.* at 182, who "are simply too varied and too dissimilar to support any generalizations," *id.* at 193. Here, it is unquestionably true that foodservice distribution customers are incredibly varied in their needs, buying habits, and price sensitivities. But *Sungard* differs in one critical respect. The court there observed that "the striking heterogeneity of the market, particularly as reflected by the *conflicting evidence relating to customer perceptions and practices*," undercut the government's market definition. *Id.* at 182-83 (emphasis added). Here, that simply is not the case. Though the customers may be varied, the court has little doubt that the industry, from the perspective of both sellers and buyers, perceives broadline to be a separate mode of food distribution. Witnesses of all stripes had little trouble distinguishing among the different channels of distribution, and Defendants offered no evidence of any industry confusion among them. Those facts make this case fundamentally different from *Sungard*. *See id.* at 183 ("Customer responses were also often vague and confused" and product definitions were "consistently unclear.").

Defendants also argue that the FTC's definition of broadline as the relevant market improperly excludes other modes based on "a small number of customers' subjective preferences for broadline distribution." Defs.' Opp'n Br. at 17 (footnote omitted). But the evidence, as it relates to broadline versus other distribution channels, is hardly selective. Defendants' own executives acknowledged the fundamental differences between broadline and other modes of

distribution.[5] So, too, did executives of regional broadliners, such as PFG,[6] Shamrock,[7] Reinhart Foodservice,[8] and Shetakis[9]; consortiums, such as UniPro[10]; systems distributors, such as Maines[11]; and cash-and-carry stores, such as Restaurant Depot.[12] Likewise, customers of every size recognized the differences between broadline and the other food distribution modes. In short, this is not the kind of case in which the testimonial evidence failed to demonstrate a consensus among the industry's players regarding the boundaries of the product market.

3. *Expert Testimony*

Having concluded that the *Brown Shoe* "practical indicia" support a product market for broadline foodservice distribution, the court turns next to the second type of evidence that courts consider in product market definition: expert testimony in the field of economics. One of the primary methods used by economists to determine a product market is called the "hypothetical monopolist test." This test asks whether a hypothetical monopolist who has control over a set of substitutable products could profitably raise prices on those products. If so, the products may comprise the relevant product market. *See H&R Block*, 833 F. Supp. 2d at 51-52. The theory behind the test is straightforward. If enough consumers are able to substitute away from the

[5] *See, e.g.*, DX-00319 at 32-36 (Sysco's CEO, William DeLaney, explained that systems is a "tailored, customized approach to certain types of customers" and the "model is not to serve GPO customers"); Hr'g Tr. 1369-70 (DeLaney stated that, compared to cash-and-carry, broadline is a "value package" that includes delivery services and menu consulting); Hr'g Tr. 1452 (David Schreibman of USF stated that "specialty distributors compete by having a broader array of products within their expertise" that "broadliner[s] may not have in [their] portfolio"); Investigat'l Hr'g Tr., PX00580-008-010 at 32-39 (DeLaney explained that broadline and specialty are "two different businesses," whereas broadline distribution includes "a full range of products"); Investigat'l Hr'g Tr., PX00584-060 at 239-40 (Louis Nasir, the Pacific Market President for Sysco, maintained that cash-and-carry stores "don't have the same selection" of products and "also don't have consistent inventory" compared with broadliners); Investigat'l Hr'g Tr., PX00590-011 at 42 (Schreibman stated that he was not aware of a cash-and-carry store that delivers).

[6] *See* PX00429-002-007; Hr'g Tr. 571-73.

[7] DX-00285 at 115-16, 164-66.

[8] DX-00295 at 16-17, 22.

[9] PX00414-001.

[10] DX-00260 at 139.

[11] DX-00264 at 64, 141; PX00424-001 (Maines is predominantly systems, but █ percent of 2013 revenues were from broadline sales).

[12] DX-00314 at 146-47.

hypothetical monopolist's product to another product and thereby make a price increase unprofitable, then the relevant market cannot include only the monopolist's product and must also include the substitute goods. On the other hand, if the hypothetical monopolist could profitably raise price by a small amount, even with the loss of some customers, then economists consider the monopolist's product to constitute the relevant market.

The hypothetical monopolist test, which courts have applied, is set forth in the U.S. Department of Justice and FTC's Horizontal Merger Guidelines. *See* U.S. Dep't of Justice & FTC Horizontal Merger Guidelines § 4.1.1 (2010) [hereinafter Merger Guidelines]; *H&R Block*, 833 F. Supp. 2d at 51-52; *CCC Holdings*, 605 F. Supp. 2d at 40; *Arch Coal*, 329 F. Supp. 2d at 120 & n.7. As stated in the Merger Guidelines:

> [T]he test requires that a hypothetical profit-maximizing firm, not subject to price regulation, that was the only present and future seller of those products . . . likely would impose at least a small but significant and non-transitory increase in price ("SSNIP") on at least one product in the market, including at least one product sold by one of the merging firms.

Merger Guidelines § 4.1.1. The SSNIP "is intended to represent a 'small but significant' increase in the prices charged by firms in the candidate market" and is typically assumed to be "five percent of the price paid by customers for the products or services to which the merging firms contribute value." Merger Guidelines § 4.1.2.

As applied to this case, the hypothetical monopolist test asks: If there was only one broadline food distributor, could it profitably raise price by five percent, or would that price increase result in a substantial number of customers moving enough of their spend to other modes of distribution—systems, specialty, or cash-and-carry—such that the price increase would be unprofitable? If the price increase would be profitable, then the relevant product market is broadline distribution; if unprofitable, it means that the relevant market must include at least one other channel

of distribution. Each side presented expert testimony from economists who performed the hypothetical monopolist test but who came to different results.

a. Dr. Mark Israel

For its expert economic evidence, the FTC presented the testimony of Dr. Mark Israel, who received a doctorate in economics from Stanford University and now serves as Executive Vice President at Compass Lexecon, a consulting firm. Dr. Israel's testimony served two primary functions. First, he acted as a *de facto* summary witness, synthesizing the mass of testimonial and documentary evidence gathered by the FTC. Dr. Israel's summary of that evidence parallels the discussion in the above sub-sections, so the court does not revisit it here. Second, Dr. Israel conducted a SSNIP test, using what is known as an "aggregate diversion analysis." Its purpose is to determine the amount of sales that a hypothetical monopolist of broadline distribution could lose before a price increase becomes unprofitable. *See Swedish Match*, 131 F. Supp. 2d at 160 (describing the related methodology of "critical loss analysis"); *H&R Block*, 833 F. Supp. 2d at 63 (same). A detailed recitation of Dr. Israel's aggregate diversion analysis is necessary because Defendants challenge the basic elements of his work.

Aggregate diversion analysis has three basic steps. The first is to determine the threshold aggregate diversion ratio, which is the percentage of customers that would need to stay within the broadline market to make a price increase profitable. *See H&R Block*, 833 F. Supp. 2d at 63. This is strictly a mathematical step, with the aggregate diversion ratio a function of the subject product's gross margin. The gross margin is defined as the price of selling one additional product minus the cost of selling the additional product.[13] The second step is to determine the *actual* aggregate diversion—that is, the actual percentage of customers of a single broadliner that would switch to

[13] Gross margin is calculated as follows: (Revenue-Cost of Goods Sold)/Revenue.

another broadliner after a price increase. "Since these lost sales are recaptured within the proposed market, they are not lost to the hypothetical monopolist." *Id.* As will be seen, this step involved an analysis of Defendants' actual sales data. The final step is to compare the two: if the actual aggregate diversion is greater than the threshold ratio, then the hypothetical monopolist could profitably raise prices and the candidate market is the relevant product market. *See id.* In other words, as applied here, if the percentage of customers of a single broadliner who would switch to another broadliner (as opposed to another mode of distribution) in response to a price increase is greater than the percentage of customers needed to stay within the market to make a price increase profitable, then the relevant product market is properly defined as broadline distribution.

At step one of his aggregate diversion analysis, Dr. Israel assumed a gross margin of 10 percent, a figure lower than the gross margin contained in the parties' financial reporting.[14] A 10 percent gross margin, according to Dr. Israel, yields a 50 percent threshold aggregate diversion ratio based on a formula devised by two economists, Michael Katz and Carl Shapiro.[15]

Next, Dr. Israel calculated the actual aggregate diversion based on three different data sets. He constructed the first two data sets from national and regional requests for proposals ("RFPs") and "bidding" summary information and documents produced by each Defendant to the FTC. Based on this information, Dr. Israel built a database for each company that tracked, for each bidding opportunity, the incumbent distributor, the winning distributor, and the competing bidders. PX09350-104. Based on Sysco's RFP/bidding data, he found that, when Sysco lost a bid, [over 70%] of the time (based on potential revenue from sales opportunities) it was to another

[14] Dr. Israel testified that the parties' reported gross margins are between 15 and 20 percent, but to be conservative he used a 10 percent margin. Hr'g Tr. 1004-05.

[15] The Katz-Shapiro formula that Dr. Israel used is $L = X/(X + M)$, where L is the aggregate diversion ratio, or "critical loss," X is the price increase, and M is the margin. PX09350-055 at n.134. For his aggregate diversion analysis, Dr. Israel used a 10 percent price increase and a 10 percent margin, for a resulting critical loss of 50 percent, *i.e.*, $.50 = .10/(.10 + .10)$. Hr'g Tr. 1004-07.

broadliner; the remaining losses were to another mode of distribution. PX09350-056. Based on USF's RFP/bidding data, the percentage was even higher—USF lost to other broadliners [over 70%] of the time. *Id.*

Dr. Israel constructed his third data set from USF's "Linc" database. Linc is a customer relations management tool that USF local sales representatives used until recently to track sales opportunities. The Linc database contains fields that sales representatives can complete to describe a sales opportunity, including a "main competition" field. Dr. Israel assumed that, if USF did not win an opportunity, it was won by the identified "main competitor." The Linc database contained hundreds of thousands of observations, about a third of which included information on the "main competitor." Based on this data, Dr. Israel concluded that [over 70%] of the local sales opportunities lost by USF (again, based on potential revenue of those sales opportunities) were lost to other broadliners. PX09350-056.

At the third step, Dr. Israel compared the aggregate diversion ratio of 50 percent to the actual diversion percentages derived from the three data sets. He concluded that, because each of the three actual diversion percentages was higher than the 50 percent threshold aggregate diversion ratio, broadline distribution was the relevant product market. In other words, Dr. Israel found that only 50 percent of broadline customers would need to remain within the broadline market to make a price increase profitable, while according to three different data sets, the actual percentage of customers who would remain within the broadline market (by switching to another broadliner) was greater than 50 percent. Therefore, Dr. Israel's calculations indicated that broadline distribution was the relevant product market.

b. Defendants' experts

Defendants mounted an aggressive challenge to Dr. Israel's work through their own expert witnesses. Defendants first presented Dr. Jerry Hausman, a professor of economics at Massachusetts Institute of Technology. Dr. Hausman testified, in short, that Dr. Israel's aggregate diversion analysis was wrong because (i) he used the wrong gross margin and (ii) he used the wrong mathematical formula to calculate the threshold aggregate diversion ratio. According to Dr. Hausman, Dr. Israel excluded certain variable costs from his gross margin. The actual gross margin was not 10 percent, according to Dr. Hausman, but between ■ percent and ■ percent. Also, Dr. Hausman testified that the aggregate diversion formula Dr. Israel used was incorrect and led to an overly narrow market definition.[16] Using the proper margins and the correct formula, Dr. Hausman opined, the aggregate diversion ratio is not 50 percent, but rather over 100 percent, which is an impossibility (*i.e.*, more than 100 percent of customers cannot switch in response to a price increase). Thus, he concluded, the relevant product market is not broadline, but all channels of food distribution.

While Dr. Hausman challenged Dr. Israel's calculation of the threshold aggregate diversion ratio, Defendants' other expert, Dr. Timothy Bresnahan, a professor of economics at Stanford University, critiqued Dr. Israel's use of the RFP/bidding and Linc data sets to calculate the actual aggregate diversion. Regarding the RFP/bidding data, Dr. Bresnahan described the data as contrived and unreliable—a point that Defendants consistently articulated to the FTC during the investigation phase. Dr. Bresnahan explained that the companies do not keep comprehensive RFP

[16] According to Dr. Hausman, the correct formula is L = X/M, where L is the aggregate diversion ratio, or "critical loss," X is the price increase, and M is the margin. Dr. Hausman testified that this is the more appropriate formula in an asymmetric market, like food distribution, which involves suppliers and customers with different costs, different types of customers, and a different mix of products. Hr'g Tr. 1960-64; DFF at 285-86 (citing to DX-05028 at 11). The formula used by Dr. Israel, on the other hand, is more appropriate in a symmetric market, that is, a market marked by homogeneity among suppliers and customers. Hr'g Tr. 1960, 1965-66; DX-05028 at 10-11.

or bidding data in the ordinary course of business and that the information Dr. Israel relied upon was pulled together at the insistence of the FTC, in part based on employees' unreliable notes and memories. As for the Linc data, it too was flawed, Dr. Bresnahan suggested, because it is a prospective sales database, not an actual transactions database in which USF sales personnel were accurately recording wins and losses. Moreover, neither the RFP/bidding data nor the Linc data describes whether Sysco or USF lost a customer for a price-based reason or some reason having nothing to do with price.

c. The court's finding as to the expert testimony

Having weighed the competing expert testimonies and considered them in light of the evidentiary record as a whole, the court finds Dr. Israel's aggregate diversion analysis and conclusion to be more persuasive than that advanced by Defendants' expert, Dr. Hausman.[17] Dr. Israel's reliance on the RFP/bidding and Linc data sets for calculating the aggregate diversion is problematic for the reasons Defendants have identified and, for those reasons, the court hesitates to rely on Dr. Israel's precise aggregate diversion percentages. But, when evaluated against the record as a whole, Dr. Israel's conclusions are more consistent with the business realities of the food distribution market than Dr. Hausman's. *See Cardinal Health*, 12 F. Supp. 2d at 46 (stating that "the determination of the relevant market in the end is 'a matter of business reality—[ ] of how the market is perceived by those who strive for profit in it.'" (alteration in original) (quoting *FTC v. Coca-Cola Co.*, 641 F. Supp. 1128, 1132 (D.D.C. 1986), *vacated as moot*, 829 F.2d 191 (D.C. Cir. 1987)); *Arch Coal*, 329 F. Supp. 2d at 116 ("[A]ntitrust theory and speculation cannot

[17] In finding Dr. Israel's conclusion more persuasive than that advanced by Defendants' expert, the court might be doing more than it is required to do. As Judge Tatel stated in *Whole Foods*: "Although courts certainly must evaluate the evidence in section 13(b) proceedings and may safely reject expert testimony they find unsupported, they trench on the FTC's role when they choose between plausible, well-supported expert studies." *Whole Foods*, 548 F.3d at 1048 (Tatel, J.).

trump facts[.]"); *H&R Block*, 833 F. Supp. 2d at 65 (bearing in mind the shortcomings of the expert's analysis and treating the analysis as "another data point" in determining the relevant market, rather than as conclusive).

The court finds Dr. Hausman's conclusion—that the actual aggregate diversion ratio is greater than 100 percent—inconsistent with business reality. On cross-examination, Dr. Hausman admitted that his conclusion meant that a hypothetical monopolist who had control over *every single broadline distributor* in the country could *not* profitably impose a SSNIP on customers, because enough customers would switch to other channels of distribution. Hr'g Tr. 2003-04. Yet many industry leaders testified either that other channels of distribution did not constrain the prices charged by broadliners or that other channels were not substitutes for broadline distribution. For instance, PFG's President and CEO, George Holm, testified that systems and specialty distributors do not significantly affect the pricing and services that PFG's broadline division offers to its customers. Hr'g Tr. 575-76. He also testified that systems and specialty distributors were not substitutes for broadliners. Hr'g Tr. 573. Such evidence from industry leaders,[18] which the court credits, contradicts Dr. Hausman's conclusion that a hypothetical monopolist of broadline services would not be able to impose a SSNIP because enough customers would switch to other channels of distribution.

[18] *See also* PX00429-004-007 (George Holm, President and CEO of PFG, explaining that systems, specialty, and cash-and-carry distributors are not substitutes for customers needing broadline distribution); DX-00285 at 125-26 (John Roussel, COO of Shamrock Foods, stating that it's "not possible" or "practical" for a broadline customer to use a systems distributor); DX-00260 at 139 (Bob Stewart, interim CEO of Unipro, explaining that a broadline customer cannot easily switch to a systems distributor and a broadline customer's needs are different than a systems customer's needs).

4. *Conclusion as to the Broadline Product Market*

In conclusion, based on the vast record of evidence the parties have presented, the court finds that the FTC has carried its burden of demonstrating that broadline distribution is the relevant product market.

B. National Broadline Distribution as a Relevant Product Market

The FTC asserts that, within the broader product market for broadline distribution, there is a narrower but distinct product market for "broadline foodservice distribution services sold to National Customers." Compl. ¶ 44. According to the FTC, "[d]ue to [their] geographic dispersion, National Customers typically contract with a broadline foodservice distributor that has distribution centers proximate to all (or virtually all) of their locations." *Id.* ¶ 42.

> National Customers typically contract with a broadliner that can provide—across all of their locations—product consistency and availability, efficient contract management and administration (e.g., centralized ordering and reporting, a single point of contact, and consistent pricing across all locations), volume discounts from aggregated purchasing, and the ability to expand geographically with the same broadline foodservice distributor.

Id. National customers include healthcare GPOs; foodservice management companies; and large hotel and restaurant chains. *Id.* ¶ 41. The FTC contends that Sysco and USF "are the only two single-firm broadline distributors with national geographic reach and, as such, are best positioned to serve National Customers." *Id.* ¶ 63.

Defendants vigorously dispute that there is such a thing as a "National Customer." They contend that a product market built around so-called national customers is "contrived," Defs.' Opp'n Br. at 16, and that the FTC's distinction between national and local customers is "factually and economically meaningless," *id.* at 13. They counter that the national-local distinction is not, as the FTC claims, built on differentiating customer characteristics, but is improperly based on an administrative distinction as to whether the customer prefers to be managed at the corporate level

(making it a "national" customer) or at the local distribution center (making it a "local" customer). *Id.* at 12-15. The so-called national customer category, they also argue, is improperly based on a "few core customers who say they prefer the merging parties." *Id.* at 13. In addition, Defendants assert that Dr. Israel did not perform a SSNIP test to assess the existence of a national customer market. *Id.* at 12.

1. Legal Basis for Defining Relevant Product Market Based on Customer Type

Before turning to the evidence, the court first considers the legal basis for defining a product market based on a type of customer. Neither side comprehensively addressed this issue. Admittedly, defining a *product* market based on a type of *customer* seems incongruous. After all, one ordinarily thinks of a customer as purchasing a product in the market, and not as the product market itself. But, in this case, according to the FTC, the national customer and broadline product converge to define a market for broadline products sold to national customers. Broadline distributors must offer a particular kind of "product"—a cluster of goods and services that can be delivered across a broad geographic area—to compete for national customers. In that sense, the customer's requirements operate to define the product offering itself.

The clearest articulation of this approach to product market definition comes from the Merger Guidelines. The Merger Guidelines are not binding, but the Court of Appeals and other courts have looked to them for guidance in previous merger cases. *See, e.g.*, *Heinz*, 246 F.3d at 716 n.9; *H&R Block*, 833 F. Supp. 2d at 52 n.10. Section 4.1.4 of the Merger Guidelines provides that "[i]f a hypothetical monopolist could profitably target a subset of customers for price increases, the Agencies may identify relevant markets defined around those targeted customers, to whom a hypothetical monopolist would profitably and separately impose at least a SSNIP." Merger Guidelines § 4.1.4. Markets to serve targeted customers are also known as "price

discrimination markets." *Id.* Professors Areeda and Hovenkamp have endorsed market definition of this kind, as well: "Successful price discrimination means that the disfavored geographic or product class is insulated from the favored class and, if the discrimination is of sufficient magnitude, should be counted as a separate relevant market." 2B Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law: An Analysis of Antitrust Principles and Their Application* ¶ 534d (3d ed. 2007). The concern underlying price discrimination markets is that certain types of captured or dedicated customers could be targeted for monopolist pricing even if a price increase for all customers would not be profitable. *See* Merger Guidelines § 3; Areeda & Hovenkamp 3d ed., *supra*, ¶ 533d ("[S]ellers may be able to discriminate against buyers who have fewer alternatives or for whom the product performs a more valuable function[.]").

Defining a market around a targeted customer, as the FTC urges here, is not free from controversy, as the different opinions in *Whole Foods* demonstrate.[19] Relying on an earlier version of the Merger Guidelines that recognized price discrimination against "targeted buyers," Judge Brown explained that "core consumers"—in that case, those committed to premium and natural organic supermarkets—"can, in appropriate circumstances, be worthy of antitrust protection." *Whole Foods*, 548 F.3d at 1037 (Brown, J.) (citing DOJ and FTC, 1992 Horizontal Merger Guidelines § 1.12, 57 Fed. Reg. 41,552, 41,555 (1992)). Judge Brown went on to say:

> In particular, when one or a few firms differentiate themselves by offering a particular package of goods or services, it is quite possible for there to be a central group of customers for whom "only [that package] will do." . . . Such customers may be captive to the sole supplier, which can then, by means of price discrimination, extract monopoly profits from them while competing for the business of marginal customers.

[19] The FTC cites to the "distinct customers" factor in *Brown Shoe* as support for defining a market around a targeted customer. However, *Brown Shoe* only listed "distinct customers" as one of many factors for courts to consider in defining a market. *Brown Shoe*, 370 U.S. at 325. It did not endorse defining a market around a group of targeted customers.

Whole Foods, 548 F.3d at 1038 (Brown, J.) (quoting *Grinnell*, 384 U.S. at 574) (alteration in original).

Judge Kavanaugh, in dissent, rejected defining a market around a "core customer." *Whole Foods*, 548 F.3d at 1062 (Kavanaugh, J., dissenting). According to Judge Kavanaugh, "there is no support in the law for that singular focus on the core customer. Indeed, if that approach took root, it would have serious repercussions because virtually *every* merger involves some core customers who would stick with the company regardless of a significant price increase."[20] *Id.* The relevant question for market definition, according to Judge Kavanaugh, is not whether a die-hard group of core customers would be impacted by a substantial price increase, but whether the merged company "could increase prices by five percent or more without losing so many marginal customers as to make the price increase unprofitable." *Id.*

2. Evidence Supporting a National Broadline Product Market

Ultimately, the court here need not resolve the *Whole Foods* disagreement over defining a market around a "core" customer. That is because the ordinary factors that courts consider in defining a market—the *Brown Shoe* practical indicia and the Merger Guidelines' SSNIP test—support a finding that broadline distribution to national customers is a relevant product market. *See, e.g.*, Areeda & Hovenkamp 3d ed., *supra*, ¶ 533d ("If the defendant *can* profit by charging pharmacies a price significantly over its cost, then the pharmacy sales are a relevant market[.]").

[20] The Merger Guidelines do not, for instance, set forth how a court is to distinguish a "targeted" group of customers from customers in general. This gives rise to the question of what limiting principles or factors a court should apply in defining a price discrimination market. Absent limitations, price discrimination against a single customer might be used to justify blocking a merger. This is not a mere theoretical possibility. According to the Merger Guidelines, "[i]f prices are negotiated individually with customers, the hypothetical monopolist test may suggest relevant markets that are *as narrow as individual customers*." Merger Guidelines § 4.1.4 (emphasis added).

a. Industry and public recognition

Among the most compelling evidence supporting a product market for national customers is the fact that regional broadliners have formed cooperatives, such as DMA and MUG, to compete for customers with a geographically dispersed footprint. Regional distributors, because of their limited footprints, do not have the capacity to serve customers with multi-regional needs across all of their locations. Only Sysco and USF have that capacity. These cooperatives were formed specifically to compete against Sysco and USF, by enabling regional competitors to combine to provide nationwide or multi-regional delivery and, importantly, to offer a single point of contact for the customer. Dan Cox, the President and CEO of DMA, explained that DMA was formed in 1988 as a competitive response to Sysco's merger with another company, Continental. *See* PX00565-051 at 202. He explained that "[w]hen that industry event took place, it was the first time that there was truly a national platform for foodservice distribution." *Id.* Put simply, business ventures like DMA would not exist if there were not a separate market for customers who have national or multi-regional distribution needs. *See Rothery Storage*, 792 F.2d at 218 n.4 (stating that courts must "assume that economic actors usually have accurate perceptions of economic realities").

Equally compelling evidence of the national-local distinction comes from a report done by the management consulting firm, McKinsey & Co., whom Sysco hired to assist with merger integration. After closely analyzing the two companies' operations, McKinsey prepared a presentation in July 2014, titled "National, Intermediate, and Field Coverage Models." The presentation observed that "Sysco and US Foods have different approaches to *grouping customers* and determining service models. . . . Both companies effectively operate two service models with distinct capabilities to serve *two types of customers*." PX09010-002 (emphasis added). The

presentation described "National Customers" as those who "use complex contracts with margin schedules, make online purchases of proprietary products, require auditing support, and coordinate across multiple markets." *Id.* By contrast, "Field Customers" were those who "make weekly purchases through in-person consultations, receive specialist support tailored to independent restaurants, require minimal auditing support, and operate in 1 or few markets." *Id.* McKinsey further observed that national customers' "requirements" included "[s]et margin schedule contract[s]"; "[e]fficient ordering across multiple locations"; "[l]arge number[s] of deviated, proprietary and close-coded products"; "[r]egulatory and audit support"; "[i]n-depth reporting"; and "[c]onsistency of service, pricing and products across multiple [m]arkets." PX09010-004. Field customers' "requirements," on the other hand, included the "[a]bility to make decisions each week along with consultation"; "[a]ccess to national, commodity, and some proprietary products"; "[f]ull business, culinary, and product support for independent businesses"; and "minimal" "[c]oordination across geographies." *Id.* McKinsey ultimately recommended that the companies recognize and build a new service model around a third kind of customer—an "Intermediate" customer—who would be identifiable based on five variables: (i) national contract/no contract; (ii) nature of industry; (iii) number of markets; (iv) number of regions; and (v) size of annual sales. PX09010-007. The McKinsey presentation identified as "conclusively" national those customers who operate in three or more markets or two or more regions. *Id.*

McKinsey is not the only industry analyst or expert to acknowledge that national customers form a market distinct from local buyers. Cleveland Research Company, an investment research firm, produced an analyst report on Sysco after the merger's announcement and recognized that Sysco and USF serve a distinct group of national customers. One of the report's conclusions was that "Sysco/USF will [be] able to keep most of their larger contracted and *national account*

customers for the near- and medium-term due to national scale and existing contracts . . . . Based on our research, most national operators prefer to deal with one distributor because it is more efficient and less expensive than dealing with several regional players." PX09332-006 (emphasis added).

The industry's trade group, the International Food Distributors Association ("IFDA"), also recognizes a distinction between national and local customers. IFDA produces a Quarterly Operations survey that reports separate sales figures for "national" and "street" accounts. PX00570-004 at 78. IFDA's President, Mark Allen, explained that IFDA distinguishes between the two because "the dynamics between the two [types of] businesses might be a little bit different. The operating metrics might be a little bit different." *Id.* at 80.

Defendants' ordinary course documents also recognize the national-local distinction and tout their strategic advantage as to the former. *See H&R Block*, 833 F. Supp. 2d at 52 ("When determining the relevant product market, courts often pay close attention to the defendants' ordinary course of business documents."). A Sysco "Investor Day" presentation from 2010 distinguishes the company's "Contract Sales (Broadline)" from "Street Sales," PX03101-010, and separates its "Key Competitors - National," from regional competitors, PX03101-020. Similarly, a presentation entitled "Board of Directors Strategy Sessions," dated July 2010, distinguishes between Sysco's market size for "corporate contracts"—defined to include "major foodservice management (FSM) sales, major group purchasing organization (GPO) sales, and major chain sales (non FSM or GPO)"—and "Street" business. PX01008-006.

USF has similar documents. An internal USF presentation, titled "Business Overview," describes "[USF's] Customers" as falling into three categories: (i) "Street: Independent restaurants or small local chains"; (ii) "National Accounts: Contracted customers located across the country,"

including acute and long-term healthcare facilities, hotels and the hospitality industry, schools, and U.S. military and government agencies; and (iii) "National Chain Restaurants: Fast food and quick-serve establishments." PX03122-004. *See also* PX03034-006 (similarly categorizing the company's customers). A USF "Investor Presentation" from November 2012 describes USF as the "2nd largest national broadline distributor," PX03000-006, and touts its "[a]bility to leverage our national scale to cost effectively service customers nationally," PX03000-014. Further, it distinguishes between "National Scale," where "US Foods is the second-largest broadline foodservice distributor in the U.S.," and "Local Scale," where "US Foods is estimated #1 or #2 position in ■ of served markets," PX03000-014. *See also* PX03007-007 (internal document in which KKR & Co., one of USF's private equity owners, distinguishes between "Street and National Account customer segments").

Other key players in the industry also recognize that national customers are different. For instance, the President and CEO of PFG, George Holm, agreed that "Sysco and US Foods are the only two distributors for broadline with the capability to serve national broadline customers with locations dispersed throughout the United States," including foodservice management companies, GPOs, large healthcare systems, and certain restaurant chains. Hr'g Tr. 596. Representatives of DMA and Reinhart likewise referred to national customers as those that are geographically dispersed and need a single point of contact. *See* PX00412-002-003; PX00415-004.

b. Distinct customer needs

There is ample record evidence that national customers' needs differ from those of local customers. The McKinsey analysis described above concisely summarized those distinctions. PX09010-004.

For starters, national customers, because of their dispersed geographic presence, often require a broadliner to meet their foodservice needs in more than one region. As a result, the number of distribution centers in a broadliner's network is often an important factor for such customers. In sharp contrast, according to Sysco, "all, or almost all," of its "local contract customers" are served by only one distribution center. PX01400-001.

The Defendants' ordinary course documents highlighted their comprehensive distribution networks as a competitive advantage for serving national customers. *See, e.g.*, PX03000-014 (USF presentation touting its "[a]bility to leverage our national scale to cost effectively service customers nationally"); PX00247-001-002 (USF email communication to [REDACTED] describing the "US Foods Value Proposition" as including "Privately held National Distribution footprint company"; "Single IT operating platform nationally"; and a "Single Point of Contact"); PX01062-005 (Sysco presentation to Aramark highlighting that Sysco's "national footprint, strong service approach and our breadth of product offerings is what differentiates us from our competition"). As USF's David Schreibman acknowledged during the evidentiary hearing, "US Foods['] leading national market position is due to US Foods['] geographic presence that includes 62 distribution centers across the United States." Hr'g Tr. 1520-21. He also acknowledged that Sysco was the only company with greater scale than USF. *Id.* at 1522.

In addition to multi-regional distribution capabilities, national customers generally demand a set margin contract that applies across multiple locations. As PFG's George Holm testified, a single contract enables customers to simplify contract administration and to reduce administrative costs. *Id.* at 600-02. Additionally, national customers often use RFPs and/or bilateral negotiations to award broadline foodservice distribution contracts. *Id.* at 1595-97. In sharp contrast, pricing for local or "street" customers, according to Sysco, "[is] ultimately the result of individual

negotiations between the customer and [broadliner]" and "can vary on a weekly and even daily basis." PX06057-032.

National customers also seek a single technology platform for handling their purchases. Consolidating purchasing through a single ordering platform creates efficiencies and cost savings, particularly as it relates to managing direct contracts with manufacturers and administering price changes. The importance of this feature is evidenced by DMA's development of a single ordering platform that enables customers to purchase from its members. Indeed, DMA promotes its technology platform as superior to Sysco's and USF's. PX00565-006 at 23-24. If national customers had not demanded such a feature, DMA would not have developed it.

Finally, product consistency is a factor for some national customers, particularly for those who wish to purchase private label products. *See* PX09010-004 (McKinsey report identifying as a "Customer requirement[]" for "National" customers "consistency of service, pricing, and products across multiple Markets"). Large customers can achieve a high degree of product consistency through direct contracting with product manufacturers or by purchasing proprietary brands stocked by Defendants. DX-01359 at 73 (Dr. Bresnahan report observing that "one way customers that value consistency achieve it is through direct negotiation with manufacturers to create propriety products" and that "[c]ustomers can also rely on national brands to ensure consistency"). However, because private label goods offer a strong value benefit, if a national customer wishes to purchase such goods and have them available across all of its locations, it can do so most efficiently through a broadliner with national geographic scope. *See* Hr'g Tr. 600 (George Holm of PFG stating that one reason national customers prefer to contract with Sysco or USF is that "[w]here they have a preference for a private brand, [ ] it is the same product [across] their system").

c. Defendants' Operations

Both Sysco and USF operate dedicated sales groups from their national headquarters that are responsible for negotiating and managing contracts with customers who use multiple distribution centers. *See Grinnell*, 384 U.S. at 572-74 (holding that centralized station security services operated on a national level is a relevant product market). Sysco refers to these customers as "corporate multi-unit customers," or CMUs. USF refers to them as "national sales customers." According to USF's Senior Vice President for National Sales, Tom Lynch, each national customer in his group has a single USF representative who is responsible for that customer. The largest customers are assigned a full-time dedicated employee to manage the account. PX00517-014-015 at 56-58.

d. SSNIP Test

Contrary to what Defendants contend, Dr. Israel did perform a SSNIP test to determine whether there is a separate product market for national customers. That SSNIP test was performed as an element of the SSNIP test that Dr. Israel used to assess whether broadline distribution was a relevant product market. As Dr. Israel testified, he applied to national customers the same 10 percent gross margin that he used to calculate the aggregate diversion ratio for all customers. Hr'g Tr. 1005 (stating that he used a 10 percent gross margin "to both local and national customers"). He derived the actual diversion for national customers based on the RFP/bidding data provided by the defendant companies. *Id.* at 1009 (describing the "RFP/bidding data" as "really national [customer] data"). Using the same methods discussed above, Dr. Israel calculated the actual diversion for Sysco's national customers to be [over 70%] and the actual diversion for USF's national customers to be [over 70%]. In other words, over [70%] of the time (based on potential revenue from sales opportunities), when Sysco or USF lost a bid opportunity for a

national customer, it was to another broadliner. Because these percentages were greater than the aggregate diversion ratio of 50 percent, Dr. Israel concluded that broadline service to national customers was a relevant market. In other words, Dr. Israel found that only 50 percent of national broadline customers would need to remain within the broadline market to make a price increase profitable, while the actual percentage of national customers who would remain within the broadline market (by switching to another broadliner) was greater than 50 percent. Dr. Israel's calculations, therefore, indicated that broadline distribution to national customers was the relevant product market.

The court already has expressed its reservations about relying on the RFP/bidding data to precisely calculate the aggregate diversion ratio. But, as before, the court finds that the ultimate conclusion of the SSNIP test—that broadline foodservice to national customers is a relevant product market—is supported by the weight of the evidence. Numerous national customer witnesses testified that other channels of distribution were not adequate substitutes for broadline distribution.[21] Although Defendants have shown that some national customers who were served by broadliners are now served by systems or systems-like distributors—most notably, Subway and Five Guys—those are the exceptions. Subway and Five Guys, because of their limited menus, are more amenable to substituting to a systems model. The same simply cannot be said of other large national customers, like GPOs, foodservice management companies, and hospitality chains, which rely heavily on broadliners.

[21] *See* Hr'g Tr. 143-145 (Christine Szrom, fact witness for U.S. Department of Veteran Affairs, explaining that she is not familiar with systems distribution and could "absolutely not" use a cash-and-carry distributors); Hr'g Tr. 214-17 (James Thompson, Head of Procurement for Interstate Hotels and Resorts, stating that "it would be very difficult if not impossible" to operate Interstate's foodservice distribution without a broadliner and that specialty is not a substitute for broadline distribution); PX[redacted]-002 (Joan Ralph, Group Vice President at Premier, Inc., saying that "[e]ven if we choose one day to contract with systems distributors, specialty distributors, or cash and carry stores, each would be as an additional, distinct service for our members who may need a quick, last-minute item or two; none could replace or serve as a substitute for broadline distribution services"); PX[redacted]-002 ([redacted], noting that [redacted] cannot contract with a systems distributor or use other forms of distribution).

e. Defendants' arguments against a national customer market

Asserting that there is no separate product market for national broadline customers, Defendants first argue that the national-local distinction is "arbitrary" because it is based on nothing more than customer preference about account management. Defendants' executives testified that Sysco's CMU customers and USF's national customers are so designated, not because of any particular characteristic or group of characteristics, but purely because the customer prefers to have its account managed by the headquarters sales team, instead of by its local distribution center. The FTC's and Dr. Israel's reliance on the companies' administrative designation, Defendants argue, leads to arbitrary classifications. For example, some of Defendants' customers who use a small number of distribution centers are counted by the FTC as "national" customers. As Dr. Hausman demonstrated, 37 percent of Sysco's CMU customers use five or fewer distribution centers and 55 percent use ten or fewer. And, for USF, 51 percent of their national customers use five or fewer distribution centers and 67 percent use ten or fewer. Hr'g Tr. 1976. Additionally, similarly situated customers—in terms of size, number of distribution centers, revenues, etc.—are sometimes treated differently. One customer may be identified as national and another as local, simply because one prefers to be managed from headquarters and the other from the local distribution center.

Defendants are correct that their "national" customer lists are over-inclusive—not every customer on those lists has multi-regional distribution needs. And they are also correct that the FTC could have more accurately defined a class of "national" customers by testing each candidate national customer against specific "national" criteria, such as the number of distribution centers used. But, ultimately, for the purpose of defining a product market, the court finds that the parties'

"national" customer designation is a useful proxy for customers requiring geographically dispersed distribution and attendant services.

As the graphic below prepared by Dr. Israel shows, if the merger were to occur, a significant proportion of the combined company's national customer revenues would come from customers who use a large number of distribution centers. PX09375-077, Figure 3. National customers using more than 35 distribution centers would account for ■ percent of a merged Sysco-USF's revenue; national customers using more than 24 distribution centers would account for ■ percent of revenue; and national customers using at least 10 distribution centers would account for ■ percent of revenue. Those figures demonstrate that Defendants' national-customer designations capture those key customers (based on revenues) who use a large number of distribution centers. The "national" designation includes, among others, the largest GPOs, like Premier, Novation, and MedAssets, each of whom uses over ■ distribution centers; the largest foodservice management companies, like Sodexo, Aramark, and Compass, each of whom uses more than ■ distribution centers; the largest hotel management company, Hilton, which uses ■ distribution centers; and the second largest government customer, the U.S. Department of Veterans Affairs, which uses ■ distribution centers (the largest is the U.S. Department of Defense, which uses ■ distribution centers). PX09375-076, Table 5. Thus, for these customers, the label "national" is not merely administrative; it accurately reflects this high revenue-generating group's actual needs. The fact

that some smaller customers are included among the Defendants' "national" designations does not mean that the designation lacks evidentiary value for defining a market for national customers.

Figure 3

Sysco and USF 2013 Revenues by Number of Distribution Centers Used

Next, Defendants assert that defining a price discrimination market around national customers is untenable because the FTC failed to show that so-called national customers shared any objectively observable characteristics that would enable the combined company to price discriminate against that group. *See* Merger Guidelines § 3 (stating that "differential pricing" is an essential element of price discrimination, which "may involve" offering different pricing to different types of customers "based on observable characteristics"). In other words, they argue that this grouping of customers is so heterogeneous that there is no common, identifiable

characteristic that could serve as a proxy for determining which customers in the broadline market have inelastic demand.

Defendants are undoubtedly correct that, even among their largest customers, there is great variety in the customers' servicing needs and requirements. But price discrimination can occur even when customers do not have common observable characteristics. As the Merger Guidelines state, markets for targeted customers may exist "when prices are individually negotiated and suppliers have information about customers that would allow a hypothetical monopolist to identify customers that are likely to pay a higher price for the relevant product." Merger Guidelines § 4.1.4; *see also* Carl Shapiro, *The 2010 Horizontal Merger Guidelines: From Hedgehog to Fox in Forty Years*, 77 Antitrust L.J. 49, 93 (2010) (observing that, in markets for intermediate goods and services, "prices typically are negotiated and price discrimination is common").

Here, the evidence is clear that Defendants engage in individual negotiations with their national customers and possess substantial information about them. Indeed, the fact that Defendants employ substantially more sales representatives than other broadliners, PX09350-218, Table 30, and assign full-time dedicated employees to some of their largest customers is indicative of the "know-your-customer" philosophies of both firms. Defendants, therefore, already have substantial customer information that would allow them to predict which of their customers have inelastic demand and which do not. Price discrimination can occur in such a marketplace, even if the targeted customers do not share specific identifiable traits.

Finally, Defendants contend that a product market of targeted national customers does not comport with business realities. This argument has two main elements. First, they assert that, contrary to what the FTC contends, Compl. ¶¶ 5, 42, national customers do not require a broadline foodservice distributor that is national in scope. Rather, they argue, even at current prices, many

large customers spread their distribution needs over multiple regional suppliers. For instance, Defendants cite GPOs, like ███, ███, Amerinet, and large government agencies, like the Defense Logistics Agency, as using a regional contracting approach. Defs.' Opp'n Br. at 15. They also refer to one of the largest foodservice management companies, Sodexo, which splits its distribution into █ regions. *Id.* And, then there is Subway and Five Guys, two large chain restaurants that have regionalized and purchase from multiple suppliers. *Id.* at 15-16. Because these types of customers can regionalize or credibly threaten to regionalize, Defendants argue, the merged company would not be able to discriminate against them on price.

But Defendants' argument founders when faced with the actual purchasing habits of the industry's largest customers. The evidence shows that the bulk of the broadline purchasing done by most geographically dispersed broadline customers is still done through Sysco and USF. Of Avendra's members' broadline spend, █ percent is with Sysco and USF. Pl.'s Corrected Proposed Findings of Fact and Conclusions of Law, ECF No. 173 at 114 [hereinafter PFF]. Members of other GPOs similarly purchase a large percentage of their goods from Sysco and USF. The total broadline spend of Premier,[22] Novation, MedAssets, and HPSI members with Sysco and USF is, respectively, █ percent, █ percent, █ percent, and █ percent. *Id.* at 113-15; FTC Closing Arg. Slides at 35. Large foodservice management companies similarly make the bulk of their broadline purchases from Sysco and USF. Sodexo, Aramark, Compass, and Centerplate, respectively, spend █ percent, █ percent, █ percent, and █ percent of their broadline foodservice distribution dollars with Sysco and USF. PFF at 113-16; FTC Closing Arg. Slides at 35. The story is similar for large hospitality customers. Two of the largest, Hilton and Interstate,

[22] As to Premier, the person responsible for its foodservice program, Joan Ralph, testified that ███ ███. Hr'g Tr. 474; PX00475-001-002.

allocate █ percent and █ percent of their broadline spend, respectively, to the two companies. PFF at 114, 116; FTC Closing Arg. Slides at 35. Even the Defense Logistics Agency, which contracts regionally, dedicates █ percent of its broadline spend to Sysco and USF. PFF at 116; FTC Closing Arg. Slides at 35.

The court infers from this evidence that geographically dispersed customers view Sysco and USF as having significant comparative advantages over regional distributors, particularly because of their far-reaching distribution networks. Though some customers have spread their business over multiple broadliners, a significant portion (as measured by total revenues) have not. Indeed, PFG's George Holm observed that the "*clear trend* amongst national broadline customers is to move toward a single nationwide provider." Hr'g Tr. 598 (emphasis added); PX09081-002 (letter from PFG's counsel to FTC, dated November 14, 2014, stating the same). *See Brown Shoe*, 370 U.S. at 332 (footnote omitted) ("Another important factor to consider is the trend toward concentration in the industry."). Mr. Holm further admitted that either Sysco or USF essentially wins every RFP issued by a national customer. Hr'g Tr. 598-99. And PFG acknowledged by letter to the FTC that, even as the country's third-largest broadliner, "PFG has difficulty competing for national broadline accounts because it does not have a nationwide footprint of broadline distribution centers." PX09081-001. Other large regional broadliners have said the same about their own businesses models.[23] Defendants' contention—that a product market defined around national customers does not comport with business reality because such customers have regionalized or can regionalize—is thus belied by the record evidence.

[23] *See, e.g.*, PX00415-004 (Reinhart); PX00416-003 (Merchants); PX00434-003-004 (Labatt); PX00438-002-003 (Cash-Wa); PX00443-005 (Ben E. Keith); PX00449-003 (Jacmar); PX00451-005 (Services Group of America); PX00458-004 (Nicholas & Co.); PX00460-002-003 (Shamrock); PX00529-047-048 at 188-89 (Gordon).

Second, Defendants argue that margin data shows that, as a merged entity, they would not be able to price discriminate against national customers. Dr. Hausman demonstrated that Defendants' margin on sales to customers who use fewer distribution centers is actually *higher* than their margin on sales to those who use more. DX-01355 at 58-61. Defendants contend that under the FTC's theory, they presently have a duopoly as to national customers, yet they do not earn duopoly profits on that customer class. Defendants thus maintain that, just as they cannot today price discriminate to earn duopoly profits, they would not be able to price discriminate after the merger to earn monopoly profits.

Defendants' argument, however, is unconvincing. Defendants' present inability to earn duopoly profits on national customers is probably because large customers can keep prices down by leveraging the defendant companies against one another. As the Cleveland Research Company observed: "Based on our research, **we believe both Sysco and US Foods have priced each other down competing for larger national/regional contract accounts** over the last several years." PX09332-004. The ability of large buyers to keep prices down, functioning as what is known in antitrust literature as "power buyers," *see Cardinal Health*, 12 F. Supp. 2d at 58-59; Merger Guidelines § 8, depends on the alternatives these large buyers have available to them, *see* Shapiro, *supra*, at 95; Areeda & Hovenkamp 3d ed., *supra*, ¶ 943a. If a merger reduces alternatives, the power buyers' ability to constrain price and avoid price discrimination can be correspondingly diminished. *See* Merger Guidelines § 8 ("Normally, a merger that eliminates a supplier whose presence contributed significantly to a buyer's negotiating leverage will harm that buyer."). Thus, the fact that Defendants are currently unable to price discriminate against national customers does not mean that they would be unable to do so as a merged firm.

C. Product Market Summary

Having considered and weighed the parties' arguments and evidence, the court concludes that the FTC has carried its burden of showing that, for purposes of merger analysis, (i) broadline foodservice distribution is a relevant product market, and (ii) broadline foodservice distribution to national customers is also a relevant product market.

D. Relevant Geographic Market

The court now turns to the second part of defining the relevant market, which involves determining the relevant geographic market. The Supreme Court has stated that, for Section 7 of the Clayton Act, the relevant geographic market is "the area in which the goods or services at issue are marketed to a significant degree by the acquired firm." *Marine Bancorp.*, 418 U.S. at 620-21. Stated differently, "[t]he proper question to be asked . . . [is] where, within the area of competitive overlap, the effect of the merger on competition will be direct and immediate." *Phila. Nat. Bank*, 374 U.S. at 357; *see also Cardinal Health*, 12 F. Supp. 2d at 49 (citation omitted) (internal quotation marks omitted) (stating that the relevant geographic market is "the area to which consumers can practically turn for alternative sources of the product and in which the antitrust defendants face competition"). Like the product market, the geographic market must "correspond to the commercial realities of the industry and be economically significant." *Brown Shoe*, 370 U.S. at 336-37 (footnote omitted) (internal quotation marks omitted). The Supreme Court has recognized that an "element of 'fuzziness would seem inherent in any attempt to delineate the relevant geographical market,'" and therefore "such markets need not—indeed cannot—be defined with scientific precision." *Conn. Nat. Bank*, 418 U.S. at 669 (quoting *Phila. Nat'l Bank*, 374 U.S. at 360 n.37). That said, the relevant geographic market "must be sufficiently defined so that the

[c]ourt understands in which part of the country competition is threatened." *Cardinal Health*, 12 F. Supp. 2d at 49.

The FTC contends that there are two relevant geographic markets in this case. For national broadline customers, the relevant geographic market is nationwide. For local broadline customers, the relevant geographic markets are localized around Defendants' distribution centers.

With regard to national customers, for essentially the same reasons that the FTC asserts that there is a product market for broadline distribution to national customers, the FTC asserts that the geographic market for those customers is nationwide. The FTC relies on the fact that Defendants plan on a national level and have "national account" teams dedicated to national customers; their contractual pricing and service terms with national customers apply across regions; and their competition for national customers is largely other broadliners with nationwide coverage.

As for local customers, as discussed in more detail below, the FTC's local geographic markets were constructed by Dr. Israel and are premised on customers' proximity to Defendants' distribution centers. The basic idea is that, for local customers, distance to a distribution center is a key service factor and, for Defendants, distance traveled from a distribution center to make deliveries is a critical cost component. The FTC alleges that the merger threatens to harm competition in 32 local geographic markets where Sysco and USF together currently have dominant market shares. Compl. ¶ 60.

Defendants dispute that there is a nationwide geographic market for the same reasons that they contend that there is no national customer product market. As for the local geographic markets, Defendants aggressively challenge the methodology that Dr. Israel used in defining local markets. Their primary criticism is that the geographic areas are drawn so narrowly that they

exclude actual competition from the relevant market. This results, they contend, in local market concentrations that artificially inflate Defendants' market shares.

1. National Market

Although the physical act of delivering food products occurs locally, for national customers the relevant geographic area for competitive alternatives is nationwide, primarily because of their geographically dispersed footprint. Defendants compete within this market by touting their nationwide distribution capabilities to these customers; bidding against other broadliners with multi-regional capabilities (which is to say, against each other and the regional cooperatives); coordinating the marketing, negotiating, and managing of these customers through their "national account" teams; and entering with these customers into a single contract whose terms, including pricing, apply across regions. For these reasons, the court finds that the relevant geographic market for broadline foodservice to national customers is nationwide. *See Grinnell*, 384 U.S. at 575-76 (finding a national geographic market where central station services "operated on a national level," and there was "national planning," a nationwide schedule of prices, and nationwide contracting for multi-state businesses); *Cardinal Health*, 12 F. Supp. 2d at 50 (finding a national geographic market where evidence showed that "GPOs negotiate contracts with several wholesalers, making the same prices available throughout the country to all of their members—local, regional, or national").

2. Local Markets

Defining the local geographic market presents a far greater challenge. Not surprisingly, there is no industry standard for delineating the area that makes up a local geographic market for broadline distribution. Each local market has its own unique attributes. Customer composition and concentration differs across markets; so does the demand for products, with SKU variations

reflecting local tastes and palettes. Average driving distances for foodservice distributors vary depending on the density of the area, with longer hauls more common in rural parts of the country and shorter trips more prevalent in urban areas. And, of course, the competitors vary from market to market.

The FTC tasked Dr. Israel with defining the local geographic markets. He constructed them as follows. In his first step, Dr. Israel drew circles around the location of each Sysco and USF distribution center. To determine the size of each circle, Dr. Israel used a radius, referred to as the "draw distance," that, on average, captured 75 percent of the distribution center's sales to local customers. The length of each distribution center's 75 percent draw radius differed. For example, the 75 percent draw distance around Sysco's Billings, Montana, facility was 262 miles, whereas the 75 percent draw distance around Sysco's Jersey City, New Jersey, facility was only 24 miles. PX09350-221-224, Table 38. What that means is Sysco drives over 200 miles further to capture 75 percent of its local sales in Billings than it does in Jersey City. That disparity makes sense, as more populated areas correspond to higher customer concentrations and shorter delivery distances.

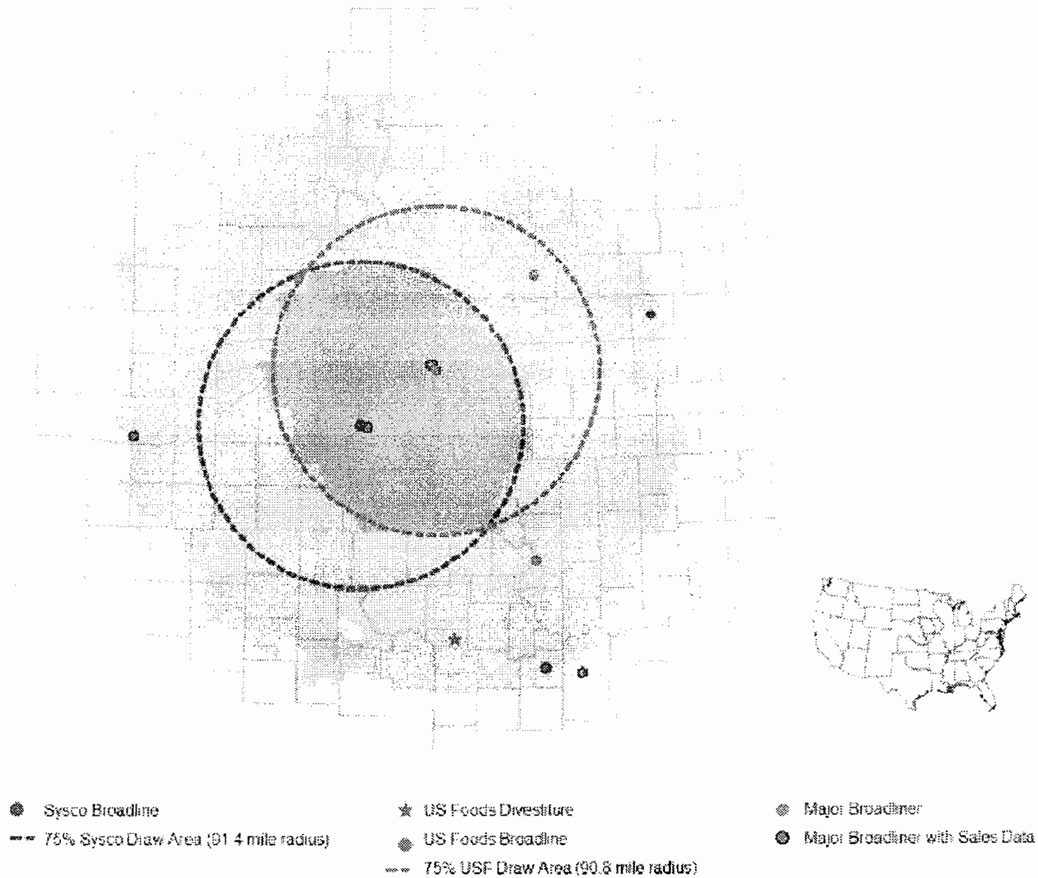
In his second step, Dr. Israel identified each company's local customers that fell within an area of intersection between the draw circle around the Sysco distribution center and the draw circle around the USF distribution center. This area of intersection was termed the "overlap area." These "overlap customers," according to Dr. Israel, were the customers most likely to suffer harm from the merger, because these were the customers who would be left with one less alternative supplier after the merger. Exhibit 40 from Dr. Bresnahan's report, which is reproduced below, shows Dr. Israel's methodology in the Omaha, Nebraska, area. The blue-dotted circle corresponds

to Sysco's 75 percent draw area, and the green-dotted circle corresponds to USF's. The dark gray area corresponds to the "overlap customers." DX-01359, Ex. 40.

EXHIBIT 40

DISTRIBUTION CENTERS LOCATED NEAR THE FTC'S CONTESTED LOCAL AREAS

OMAHA, NE/COUNCIL BLUFFS, IA



In his third step, Dr. Israel identified the broadline distributors who could compete for the customers in the overlap area. To do this, Dr. Israel drew circles around each overlap customer using the 75 percent draw radius. This created a larger circle that moved the outer boundaries of the overlap area by the same radius as the 75 percent draw area, which is represented by the light gray area in Exhibit 40 above. According to Dr. Israel's analysis, the light gray area is the area to which customers can practically turn for alternative sources of broadline distribution. All of the

competitors located within the light gray area were factored into Dr. Israel's local market share computations.

Defendants attack Dr. Israel's "circle drawing exercise" as "arbitrary" and not reflective of industry realities. Defs.' Opp'n Br. at 27. Specifically, they assert that Dr. Israel's methodology is flawed because it assumes that competitors will drive no greater distance than Sysco's or USF's 75 percent draw radius to serve customers. Defendants point to competitor declarations and testimony showing that in many of the 32 local markets in which the FTC claims Defendants have a dominant market share, competitors are willing to, and do, drive distances greater than the 75 percent draw radius to compete for and deliver to customers.

Notwithstanding this criticism, the court finds that there is nothing inherently "arbitrary" about Dr. Israel's methodology in defining the local markets. To the contrary, given the absence of an industry standard for defining a local market, Dr. Israel's methodology provides a practical approach and solution to an otherwise thorny problem. Dr. Israel's premise in defining these markets—that driving distance matters—is amply supported by the record and common sense. Customers who are farther away from a distribution center cost more to service. Longer distances correspond to, among other things, higher gas usage, more labor hours, and increased wear and tear on trucks. Given that the geographic market need not be defined by "metes and bounds," *Conn. Nat'l Bank*, 418 U.S. at 669 (citation omitted) (internal quotation marks omitted), Dr. Israel's 75 percent draw methodology identifies "the area of competitive overlap, [where] the effect of the merger on competition will be direct and immediate," *Phila. Nat'l Bank*, 374 U.S. at 357. *See also Conn. Nat'l Bank*, 418 U.S. at 670 n.9 (remanding to the district court to define the local market and observing that the "federal bank regulatory agencies define a bank's service area as the geographic area from which the bank derives 75% of its deposits"). The court therefore

concludes that the relevant local geographic markets are the areas of overlap resulting from Dr. Israel's 75 percent draw methodology.

Ultimately, what really troubles Defendants about Dr. Israel's "circle drawing exercise" is not the resulting geographic areas, but what those areas mean for calculating Defendants' local market shares. The court considers those arguments in the next section.

II. THE PROBABLE EFFECTS ON COMPETITION

Having concluded that the FTC has carried its burden of establishing a relevant market—both a nationwide market for broadline foodservice to national customers and various local markets for broadline foodservice to local customers—the court turns next to "the likely effects of the proposed [merger] on competition within [those] market[s]." *Swedish Match*, 131 F. Supp. 2d at 166. As the Court of Appeals explained in *Heinz*, the government "must show that the merger would produce 'a firm controlling an undue percentage share of the relevant market, and [would] result[ ] in a significant increase in the concentration of firms in that market.'" 246 F.3d at 715 (quoting *Phila. Nat'l Bank*, 374 U.S. at 363). "Such a showing establishes a 'presumption' that the merger will substantially lessen competition." *Id.* (citation omitted).

The Court of Appeals has held that the FTC can establish its *prima facie* case by showing that the merger will result in an increase in market concentration above certain levels. *Id.* "Market concentration is a function of the number of firms in a market and their respective market shares." *Arch Coal*, 329 F. Supp. 2d at 123. A common tool used to measure changes in market concentration is the Herfindahl-Hirschmann Index (HHI). *Heinz*, 246 F.3d at 716; *see also* Merger Guidelines § 5.3. HHI figures are "calculated by summing the squares of the individual firms' market shares," a calculation that "gives proportionately greater weight to the larger market shares." Merger Guidelines § 5.3. "Sufficiently large HHI figures establish the FTC's prima facie

case that a merger is anti-competitive." *Heinz*, 246 F.3d at 716. The Merger Guidelines, which provide "a useful illustration of the application of HHI," *FTC v. PPG Indus., Inc.*, 798 F.2d 1500, 1503 n.4 (D.C. Cir. 1986), state that a market with an HHI above 2,500 is considered "highly concentrated"; a market with an HHI between 1,500 and 2,500 is considered "moderately concentrated"; and a market with an HHI below 1,500 is considered "unconcentrated," Merger Guidelines § 5.3. Furthermore, a merger that results in "highly concentrated markets that involve an increase in the HHI of more than 200 points will be presumed to be likely to enhance market power." *Id.* In *Heinz*, the Court of Appeals recognized that an increase in HHI by 510 points "creates, by a wide margin, a presumption that the merger will lessen competition." 246 F.3d at 716.

A. Concentration in the National Broadline Customer Market

1. Dr. Israel's National Broadline Customer Market Shares Calculations

In some cases the merging parties' market shares and post-merger HHIs are seemingly uncontroversial. *See, e.g.*, *Staples*, 970 F. Supp. at 1081-82; *H&R Block*, 833 F. Supp. 2d at 71-72. Not so here. Because there are no industry-recognized market shares for national broadline customers, the FTC tasked Dr. Israel with calculating the market shares and the HHIs. Not surprisingly, Defendants vigorously contested his methodology and conclusions.

Dr. Israel calculated Defendants' national customer shares as follows. As his first step, he identified Defendants' individual sales to national broadline customers, *i.e.*, the numerator for the market share calculation. Those sales figures came directly from the parties' "national" customer designations: for Sysco, its sales to CMU customers, and for USF, its sales to national customers.

Next, Dr. Israel determined the total sales by all broadline distributors to national customers, *i.e.*, the denominator for the national share calculation. Again, because there is no

industry-recognized figure for such sales, Dr. Israel estimated them. He did so in two ways. First, he aggregated the national sales of the three principal competitors for national customers—Sysco, USF, and DMA—and added in another share equal to DMA's. This total comprised the denominator for his "baseline" shares calculation. PX09350-074. The addition of another DMA-sized share to the denominator was premised on his observation from the RFP/bidding data that the size of sales to national customers by all broadliners other than Sysco, USF, and DMA was about the same as DMA's.

Dr. Israel also used a second method to calculate the total sales to national customers. He aggregated the national sales reported by the largest 16 broadliners, including DMA and MUG, in response to the FTC's civil investigative demands. This data is referred to as CID data. Dr. Israel ran several "sensitivities" on this sum, adding in sales to account for variations in CID responses (*e.g.*, some distributors did not segregate "national" from total sales). Dr. Israel also aggregated the national sales of Sysco, USF, DMA, and MUG, plus an estimate of national sales for *all* other responding distributors based on the assumption that each distributor's national-local sales ratio was the same as Defendants' ratio. Dr. Israel's various approaches yielded a total national broadline sales estimate of $28 to $30 billion. Hr'g Tr. 1177-78; *see also* PX09060-006 (PFG business plan estimating the size of the national customer market to be approximately $20 billion).

As his last step, Dr. Israel adjusted his market shares to account for the divestiture to PFG. The chart below reflects Dr. Israel's post-merger, post-divestiture market share and HHI calculations. For his "baseline" calculation, Dr. Israel determined that the parties' post-merger national broadline customer market share would be 71 percent with an HHI increase of nearly 2,000 points. His CID data-based calculations, shown as (i) through (vi) in the chart, also yielded high post-merger shares and significantly increased HHIs. Dr. Israel's most conservative

approach, in which he assumed that the top 16 broadliners had national to local sales ratios that were equal to Defendants' ratio of such shares—(iv) in the chart below—resulted in a post-merger market share of 59 percent and an HHI increase of 1,500 points. PX09350-186, Table 18.

Table 18

Shares of Sales to National Broadline Customers, After Accounting for the Proposed Divestiture

	Post-Divestiture Shares	Post-Divestiture HHI's	
	Combined Share	HHI	Δ HHI
Baseline	71%	5,119	1,966
(i) National	68%	4,935	1,953
(ii) National + Imputed National	65%	4,549	1,799
(iii) National + Regional	66%	4,614	1,822
(iv) National + Systems	62%	4,217	1,643
(v) National + Regional + Systems	61%	4,087	1,590
(vi) Parties' Ratio of National	59%	3,809	1,500

2. *Defendants' Arguments*

Defendants raise a host of objections to the reliability of Dr. Israel's methodology and calculations. They contend that his use of their "national" sales in the numerator was arbitrary because, as discussed above, not all of Defendants' "national" sales are to customers with a multi-regional footprint. The inclusion of those sales, they contend, overstated Defendants' national market share. They also argue that Dr. Israel's numerator included some sales to systems-like customers, such as to Five Guys, but his denominator excluded competitors' systems sales. This asymmetry, they assert, also resulted in an overstatement of Defendants' share. They further contend that the denominator used in Dr. Israel's "baseline" calculation is unreliable because it relies on the flawed RFP/bidding data set. And, finally, they argue that the denominator in the CID data calculation excludes over $30 billion in sales—though the source of this number is

unclear.[24] They contend that these errors in developing the numerator resulted in biased market share calculations.

None of these arguments ultimately persuade the court that Dr. Israel's methodology or his market shares and HHI calculations are unreliable. The FTC need not present market shares and HHI estimates with the precision of a NASA scientist. The "closest available approximation" often will do. *PPG*, 798 F.2d at 1505 (citation omitted); *see also H&R Block*, 833 F. Supp. 2d at 72 (stating that a "reliable, reasonable, close approximation of relevant market share data is sufficient"). Indeed, in *PPG*, the FTC presented, and the Court of Appeals accepted, share calculations for "every market the evidence suggests is remotely possible," which "yield[ed] results of similar magnitudes in market concentration." 798 F.2d at 1506. Similarly, Dr. Israel ran multiple variants of his market shares and concentration analysis, using two different data sets and modifying one of these data sets, the CID data, in six different ways. Most convincing to the court was Dr. Israel's final method of calculating shares using the CID data, which assumed that all 16 of the top broadliners had the same national-local sales ratio as Defendants did. That approach yielded a low-end market share of 59 percent and an HHI increase of 1,500 points—almost three times the 510 points that the Court of Appeals in *Heinz* found created a presumption of harm by a "wide margin." 246 F.3d at 716. This variation almost certainly *underestimated* Defendants' market shares, as smaller broadliners are unlikely to have a ratio of national-local sales comparable to Defendants' ratio.

Another reason Defendants' arguments do not sway the court is that other evidence in the record supports Dr. Israel's calculations. As discussed above, the largest customers for broadline

[24] "Dr. Israel acknowledged that he left out $30 billion in systems distribution in the "sensitivity analysis purporting to account for systems sales." Defs.' Proposed Findings of Fact and Conclusions of Law, ECF No. 171 at 263 (citing Hr'g Tr. 1259-60).

distribution in the country—healthcare GPOs, foodservice management companies, hospitality companies, and large government agencies—make the vast majority of their broadline purchases from Defendants. These customers individually spend hundreds of millions of dollars (or more) on broadline distribution—totaling approximately half of the national broadline market (based on Dr. Israel's calculation of a total market of $28 to $30 billion). *See* FTC Closing Arg. Slides at 35. If the largest customers are presently spending between 60 to 100 percent of their total food budget with Defendants, *id.*, then Dr. Israel's low-bound, post-merger combined market share of 59 percent is consistent with market realities.

In addition, the only independent market share analysis of the broadline industry identified by the parties corroborates Dr. Israel's conclusions. The foodservice industry research firm Technomic collected 2014 sales data from the country's 43 largest broadliners. DX02016. Taken together, Technomic estimated total broadline sales to be $125 billion. Of that total, Sysco accounted for $35.7 billion and USF $23 billion, for a combined sum of $58.7 billion—nearly 47 percent of U.S. sales. *See id.*; *see also* PX09045-015 (PFG presentation to FTC stating that "[t]he two largest broadliners (Sysco and US Foods) accounted for 51% of all broadline sales in 2010," based on a study by Hale Group, "Focus on Foodservice Distribution," dated April 11, 2013); PX09045-014 (PFG presentation to FTC highlighting a 2011 Technomic study showing that Sysco and USF had a combined market share of 58 percent among the top 10 broadline food distributors).

Technomic's 47 percent combined market share estimate for *total broadline* sales is consistent with Dr. Israel's low-end, post-divestiture estimate of 59 percent for *national broadline* sales. The Technomic data did not segregate national and local broadline customers. However, because the largest customers buy disproportionately from Sysco and USF, it stands to reason that

the companies' combined market share for national customers would be greater than 47 percent, as Dr. Israel found. Even a combined market share of 47 percent (admittedly, a pre-divestiture number) can give rise to a presumption of harm. *See Phila. Nat'l Bank*, 374 U.S. at 364 ("Without attempting to specify the smallest market share which would still be considered to threaten undue concentration, we are clear that 30% presents that threat.").

3. The Court's Finding as to National Broadline Customer Market Shares

The court thus finds that the FTC has shown, through Dr. Israel's testimony and other evidence, that a merger of Sysco and USF will result in a significant increase in market concentration in the market for national broadline customers. The FTC therefore has established a rebuttable presumption that the merger will substantially lessen competition in the market for national broadline distribution.

B. Concentration in the Local Markets

1. Dr. Israel's Local Broadline Customer Market Shares Calculations

In addition to the market for national customers, the FTC also contends that the merged firm would create highly concentrated local markets for broadline foodservice distribution. To be precise, the FTC asserts that, in 32 different local markets, the merger between Sysco and USF would result in dramatic increases in HHIs, thereby substantially lessening the competition in those markets. Compl. ¶ 60, App. A. The FTC also maintains that the divestiture to PFG will not resolve Defendants' post-merger local market dominance.

As with the market for national customers, there is no industry study of local market shares. *See* PX09045-019 ("PFG is not aware of any systematic industry market share data."). The FTC again relied on Dr. Israel for those numbers. His starting point for calculating local share percentages was his 75 percent draw area methodology for defining the local geographic markets.

See PX09350-058. As already discussed, Dr. Israel first identified the 75 percent overlap area in each local market and then identified the competitors that could serve those customers by drawing a circle with a radius equal to the 75 percent draw distance around each overlap customer. Next, to calculate the overall local market shares, Dr. Israel calculated a customer-specific market share. That is, for each customer in the overlap area, he calculated the market shares for the competitors who were located within the customer's 75 percent draw distance radius. Dr. Israel then aggregated each of these customer-specific shares to the local level, using weighted averages across all overlap customers. The consequence of this methodology was that, the greater the competitor's distance from the center of the overlap area, the less weight that competitor would receive in the overall local market share calculations. Stated differently, because these distant competitors' market shares would only come into the calculation due to customers on the borders of the overlap area, those competitors' shares would be smaller than the shares of competitors whose distribution centers were closer to the middle of the overlap area—namely, Sysco and USF.

When calculating market shares, Dr. Israel used three different metrics: (i) square footage of distribution centers; (ii) local broadline sales; and (iii) number of sales representatives. Dr. Israel used the first and third variables as proxies for revenues and as a way to confirm the market share calculations that were based on the second variable, sales revenues. To calculate shares based on revenues, Dr. Israel used the Defendants' sales data for the numerator. For the denominator, he used the sales numbers, where available, for local broadliners. For those local competitors for whom he did not have actual sales data, he estimated the sales revenue based on the size of the distribution center. PX09350-134 at n.410. Based on those metrics, in local markets with the 20 highest increases in pre-divestiture HHIs, Defendants' combined market shares ranged

from 100 percent in San Diego, California, to over 65 percent in multiple markets. The HHI increases in each of top 20 markets were over 2,000 points. PX09350-135-137.

Dr. Israel also calculated post-divestiture market concentrations and HHI increases. According to the table below, in Memphis, Tennessee; Omaha, Nebraska; Sacramento, California; and Charleston, South Carolina, the post-divestiture combined markets shares remain above 80 percent with HHI increases in excess of 4,100, 1,400, 2,900, and 2,900 points, respectively. PX09350-213, Table 21. In seven other local markets, Dr. Israel calculated the post-divestiture combined market shares to be between 57 percent and 76 percent, with HHI increases in each case in excess of 1,500 points. *Id.*

Table 21

Examples of Areas with Large Change in HHI despite Divestitures

CBSA	Post-Merger Combined Share	Delta HHI
Omaha-Council Bluffs, NE-IA	90.3%	1,410
Sacramento--Roseville--Arden-Arcade, CA	88.6%	2,974
Durham-Chapel Hill, NC	75.4%	2,807
Charleston-North Charleston, SC	80.2%	2,947
Birmingham-Hoover, AL	57.5%	1,542
Jackson, MS	66.0%	2,155
Memphis, TN-MS-AR	93.8%	4,123
Columbia, SC	72.8%	2,315
Raleigh, NC	71.3%	2,188
Lynchburg, VA	63.3%	1,588
Rochester, NY	63.7%	1,574

2. *Defendants' Arguments*

Defendants attack Dr. Israel's local market share calculations in much the same way they did his national market share calculations—by contesting his methodology and inputs. Defendants assert that Dr. Israel's methodology was premised on the unreliable assumption that no competitor

would drive a greater distance than Sysco or USF currently does to provide broadline services. In other words, they criticize Dr. Israel's use of the same draw radius to identify the relevant local competition as he did to identify the overlap area. As a result, they argue, Dr. Israel's local market share calculations excluded sales from broadliners who travel greater distances and thereby overstated Defendants' combined market shares.

To demonstrate this point, Dr. Bresnahan presented an analysis of the Omaha, Nebraska market. He testified that, according to Dr. Israel's analysis, Defendants had combined sales in Omaha of $95 million and a combined market share of 90 percent. According to Dr. Bresnahan, Dr. Israel's methodology did not factor in at least $█ million in sales by another local distributor, Cash-Wa, whose distribution facility is 129 miles west of Omaha—farther out than the 91-mile 75 percent draw radius that Dr. Israel had used for the area. Dr. Bresnahan based his conclusion on sales data per zip code produced by Cash-Wa, which Dr. Israel had not considered in his analysis. According to Dr. Bresnahan, the zip code data showed that in 2013, Cash-Wa made sales to customers in zip codes within the 75 percent overlap area—at least $█ million worth—which Dr. Israel did not account for because of his driving distance assumption. Had these Cash-Wa sales been taken into account, Defendants' combined market shares and increase in HHIs would have been lower. As illustrated by his Omaha study, Dr. Bresnahan concluded that Dr. Israel's local market share methodology produced unreliable results.

Dr. Bresnahan's Omaha study convincingly demonstrated that Dr. Israel's 75 percent draw area methodology resulted in underreported competitor sales in the Omaha market. But what it did not show convincingly was by *how much*. Dr. Bresnahan's initial expert report stated that Cash-Wa's sales in the overlap area were over $█ million. DX01359-139. At the evidentiary hearing, however, he said that Cash-Wa's sales into that area were "at least $█ million," DX-

05029 at 42, and he did not explain why that number differed from his report.[25] More fundamentally, Dr. Bresnahan's reliance on zip code data had its limits. As Dr. Bresnahan conceded, the zip code data did not differentiate between local and national customers or broadline and systems customers. Hr'g Tr. 2186. Dr. Israel explained that he did not use the zip code data for that very reason, as well as the additional reason that he did not have zip code data for all local market competitors. In addition, Cash-Wa does substantial business selling tobacco products; however, the zip code data does not segregate those sales. *Id.* As a result, although the court agrees with Defendants that Dr. Israel's methodology excluded some local broadline sales in Omaha, the court cannot reliably determine the extent of the underestimation. And, notably, even if Dr. Bresnahan's $█ million figure consisted entirely of local broadline sales, Defendants would still have a high combined local market share of █ percent ($95 million/($█ million + $95 million) = █ percent).

Ultimately, the court finds that Dr. Israel's specific local market calculations is informative, but not conclusive evidence, of the merger's potential harm to local broadline customers. As the Omaha study showed, because Dr. Israel's 75 percent draw methodology excluded some competitor sales and because each local market has nuances that cannot be captured by his methodology, the court cannot rely conclusively on Dr. Israel's precise local share calculations as a measure of competitive harm.

The court, however, finds variations on Dr. Israel's 75 percent draw methodology to provide persuasive evidence of the merger's impact on local markets. Dr. Israel did more than

[25] The court infers that the sales figure was reduced, in part, to estimate only Cash-Wa's *broadline* sales, as opposed to all sales. But that reason, if correct, was not made clear on the record. Additionally, in his report, Dr. Bresnahan reported over $█ million in sales by another broadliner, Reinhart. However, he made no mention of Reinhart's sales in his testimony. That may be because Reinhart reported that █████████████████████ ███████. PX09034-019.

calculate local share percentages based on 75 percent draw areas. He also used a 90 percent draw area and a weighted 95 percent draw area. Those increased draw areas captured some of the competitor sales that the 75 percent draw area excluded.[26] Dr. Israel then aggregated the local market share figures across all overlap customers in all markets, using distribution center square footage, adjusted revenues, and number of sales representatives to estimate market share. PX09350-137-139. As shown in the table below,[27] these alternative approaches—designated as variations (i) and (ii)—demonstrate that for half of the customers in overlap areas, Defendants would have a post-merger combined local market share of more than 50 percent and the HHI would increase at least 1,300 points. PX09350-139, Table 7. A quarter of the overlap customers would face even greater market concentrations: Defendants post-merger would have at least 68 percent in combined local market share and the HHI would increase by at least 2,000 points. And, 10 percent of the overlap customers would face a combined market share north of 74 percent and an HHI increase of greater than 2,500 points. The picture that clearly emerges from these numbers is that, in many areas across the country, USF and Sysco already control a substantial share of the market for local broadline distribution. A merger between the two would lead to a significant increase in market concentration in many areas.

[26] In a third variant, Dr. Israel went beyond the overlap areas and performed market calculations that took into account all local broadline customers, regardless of whether they fell into the overlap area. Dr. Israel also used a fourth variant—though not entirely clear from his report—in which he appears to have re-run his 75 percent draw methodology using all of Defendants' broadline customers in the overlap area, not just local broadline customers. PX09350-137-138.

[27] These figures are pre-divestiture share calculations. But the local market share percentages and HHI increases are so high that, even taking into account the divestiture, when aggregated across numerous markets, these figures are unlikely to decrease enough to change the overall picture. *See* PX09375-103-104.

Table 7

Summary Statistics for Local Market Shares under Alternative Methodologies

	Combined Share			Δ HHI		
	Median	75th Pctile	90th Pctile	Median	75th Pctile	90th Pctile
Square footage shares						
Baseline	59.8%	71.8%	81.5%	1.763	2.375	3.169
(i) 90% distribution distance	58.3%	68.3%	75.3%	1.557	2.149	2,621
(ii) Continuous distribution distance	55.7%	68.3%	82.6%	1.369	2.013	2.765
(iii) All local CBSA customers	58.9%	70.4%	80.8%	1,603	2,364	3.081
(iv) All overlap CBSA customers*	60.9%	70.6%	78.3%	1,851	2,420	2,775
Adjusted revenue shares**						
Baseline	62.6%	74.7%	86.0%	1.574	2,778	3.094
(i) 90% distribution distance	57.2%	71.6%	79.2%	1.471	2.342	2,886
(ii) Continuous distribution distance	54.6%	70.6%	83.3%	1.208	1,849	3,000
(iii) All local CBSA customers	59.8%	74.6%	85 7%	1.327	2.614	2.974
(iv) All overlap CBSA customers*	66.7%	80.2%	86.1%	1,962	2,886	3.598
Sales representative shares						
Baseline	62.5%	70.8%	80.8%	1,854	2.406	3.152
(i) 90% distribution distance	58.0%	68.0%	74.8%	1,594	2,217	2,531
(ii) Continuous distribution distance	52.7%	70.5%	86.5%	1.345	2,039	2.655
(iii) All local CBSA customers	61.1%	70.4%	80.3%	1.595	2.308	3,099
(iv) All overlap CBSA customers*	61.6%	69.8%	79.4%	1.777	2.306	2,749

* Includes all customers.
**For variation (iv), unadjusted revenues are used.

Defendants' combined strength in local markets is corroborated by documents compiled during the Defendants' ordinary course of business. For example, in an Investor Presentation, dated November 2012, USF represented that it "estimated [having the] #1 or #2 position in [redacted] of served markets." PX03000-014. Mr. Schreibman's investigational hearing testimony confirmed the present-day accuracy of that statement. Investigat'l Hr'g Tr., PX00515-017 at 65. He also confirmed that, in many of those markets, Sysco occupied the number one or two market position. *Id.*

Another USF document, a strategy document created in 2011, shows USF and Sysco with sizeable "market penetrations" in many local markets. PX03073-023-030. Mr. Schreibman testified that "market penetration" was different from "market share," as the former reflected the percentage of customers that purchased even $1 of product, whereas the latter reflected

percentages of overall sales volumes. Hr'g Tr. 1508-09. But even if "market penetration" and "market share" have different definitions, both concepts are a measure of market strength, and the "market penetration" percentages show USF and Sysco to be first and second in numerous markets. Indeed, the very same strategy document lists 54 separate markets and identifies Sysco as a competitor in each of them. Of those 54 markets, USF estimated that Sysco had the number one position in █ markets and that, within those █ markets, USF was number two in █. USF also estimated that it was number one in █ markets, with Sysco ranked number two in those same █ markets. And, in █ markets, USF viewed itself as tied for number one with Sysco. Thus, of the █ local markets, USF viewed Sysco or USF as the leading broadliner in █ and as the number two broadliner (or tied for first) in █. This internal assessment clearly supports Dr. Israel's local market share calculations.

Defendants offer a different ordinary course document to rebut Dr. Israel's market share calculations. In 2013, relying on a sizeable third-party sales database of 335,000 independent restaurants, USF calculated its share of sales to independent restaurants in 53 local markets. That study showed USF with market shares much lower than that shown by Dr. Israel's calculations, ranging from a high of █ percent in Columbia, South Carolina, to a low of █ percent in the "Northwest." DX-00397-002.

But Defendants' reliance on the independent restaurant study as an indicator of local market shares is problematic for several reasons. First, there is no evidence that the underlying database differentiated between purchases from broadline distributors and purchases from other channels of distribution. The evidence has shown that, among foodservice customers, independent restaurants are among the most likely to buy from other channels, such as specialty and cash-and-carry. In other words, unless broadline sales are segregated from the rest—which the restaurant

study appears not to have done—the resulting market share estimate will underestimate USF's actual share of only broadline purchases. A market share calculation that uses at its numerator purchases from *all channels* cannot be relied upon to determine USF's *broadline* market shares.

Second, no evidence was presented showing that the buying habits of independent restaurants is representative of other local broadline customers. Thus, by focusing only on independent restaurant purchasing, the data set does not provide an accurate picture of local market shares.

Third, the independent restaurant study's results conflict with other documents. For instance, USF's 2011 strategy document describes the company as having a "[s]olid #█" position in "Reno/Sacramento," PX03073-019, but the restaurant study finds a less than 10 percent share in Reno, DX-00397-002. Similarly, the strategy document describes USF as having the "#█ position" in St. Louis, PX03073-018, but the restaurant study reported only a 13.3 percent share in the "Missouri Group," DX-00397-002.

Finally, Dr. Israel's conclusions are corroborated by PFG's analysis of the local markets. In January 2014, PFG made a presentation to the FTC in which it addressed the state of competition in various local markets. PFG, at the time, was represented by antitrust counsel, Kirkland & Ellis. Because there was no comprehensive industry data for local market shares, PFG "estimated local broadline market shares based upon [distribution center] square footage, which PFG uses to gauge competitor strength in the ordinary course of business"—one of the very methods that Dr. Israel used for calculating market shares. PX09045-019. PFG observed that, "[w]hile not perfect, we believe this approach produces *directionally correct results* and can be useful in flagging areas that merit closer consideration." *Id.* (emphasis added). PFG's analysis showed that in six major markets—New York, Philadelphia, Detroit, Denver, Las Vegas, and Los Angeles—a combined

Sysco-USF, based on distribution center square footage, would control between 45 percent (New York City) to 80 percent (Las Vegas) of those local broadline markets. PX09045-020. PFG also calculated that a merger in those markets would result in HHI increases ranging from 1,000 points (New York City) to 3,100 points (Las Vegas). *Id.* Consistent with Dr. Israel's market shares and HHI calculations, PFG concluded that the "[p]reliminary findings indicate significant concentration in many local markets." *Id.*

3. *The Court's Finding as to Local Broadline Customer Market Shares*

The court thus finds, based on Dr. Israel's testimony and other evidence, that the FTC has shown that a merged Sysco-USF will significantly increase concentrations in local markets for broadline distribution. The FTC therefore has made its *prima facie* case and established a rebuttable presumption that the merger will lessen competition in the local markets.

C. Additional Evidence of Competitive Harm

The FTC did not rely solely on increased HHIs to establish that Defendants' proposed merger would cause competitive harm. *See Baker Hughes*, 908 F.2d at 992 ("The Herfindahl-Hirschman Index cannot guarantee litigation victories."). It offered additional evidence to strengthen its *prima facie* case, to which the court now turns.

1. *Unilateral Effects—National Customer Market*

The FTC advanced a "unilateral effects" theory to argue that the merger would harm competition in both the national and local broadline distribution markets. In this section, the court considers the evidence of unilateral effects in the national customer market and subsequently turns to the evidence regarding local customer markets.

Courts have recognized that a merger that eliminates head-to-head competition between close competitors can result in a substantial lessening of competition. *See Heinz*, 246 F.3d at 717-

19 (holding that elimination of competition between second- and third-largest jarred baby food manufacturers would weaken competition); *Swedish Match*, 131 F. Supp. 2d at 169 (finding a likelihood of unilateral price increase where merger would eliminate one of Swedish Match's "primary direct competitors"); *Staples*, 970 F. Supp. at 1083 (finding anticompetitive effects where the "merger would eliminate significant head-to-head competition between the two lowest cost and lowest priced firms in the . . . market."); *see also* Merger Guidelines § 6 ("The elimination of competition between two firms that results from their merger may alone constitute a substantial lessening of competition."). In such circumstances, a merger "is likely to have unilateral anticompetitive effect if the acquiring firm will have the incentive to raise prices or reduce quality after the acquisition, independent of competitive responses from other firms." *H&R Block*, 833 F. Supp. 2d at 81.

Unilateral anticompetitive effects can arise in a host of different settings. *See generally* Merger Guidelines § 6. Here, the FTC's case for unilateral effects rests on the fact that the broadline distribution industry is marked by negotiations between buyers and sellers. In such a market, "buyers commonly negotiate with more than one seller, and may play sellers off against one another." *Id.* § 6.2. If two competitors merge, buyers will be prevented from playing the sellers off one another in negotiations. *See id.* This elimination of competition "can significantly enhance the ability and incentive of the merged entity to obtain a result more favorable to it, and less favorable to the buyer, than the merging firms would have offered separately absent the merger." *Id.*

On the other hand, even if the merging parties had large market shares, if they were not particularly close competitors, then the market shares might overstate the extent to which the merger would harm competition. Although the merging parties need not be the top two firms to

cause unilateral effects, *see, e.g.*, *Heinz*, 246 F.3d at 717-19; *H&R Block*, 833 F. Supp. 2d at 83-84, the FTC argues that the potential for unilateral effects here is magnified because Defendants are particularly close competitors and many national customers consider them the top two choices for broadline distribution. *See* Merger Guidelines § 6.2 ("Anticompetitive unilateral effects . . . are likely in proportion to the frequency or probability with which, prior to the merger, one of the merging sellers had been the runner-up when the other won the business.").

The FTC offered various sources of evidence to show that the proposed merger will result in unilateral anticompetitive effects. The evidence includes empirical data collected and analyzed by Dr. Israel, Defendants' ordinary course documents, and testimonial evidence from other market actors.

a. Dr. Israel's RFP/bidding study

To show that Defendants were frequent head-to-head competitors—indeed, each other's closest rivals—Dr. Israel analyzed each company's bidding opportunities for national customers based on the RFP/bidding database that he compiled from the companies' records. The RFP/bidding records that Dr. Israel collected spanned a seven-year period, from 2007 to 2014. PX09375-088. He formed the database not only from the parties' reconstructed RFP data, but also from a host of ordinary course records reflecting bidding opportunities, PX09375-089-091. From this evidence, Dr. Israel concluded: "[I]n competitions for National Broadline Customer business, both USF and Sysco compete with and lose to one another much more than they compete with or lose to any other distributor and, indeed, more than all other distributors combined." PX09375-088. More specifically, based on Sysco's RFP/bidding records, Dr. Israel observed that USF appeared as a competitor for national broadline business twice as often as the next competitor and that, when Sysco lost, it lost to USF two and a half times more often than it lost to the next

competitor. Similarly, based on USF's RFP/bidding records, Dr. Israel observed that Sysco appeared as a competitor for national broadline business four times as often as the next competitor and that, when USF lost, it lost to Sysco three and a half times more often than it lost to the next competitor. PX09350-105-109.

Defendants disputed the reliability of Dr. Israel's RFP/bidding data study in two primary ways. First, as already discussed, they forcefully challenged the underlying data set, arguing that neither company keeps ordinary course RFP and bidding records and that Dr. Israel's reliance on these artificially created data sets to calculate an empirical "win-loss" analysis is inherently flawed. As previously explained, the court has found that drawing precise conclusions based on the RFP/bidding data is problematic because of the data's limitations.

Second, to demonstrate that the merger would not create unilateral anticompetitive effects, Defendants offered a "switching study" conducted by Dr. Bresnahan. A switching study, as the name implies, analyzes customers' decision to "switch" their business to other competitors. For his study, Dr. Bresnahan acquired from a company called Aggdata the location information of tens of thousands of restaurant and hotel chain customers that are on either Sysco's or USF's "national customer" roster. He then analyzed Defendants' transaction records by quarter from the first quarter of 2011 to the third quarter of 2013 to determine if either company provided broadline distribution to a specific restaurant or hotel location. If either Defendant provided broadline distribution, he tracked the company's sales to the location and noted if it lost sales to the location during the period. If the company lost sales in a particular quarter, he checked the other defendant company's transaction records to see if it picked up the customer. If it did not, Dr. Bresnahan assumed that some other competitor did.

So, for example, if USF's records showed that a particular Sonic franchise did not purchase from USF in a particular quarter, he would turn to Sysco's records to see if Sysco had picked up the customer; if it did, he counted it as a switch to Sysco; if not, he assumed that the customer purchased from another distributor and counted it as a switch to a competitor other than Sysco. Based on this analysis, Dr. Bresnahan concluded that Sysco and USF are not uniquely close competitors. He found that USF lost business to Sysco 15 percent of the time based on both revenue and number of locations, and that Sysco lost business to USF 57 percent of the time based on revenue and 39 percent of the time based on number of locations. These percentages of switches, Dr. Bresnahan testified, were much lower than what one would have expected to see if Dr. Israel's national market shares were accurate.

For a variety of reasons, the court cannot agree with Dr. Bresnahan's ultimate conclusion—that USF and Sysco are not uniquely close competitors—based on his switching study. First, though the number of observations in Dr. Bresnahan's study were significant, they were limited almost exclusively to restaurant and hotel locations (including, it appears, restaurants served by Sysco's systems division, SYGMA).[28] The observations did not include other types of large national customers, such as GPOs, foodservice management companies, and large government agencies, which, as the evidence showed, spend large percentages of their foodservice distribution budget on Defendants. As Dr. Bresnahan admitted, he does not claim that his switching analysis reflects the buying habits of these national customers. Hr'g Tr. 2180-82.

Second, the time period of Dr. Bresnahan's study—two-and-a-half years—is shorter than the seven-year time period covered by Dr. Israel's RFP/bidding analysis. Significant switches that

[28] The study did include one health care organization, Kaiser Permanente, and one GPO, Amerinet.

might have occurred between Defendants outside the two-and-a-half year period, therefore, were not counted.

Third, the switching analysis does not capture the full extent of competition between Defendants (or between other competitors, for that matter), because it only tracks switches, not instances where a customer might have played one broadliner off the other to get better pricing. That kind of situation reflects actual competition at least as much as a switch, but such competition is not reflected in the data.

Fourth, unlike an RFP or bid situation, a switch does not necessarily equate to actual competition. A switch might have occurred for any number of reasons having nothing to do with pricing or service (*e.g.*, the customer's sister-in-law went to work for a competitor), but the study treats every switch as a loss for competitive reasons.

Fifth, Dr. Israel's rebuttal report pointed out a number of limitations in Dr. Bresnahan's switching analysis, including the exclusion of certain switches between Defendants and the treatment of actual switches, such as timed phase outs from one Defendant to the other, as non-switches. PX09375-081-084. Although Dr. Bresnahan testified that he corrected for these criticisms and that the adjustments did not materially alter his results or conclusion, the need for those adjustments reflects the limitations of drawing firm conclusions from such undifferentiated data.

Finally, Dr. Bresnahan's conclusion that USF and Sysco are not close competitors brings him into conflict with Defendants' other expert, Dr. Hausman. Dr. Bresnahan testified that, although he agrees that Sysco and USF are competitors, he did not think that one was a "particularly strong price constraint" on the other. Hr'g Tr. 2183. Dr. Hausman, on the other hand, unequivocally agreed that "USF is a strong price constraint on Sysco." *Id.* at 2005. He

testified Sysco and USF "compete and they compete hard. I'd be the first to agree." *Id.* at 1986; *see id.* at 2037 ("I am not arguing with you that—or disagreeing with you that Sysco and US Foods are important competitive constraints on each other."). Defendants do not explain how Dr. Bresnahan's switching study can be reconciled with Dr. Hausman's unqualified opinion that Defendants mutually constrain each other's prices, which can only mean that they are close competitors; if they were not, the pricing of one would not matter to the other.

In the end, the court finds that Dr. Israel's RFP/bidding analysis is more persuasive than Dr. Bresnahan's switching study. Both empirical studies are imperfect for the reasons already discussed. But Dr. Israel's analysis better captures instances of actual competition across a more representative cross-section of national customers over a longer period of time. Additionally, Dr. Israel's conclusions are corroborated by other evidence in the record, which, as discussed below, indicate that Sysco and USF are close competitors, particularly for large national customers.

b. The parties' ordinary course documents

The FTC presented ordinary course documents, from both Defendants and third parties, which support Dr. Israel's conclusion that Sysco and USF are particularly close competitors. For example, a 2012 USF presentation, titled "Strategy Refresh," explains that one reason for strategic rethinking is that "[c]ustomers perceive little difference between us and *our main competitor*," identified as Sysco. PX03031-003 (emphasis added). The same presentation devotes a section to "Performance v. Sysco" and describes the companies as "[i]ndustry leaders." PX03031-010-011. Another USF document describes Sysco as USF's "major rival." PX03032-043.

Similarly, a Sysco presentation to its Board of Directors describes USF as its "next largest competitor" and puts forth "recent intelligence" about USF and two other competitors. PX01007-

018; PX01007-023. Another Sysco strategy document focusing on the healthcare sector states that "US Foodservice is our strongest competitor for Healthcare GPO dollars." PX01388-004. In addition, there are many specific instances in the record demonstrating fierce competition between Sysco and USF for national customer accounts.[29] These documents indicate that Sysco and USF compete aggressively against one another on price; non-price incentives, such as signing bonuses; service; and other value-added offerings.

Industry analysts also have recognized the close competition between Defendants. For instance, the Cleveland Research Group's January 2014 market report on Sysco noted the Cleveland Research Group's assessment that "both Sysco and US Foods have priced each other down competing for larger national/regional contract accounts over the last several years" and that "the acquisition removes a key price competitor (particularly with larger contract accounts)." PX09332-004.

c. Testimonial evidence

A number of industry actors testified that they view Sysco and USF to be close competitors for national customers. Particularly compelling testimony came from Mark Allen, the head of the foodservice distributors' trade group, IFDA. In his deposition, Mr. Allen agreed that Sysco and USF were "closest competitors" for national accounts, such as GPOs, hospitality, and foodservice management companies. PX00570-012; PX00570-014. He further described Sysco and USF as "powerful competitors" for independent customers, PX00570-113, and testified that, in his experience, GPOs, foodservice management companies, and hospitality chains use Sysco and USF to keep each other honest on price and service, PX00570-019. The testimony of the PFG's President and CEO, George Holm, was to the same effect. He testified that in his experience

[29] *See, e.g.*, PX01066-001-002; PX03064-001; PX01061-001-006.

"foodservice management companies, GPOs[,] and certain restaurant groups" have "obtained lower prices by bidding Sysco and US Foods against each other." Hr'g Tr. 651.

d. Conclusion on unilateral effects in the national customer market

The court's finding that Sysco and USF are close competitors in the national customer market is no surprise, given the uncontested facts of this case. Sysco and USF are the country's two largest broadliners by any measure. They have far more distribution centers, SKUs, private label products, sales representatives, and delivery trucks than any other broadline distributor. That they rely on these competitive advantages to compete, and compete aggressively against one another in the market for national customers, is amply born out on this record.

Based on all of the evidence presented, the court finds that, because the proposed merger would eliminate head-to-head competition between the number one and number two competitors in the market for national customers, the merger is likely to lead to unilateral anticompetitive effects in that market. Evidence of probable unilateral effects strengthens the FTC's *prima facie* case that the merger will lessen competition in the national customer market. *See Heinz*, 246 F.3d at 717 (footnote omitted) (finding that "the FTC's market concentration statistics are bolstered by the indisputable fact that the merger will eliminate competition between the two merging parties"); *Whole Foods*, 548 F.3d at 1043 (Tatel, J.) (citation omitted) (internal quotation marks omitted) (stating that "there can be little doubt that the acquisition of the second largest firm in the market by the largest firm in the market will tend to harm competition in that market").

2. Merger Simulation Model—National Customer Market

To further show that the merger would harm national customers, Dr. Israel ran a merger simulation model to predict the merger's effect. Dr. Israel used an "auction model" to estimate the harm to national customers based on his real-world observation that national customers used RFP

processes that "typically involve[d] competitive bids and bilateral negotiations between distributors and foodservice operators" to award business. PX09350-110. Under an auction model, the terms offered by the winning bidder are determined (or at least heavily influenced) by the second-best bidder, because the winning bidder will offer price and service terms that are just good enough to win the business. In theory, if the top two bidders merge, price and service terms will be determined (or at least heavily influenced) by the previously third-best bidder, who in a post-merger world would move into the number two spot. An auction model predicts harm to customers if, as here, the top two bidders merge and the next best bidder is a distant third. The magnitude of the harm is defined as the difference between the values offered by the companies that had been the pre-merger second- and third-place bidders. PX09350-113-114; *see CCC Holdings*, 605 F. Supp. 2d at 69 (describing a similar auction model for predicting a price increase).

Practically speaking, the premise of Dr. Israel's auction model was that, in the pre-merger world, Sysco and USF are national customers' top two choices and, therefore, each company sets the other company's price. But, if they were to merge, the winning bidder's price would only be subject to competitive pressure by a pre-merger third-place bidder, such as PFG or some other distant competitor. If the next best bidder is not a major competitor, and therefore does not play a significant role in affecting prices, national customers will be harmed. An email dated December 12, 2013, summarizing a "USF Senior Teams" webcast addressing the proposed merger, perfectly captures this core premise of Dr. Israel's model. The email identified as one of the "key messages": "The 'distance' between the combined company and the next set of regional players *is huge*. Those regional players will have an even harder time trying to play catch up going forward because they simply won't have the resources that the combined company has to transform the industry."

PX00103-002 (emphasis added). The "huge" distance between the merged entity and the rest of the field corresponds to the merger harm that Dr. Israel's model predicts.

To quantify the likely harm to national customers, Dr. Israel performed calculations that used as inputs, among others, his estimates of the parties' national customer market shares and their price-cost margins. PX09350-118. He concluded that, absent significant efficiencies and other mitigating factors, the merger would harm national customers on the order of more than $1.4 billion annually. PX09350-120; PX09350-220. Factoring in the divestiture to PFG and its increased market share, Dr. Israel calculated likely merger harm of more than $900 million annually. PX09350-189; PX09350-237.

Defendants assert that Dr. Israel's model is flawed for the same reason that they criticize his national market share calculations—both rely on the unreliable RFP/bidding data. Specifically, Defendants argue that, because the merger simulation model relies on the national market share calculations as a critical input, and because those market shares depend on the unreliable RFP/bidding data, Dr. Israel's estimate of likely merger harm is likewise unreliable. As discussed, the court agrees that the RFP/bidding data set is imperfect and its resulting market share calculations are imprecise to some degree. Dr. Israel's most conservative market share analysis, however, did not rely on the RFP/bidding data but rather on the CID data, and provided a reasonable approximation of the parties' share of the national customer market. Dr. Israel ran his merger simulation using that lower-bound market share estimate and still reached the conclusion that, absent significant efficiencies, the merger would likely cause significant harm. PX09350-121 n.363 ("Finally, I tested the robustness of my results to Sysco and USF having lower combined shares. I found that even when I use the lowest (and almost certainly too low) Sysco and USF shares presented in **Table 1**, the required efficiencies predicted by the model still far outweigh the

efficiencies claimed by the parties."). The court, therefore, concludes that Dr. Israel's merger simulation model strengthens the FTC's *prima facie* case that the merger will substantially lessen competition in the market for national customers.

3. *Unilateral Effects—Local Markets*

As it did for the national customer market, the FTC presented empirical, documentary, and testimonial evidence to demonstrate the potential for unilateral effects to harm local markets. That evidence, however, presented a more muddled picture of the potential for unilateral effects than did the evidence for the national customer market.

a. Dr. Israel's empirical analysis

As he did with the national customer market, Dr. Israel looked at Defendants' business records to determine how closely they compete in local markets. The data came from two sources—USF's Linc database and Sysco's request for incentives (RFI) records. The Linc database, as discussed earlier, is a customer relations management tool used by USF sales personnel to manage and store information on existing and prospective customer accounts. RFIs are internal Sysco records that sales personnel were required to submit to regional presidents to obtain approval to offer incentives to customers to either switch to Sysco or stay with the company.

Starting with the Linc database, Dr. Israel observed and analyzed nearly 100,000 business opportunities between January 2011 and June 2014 and divided them into two groups—USF wins and USF losses. When USF won the business, sales personnel identified Sysco as the main competitor 43 percent of the time (and 48 percent of the time measured by revenue); when USF lost the business, USF sales personnel identified Sysco as the main competitor 46 percent of the time (and 68 percent of the time measured by revenue). PX09350-143, Table 11. Whether USF won or lost, sales personnel identified Sysco as the main competitor eight times more frequently

than the next most mentioned competitors (PFG and Gordon Food Service). Dr. Israel also segregated the Linc database's mentions of competitors in 20 local markets. That study showed that sales personnel in every market identified Sysco as USF's main competitor by a wide margin, especially when measured by revenues. PX09350-145, Table 14.

The RFI data painted a similar picture from the Sysco perspective. Dr. Israel reviewed 224 Sysco RFIs, covering a three-year period from 2011 to 2014, when Sysco discontinued the practice. In more than 66 percent of the RFIs, Sysco sales personnel identified USF as the reason for the incentive request. No other competitor appeared more than 10 percent of the time. PX09350-146-147.

Defendants attacked Dr. Israel's reliance on the Linc database, as they did when he used it in his aggregate diversion analysis. They asserted that Dr. Israel improperly relied on the Linc database as a win-loss record, when it was never intended as such. USF's Executive Vice President of Strategy, David Schreibman, testified that sales people did not use the database consistently and would sometimes enter competitor information simply to fill in the database; ultimately, USF did not rely on it to identify market competition. Hr'g Tr. 1505-06. Defendants also presented a local switching study performed by Dr. Bresnahan, which used the same switching methodology as described above but applied to local customers. According to Dr. Bresnahan, when local customers switch away from Sysco, they switch to USF only 11 percent of the time; and when they switch away from USF, they switch to Sysco only 15 percent of the time. Hr'g Tr. 2163. In other words, according to Dr. Bresnahan's switching analysis, when local customers switched away from Sysco it was typically to distributors other than USF.[30]

[30] Dr. Bresnahan also did another switching study to support his findings. He conducted a study of fresh chicken purchases by customers in San Diego, from which he concluded that customers "turn off and on buying fresh chicken from Sysco" and that most of the time when they "turn off" Sysco they buy from someone other than USF. Hr'g Tr. 2162.

The court finds that the empirical evidence, on balance, shows that Sysco and USF are close competitors for local customers. As the court has already observed, relying on the Linc database to draw firm conclusions is problematic for the reasons raised by Defendants. That said, even recognizing the data's limitations, it so overwhelmingly demonstrated primary competition between Sysco and USF based on a sizeable number of observations (nearly 100,000 entries) that it cannot be wholly disregarded as evidence of close competition. Furthermore, the court found the RFI analysis especially compelling; indeed, Defendants did little to contest it. Although the number of observations was low, the RFI data overwhelmingly showed Sysco seeking incentives to attract or keep local customers in response to USF's efforts far more often than Sysco attempted to respond to any other competitor's efforts.

Dr. Bresnahan's switching study provided some counterweight to Dr. Israel's work. Like his national switching analysis, however, it did not account for competition when customers used Sysco and USF as leverage against each other, as many local customers said regularly occurred. The local switching study also relied heavily on chain restaurants and hotels and thus did not factor in the buying habits of other types of local customers, particularly independent restaurants. Therefore, notwithstanding the limits of the data sets relied on by Dr. Israel, the court finds that the empirical evidence supports the conclusion that Sysco and USF are close competitors in local markets.

b. The parties' ordinary course documents

Two notable ordinary course documents also support the conclusion that Sysco and USF are close competitors for local customers. The first is USF's November 2012 "Investor Presentation," which represented that "US Foods is estimated #1 or #2 position in █ of served markets." PX03000-014; *see also* PX03118-006. As previously noted, USF's David Schreibman

confirmed both the present-day accuracy of that statement and the fact that, in many of those markets, Sysco occupied the number one or two position. DX-00272 at 62, 65. The second is the July 2011 USF acquisitions strategy document, which estimated USF's position in 54 separate markets, apparently based on market penetration rather than market share. USF estimated that either Sysco or USF was the leading broadliner in █ of those markets and was the number two broadliner (or tied for first) in █. *See also* PX03002-009 (Clayton, Dubilier & Rice document, titled "Operating Review," acknowledging that one of Sysco's strengths is "[g]eographic coverage in all the key markets in the U.S. - #1 or #2 in virtually all the markets in which they operate"); PX03004-001 (Clayton, Dublier & Rice memo stating that USF is a "leader in both national and local markets" and that "Sysco [is the] closest competitor with similar business mix"). Sysco's and USF's leading positions in multiple local markets shows that they are close competitors in those markets.

c. Testimonial evidence

The testimonial evidence was more equivocal about the closeness of competition between Defendants. It demonstrated that Sysco and USF are strong competitors for local customers in several markets, but it also showed that other broadliners are competing effectively in many of those areas. The FTC's case featured four local markets: (i) Columbia/Charleston, South Carolina; (ii) Omaha, Nebraska; (iii) Raleigh/Durham, North Carolina; and (iv) Southwest Virginia. For each of those markets, the FTC presented testimonial evidence supporting Defendants' leading market positions. For instance, PFG's George Holm agreed that Sysco and USF were the largest and two most "competitively significant" broadline distributors in Columbia/Charleston, Raleigh/Durham, and Southwest Virginia. Hr'g Tr. 653-57; DX-00276 at 70-72. Mark Allen, IFDA President, agreed with those assessments, calling Defendants the

"dominant" or "strongest" competitors in those three markets (and Las Vegas). DX-00294 at 170; *see also* Hr'g Tr. 1800 (testimony from Sysco Mid-Atlantic President Mike Brawner stating that USF is a "strong competitor" in Columbia, Raleigh/Durham). USF's ordinary course materials corroborate those observations, at least in terms of market penetration. PX03118-007-008 (showing USF as a "Strong #█," based on market penetration, in Raleigh, Columbia, and Roanoke, with Sysco as number two in those areas, and showing Sysco as the number one broadliner in Omaha with USF a "Distant #█").

Yet, when customer-level testimony is considered, the evidence of Defendants' leading market positions and their post-merger ability to increase prices becomes less clear. Both sides deposed and obtained numerous declarations from various customers in these local markets. The customer testimony obtained by the FTC invariably decried the merger's impact on local markets, whereas Defendants' customer witnesses emphasized alternatives in the marketplace and the ability to switch broadliners if the merged company attempted to impose a price increase.[31]

[31] *Compare* PX07020-002 (Champ McGee, owner of Little Pigs Barbeque and FTC-sponsored declarant expressing "serious concerns" about merger's effect on business in the Columbia market), *and* Hr'g Tr. 344 (FTC witness, Gary Hoffman, Vice President and Corporate Executive Chef of Upstream Brewing Company from the Omaha market, expressing concern that the proposed merger would prevent him from playing Defendants off one another), *and* PX00487-005 (FTC-sponsored declarant Jason Smith of 18 Restaurant Group, from the Raleigh/Durham market, expressing concerning about the merger "because it eliminates one of our only two options for broadline distribution services" and rejects other competitors), *and* Hr'g Tr. 544-45 (FTC witness, Daniel Schablein, Controller at Wintergreen Resort from the southwestern Virginia market, stating that Sysco and USF were the only legitimate broadliners for his business), ***with*** DX-00227 at 2 (Justin Brooks, owner of Frayed Knot Restaurant and Defendants-sponsored declarant, stating "I do not believe that Sysco could raise prices or reduce services on my business" in the Columbia market because of competition from PFG, Merchants, Reinhart, and Gordon Food Service), *and* DX-00191 at 2 (Defendants-sponsored declarant Anthony Fucinaro of Anthony's Steakhouse, from the Omaha market, stating, "If Sysco were to raise prices or lower service levels, I would move my contract to Reinhart, Martin Brothers, and/or Cash-Wa"), *and* DX-00232 at 2 (Defendants-sponsored declarant Patrick Cowden of Tobacco Road Sports Cafe, from the Raleigh/Durham market stating, "If Sysco tried to raise prices or decrease service quality following the merger, I could and would replace them with any of the other bidders in a heartbeat"), *and* DX-00209 at 1 (Defendants-sponsored declaration from George Huger of Southern Inn Restaurant, from the southwestern Virginia market, stating that he would have alternatives, including PFG and Staunton Foods, if he became dissatisfied with Sysco's prices or service after the merger).

Because of these conflicting local market assessments, the court cannot draw firm conclusions about the competitiveness of the local broadline markets from the testimonial evidence.[32]

d. Conclusion on unilateral effects in the local markets

In the final analysis, after considering all of the record evidence on local markets, the court finds that the FTC has shown that unilateral effects are likely to occur in many local markets because the merger will eliminate one of the top competitors in those markets. Though the court finds the evidence of unilateral effects in the local markets to be less convincing than in the national customer market, the evidence nevertheless strengthens the FTC's *prima facie* case of merger harm.

4. Local Event Studies

To further show that the merger would adversely impact local customers, the FTC presented the results of an econometric event study conducted by Dr. Israel. Dr. Israel analyzed Sysco's opening of two distribution centers—one in Long Island, New York, in July 2012, and one in Riverside, California, in June 2013—to determine the impact those openings had on prices paid by USF customers served from a nearby competing facility. Known as an "entry study," Dr. Israel selected the Long Island and Riverside events because they were the only two recent instances in which Sysco had opened a new distribution center in the same market as a USF distribution center. From these event studies, the FTC hoped to show that prices fell when Sysco and USF directly competed and that the merger's elimination of USF as a competitor would have an upward effect on pricing.

[32] The FTC did not present testimony or customer declarations about many of the markets that it claims will be highly concentrated after the merger. That is not, however, fatal to its case. *See Brown Shoe*, 370 U.S. at 339, 341 (rejecting the argument that the government had not proven its case because it did not present evidence "in each line of commerce and each section of the country" and stating that "[t]here is no reason to protract already complex antitrust litigation by detailed analyses of peripheral economic facts, if the basic issues of the case may be determined through study of a fair sample").

Dr. Israel found that Sysco's entry in Long Island resulted in a 1.4 percent decline in USF's prices for customers in the 75 percent overlap area. PX09350-148. He also ran variations of his regression analysis on other groupings—customers within a 50 percent overlap area, customers purchasing more than 100 SKUs, and customers buying private label products—and found that the price decrease on these groupings was even greater. PX09350-148. By contrast, Dr. Israel found a less significant price impact in the Riverside entry study—a negligible price decline of only .06 percent.

Dr. Israel explained that neither of these events were clean entry studies because, in both cases, Sysco already had an existing distribution facility in the area, and thus already was competing against USF. In his opinion, the resulting price effects, therefore, were actually understated. Dr. Israel also found the results of the Long Island event more compelling than the Riverside event for two reasons. First, the Long Island facility was a greater distance away from Sysco's existing facility than the new Riverside facility was from its existing facility. Second, the Long Island facility served more new business than the Riverside facility. For those reasons, he concluded, the Long Island study better approximated a true entry event. Hr'g Tr. 1097-98. Dr. Israel ultimately concluded, based largely on the Long Island study, that the merger's elimination of USF as a competitor would have an upward pricing effect in local markets.

The court does not find Dr. Israel's entry studies to be convincing evidence that the merger will harm local customers. Dr. Israel's efforts to distinguish the Long Island and Riverside events simply do not hold up. Defendants' expert, Dr. Bresnahan, showed that the difference in distance between the Riverside facility and its nearby existing facility, on the one hand, and the Long Island facility and its nearby existing facility, on the other, was a mere 14 miles. He also showed that both new Sysco facilities served a similar fraction of existing Sysco customers. Thus, the two

entry events were not as dissimilar as Dr. Israel testified, yet they produced very different results—one showing a significant price decrease, the other showing a negligible one. There may be location-specific reasons for the different results, but the reasons offered by Dr. Israel do not withstand scrutiny and no other evidence explained the difference. The court thus cannot conclude from these seemingly conflicting entry studies that the merger will harm local customers.

The court further notes that the pricing evidence here is far weaker than that found in other merger cases. In *Staples*, for instance, there was "compelling evidence" showing that prices were 13 percent higher in markets where Staples did not have competition from another office superstore. 970 F. Supp. at 1075-76 (pricing study). Similarly, in *Whole Foods*, an entry study showed that Whole Foods dropped its prices by five percent when another organic supermarket opened in the area. 548 F.3d at 1046-47 (Tatel, J.). In fairness, the FTC was unable to conduct pricing studies like those done in *Staples* and *Whole Foods* here because Defendants have competing facilities in nearly every local market. But the absence of convincing pricing effects evidence is the weakest aspect of the FTC's case.

5. *Summary*

In summary, the FTC has bolstered its *prima facie* case with additional proof that the merger would harm competition in both the national and local broadline markets. Although the FTC's case would have been strengthened with more convincing pricing effects evidence, the court nevertheless finds that the FTC has presented a compelling *prima facie* case of anticompetitive effects. *See Baker Hughes*, 908 F.2d at 991 ("The more compelling the prima facie case, the more evidence the defendant must present to rebut it successfully."). The court now turns to Defendants' rebuttal arguments.

III. DEFENDANTS' REBUTTAL ARGUMENTS

The FTC has established a presumption that the proposed merger will substantially lessen competition. Defendants, however, may rebut that presumption by showing that the traditional economic theories of the competitive effects of market concentration are not an accurate indicator of the merger's probable effect on competition or that the procompetitive effects of the merger are likely to outweigh any potential anticompetitive effects. *Heinz*, 246 F.3d at 715. The more "compelling the [FTC's] prima facie case, the more evidence the defendant must present to rebut [the presumption] successfully." *Baker Hughes*, 908 F.2d at 991. "A defendant can make the required showing by affirmatively showing why a given transaction is unlikely to substantially lessen competition, or by discrediting the data underlying the initial presumption in the government's favor." *Id.*

Defendants advance four arguments to support their claim that the food industry will remain competitive after the merger: (i) a post-divestiture PFG will be a strong competitor for customers seeking nationwide distribution; (ii) competition from other broadliners and other distribution channels will continue and grow; (iii) the entry of new competition and the repositioning of existing competitors will keep the industry competitive; and (iv) customers will benefit from efficiencies arising from the merger. The court addresses each of those arguments in turn and finds that, even taken collectively, Defendants cannot overcome the FTC's strong presumption of anticompetitive harm.

A. PFG Divestiture

Aside from the Supreme Court's guidance that "[t]he relief in an antitrust case must be 'effective to redress the violations' and 'to restore competition,'" *Ford Motor Co. v. United States*, 405 U.S. 562, 573 (1972) (footnote omitted) (quoting *United States v. E.I. Du Pont De Nemours*

& Co., 366 U.S. 316, 326 (1961)), there is a lack of clear precedent providing an analytical framework for addressing the effectiveness of a divestiture that has been proposed to remedy an otherwise anticompetitive merger. *Compare CCC Holdings*, 605 F. Supp. 2d at 56-59 (applying the framework for market entry analysis in assessing the effectiveness of a licensing agreement that would enhance the competitiveness of an existing competitor) *with FTC v. Libbey, Inc.*, 211 F. Supp. 2d 34, 47-48 (D.D.C. 2002) (finding defendants' proposed "fix" inadequate—without going into market entry analysis—because competitor would face higher costs).

Here, both sides cite to the 2004 U.S. Department of Justice's "Policy Guide to Merger Remedies," which provides the following guidance: "Restoring competition requires replacing the *competitive intensity* lost as a result of the merger rather than focusing narrowly on returning to premerger HHI levels." Antitrust Div., U.S. Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies 5 (Oct. 2004) [hereinafter 2004 Policy Guide] (emphasis added); *see also* Areeda & Hovenkamp 3d ed., *supra*, ¶ 990d (citing 2004 Policy Guide). A more recent U.S. Department of Justice Policy Guide provides: "The touchstone principle for the Division in analyzing remedies is that a successful merger remedy must effectively preserve competition in the relevant market." Antitrust Div., U.S. Dep't of Justice, Antitrust Division Policy Guide to Merger Remedies 1 (June 2011) [hereinafter 2011 Policy Guide] (footnote omitted). Both the 2004 Policy Guide and the 2011 Policy Guide add that an effective divestiture should address:

> [W]hatever obstacles (for example, lack of a distribution system or necessary know-how) lead to the conclusion that a competitor, absent the divestiture, would not be able to discipline a merger-generated increase in market power. That is, the divestiture assets must be substantial enough to enable the purchaser to *maintain the premerger level of competition*, and should be sufficiently comprehensive that the purchaser will use them in the relevant market and be unlikely to liquidate or redeploy them.

2004 Policy Guide at 9 (emphasis added) (footnotes omitted); *see also* 2011 Policy Guide at 8. With these principles in mind, the court analyzes the effect of the proposed divestiture.

1. Competitive Pressure Exerted by Post-Divestiture PFG

Defendants argue that the divestiture of 11 "strategically located" USF distribution centers to PFG, coupled with PFG's "aggressive" expansion across the country, will "replace [any] competitive intensity lost as a result of the merger." Defs.' Proposed Findings of Fact and Conclusions of Law, ECF No. 171 at 156 [hereinafter DFF] (alteration in original) (quoting 2004 Merger Guidelines at 5). In addition to the 11 divested distribution centers, PFG's owner, The Blackstone Group, a leading private equity firm, has committed $490 million to develop seven more distribution centers (called "foldouts") and to expand capacity in 16 existing facilities. Hr'g Tr. 724, 767-69; DFF at 155. Defendants also point to the industry acumen and experience of PFG's executives, particularly that of its President and CEO, George Holm, who has over 37 years of experience in the foodservice distribution industry. The court does not doubt Blackstone's financial commitment to PFG or Mr. Holm's leadership capabilities. However, based on the evidence presented, the court is not persuaded that post-merger PFG will be able to step into USF's shoes to maintain—certainly not in the near term—the pre-merger level of competition that characterizes the present marketplace.

PFG's five-year business plan shows that post-merger PFG will not be nearly as competitive as USF is today. In the lucrative market for national customers, the plan projects that PFG will have approximately $[redacted] billion in national broadline sales by 2019—*less than half* of USF's 2013 national broadline sales of $[redacted] billion. PX09350-074; PX09060-002; PX09060-004; PX09060-006; PX09253-023. Stated in terms of market share, PFG estimates that it will grow to 20 percent of the national broadline market over five years, with the merged Sysco-USF

company having the "remaining share of the national broadline business." PFF at 220; Hr'g Tr. 719, 721-22. That percentage is smaller than USF's share of the national broadline customer market today. PX09350-187 (Dr. Israel's report stating "the best case scenario under the divestiture is the emergence of a significantly smaller competitor than USF even several years into the future"). Defendants are correct that the divestiture does not have to replicate pre-merger HHI levels. However, the fact that PFG only expects to achieve less than *half* of USF's current national customer sales in five years—assuming that its planned expansion efforts are successful—does not demonstrate that PFG will be sufficiently able to "discipline a merger-generated increase in market power." *See* 2011 Policy Guide at 8 (footnote omitted).

The court's concern about PFG's ability to compete effectively in the post-merger world is not limited to sales and market share projections. PFG's short-term effectiveness will depend in large part on its ability to incorporate the 11 formerly-USF-held distribution centers. Even assuming that PFG can do so seamlessly, the new PFG will have only 35 distribution centers—far fewer than the at least 100 distribution centers owned by the combined Sysco/USF. Having only one-third of the merged company's distribution centers will put PFG at a significant disadvantage in competing for national customers. Indeed, as Dr. Israel demonstrated, Defendants' largest national customers use more than 35 distribution centers. Those customers represent █ percent of Sysco's national broadline revenues, and █ percent of USF's national broadline revenues. PX09375-075-077, Figure 3. The court is not convinced that these large national customers will consider a post-merger PFG to be as capable of meeting their needs as USF is today.

Defendants counter that "PFG will be able to compete aggressively with its additional distribution centers because the fewer the distribution centers used for a particular customer, the greater the inbound efficiencies." DFF at 161-62. Because of higher volume per warehouse and

lower freight costs, Defendants claim, many customers *prefer* to be served out of fewer distribution centers—so having a larger number of distribution centers is not necessarily a competitive advantage. *Id.* at 28, 161-62; Hr'g Tr. 1570-71, 1573-74; DX-00264 at 122-23. For example, to serve Zaxby's, a regional quick serve chain, PFG trucks drive past some of their own distribution centers because the longer drive "proves cheaper for the customer." DFF at 161; Hr'g Tr. 852. PFG can also take advantage of "shuttling," a technique of caravanning multiple trailers on a single truck, to increase efficiencies. DFF at 162; Hr'g Tr. 855-57. Mr. Holm even stated at his deposition that he believed that PFG would be able to serve [redacted] out of 35 distribution centers more effectively than USF currently does out of [redacted] DX-00276 at 96.

The court is skeptical of Defendants' claim that, even with far fewer distribution centers, PFG will be on equal competitive footing with the merged firm, especially for national customers. Defendants' own growth belies this fact. Both Sysco and USF have, over time, increased their number of distribution centers, demonstrating that Defendants view more distribution centers to be a competitive advantage. Indeed, when Defendants presently compete for national business, they highlight their nationwide geographic coverage to potential customers. *See, e.g.*, PX03000-014 (USF presentation touting its "[a]bility to leverage our national scale to cost effectively service customers nationally); PX00247-001-002 (USF email communication to [redacted] describing the "US Foods Value Proposition" as including a "Privately held National Distribution footprint company"); PX01062-005 (Sysco presentation to [redacted] highlighting that Sysco's "national footprint, strong service approach and our breadth of product offerings is what differentiates us from our competition"); PX00279-001 (USF email to [redacted] (a restaurant chain), mentioning "national footprint and scale" as a selling point); PX00281-006 (slide presentation to [redacted] touting USF's "extensive" distribution network). USF's Executive Vice

President of Strategy David Schreibman also testified that USF has the ability to leverage its national scale to cost-effectively service customers, and that USF views its national scale as a significant competitive advantage. Hr'g Tr. 1521-22; *see also* PX03010-001 (internal USF document stating that the "[o]nly 'true' options for both Premier and Novation is either Sysco or USF[;] [t]he regional players will bid, but not be seriously considered"). Furthermore, there was no evidence presented that Defendants have moved to consolidate their distribution facilities to take advantage of the supposed benefits of having fewer distribution centers.[33]

Notably, not even PFG has always considered the divestiture of only 11 distribution centers to be sufficient for it to compete on a national level. A PFG internal strategy document, dated April 3, 2014, sets forth two "final" proposals for additional distribution centers "necessary to establish a national broadline network." One proposal included options of 16 to 20 distribution centers, and the other included a list of 14 to 15. Hr'g Tr. 669-71 (discussing PX09193). Six months later, in October 2014, after PFG had started negotiations with Sysco about the divestiture, internal PFG communications re-affirmed the need for more than 11 distribution centers. Following Sysco's proposal to sell only seven distribution centers, a PFG board member wrote to George Holm:

> I would still find a way to tell the FTC that we think it takes 13 but that Sysco won't let us look at more than 7 *which will get us nowhere near a national solution.* We need the package size to be bigger to have any chance of winning *and to ever compete nationally*. . . . [We] should proactively educate the FTC why 13 opcos [another word for distribution center] is the *bare mimimum*.

PX09192-001 (emphasis added); *see also* PX00526-036; PX00526-141-142; PX09190. PFG did just that when it met with the FTC, making the case that it needed 13 distribution centers to

[33] Defense counsel at oral argument represented that USF recently had closed two distribution centers, Closing Arg. Hr'g Tr. 113, but counsel for the FTC noted that USF also recently had opened a new distribution center, *id.* at 125-26.

"compete effectively for national business." PX00526-039 at 153; PX09070 (PFG's presentation to the FTC with a map of 13 USF distribution centers needed by PFG, which included the four metropolitan areas mentioned below). Ultimately, PFG was not able to negotiate the sale of more than 11 distribution centers, with Sysco having made the decision that it "would rather litigate w[ith] the FTC than sell more than 11." PFG felt that it was "prudent to engage on 11 for now to keep the momentum/dialogue going." PX09157-002; PX00526-041 at 163.

Having fewer distribution centers means that PFG will face coverage gaps in the geographic areas where it sought, but did not receive, a distribution center. Those areas include: Cincinnati, Ohio; Omaha, Nebraska; Oklahoma City, Oklahoma; and Los Angeles, California, where PFG received a different, smaller distribution center than it requested. PX00526-039 at 155-56; *see also* PX09070.

Defendants argue that PFG's requests to Sysco for a larger number of distribution centers than they actually received was part of a bargaining strategy. Closing Arg. Hr'g Tr. 115-16. However, PFG's recognition that it needed more than 11 distribution centers to compete nationally is reflected in internal documents that were created months before PFG began negotiating with Sysco. The court credits those internal projections over PFG's current position that an additional 11 distribution centers is enough to compete for national customers. *See* Amicus Br. of PFG, ECF No. 133 at 22-24 (arguing that PFG will be able to compete effectively with 35 distribution centers).

Defendants argue that, with the planned "foldouts," *i.e.*, new distribution facilities located in contiguous geographic markets, PFG will have more than the 13 distribution centers it was seeking, including one in Cincinnati. DX-01706 at 14. However, PFG has never done a foldout, and according to internal estimates, these facilities may not be operational until, at the earliest,

several years following the merger.[34] Defendants assert that "PFG will be well-positioned to *bid* on Day One," because even after the bids are submitted, discussions between a customer and a distributor can take up to a year before a contract is finalized, and PFG can continue its foldout efforts in the meantime. DFF at 160 (emphasis added). According to Defendants, if the customer needs service sooner, PFG can provide service via shuttling until the foldout is complete. *Id.* at 161. However, there is substantial evidence showing that customers value having distribution centers close to their locations and that distribution costs increase with driving distance. Thus the court is not persuaded that—even with promises of foldouts and the use of shuttling—a sufficient number of national customers will view PFG as a viable alternative to the merged entity "on day one" to maintain the intensity that characterizes the present competition between Sysco and USF.

2. *Additional Disadvantages Faced by Post-Merger PFG*

In addition to its lack of nationwide geographic coverage, the court has other concerns about PFG's ability to compete against the merged entity. Because it will purchase in smaller product volumes than the merged Sysco entity, PFG could face higher product acquisition costs, or cost of goods sold ("COGS"), than its competitor. PX05051-003 (Blackstone Memorandum indicating that "due to its scale, USF has better procurement than PFG and the 11 [distribution centers] will likely spend more to acquire private label products and get less supplier rebate dollars"); PX09350-205 (Dr. Israel's opinion that, even with the divestiture, PFG is unlikely to make up the gap in COGS between itself and the parties today). PFG also will offer substantially fewer SKUs than the merged entity. PFG today sells less than half the total number of SKUs as USF and one third the number of private label SKUs. PX06055-004 (USF offers 350,000 SKUs,

[34] PFG's Senior VP of Operations estimated that PFG's "priority" foldouts in Cincinnati, Ohio, Detroit, Michigan and Buffalo, New York, will not be operational until fiscal year 2018, and Montgomery, Alabama will not be operational until 2017. Hr'g Tr. 735-38.

of which 30,000 are private label); PX09507-007; PX09507-013 (PFG offers 150,000 SKUs, of which [redacted] are private label). PFG's fewer SKU offerings will be a competitive disadvantage.

PFG also will face disadvantages in terms of human resources. Defendants point out that, as part of the divestiture package, PFG would acquire over "4,400 USF personnel, including senior executives and personnel with healthcare expertise at the 11 distribution centers, and corporate regional leadership, national sales personnel, merchandising personnel, and others with national sales expertise; [and] a 12 month non-solicit of PFG employees at the 11 distribution centers." DFF at 155 (citing Hr'g Tr. 815-25; DX-06100 at 1). However, even assuming that every USF employee at the 11 distribution centers becomes a PFG employee, PFG will still have fewer than half the sales representatives of either Sysco or USF today and less than one-quarter of the sales representatives of the combined firm. PX09350-181-184, Figure 18. And, PFG will only receive, at most, one-fifth of the national sales employees at USF dedicated to serving national customers. Hr'g Tr. 1528-31 (stating that only about 20 percent of USF's national account team will be made available for PFG to hire).

Moreover, PFG will be at a competitive disadvantage in its ability to offer value-added services. The lucrative healthcare segment is illustrative. George Holm conceded that PFG has had limited success with national healthcare customers. Hr'g Tr. 716-17. Some of that lack of success is due to PFG's limited footprint, but it is also attributable to PFG's lack of expertise in the healthcare segment and its inability to deliver value-added services to those customers. *See, e.g.*, PX00594-025 at 100 (PFG has a very small portion of [redacted] members' business because PFG lacks acute care expertise); PX00474-001 ("PFG offers a more limited selection of healthcare-specific products than US Foods."). Even if over time PFG can acquire health care expertise, in the short run it will be at a competitive disadvantage as compared to the merged

entity.[35] For instance, Joan Ralph, Group Vice President of Premier testified that, even with the healthcare employees PFG acquires through the divestiture, PFG will have significantly less healthcare expertise than USF today. Hr'g Tr. 413; PX09350-211-212. And, as IFDA President Mark Allen testified, Sysco and USF have the best understanding of the healthcare class of trade. DX-00294 at 121. The merger would only enhance that strategic advantage.

3. *Post-Merger PFG as an Independent Competitor*

A final factor that cuts against the divestiture as a proposed fix is that PFG will be dependent on the merged entity for years following the transaction. "In order to be accepted, curative divestitures must be made to . . . a willing, *independent* competitor capable of effective production . . . ." *CCC Holdings*, 605 F. Supp. 2d at 59 (quoting *White Consol. Indus. v. Whirlpool Corp.*, 781 F.2d 1224, 1228 (6th Cir. 1986)) (internal quotation marks omitted). As the court observed in *CCC Holdings*, it can be a "problem" to allow "continuing relationships between the seller and buyer of divested assets after divestiture, such as a supply arrangement or technical assistance requirement, which may increase the buyer's vulnerability to the seller's behavior." *Id.* (internal quotation marks omitted). Under the Transition Services Agreement, PFG will have complete access to USF private label products for three years at its 11 new distribution centers, and therefore will be relying on the merged entity to license those products to PFG. *See* DX-06100 at 1; PX09060-005. PFG will also have the right to license USF's database for at least five years, with a continuing option for five more. PFG, therefore, will not be a truly independent competitor.

[35] PX[redacted]-002 ([redacted] stating that USF is able to offer "certain value-added services that are especially important to healthcare facilities"); PX[redacted]-002 (Joan Ralph of Premier stating, "[i]t is critical to Premier that its members have access to foodservice representation with healthcare expertise who can provide nutritional guidance, menu-planning services, and [redacted]."); PX[redacted]-004 ([redacted] discussing his concern that PFG "may lack the ability to provide the information technology services" like dynamic item ordering [redacted] currently receives from USF); PX[redacted]-009 ([redacted] stating "I do not know whether PFG has the healthcare experience, which [redacted] highly values.").

For the foregoing reasons, the court is not persuaded that the proposed divestiture will remedy the anticompetitive effects of the merger.

B. Existing Competition

1. Regionalization

Defendants assert that existing competition can and will constrain potential price increases or other unilateral effects in the national customer market. Their primary argument is that the ability of national customers to switch or threaten to switch to a network of regional distributors will inhibit anticompetitive behavior by the merged company. *See* Defs.' Opp'n Br. at 40-41. Defendants point to many large national customers who multi-source their foodservice distribution needs, including using various regional broadliners to service individual locations. Defendants cite as examples Amerinet, Sodexo, the Defense Logistics Agency, [redacted], Subway, and [redacted], all of whom operate regionally under multiple contracts. *See id.* at 15.

But, for several reasons, the ability to regionalize is not likely to inoculate national customers from potential anticompetitive effects. The decision of many large customers to predominantly use one broadline distributor is not simply a preference, as Defendants would characterize it, but a rational business decision. As already discussed, for the most part, the largest national customers—particularly GPOs, foodservice management companies, and hospitality companies—predominantly rely on Sysco or USF for their broadline distribution needs. The largest customers, generally speaking, make from 61 percent to 100 percent of their broadline purchases from Sysco or USF. *See* FTC Closing Slide 35; PFF at 113-16. Even customers who contract regionally, such as [redacted] and [redacted], buy in very high quantities from Defendants. Regionalization is available today, as it will be after the merger. But market actors are not moving to that model. To the contrary, as PFG's George Holm testified, the "clear trend" among large

customers is to move to a single nationwide provider. Hr'g Tr. 597-98. The court can only infer from this trend that regionalization is not a reasonable option for many national customers.

Regionalization likely has not taken hold for a variety of reasons. The record shows that when a customer increases its number of distributors, it incurs greater management and supply chain costs, making it far less desirable to switch to a multi-regional model. The court found the deposition testimony of Dan Cox, the President and CEO of DMA, particularly illuminating, given that the reason for DMA's existence is to consolidate the product and service offerings of multiple regional distributors and compete for national customers. Mr. Cox testified that using a sole source broadliner "forms the most efficient supply chain." DX00265 at 44. He explained that "[m]ore products at each delivery reduces our cost to service and therefore reduces their supply chain costs. . . . By aggregating [customers'] spend it makes the delivery system more efficient." *Id.* at 44-45.

A regional arrangement also brings with it the disadvantage of multiple points of contact. As Mr. Cox testified, a single point of contact simplifies communications, which DMA touts as an advantage over multi-sourcing broadline distribution. *Id.* at 14, 46, 68. He also added that a single information technology system is important to national customers, and DMA offers such a platform to attract them. As Mr. Cox explained: "[I]f they come to DMA and deal with five different members, they wouldn't have to learn and understand five different order entry platforms. We have just one platform." *Id.* at 68. A multi-regional approach thus likely would require a customer to develop greater information technology capabilities to manage its foodservice distribution contracts.

Another downside of a multi-regional model is the difficulty in obtaining consistent products—particularly private label products—across a national customer's different locations. Mr. Cox offered the example of [REDACTED], with which DMA does over $[REDACTED] million in business.

█████ demands that DMA comply with its product specifications "at a level of 90 percent," *id.* at 74, indicating that even when a large customer uses multiple regional distributors, they impose rigorous demands with regard to product consistency. Product consistency, of course, can be achieved by purchasing from multiple distributors who carry the same brand-named products. But that approach would limit a customer's ability to purchase private label products, which typically offer a better value proposition than branded products.

PFG's George Holm concurred with Dan Cox's assessment of national customers' business needs and why they avoid regionalization. When asked why large national customers contract mainly with either Sysco or USF and why there is a clear trend toward those customers using a single broadliner, Holm offered numerous reasons: the "ability to get SKUs in quickly"; "one place to contact"; "[o]ne IT system"; "[o]ne sales contract"; "[o]ne person to deal with"; "the same product [across] their system"; writing "one check as opposed to several"; "simplified contract administration"; and easier "management of approved item lists and specifications." Hr'g Tr. 600-04. The court thus concludes that the possibility of regionalizing broadline foodservice is not likely to protect national customers from the merger's anticompetitive effects.

2. DMA

Today, the only other competitor with a nationwide footprint is DMA. Defendants claim that DMA is capable of effectively competing against the merged entity because it provides a single point of contact, a single contract with consistent terms across customer locations, and a single ordering platform. DFF at 165-66 (citing DX-00265 at 63-64, 66, 68). The court disagrees.

Defendants acknowledge that DMA is not a one-stop-shop for national customers as Sysco and USF are today. Indeed, Defendants recognize that "larger customers 'look to [DMA's]

members regionally . . . rather than DMA as a national solution.'" *Id.* at 164-65 (quoting DX-00265 at 86).

As Dan Cox, the President and CEO of DMA, explained:

DX-00265 at 64-65. As a result,

Id. at 65.

National customers who value private label products, such as GPOs or foodservice management companies,

Id. at 79-80.

See id. at 224-26.

And, even if a national customer wanted to switch to DMA,

As Mr. Cox explained, "

" *Id.* at 99.

[REDACTED] *Id.* at 100, 157. For example, [REDACTED] recently considered switching its business to DMA, but decided to stay with Sysco [REDACTED]. *Id.* at 227-29. [REDACTED], the court does not view DMA as a viable competitor that can constrain a post-merger Sysco.

3. *Conclusion as to Existing Competition*

Based on the evidence presented, the court is convinced that national customers will be better off in a marketplace that has two strong competitors capable of nationwide broadline distribution than in a marketplace in which there is a single undisputed heavyweight of broadline distribution whose only competitive constraints is a transitioning PFG, DMA, and a collection of regional players.

C. Entry of New Firms and Expansion of Existing Competitors

Defendants argue that the entry of new competitors and the expansion of existing competitors will keep the industry competitive. If a court finds that "there exists ease of entry into the relevant product market," that finding "can be sufficient to offset the government's prima facie case of anti-competitiveness." *Cardinal Health*, 12 F. Supp. 2d at 55. "The prospect of entry into the relevant market will alleviate concerns about adverse competitive effects only if such entry will deter or counteract any competitive effects of concern so the merger will not substantially harm customers." Merger Guidelines § 9. Ease of entry must be "*timely*, *likely*, and *sufficient* in its magnitude, character, and scope to deter or counteract the competitive effects of concern." *Id.* (emphasis added). As with their other rebuttal arguments, Defendants bear the burden of demonstrating the ability of other distributors to "fill the competitive void" that will result from

the proposed merger. *See Swedish Match*, 131 F. Supp. 2d at 169. Defendants assert that a lack of technological, legal, and regulatory barriers makes entry into the foodservice distribution industry relatively easy. Yet although all it may take is a "guy and a truck" to become a foodservice distributor, becoming a *broadline* foodservice distributor with the ability to compete for national customers is another thing altogether.

The broadline foodservice distribution industry is extraordinarily capital and labor intensive. It costs roughly $35 million to build a single distribution center. Hr'g Tr. 586. In addition, the distribution center must be stocked with goods. A fleet of expensive, refrigerated trucks is required to deliver the products. People—lots of them—are needed to sell the broadline service, maintain and stock the warehouse, and deliver the products. *See Swedish Match*, 131 F. Supp. 2d at 171 (finding high barriers to entry where the evidence showed "substantial sunk costs in plant construction, product development, and marketing" required to compete). And, even if a newcomer were to make the substantial investment to start a broadline distribution company, there is no guarantee that customers will follow. Incumbency is a powerful force in the foodservice distribution industry. *See H&R Block*, 833 F. Supp. 2d at 75 (finding that "importance of reputation and brand in driving consumer behavior" limited an existing competitor's ability to expand). Even if it were possible for a new entrant to overcome the incumbent's advantage, it would take years. These high barriers to entry will further entrench the merged company's market power. PX03003-005 (USF lender presentation describing broadline foodservice distribution as having "High barriers to entry for scale players").

Defendants also contend that existing firms have demonstrated the capacity to expand to compete against the merged firm. They highlight the fact that other broadline distributors—including Shamrock, Ben E. Keith, and Reinhart—started out as small businesses serving only

limited items to local customers, but were able to grow to regional prominence. They describe examples of competitors that have recently opened new facilities or plan to do so.

But none of these examples overcome the fundamental problem with expansion as a constraint on the merged company—like new entry, successful expansion is extraordinarily capital intensive and demands a long time horizon. Based on their assessment that expansion would not be an economically viable strategy, regional distributors have said that they have no plans to expand or reposition in order to serve national customers. [REDACTED], which has [REDACTED] distribution centers mostly located in the [REDACTED], has told the FTC that such a massive expansion would not be "viable" in the short term, given the "time and cost required." PX[REDACTED]-006. Other regional distributors, including [REDACTED] have similarly been dissuaded by the time, costs, or risks of expansion. PX[REDACTED]-036 at 139-42; PX[REDACTED]-004; PX[REDACTED]-003; PX[REDACTED]-005-006; PX[REDACTED]-048-049.

Companies rarely enter new markets without an existing customer base because the costs and risks are prohibitive. There is a real "chicken-and-egg" problem with such expansion, known in the industry as "greenfield" expansion. Companies will not make the significant capital expenditure of building a new distribution center unless they already have customers to serve, but customers will not commit to a distributor unless it has demonstrated the ability to serve its needs. As a result, expansion in the industry is typically done through "foldouts"—building distribution centers in contiguous geographic areas—so that customers can be served from an existing facility until the new facility is built. But even foldouts take time to succeed. They can take from one to three years to complete, and it can take four to five years for a foldout facility to achieve sales per square foot similar to established broadline facilities. PX00529-042 at 166-68; Hr'g Tr. 837-39; *see also* PX00558-051 at 201-04. Although a foldout strategy may preserve competition in a

particular local market, it cannot effectively be used to replace the competition benefitting national customers lost by the merger. The only way in which a regional player could expand sufficiently and quickly enough to compete with the merged company would be through a sizeable acquisition of multiple distribution centers.

In summary, the court finds that, absent a substantial acquisition opportunity, expansion by regional players will not be timely, likely, and of sufficient magnitude to counteract anticompetitive harm. *See Cardinal Health*, 12 F. Supp. 2d at 58 ("Although the smaller wholesalers may adequately compete and expand to service both the primary and secondary needs of local customers, this Court finds that they would not sufficiently expand to compete with the nationals.").

D. Efficiencies

1. Requirement for Merger-Specific and Verifiable Efficiencies

Although the Supreme Court has never recognized the "efficiencies" defense in a Section 7 case, the Court of Appeals as well as the Horizontal Merger Guidelines recognize that, in some instances, efficiencies resulting from the merger may be considered in rebutting the government's *prima facie* case. *Heinz*, 246 F.3d at 720 (citations omitted). Where, as in this case, the court finds high market concentration levels, defendants must present "proof of extraordinary efficiencies" to rebut the government's *prima facie* case. *Id.* (citations omitted) (requiring "extraordinary" efficiencies to rebut an increase in HHI of 510 points); *see also* Areeda & Hovenkamp 3d ed., *supra*, ¶ 971f (requiring "extraordinary" efficiencies where the "HHI is well above 1800 and the HHI increase is well above 100"). The court is not aware of any case, and Defendants have cited none, where the merging parties have successfully rebutted the government's *prima facie* case on the strength of the efficiencies. *See CCC Holdings*, 605 F. Supp. 2d at 72 (stating that "courts

have rarely, if ever, denied a preliminary injunction solely based on the likely efficiencies"). Yet even if evidence of efficiencies alone is insufficient to rebut the government's *prima facie* case, such evidence may nevertheless be "relevant to the competitive effects analysis of the market required to determine whether the proposed transaction will substantially lessen competition." *Arch Coal*, 329 F. Supp. 2d at 151 (citations omitted).

The court must "undertake a rigorous analysis of the kinds of efficiencies being urged by the parties in order to ensure that those 'efficiencies' represent more than mere speculation and promises about post-merger behavior." *Heinz*, 246 F.3d at 721. Specifically, the court must determine whether the efficiencies are "merger specific"—meaning they represent "a type of cost saving that could not be achieved without the merger"—and "verifiable"—meaning "the estimate of the predicted saving must be reasonably verifiable by an independent party." *H&R Block*, 833 F. Supp. 2d at 89 (internal quotation marks omitted) (citing Merger Guidelines § 10); *Cardinal Health*, 12 F. Supp. 2d at 62 ("In light of the anti-competitive concerns that mergers raise, efficiencies, no matter how great, should not be considered if they could also be accomplished without a merger."). Defendants bear the burden of demonstrating that their claimed efficiencies are merger specific, *H&R Block*, 833 F. Supp. 2d at 90, which requires demonstrating that the efficiencies "cannot be achieved by either company alone," *Heinz*, 246 F.3d at 722. And, Defendants must also demonstrate that their claimed efficiencies would benefit customers. *CCC Holdings*, 605 F. Supp. 2d at 74.

Defendants claim that the merger will generate over one billion dollars in annual cost savings and operational synergies and, "[e]ven when discounted substantially for unforeseen integration complications, possible customer loss, and the divestiture, the merged company's efficiencies are expected to generate over $600 million in savings." DFF at 178. Defendants argue

that the $600 million efficiencies estimate is "the product of meticulous analysis and planning," which occurred over the course of eight months and involved over 100 employees at McKinsey, an independent consulting firm, and over 170 Sysco and USF employees who are extremely familiar with the business. *Id.* at 179. As Defendants explained, "Sysco, USF, and McKinsey reviewed a back-breaking amount of information from the merging firms, analyzed historical integration data, modeled possible cost-savings opportunities, and built a new organizational structure around the companies' combined customer base, and designed detailed day 1, day 100, and year 1 plans for integration." *Id.* Of the $600 million cost savings identified by McKinsey, Defendants' expert Dr. Hausman identified more than $490 million as merger specific. To rebut Dr. Hausman's opinion on efficiencies, the FTC presented Mr. Rajiv Gokhale of Compass Lexecon as an expert in financial economics. He opined that at least 65 percent of Defendants' efficiencies were not merger specific. PX09351-007.

The court does not question the rigor and scale of the analysis conducted by McKinsey. Nor does the court have any reason to question the accuracy of McKinsey's total annual cost savings estimate. But that is not the issue before the court. The issue is whether Defendants have shown that the projected "merger-specific" cost savings are substantial enough to overcome the presumption of harm arising from the increase in market concentration and other evidence of anticompetitive harm. As to that question, the court is unpersuaded that Defendants' combination would result in $490 million in merger-specific cost savings. Defendants have not shown that that amount, or at least a substantial portion of it, could not be achieved independently of the merger. Nor does it appear that Dr. Hausman conducted any independent analysis of the McKinsey estimate to determine which savings, if any, can be achieved without the merger.

Sysco did not hire McKinsey to identify merger-specific savings for antitrust purposes. Rather, it initially hired McKinsey in the fall of 2013 to determine whether a merged company could achieve enough cost savings to make the combination worthwhile. Hr'g Tr. 1862-63. After McKinsey concluded that the merger would generate sufficient cost savings and Sysco and USF announced the merger, McKinsey began a more in-depth analysis beginning in January 2014 to identify "particular synergies that would arise from the deal." *Id.* at 1864-65. Carter Wood, the McKinsey Director who led the effort, testified that his firm was hired "to estimate what is possible by combining these two companies such that, number one, they would have confidence or not to go ahead with the deal; and two, to create value for the newly integrated company." *Id.* at 1914. McKinsey was not given instructions on identifying merger-specific savings, and Mr. Wood testified that he was not familiar with the term "merger specific." *Id.* at 1904.

Dr. Hausman used McKinsey's projections as his baseline for identifying merger-specific savings. *Id.* at 2053. However, it is not clear what independent analysis Dr. Hausman did to reduce McKinsey's projected savings of $600 million annually to $[redacted] million in merger-specific savings. In his report, Dr. Hausman explained:

> In my previous academic research I have emphasized the effect of cost saving efficiencies on marginal cost, which can be approximated by average variable cost. Thus I will take a conservative approach to the estimated efficiencies and focus on cost savings from changes in variable costs that arise from the merger and would not occur otherwise.

DX-01355 at 67 (footnote omitted). It is not apparent, however, how Dr. Hausman calculated merger-specific savings using this approach, as neither his testimony nor his report spell out precisely how he went about identifying the amount of variable cost savings to include in his merger-specific estimate.

Table 4a of Dr. Hausman's rebuttal report illustrates the difficulties with verifying his analysis. Dr. Hausman itemized the "run-rate of merger-specific variable cost synergies" into four

Table 4a: Estimated Cost Efficiencies[1]

Adjusted for Divestiture, Customer Loss, and Contingencies

Category	Run-Rate Synergies	Run-Rate of Variable Cost Synergies	Run-Rate of Merger Specific Variable Cost Synergies
Merchandising Total			
Best cost and terms			
Enhance terms			
Consolidate suppliers			
Full category management			
Corporate billing			
Operations Total			
Network Optimization			
Driver Efficiency[**]			
Reduce average cost per mile for inbound freight*			
Leverage network			
Dis-synergy (LEI loss) from consolidation			
Indirect Sourcing[**]			
Sales Total			
Sales associate headcount			
DSM and RSM headcount			
Reduce variable opex			
Corporate Total			
Combined Total:			

categories: (i) Merchandising, (ii) Operations, (iii) Sales, and (iv) Corporate. In each of those four categories, Dr. Hausman listed the component parts (in the first column) and the corresponding amounts (in the fourth column) that comprise the category cost savings estimate. Yet for each of

these elements, Dr. Hausman relied exclusively on documents created by either McKinsey or Defendants. *See* DX-01353 at Ex. C, 2 n.i. He performed no independent analysis to verify these numbers. *Id.* ("All source material is either Sysco, US Foods, or McKinsey material and I take those materials at face value.").

But even taking Dr. Hausman's variable cost savings numbers as presented, the court is not convinced that the full $490 million in projected savings is merger specific. For example, nearly half of the $█ million in merger-specific savings identified by Dr. Hausman come from the "Merchandising" category, also known as "category management." The $281 million that Dr. Hausman attributed to category management cost savings comes directly from McKinsey's calculations. Category management refers to a process of optimizing a distributor's product assortment by gaining insights into which SKUs its customers value and then optimizing the SKU inventory to match customers' demands and procure those products in the most cost-efficient manner. Hr'g. Tr. 1881. Both companies prior to the merger already were undertaking category management efforts. PX00592-035 at 137-40; PX00592-049 at 193-94.

Although McKinsey Director Mr. Wood testified that McKinsey made an effort to identify only incremental merchandising savings, that is, savings arising only because of the merger, he could not say whether the $281 million included some cost savings that Defendants might have been able to achieve separately. For instance, before the merger, Sysco was undergoing a category management program, called Project Naples, which was due to end in June 2015. However, Project Naples covered only two-thirds of Sysco's product categories; Sysco planned to complete the remaining categories at a later date. Mr. Wood testified that the $281 million figure was in addition to the Project Naples costs savings, but he could not say whether or not that number was

in addition to the cost savings that Sysco could achieve through its continued cost savings efforts beyond June 2015.

USF, meanwhile, suspended its category management project after the merger's announcement. At the time the merger was announced, USF had only conducted category management on █ to █ categories out of 300. PX00592-035 at 139; PX00592-048-049 at 192-93. Mr. Wood could not say whether the $281 million was in addition to cost savings that USF might have achieved had it continued its category management program. Thus, Dr. Hausman's estimate of $281 million in "merger-specific" savings in Merchandising—a number that, again, relied exclusively on McKinsey's calculations—likely overstates the achievable merger-specific category management savings.

The FTC has pointed to, and Defendants have not rebutted, other ways in which Dr. Hausman's reliance on McKinsey's estimates likely overstated the savings arising from the merger. During the hearing, Mr. Wood acknowledged that part of the sales synergy estimate—which represents savings from combining the salesforces of the two companies—would be achieved by having customers place orders via an e-commerce platform. However, migration to electronic ordering can be achieved by either company independently of the merger. Hr'g Tr. 1904-05. Another savings strategy identified by McKinsey, "maximizing backhaul," refers to having delivery trucks stop by suppliers to reload goods on their way back to the warehouse, in order to save an extra trip to those suppliers. Hr'g Tr. 1894-95. However, backhaul savings can also be achieved independently of the merger. *See* Hr'g Tr. 1905-06.

2. *Insufficiency of Estimated Merger-Specific Savings*

Even if the court were to credit Dr. Hausman's total estimate of merger-specific efficiencies, the figure would only amount to less than one percent of the merged entity's annual

revenue. PX09375-118 (Dr. Israel's rebuttal report stating that Dr. Hausman's original estimate of merger-specific, variable cost efficiencies of $███ million per year represents only one percent of Sysco and USF's combined annual broadline revenue).[36] Even assuming that 100 percent of the cost savings would be passed on to customers, the savings are unlikely to outweigh the competitive harm to customers. Since the savings are equal to a small percentage of the combined company's total revenue, even a modest increase in price could offset any cost savings generated by the efficiencies. At oral argument, Defendants' response to this concern was that the market would not allow even a slight price increase, as customers would exercise their other options, such as regionalizing. *See* Closing Arg. Hr'g Tr. 117-18. Having found that this merger will result in high national customer and local market concentration levels, the court does not share Defendants' confidence that the market would not tolerate such a price increase. As the court observed in *Cardinal Health*, "[t]he critical question raised by the efficiencies defense is whether the projected savings from the merger[ ] are enough to overcome the evidence [showing] that possibly greater benefits can be achieved by the public through existing, continued competition." 12 F. Supp. 2d at 63. Here, Defendants have fallen short of making that showing.

E. Conclusion

Upon consideration of all of the evidence presented, the court concludes that Defendants' rebuttal evidence is not sufficient to overcome the presumption of anticompetitive harm that the FTC was able to establish through evidence of high post-merger market concentrations and other evidence of competitive harm. The court thus concludes that the FTC has met its burden of demonstrating a likelihood of success. That is, the FTC has raised "questions going to the merits so serious, substantial, difficult and doubtful as to make them fair ground for thorough

[36] In 2013, Sysco and USF's combined broadline revenue was [over $50 B] PX09350-216, Table 27. One percent of that sum is greater than Dr. Hausman's merger-specific cost savings estimate of $███ million.

investigation, study, deliberation and determination by the FTC in the first instance and ultimately by the Court of Appeals." *Heinz*, 246 F.3d at 714-15 (citation omitted) (internal quotation marks omitted).

IV. THE EQUITIES

Although the court has found that the FTC has shown a likelihood of success on the merits and thus created a presumption in favor of injunctive relief, *see Swedish Match*, 131 F. Supp. 2d at 172, Section 13(b)'s "public interest" standard still requires the court to weigh the public and private equities of enjoining the merge, *Heinz*, 246 F.3d. at 726. Here, the primary public interests to be considered include (i) the public interest in effectively enforcing antitrust laws and (ii) the public interest in ensuring that the FTC has the ability to order effective relief if it succeeds at the merits trial.

The public's interest in enforcing antitrust law plainly favors enjoining Defendants' proposed merger. *See id.* ("The principle public equity weighing in favor of issuance of preliminary injunctive relief is the public interest in effective enforcement of the antitrust laws."); *Swedish Match*, 131 F. Supp. 2d at 173 ("There is a strong public interest in effective enforcement of the antitrust laws that weighs heavily in favor of an injunction in this case.").

The second public interest factor—preserving the FTC's ability to order effective relief after the administrative hearing—also supports an injunction. As stated by the Court of Appeals, "if the merger were ultimately found to violate the Clayton Act, it would be impossible to recreate pre-merger competition" because the merging parties would have already combined their operations and they would be difficult to separate, even by a subsequent divestiture order. *Id.* ("Section 13(b) . . . embodies Congressional recognition of the fact that divestiture is an inadequate and unsatisfactory remedy in a merger case."). That problem is amplified here because the

proposed merger involves two transactions, not just one: (i) Sysco's merger with USF and (ii) PFG's purchase of USF's distribution centers and other assets. The parties have represented that, absent an injunction, Sysco and USF will merge their operations and divest 11 distribution centers and associated assets—including personnel, IT Systems, and USF private label products—to PFG, which will incorporate those assets into its own operations. As the FTC has pointed out, it would face an especially daunting and potentially impossible task of "unscrambling" the eggs (*i.e.*, returning the merging companies to their pre-merger state) if the ensuing administrative proceedings were to determine that the merger violates Section 7 of the Clayton Act. Additionally, it is difficult to conceive how a subsequent divestiture order—which would attempt to restore the parties to their pre-merger state—could be fulfilled without causing significant disruption to the foodservice distribution industry, its customers, and the ultimate consumers—Americans who eat outside the home.

Defendants contend that the public equities weigh against granting the preliminary injunction because the merger will generate substantial efficiencies that will be passed on to customers. They claim that, if the FTC obtains the injunction, Defendants and their customers will be harmed because "Sysco and US Foods will abandon the merger and consumers will be deprived of its benefits." DFF at 186-87 (citing Hr'g Tr. 1516-17). But the court cannot conclude, on this record, that the merger's cost savings will outweigh the potential harm to customers from losing the country's second largest broadline distributor as a competitor for their business. Dr. Israel's merger simulation model predicted that, even taking into account the estimated cost savings, the merger would harm customers. PX09350-114-121, Table 3. Although the court has reservations about some of Dr. Israel's merger simulation model inputs, the court finds that the record as a

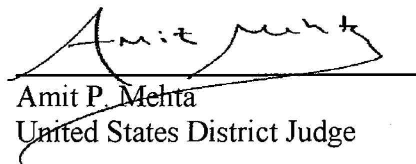
whole—at the very least—raises substantial questions about whether the merger will harm consumers. Therefore, the public equities here favor granting the preliminary injunction.

The court recognizes the extraordinary amount of time, energy, and money that Sysco, USF, and PFG have devoted to the proposed merger. Their efforts, and the risk that the parties will abandon the merger rather than proceed to an administrative trial on the merits is, however, "at best, a private equity" which cannot overcome the significant public equities weighing in favor of a preliminary injunction. *See Heinz*, 246 F.3d at 727 (internal quotation marks omitted).

CONCLUSION

In the end, after considering the record in its entirety, the court returns to Judge Tatel's observation in *Whole Foods*: "[T]here can be little doubt that the acquisition of the second largest firm in the market by the largest firm in the market will tend to harm competition in that market." *Whole Foods*, 548 F.3d at 1043 (Tatel, J.) (citation omitted) (internal quotation marks omitted). The court finds that the FTC has carried its burden of showing a "reasonable probability" that a merger of the country's two largest broadline foodservice distributors, Sysco and USF, would harm competition. Defendants' merger is likely to cause unduly high market concentrations in two relevant markets—broadline foodservice distribution to national customers and broadline foodservice distribution to local customers—and eliminate a key competitor in those markets, USF. The evidence offered by Defendants to rebut the FTC's showing of likely harm was unavailing. The equities also favor granting the requested preliminary injunction. The FTC, therefore, has established that it is likely to succeed in proving, after a full administrative hearing, that the effect of Sysco's proposed acquisition of USF "may be substantially to lessen competition, or to tend to create a monopoly" in violation of Section 7 of the Clayton Act.

The court thus grants the FTC's Motion for Preliminary Injunction. A separate order accompanies this Memorandum Opinion.



Dated: June 23, 2015

Amit P. Mehta
United States District Judge

Press Releases

Sysco Responds to District Court's Ruling on Merger With US Foods

HOUSTON, June 23, 2015 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) issued the following statement today from President and Chief Executive Officer Bill DeLaney after the U.S. District Court in the District of Columbia granted the Federal Trade Commission's (FTC) request for a preliminary injunction to block Sysco's proposed merger with US Foods. DeLaney said:

"While we respect the Court's decision, we are profoundly disappointed with this outcome. We diligently pursued this transaction for nearly two years because we strongly believed the merger of Sysco and US Foods would be procompetitive and good for customers, associates and shareholders. Nevertheless, we certainly understood this outcome to be possible and have been developing plans for the business moving forward. We will take a few days to closely review the Court's ruling and assess our legal and contractual obligations, including the merits of terminating the merger agreement. This work will be conducted in close collaboration with Sysco's Board of Directors and the primary owners of US Foods. We will provide additional clarity in the coming days."

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 194 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2014 that ended June 28, 2014, the company generated sales of more than $46 billion. For more information, visit **www.sysco.com** or connect with Sysco on Facebook at **www.facebook.com/SyscoCorporation** or Twitter at **https://twitter.com/Sysco**. For important news regarding Sysco, visit the Investor Relations portion of the company's Internet home page at **www.sysco.com/investors**, follow us at **www.twitter.com/SyscoStock** and download the new Sysco IR App, available on the **iTunes App Store** and the **Google Play Market**. In addition, investors should also continue to review our news releases and filings with the Securities and Exchange Commission. It is possible that the information we disclose through any of these channels of distribution could be deemed to be material information.

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Sysco Corporation

Source: Sysco Corporation

Press Releases

Sysco Terminates Merger Agreement With US Foods

06/29/2015

Company Reaffirms Commitment to Leverage Core Business Growth, Announces $3 Billion Share Repurchase, Plans to Redeem Merger-Related Debt

HOUSTON, June 29, 2015 (GLOBE NEWSWIRE) -- Sysco Corporation (NYSE:SYY) announced that it has terminated its merger agreement with US Foods, days after the U.S. District Court in Washington, D.C., granted the Federal Trade Commission's request for a preliminary injunction to block the proposed Sysco-US Foods merger. This action also terminates an agreement with Performance Food Group (PFG) to purchase US Foods facilities in 11 markets.

Under terms of the merger agreement, the termination of the transaction requires Sysco to pay break-up fees of $300 million to US Foods and $12.5 million to PFG.

"After reviewing our options, including whether to appeal the Court's decision, we have concluded that it's in the best interests of all our stakeholders to move on," said Bill DeLaney, Sysco president and chief executive officer. "We believed the merger was the right strategic decision for us, and we are disappointed that it did not come to fruition. However, we are prepared to move forward with initiatives that will contribute to the success of Sysco and our stakeholders."

Unwavering Focus on Customer Service

DeLaney underscored Sysco's confidence in its existing business with a collective focus on the highest levels of customer service and satisfaction, growing the business, reducing costs and generating substantial value for Sysco's shareholders.

"Everything starts with the customer," DeLaney said. "Our vision remains clear: to be our customers' most valued and trusted business partner. If our customers succeed, then we succeed. Our relentless focus on providing exceptional customer service and differentiated solutions to help our customers grow is unwavering."

Leverage Core Business Growth

"We also will continue to drive earnings through commercial and supply chain initiatives, including category management and revenue management in our core business, as well as pursuing cost-saving opportunities," he said. "We are confident in our ability to achieve these initiatives because of our success to date in transforming nearly all aspects of our business, standing up several commercial and functional capabilities, and taking out or avoiding more than $750 million in annual product and operating costs."

Sysco continues to generate strong and stable cash flow. "We have improved our discipline and efficiency in how we manage our substantial cash flow, and we are committed to grow our free cash flow over time as we move forward," DeLaney said. "We will continue to make prudent investments in our business. We also remain committed to growing our dividend because we know that's important to our shareholders. And, we will continue to look for strategic acquisitions that will enhance shareholder value over time."

Share Repurchases

Sysco's Board of Directors has authorized the company to spend an additional $3 billion to buy back shares (approximately 13 percent of current outstanding shares at recent prices) over the next two years. The share repurchases will be in addition to the amount normally purchased to offset benefit plans and stock option dilution. The company intends to fund these purchases from new borrowings and cash flow from operations. The intent is to repurchase approximately $1.5 billion in shares in each of the next two years and, as part of the first year's purchases, the company expects to put in place an accelerated share repurchase program. Sysco will continue to assess the merits of repurchasing shares over time.

"While we are very comfortable leveraging our balance sheet to enhance returns to our shareholders, we remain committed to maintaining a solid investment-grade credit rating and a strong balance sheet," DeLaney said. "A strong balance sheet provides the capacity and flexibility to continue to pursue strategic opportunities as they may arise. While we anticipate the possibility that our credit rating may be downgraded as a result of this new share repurchase program, we are comfortable operating our company with higher levels of debt."

Merger Debt Redemption

Sysco also will begin the process of redeeming the $5 billion of merger-related debt under the mandatory redemption provisions contained within those notes. This process is expected to take no more than 40 days.

Conference Call & Webcast

Additional details about the termination of the merger agreement, the share repurchase program, debt redemption and operational initiatives will be discussed on a conference call at 10 a.m. (Eastern), Monday, June 29. A live webcast of the call and a copy of this news release will be available online at **www.sysco.com** in the Investors section.

About Sysco

Sysco is the global leader in selling, marketing and distributing food products to restaurants, healthcare and educational facilities, lodging establishments and other customers who prepare meals away from home. Its family of products also includes equipment and supplies for the foodservice and hospitality industries. The company operates 194 distribution facilities serving approximately 425,000 customers. For Fiscal Year 2014 that ended June 28, 2014, the company generated sales of more than $46 billion. For more information, visit **www.sysco.com** or connect with Sysco on Facebook at **www.facebook.com/SyscoCorporation** or Twitter at **https://twitter.com/Sysco**. For important news regarding Sysco, visit the Investor Relations portion of the company's Internet home page at **www.sysco.com/investors**, follow us at **www.twitter.com/SyscoStock** and download the new Sysco IR App, available on the **iTunes App Store** and the **Google Play Market**. In addition, investors should also continue to review our news releases and filings with the Securities and Exchange Commission. It is possible that the information we disclose through any of these channels of distribution could be deemed to be material information.

Forward-Looking Statements

Statements made in this news release that look forward in time or that express management's beliefs, expectations or hopes are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements reflect the views of management at the time such statements are made and are subject to a number of risks, uncertainties, estimates, and assumptions that may cause actual results to differ materially from current expectations. These statements include our plans and expectations related to dividend growth, strategic acquisitions, and share repurchases. Our success with regard to each of these matters, including the timing and benefits thereof, is subject to the general risks associated with our business, including the risks of interruption of supplies due to lack of long-term contracts, severe weather, crop conditions, work stoppages, intense competition, technology disruptions, dependence on large regional and national customers, inflation risks, the impact of fuel prices, adverse publicity, and labor issues. Risks and uncertainties also include risks impacting the economy generally, including the risks that the current general economic conditions will deteriorate, or consumer confidence in the economy may not increase and decreases in consumer

spending, particularly on food-away-from-home, may not reverse. Market conditions may not improve. If sales from our locally managed customers do not grow at the same rate as sales from regional and national customers, our gross margins may continue to decline. Our ability to meet our long-term strategic objectives to grow the profitability of our business depends largely on the success of our Business Transformation Project. There are various risks related to the project, including the risk that the project and its various components may not provide the expected benefits in our anticipated time frame, if at all, and may prove costlier than expected; the risk that the actual costs of the ERP system may be greater or less than currently expected because we have encountered, and may continue to encounter, the need for changes in design or revisions of the project calendar and budget, including the incurrence of expenses at an earlier or later time than currently anticipated; the risk that our business and results of operations may be adversely affected if we experience delays in deployment, operating problems, cost overages or limitations on the extent of the business transformation during the ERP implementation process; and the risk of adverse effects to our business, results of operations and liquidity if the ERP system, and the associated process changes, do not prove to be cost effective or do not result in the cost savings and other benefits at the levels that we anticipate. Planned deployments in the coming quarters are dependent upon the success of the ERP system and the updates at the current locations. We may experience delays, cost overages or operating problems when we deploy the system to additional locations. Our plans related to and the timing of the implementation of the ERP system, as well as the cost transformation and category management initiatives, are subject to change at any time based on management's subjective evaluation of our overall business needs. We may fail to realize anticipated benefits, particularly expected cost savings, from our cost transformation initiative. If we are unable to realize the anticipated benefits from our cost cutting efforts, we could become cost disadvantaged in the marketplace, and our competitiveness and our profitability could decrease. We may also fail to realize the full anticipated benefits of our category management initiative, and may be unable to successfully execute the initiative in our anticipated timeline. Capital expenditures may vary from those projected based on changes in business plans and other factors, including risks related to the implementation of our business transformation initiatives and our regional distribution centers, the timing and successful completions of acquisitions, construction schedules and the possibility that other cash requirements could result in delays or cancellations of capital spending. Periods of high inflation, either overall or in certain product categories, can have a negative impact on us and our customers, as high food costs can reduce consumer spending in the food-away-from-home market, and may negatively impact our sales, gross profit, operating income and earnings. Expanding into international markets presents unique challenges and risks, including compliance with local laws, regulations and customs and the impact of local political and economic conditions, and such expansion efforts may not be successful. Any business that we acquire may not perform as expected, and we may not realize the anticipated benefits of our acquisitions. Expectations regarding the accounting treatment of any acquisitions may change based on management's subjective evaluation. Expectations regarding tax rates are subject to various factors beyond management's control. For a discussion of additional factors impacting Sysco's business, see the Company's Annual Report on Form 10-K for the year ended June 28, 2014, as filed with the Securities and Exchange Commission, and the Company's subsequent filings with the SEC. Sysco does not undertake to update its forward-looking statements.

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Sysco Corporation

Source: Sysco Corporation

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 8-K

CURRENT REPORT
PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Date of Report (date of earliest event reported): June 29, 2015 (June 26, 2015)

SYSCO CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	1-06544	74-1648137
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification No.)

1390 Enclave Parkway, Houston, TX	77077-2099
(Address of principal executive office)	(Zip Code)

Registrant's telephone number, including area code: (281) 584-1390

N/A
(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 1.01. Entry Into a Material Definitive Agreement

The disclosure set forth below under Item 1.02 of this Form 8-K is incorporated by reference herein.

Item 1.02. Termination of a Material Definitive Agreement

On June 26, 2015, Sysco Corporation (the "Company"), USF Holding Corp. ("USF") and two merger subsidiaries of Sysco ("Merger Subs") entered into an Agreement and Release (the "Termination Agreement") to terminate the Agreement and Plan of Merger, dated December 8, 2013, among the Company, USF and the Merger Subs (the "Merger Agreement"). Upon the termination of the Merger Agreement, the Asset Purchase Agreement, dated February 2, 2015, among the Company, USF, US Foods, Inc., a wholly owned subsidiary of USF, a number of subsidiaries of US Foods, Inc. and Performance Food Group, Inc. (the "APA") automatically terminated.

The parties mutually agreed to terminate the Merger Agreement following the decision of the U.S. District Court for the District of Columbia to grant the Federal Trade Commission's request for a preliminary injunction to block the transactions contemplated by the Merger Agreement.

The Company has paid a termination fee of $300 million to USF in connection with the termination of the Merger Agreement. The foregoing description of the Termination Agreement does not purport to be complete and is subject to, and qualified in its entirety by, the full text of the Termination Agreement, which is filed herewith as Exhibit 10.1 and incorporated herein by reference.

Upon the termination of the Merger Agreement, the APA automatically terminated. The Company has paid a termination fee of $12.5 million to Performance Food Group, Inc. pursuant to the terms of the APA.

Pursuant to the indentures governing the $5 billion in aggregate principal amount of senior unsecured notes (the "Notes") issued in six series by the Company on October 2, 2014, the Company is required, due to the termination of the Merger Agreement, to redeem within 40 calendar days each series of Notes in whole, at a redemption price equal to 101% of the aggregate principal amount of such series of Notes, plus accrued and unpaid interest. The Company issued a redemption notice with respect to each series of Notes on June 29, 2015, and expects to complete the redemption within the 40 calendar day period referenced above.

Item 2.04. Triggering Events That Accelerate or Increase a Direct Financial Obligation or an Obligation under an Off-Balance Sheet Arrangement.

The disclosure set forth above under Item 1.02 of this Form 8-K is incorporated by reference herein.

Item 8.01. Other Information.

On June 29, 2015, the Company issued a press release announcing the termination of the Merger Agreement. A copy of the press release is attached hereto as Exhibit 99.1 and is incorporated herein by reference.

Item 9.01. Financial Statements and Exhibits.

Exhibit Number	Description
10.1	Agreement and Release, dated June 26, 2015, among USF Holding Corp., Sysco Corporation, Scorpion Corporation I, Inc. and Scorpion Company II, LLC.
99.1	Press Release dated June 29, 2015.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, Sysco Corporation has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

Sysco Corporation

Date: June 29, 2015

By: /s/ Russell T. Libby
Russell T. Libby
Executive Vice President-Corporate Affairs,
Chief Legal Officer and Corporate Secretary

Exhibit Number	Description
10.1	Agreement and Release, dated June 26, 2015, among USF Holding Corp., Sysco Corporation, Scorpion Corporation I, Inc. and Scorpion Company II, LLC.
99.1	Press Release dated June 29, 2015.

Exhibits omitted

FEDERAL TRADE COMMISSION
PROTECTING AMERICA'S CONSUMERS

Following Sysco's Abandonment of Proposed Merger with US Foods, FTC Closes Case

Share This Page

FOR RELEASE

July 1, 2015

TAGS: Bureau of Competition | Competition

Following a June 23, 2015 ruling by the U.S. District Court for the District of Columbia granting the Federal Trade Commission request for a preliminary injunction, Sysco and US Foods abandoned their proposed merger, and the Commission has now dismissed its administrative complaint.

In light of those events, FTC Chairwoman Edith Ramirez issued the following statement:

"The parties' decision to abandon their merger following the federal district court decision in favor of the FTC is a good outcome," said FTC Chairwoman Ramirez. "This proposed merger between the country's two largest foodservice distributors would have likely increased prices paid by restaurants, hotels, cafeterias, and hospitals across the country for food products and related services, and ultimately the prices paid by people eating at those establishments. The FTC is committed to maintaining vigorous competition in markets like this one that directly impact prices consumers pay for everyday purchases."

In February 2015, the Commission challenged Sysco's proposed $8.2 billion merger with rival US Foods, alleging that the deal would significantly reduce competition in broadline foodservice distribution, both nationwide and in a large number of local markets. The complaint alleged that the merged entity would account for 75% of the sales to national customers of broadline services, where the merging parties are the only firms with a truly

national footprint that allows them to compete to serve customers, such as restaurants, group-purchasing organizations (GPOs), and foodservice companies, with locations nationwide. No other company could offset the competition that would have been lost to this merger.

Broadline distributors offer extensive product lines, including national-brand and private-label food products, and provide frequent and flexible delivery, high levels of customer service, and other value-added services such as order tracking, menu planning, and nutritional information.

In his 128-page opinion preliminarily stopping the deal, District Court Judge Amit Mehta ruled that "because the proposed merger would eliminate head-to-head competition between the number one and number two competitors in the market for national customers, the merger is likely to lead to unilateral anticompetitive effects in that market."

The court also rejected the parties' argument that their agreement with the country's third-largest broadline distributor, Performance Food Group, to divest 11 distribution centers, would offset the significant competitive harm likely to result from the merger.

The administrative trial was scheduled to begin on July 21, 2015. In light of the parties' decision to abandon the transaction, the Commission has voted 5-0 to dismiss the administrative complaint.

The FTC's Bureau of Competition works with the Bureau of Economics to investigate alleged anticompetitive business practices and, when appropriate, recommends that the Commission take law enforcement action. To inform the Bureau about particular business practices, call 202-326-3300, send an e-mail to antitrust{at}ftc{dot}gov, or write to the Office of Policy and Coordination, Bureau of Competition, Federal Trade Commission, 600 Pennsylvania Ave., NW, Room CC-5422, Washington, DC 20580. To learn more about the Bureau of Competition, read Competition Counts. Like the FTC on Facebook, follow us on Twitter, and subscribe to press releases for the latest FTC news and resources.

PRESS RELEASE REFERENCE:

Statement of FTC Bureau of Competition Director Debbie Feinstein on Sysco and U.S. Foods' Abandonment of Their Proposed Merger

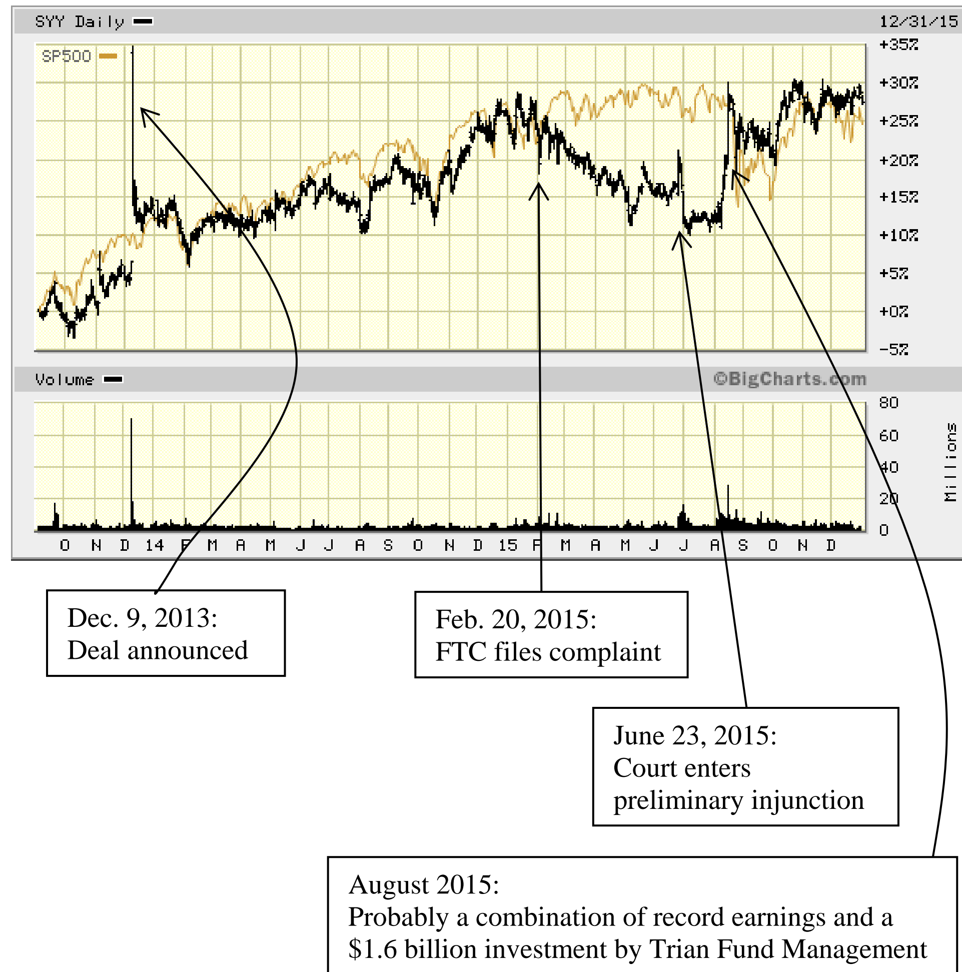
Contact Information

MEDIA CONTACT:

Betsy Lordan
Office of Public Affairs
202-326-3707

ftc.gov

Sysco Corporation (SYY): September 1, 2013 – December 31, 2015
(compared to the S&P 500 Index)



There is no corresponding stock chart for US Foods, since at the time US Foods was privately held by two private equity firms. On May 2, 2007, at the height of the leveraged buyout boom, Clayton, Dubilier & Rice, Inc. and Kohlberg Kravis Roberts & Co. L.P. (KKR), had purchased US Foods (then known as US Foodservice) from Royal Ahold N.V. in a transaction valued at $7.1 billion.

Targeted Customers and Sellers

UNITED STATES V. BERTELSMANN SE & CO. KGAA,
646 F. Supp. 3d 1, 23-34 (D.D.C. Nov. 15, 2022)
(excerpt on targted sellers[1])

FLORENCE Y. PAN, United States Circuit Judge

[The Department of Justice brought an action alleging that the proposed $2.18 billion acquisition by Bertelsmann, the owner of Penguin Random House, of Simon & Schuster from ViacomCBS. The DOJ alleged that the acquisition would substantially lessen competition in the input market for the U.S. publishing rights to anticipated top-selling books (defined to be books with advances over $250K). Penguin Random House and Simon & Schuster are two of the "Big Five" largest book publishers in the United States, with market shares of 37% and 12%, respectively. The court sustained the DOJ's market definition, found that the merger was likely to substantially harm competition through both unilateral and coordinated effects, and rejected the defenses of the merging parties.]

. . .

III. Analysis

The first step in merger analysis is the identification of a relevant market. *See* [*United States v.*] *Marine Bancorp*[*oration, Inc.*], 418 U.S. [602,] at 618 [(1974)]. Market definition "helps specify the line of commerce and section of the country in which the competitive concern arises"; and allows the Court to evaluate any anticompetitive effects by "identify[ing] market participants and measur[ing] market shares and market concentration." [2010] Merger Guidelines § 4.16 "Determination of the relevant market is a necessary predicate to a finding of a violation of the Clayton Act because the threatened monop[sony] must be one which will substantially lessen competition 'within the area of effective competition.'" *United States v. E.I. du Pont de Nemours & Co*., 353 U.S. 586, 593 (1957) (quoting *Standard Oil Co. of Cal. v. United States*, 337 U.S. 293, 299 n.5 (1949)). But defining a relevant market is not an end unto itself; rather, it is an analytical tool used to ascertain the "locus of competition." *Brown Shoe* [*Co. v. United States*], 370 U.S. [294,] at 320-21 (1962); *see also* [2010] Merger Guidelines § 4.1.1 ("[T]he purpose of defining the market and measuring market shares is to illuminate the evaluation of competitive effects."). Accordingly, the Supreme Court has emphasized that market definition under the Clayton Act was intended by Congress to be "a pragmatic, factual" analysis and "not a formal, legalistic one." *Brown Shoe*, 370 U.S. at 336.

Market definition has two components: the relevant geographic market and the relevant product market. *See Brown Shoe*, 370 U.S. at 324; [*United States v.*] *Anthem*, [*Inc.*], 236 F. Supp. 3d [171.] at 193 [(D.D.C.), *aff'd*, 855 F.3d 345 (D.C. Cir. 2017)].

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[1] Record citations, internal cross-references, and footnotes omitted.

Here, the parties agree that the relevant geographic market is the global market for the acquisition of U.S. publishing rights. The parties strenuously dispute, however, the boundaries of the appropriate product market.

The government defines the relevant product market as the one for publishing rights to anticipated top-selling books. Anticipated top-selling books are those that are expected to yield significant sales, and for which authors therefore receive higher advances. The government contends that such books have distinctive characteristics, including the need for extra marketing, publicity, and sales support to allow them to reach broader audiences.

The proposed market for anticipated top-selling books is a submarket of the broader publishing market for all trade books. Under the government's monopsony theory, the authors of anticipated top-selling books are "targeted sellers" against whom the merged defendants might lower the prices paid for the authors' wares. [*S*]*ee also* Merger Guidelines § 4.1.4 (If a monopsonist could "profitably target a subset of [sellers] for price [de]creases, the [government] may identify relevant markets defined around those targeted [sellers]."); *cf. FTC v. Wilh. Wilhelmsen Holding ASA*, 341 F. Supp. 3d 27, 46-47 (D.D.C. 2018) ("[A]ntitrust markets can be based on targeted customers"); *Sysco*, 113 F. Supp. 3d at 38-40 (discussing definition of markets based on targeted customers). In the monopsony context, "[a] submarket exists when [buyers] can profitably [cut] prices to certain targeted [sellers] but not to others, in which case regulators may evaluate competitive effects separately by type of [seller]." *Anthem*, 236 F. Supp. 3d at 195 (cleaned up).

Courts evaluate relevant product markets in the monopsony context in two ways: by considering qualitative, "practical indicia" as described by the Supreme Court in the *Brown Shoe* case, 370 U.S. at 325; and by examining "supply substitution" and applying the "hypothetical monopsonist test," which are discussed in detail, *infra*. The parties in this case focus their arguments on whether "practical indicia" support the finding of a market to publish "anticipated top-selling books." Because the parties choose to fight on the battlefield of "practical indicia," that is where the Court begins its analysis.

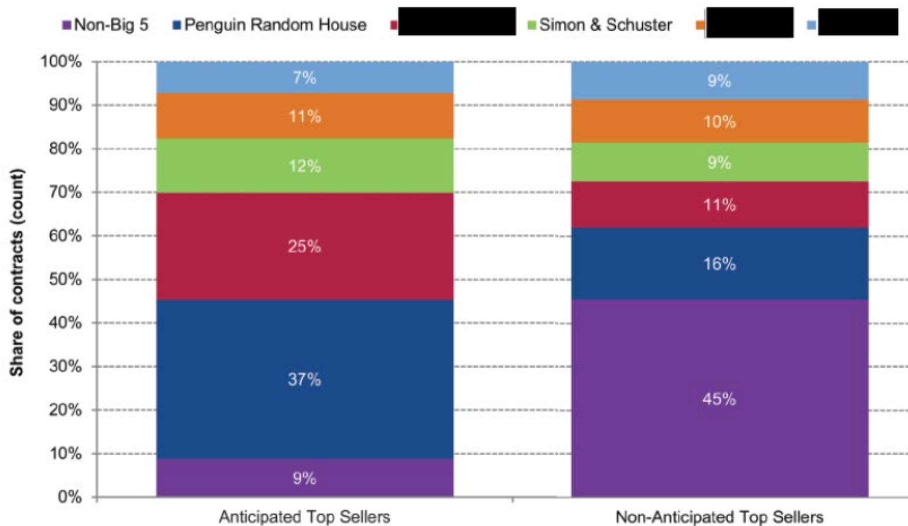
1. Practical Indicia

"[W]ithin [a] broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct [sellers], distinct prices, sensitivity to price changes, and specialized vendors." *Brown Shoe*, 370 U.S. at 325, 82 S.Ct. 1502. These indicia are "practical aids" as opposed to "talismanic" criteria "to be rigidly applied," *FTC v. Swedish Match*, 131 F. Supp. 2d 151, 159 (D.D.C. 2000) (cleaned up); thus, "submarkets can exist even if only some of these factors are present." *FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1075 (D.D.C. 1997) ("*Staples I*").

Brown Shoe's practical indicia also may help identify a market of targeted sellers. *See FTC v. Whole Foods Market, Inc*., 548 F.3d 1028, 1038-39 (D.C. Cir. 2008) (citing *Brown Shoe*, 370 U.S. at 325, 82 S.Ct. 1502). For example, a market of "distinct [sellers]," as posited by the government, may find "a particular [set of buyers] 'uniquely attractive' " and "the only realistic choice" for their products. *Id*. (first citing *Brown Shoe*, 370 U.S. at 325; then quoting *Nat'l Collegiate Athletic Ass'n v. Bd. of Regents of the Univ. of Okla.*, 468 U.S. 85, 111 (1984); and then quoting *SuperTurf, Inc. v. Monsanto Co.*, 660 F.2d 1275, 1278 (8th Cir. 1981)).

i. The $250,000 Threshold

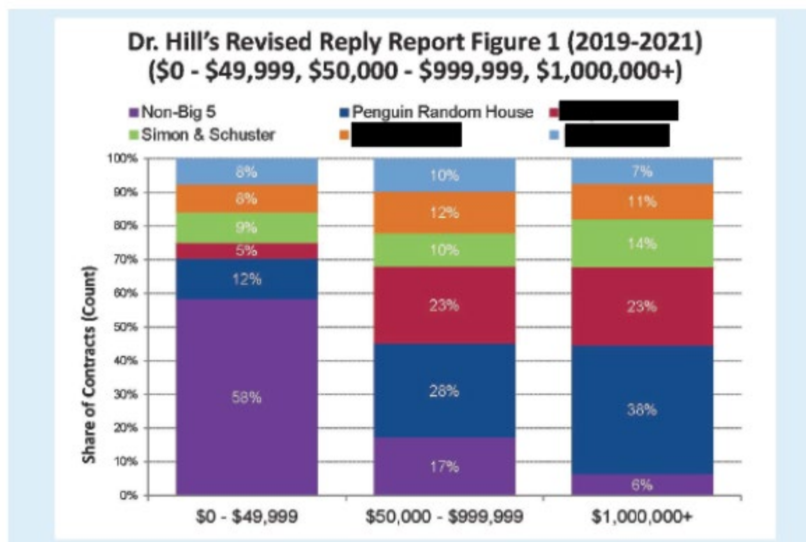
To identify the books that are anticipated to sell well, the government focuses on the criterion of "distinct pricing": For analytical purposes, it defines anticipated top-selling books as those for which publishers pay an advance of at least $250,000. See *Brown Shoe,* 370 U.S. at 325 (explaining that "distinct prices" are probative in market definition); *see also Whole Foods*, 548 F.3d at 1038-39 (explaining distinct prices paid by targeted group of customers "indicate[ ] the existence of a submarket of core customers"); *Syufy Enters. v. Am. Multicinema, Inc.*, 793 F.2d 990, 995 (9th Cir. 1986) (considering "lucrative terms offered for the pictures by exhibitors" to define relevant market). Books that meet the $250,000-advance threshold comprise only 2 percent of all book acquisitions, but they account for 70 percent of all advance spending, amounting to $1 billion annually. Government's Exhibit 963 shows that the market shares of industry participants in the proposed publishing market for anticipated top-selling books are far more concentrated than in the market for publishing books at lower advance levels:



In the publishing market for anticipated top-selling books, the Big Five publishers hold 91 percent of the market share, while smaller publishers collectively hold only 9 percent. By contrast, in the publishing market for books that earn advances below $250,000, the non-Big Five publishers have a much more substantial market share of 45 percent.

As an initial matter, the government's use of high advances as a proxy for anticipated book sales is logical and supported by market realities. In publishing, advances are correlated with expected sales because books that are expected to sell well receive higher advances. In fact, advance levels are set by using P&L's, and the defining feature of a P&L is the sales estimate. Moreover, industry practices indicate that $250,000 is a reasonable place to draw the line: S & S and two of the three PRH adult divisions require approval from senior publishers or executives for advance offers of $250,000 or more; and Publishers Marketplace, a major industry publication, categorizes deals for $250,000 or more as "significant." This evidence is probative of "industry or public recognition" of a distinct category of books that receive advances at or above the $250,000 level. *Brown Shoe*, 370 U.S. at 325.

The defendants take aim at the $250,000 threshold that the government has chosen to bound the market. Most significantly, they argue that the $250,000 threshold is either too high or too low to define a submarket for anticipated top selling books. Specifically, the defendants rely on their Exhibit 438 to argue that the advance threshold should be set at $50,000 to capture the point at which the Big Five begin to dominate the market for acquiring books:



See Defs. PFOF ¶ 37 ("[T]he data establish that if competitive conditions differ based on market shares and author preferences, the difference begins with books acquired for advances of $50,000 or more," where the market share of non-Big Five publishers is reduced from 58% to 17%.). Alternatively, the defendants contend that the threshold

should be set at $1 million to identify the books by celebrity, franchise, or award-winning authors that are most clearly destined for success. If the relevant market were properly defined at the lower ($50,000) or higher ($1 million) advance level, the defendants urge, the government could not show a sufficient decrease to competition or harm to authors.

The defendants' excessive concern over the specific dollar threshold betrays a misunderstanding of why the threshold was chosen. The market that the government seeks to define is the one for anticipated top-selling books, and the $250,000 demarcation was adopted only as an analytical tool to help it group together the books in question. The government's economic expert, Dr. Nicholas Hill, also conducted his analyses at other numerical thresholds (including $150,000, $250,000, $500,000, and $1 million) and observed consistent outcomes at those various high-dollar amounts. Thus, the $250,000 cutoff is merely useful; it is not intended to be a rigid bright line, but rather is helpful "[f]or analytical purposes" to facilitate the assessment of anticompetitive effects. *FTC v. Staples, Inc.*, 190 F. Supp. 3d 100, 118 & n.10 (D.D.C. 2016) ("*Staples II*") ("[T]here is no 'magic place that's the right place' to draw the line." (quoting government expert's testimony)). Accordingly, the Court rejects this argument against the government's defined market.

The Court is unswayed by the defendants' tactic of enumerating other markets or submarkets in which competition would not be harmed by the merger. In addition to proposing submarkets at the $50,000- and $1 million-advance levels, the defendants also declare that the government could not prove anticompetitive effects from the merger in the broad market of publishing rights for all U.S. trade books, or in the downstream market for retail book sales. Those protestations are beside the point because the Clayton Act prohibits mergers that may substantially lessen competition "in any line of commerce or in any activity affecting commerce." 15 U.S.C. § 18 (emphasis added). Thus, even if alternative submarkets exist at other advance levels, or if there are broader markets that might be analyzed, the viability of such additional markets does not render the one identified by the government unusable. *See United States v. Cont'l Can Co.*, 378 U.S. 441, 456–58 (1964) (validating a relevant product market of glass and metal containers, even though "there may be a broader product market made up of metal, glass and other competing containers"); *United States v. Aluminum Co. of Am.*, 377 U.S. 271, 275 (1964) (explaining that even though insulated aluminum conductor and insulated copper conductor could both be in "a single product market," that "does not preclude their division for purposes of [Section] 7 into separate submarkets"); *see also Brown Shoe*, 370 U.S. at 325; *Anthem*, 236 F. Supp. 3d at 201-02.

Ample precedent supports the government's use of a numerical cutoff to identify a submarket. It is common for courts to use seemingly arbitrary criteria to home in on a segment of a broader industry. *See Wilhelmsen*, 341 F. Supp. 3d at 51 (market of customers with fleets of 10 or more global maritime vessels); *Anthem*, 236 F. Supp. 3d at 195 (market of companies with 5,000 or more employees); *Staples II*, 190 F. Supp. 3d at 118 (market of customers who spend $500,000 or more annually on office supplies). In *Wilhelmsen*, Judge Chutkan approved a relevant market "defined around

the FTC's preferred set of targeted customers" — "Global Fleets." 341 F. Supp. 3d at 48, 58. The government characterized "Global Fleets" as "fleets of 10 or more globally trading vessels." *Id*. at 51. Although the defendants argued "that the Global Fleets construct is premised on arbitrary thresholds," the court found that such fleets "are a distinct group with distinct needs," even though the "choice of ten globally trading vessels was arbitrary in the sense that the number ten is not compelled by a specific market reality." *Id*. at 51-54. Judge Chutkan explained that the government's expert "chose ten as a starting point for developing a series of statistical estimates, the non-statistical implications of which support the appropriateness of regarding Global Fleets as a distinct customer group." *Id*. at 55. In other words, the cutoff of ten ships to define "Global Fleets" was an appropriate analytical tool, just as the choice of a $250,000-minimum advance level to define "anticipated top-selling books" is appropriate for analytical purposes. At bottom, such "construct[s]" provide a "useful way to discuss and predict economic conditions" because their "key aspects correspond to elements of the existing marketplace that would make it possible to profitably target a subset of customers [or sellers] for price increases [or decreases] post-merger." *Id*. at 52 (quoting *Sysco*, 113 F. Supp. 3d at 38).

The government's focus on anticipated top-selling books also is consistent with cases in which courts have recognized the "high end" of other broad markets as distinct submarkets for antitrust purposes. *See, e.g.*, *Int'l Boxing Club of N.Y., Inc. v. United States*, 358 U.S. 242, 251 (1959) (affirming district court's conclusion "that nonchampionship fights are not 'reasonably interchangeable for the same purpose' as championship contests" and explaining that defining the relevant market "involves distinction in degree as well as distinctions in kind"); *Whole Foods*, 548 F.3d at 1032 (recognizing relevant submarket of "premium, natural, and organic supermarkets" that "generally target affluent and well educated customers"); *O'Bannon v. Nat'l Collegiate Athletic Ass'n*, 7 F. Supp. 3d 955, 986-88 (N.D. Cal. 2014) (recognizing relevant submarket of "elite football and basketball recruits"), *rev'd in part on other grounds*, 802 F.3d 1049 (9th Cir. 2015). Thus, the relevant market defined here falls comfortably within the parameters set by numerous applicable precedents.

The defendants nevertheless fault the government for defining its submarket by "price alone," contending that any correlation between advance level and expected sales shows only that books "are valued along a continuum." They argue that the existence of "a spectrum of price or value" is insufficient to establish a submarket and, accordingly, that the government's market is not appropriately defined. Once again, such arguments overlook the purpose of the $250,000 threshold as an analytical tool that facilitates the examination of market shares and anticompetitive effects. The threshold number need not represent an exact point at which the market begins to distinguish a product. *See Wilhelmsen*, 341 F. Supp. 3d at 54-55; *Anthem*, Inc., 236 F. Supp. 3d at 200 (accepting a 5,000-employee threshold to define "national accounts" even though the "threshold may exclude some products that would meet the needs of smaller employers"); *Staples II*, 190 F. Supp. 3d at 118 & n.10 ("[T]here is no 'magic place that's the right place' to draw the line." (quoting government expert's testimony)). Rather, a threshold will necessarily represent a "starting point" for

"statistical estimates, the non-statistical implications of which support the appropriateness of regarding" anticipated top-selling authors as a "distinct [seller] group" that buyers can target. *Wilhelmsen*, 341 F. Supp. 3d at 55.

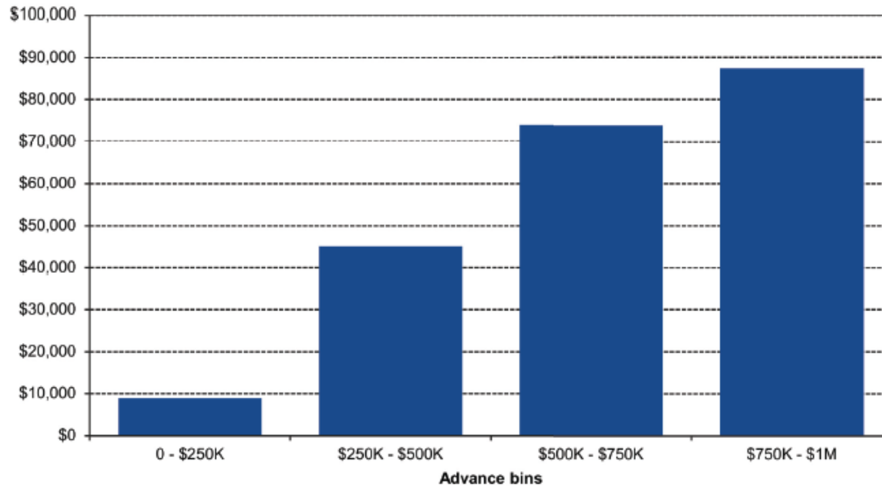
ii. The Remaining *Brown Shoe* Factors

Aside from distinct pricing, the government argues that the remaining *Brown Shoe* factors demonstrate that there is a relevant submarket for the publishing rights to anticipated top-selling books. The government contends that such books have "peculiar characteristics and uses," in that they require stronger marketing, publicity, and sales support, which allow them to reach a broader audience of readers. In addition, authors of anticipated top-selling books are "distinct sellers," in that they (1) care more about their publishers' reputation and services, which ensure wider distribution of their books; (2) may receive more favorable contract terms than other authors; and (3) face different competitive conditions, as demonstrated by the dominant market share of the Big Five (91%) in publishing anticipated top sellers. For all those reasons, the government argues, anticipated top-selling books are in a different category from books that are expected to sell relatively few copies, and publishers can target their authors for price decreases.

The defendants, however, insist that all books are in the same market. They argue that books at all advance levels go through an identical editing, marketing, and distribution process; that there is no difference in the personnel who handle such books; that the contracts for all books are negotiated in the same way; and that any special terms in the contracts for some books simply result from an agent's leverage. Further, they contend that publishers cannot predict which books will be top sellers. *See* Defs. PFOF ¶¶ 78 ("[P]ublishers generally have no objective criteria for reaching in advance a consensus on whether a book is likely to be a top selling book."), 79 (arguing that publishers "cannot easily predict top sellers," other than books by celebrity, franchise, or prize-winning authors), 75 (asserting that every book is individual and author atypical).

The Court has no trouble recognizing that anticipated top-selling books are distinct from the vast majority of books that do not carry the same expectations for success. Obviously, the entire publishing industry is dedicated to selling books; and all editors and publishers naturally are very focused on discovering and acquiring the books that they believe will drive sales. Evidence strongly supports the conclusion that, from the perspective of editors and publishers, not all books are created equal. Beyond advances, contracts for books that are expected to sell well are more likely to include favorable terms like higher royalty rates, higher levels of marketing support, "glam" packages (e.g., for hair, makeup, and wardrobe services), and airfare for authors. Publishers print more of the books they think will do well; circulate more advance copies of such books to reviewers or influencers to create excitement; push for interviews with more media outlets; and schedule book-tour appearances in more locations. Anticipated top-selling books also get more attention from marketing and sales teams. For example, Dr. Hill determined that S&S and PRH spend, on average,

under $10,000 on marketing for books with advances under $250,000, and between $40,000 and $90,000 on marketing for books with advances over $250,000:



The fact that the Big Five publish 91 percent of anticipated top sellers also supports a finding that the authors of such books have unique needs and preferences. Although smaller publishers can sometimes put out an anticipated top-selling book, it is the Big Five who have the back lists and the marketing, publicity, and sales advantages necessary to consistently provide the high advances and unique services that top-selling authors need. It is precisely those specialized needs that make the authors of anticipated top-selling books vulnerable to targeting for price reductions. Publishers of anticipated top-selling books know that such authors are not able to find adequate substitutes for publishing their books because of their unique needs and preferences. See id. Those publishers therefore can target authors of anticipated top-selling books for a decrease in advances (prices) because it is not as likely that such a price decrease will cause the publishers to lose a book. *See Wilhelmsen*, 341 F. Supp. 3d at 56-57 (finding targeted buyer market where market was characterized by individual negotiations and customers had unique needs and preferences); *Staples II*, 190 F. Supp. 3d at 127 (finding targeted buyer market where industry recognized customers as a distinct group that needed specific prices and services); *see also* [2010] Merger Guidelines § 4.1.4.

Although the defendants proclaim that no one in the industry uses the term "anticipated top seller," that does not mean that such books do not exist. *See Wilhelmsen*, 341 F. Supp. 3d at 51-52 (rejecting defendant's argument "that the definition of Global Fleets does not accord with commercial reality, given that [defendants do not] use the FTC's definition of that term . . . ."); *see also Le v. Zuffa, LLC*, 216 F. Supp. 3d 1154, 1159, 1165-66 (D. Nev. 2016) (denying motion to dismiss that was based in part on defendant's argument that "Elite Professional MMA fighters" is not a term used in the industry). In fact, market participants have other names for expected top sellers, such as "lead titles" or "priority titles." Regardless of

nomenclature, clear evidence demonstrates that the practice of identifying and giving special support to the books that will drive sales is common. The government's defined market thus reflects "commercial realities" in the publishing industry. *United States v. Grinnell Corp.*, 384 U.S. 563, 572 (1966).

The defendants' position that individual publishers are unable to anticipate which books will be top sellers is unsupportable. That contention is contradicted by the universal industry practice of making a sales estimate for every single book before offering an advance, and credible testimony that there is often consensus among editors and publishers about which books will be popular with readers. The defendants' high share of the book-acquisition market and their substantial profit margins strongly indicate that they are successfully choosing books that people want to read. To be sure, editors often offer a range of advances for any given book, and the defendants correctly note that there are many examples of books that were unexpected best sellers, such as Stephen King's Carrie, or Marie Kondo's The Life-Changing Magic of Tidying Up. But it is commonplace for multiple editors to gravitate to the same book, as evidenced by the routine occurrence of competitive auctions; and the defendants do not dispute that there is a general correlation between author advances and book sales. That is strong evidence that the book-acquisition process is not random. Indeed, whenever a publisher submits a bid of $250,000 or more for a book, that publisher has determined that the book is likely to be a top seller and knows that the competitors for the book are likely to be limited to the Big Five. These practical indicia in the publishing industry strongly support the existence of the identified relevant market.

One high-end submarket case that the Court finds highly relevant is *Syufy Enterprises v. American Multicinema, Inc*. In *Syufy*, the Ninth Circuit upheld a relevant submarket "for [the] exhibition of industry anticipated top-grossing motion pictures in the San Jose area." 793 F.2d at 994. Anticipated blockbusters, the court explained, "are identifiable . . . on the basis of such criteria as national advertising support, longer playtimes, guaranteed rentals, famous stars, directors and producers, booking in first class theatres, and lucrative terms offered for the pictures by exhibitors." *Id*. at 994-95. Those indicia are analogous to some of the features of anticipated top-selling books, such as: more substantial marketing, publicity, and sales support; authors who are prominent or have a track record of success; and higher advances. Moreover, the appellant in *Syufy* challenged the existence of the market for "anticipated top-grossing motion pictures" by making arguments similar to those pressed by the defendants here, insisting that the market was "ex post facto and ad hoc," that "all first run films are in substantial competition with each other," and that such films "possess no special characteristics that differentiate them from less successful films from an ex ante perspective." *Id*. at 994. This Court joins the Ninth Circuit in rejecting such arguments. As discussed, distinctive characteristics set anticipated top-selling books apart from the rest of the pack.

In sum, this case demonstrates that "[w]hatever the market urged by the [government], the other party can usually contend plausibly that something relevant was left out, that too much was included, or that dividing lines between inclusion and exclusion were arbitrary." *FTC v. Tronox Ltd.*, 332 F. Supp. 3d 187, 202 (D.D.C. 2018)

(quoting 2B Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law ¶ 530d (4th ed. 2014) [hereinafter Areeda, Antitrust Law]). Yet "[t]he Supreme Court has wisely recognized there is 'some artificiality' in any boundaries, but that 'such fuzziness' is inherent in bounding any market." *Id*. (quoting Areeda, Antitrust Law ¶ 530d); *Anthem*, 236 F. Supp. 3d at 193 ("The 'market,' as most concepts in law or economics, cannot be measured by metes and bounds." (quoting *Times-Picayune Publ'g Co. v. United States*, 345 U.S. 594, 611 (1953)). Market definition is more art than science, *see RAG-Stiftung*, 436 F. Supp. 3d at 312-13, and it is critical to remember that the goal of the exercise is to enable and facilitate the examination of competitive effects. *See Brown Shoe*, 370 U.S. at 320-22; *Cont'l Can*, 378 U.S. at 452–55. In this Court's view, the government has easily cleared the bar.

NOTES

1. On October 31, 2022, Judge Pan entered an order finding that the proposed acquisition by Penguin Random House of simon & Schuster, if consummated, would violate Section in the market for the U.S. publishing rights to anticipated top-selling books and entered a permanent injunction blocking the deal.

2. Although the parties initially indicated they they would to appeal the decision, in November 2022, Paramount Global (the parent company of Simon & Schuster) announced that it was exercising its unilateral right under the merger agreement to terminate the $2.175 billion deal. Following the termination, Bertelsmann paid a $200 million antitrust reverse breakup fee to Simon & Schuster's parent company, Paramount Global, as provided in the merger agrement.

3. In March 2023, Paramount Global initiated reauctioned Simon & Schuster. In August 2023, private equity firm KKR emerged as the successful bidder, agreeing to acquire Simon & Schuster for $1.62 billion in an all-cash deal $555 million less thatn the Bertelsmann purchase price. The KKR transaction was completed in October 2023. Under KKR's ownership, Simon & Schuster became a standalone company, with Jonathan Karp remaining as CEO to ensure leadership continuity.