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NANCY MAYER WHITTINGTON, CLERK
U.S. DISTRICT COURT

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

FEDERAL TRADE COMMISSION,
600 Pennsylvania Ave., N.W.
Washington, D.C. 20580

Plaintiff,

v.

BLOCKBUSTER, INC.,

Defendant.

Ci
CASE NUMBER: 1:05CV00463
JUDGE: Ellen Segal Huvelle
DECK TYPE: Antitrust
DATE STAMP: 03/04/2005

**COMPLAINT FOR INJUNCTIVE RELIEF PURSUANT
TO SECTION 7A(g)(2) OF THE CLAYTON ACT AND
SECTION 13(b) OF THE FEDERAL TRADE COMMISSION ACT**

Pursuant to Section 7A(g)(2) of the Clayton Act, 15 U.S.C. § 18a(g)(2), and Section 13(b) of the Federal Trade Commission Act, 15 U.S.C. § 53(b), the Federal Trade Commission ("Commission"), by its undersigned attorneys, seeks a temporary restraining order, injunction, and order pursuant to Section 7A(g)(2) enjoining the acquisition by defendant Blockbuster, Inc. ("Blockbuster") of any interest in Hollywood Entertainment Corporation ("Hollywood"), until Blockbuster has substantially complied with the premerger notification reporting requirements set forth in Section 7A of the Clayton Act.

Jurisdiction and Venue

1. This is a statutory cause of action against a party who failed to file a sufficient premerger submission in this district. This Court has jurisdiction over the defendants and over

the subject matter of this action pursuant to Section 7A(g)(2) of the Clayton Act, Section 13(b) of the FTC Act, and 28 U.S.C. §§ 1331, 1337, 1345.

2. Venue is proper pursuant to Section 12 of the Clayton Act, 15 U.S.C. § 22, and 28 U.S.C. § 1391(b), and (c), because the cause of action arose in this district, where Blockbuster failed to make a complete response to the Commission's Request for Additional Information.

The Parties

3. The Commission is an administrative agency of the United States government with its principal offices at 600 Pennsylvania Avenue, NW., Washington, D.C. 20580. The Commission is charged, *inter alia*, with administering the premerger notification and waiting period requirements of Section 7A of the Clayton Act, 15 U.S.C. § 18a, and enforcing Section 7 of the Clayton Act, 15 U.S.C. § 18, and Section 5 of the FTC Act, 15 U.S.C. § 45, by preventing acquisitions that may substantially lessen competition in any line of commerce in any section of the country. The Commission also is authorized to seek preliminary injunctions whenever it has reason to believe these laws are being violated (FTC Act § 13(b), 15 U.S.C. § 53), and to enforce the Hart-Scott-Rodino Antitrust Improvement Act's reporting and waiting period requirements (Clayton Act § 7A; 15 U.S.C. § 18a).

4. Blockbuster is incorporated in the State of Delaware with its principal place of business in Texas. Blockbuster is the largest movie and video game rental outlet in the United States. It operates approximately 4,600 company stores across the United States, and franchises approximately 1,800 additional store locations. Blockbuster estimates its U.S. revenues for fiscal year 2004 at \$4.2 billion.

The Cause of Action

5. On December 28, 2004, Blockbuster announced its intention to launch a cash tender offer to purchase all of the outstanding shares of Hollywood in a transaction valued at approximately \$1 billion (including Blockbuster's assumption of Hollywood debt outstanding).¹

Hollywood is a leading United States movie and video game rental outlet, second only to Blockbuster in revenues. Hollywood operates nearly 2,000 store locations in the United States, and estimates its U.S. revenues for fiscal 2004 at \$1.8 billion.

6. Section 7A(a) of the Clayton Act, as amended by Pub. L. 106-553, 114 Stat. 2762 ("2000 Amendments"), requires persons with more than \$100 million in total assets or net sales to file premerger notification reports with the Commission before acquiring, directly or indirectly, more than \$50 million in voting securities or assets of any person engaged in manufacturing with total assets or annual net sales of \$10 million. As part of the Notification and Report Form required by Section 7A, an officer of the filing party must certify that the filing is "true, correct, and complete in accordance with the statute and rules." See 16 C.F.R. § 803.6.

7. Section 7A(b) provides that upon filing a premerger notification report, a party wishing to make an acquisition must delay consummating the transaction for at least 30 days (15 in the case of a pure cash tender offer) in order to give the Commission an opportunity to review the transaction and determine whether to investigate the transaction further or challenge it.

¹ Blockbuster has modified or supplemented its offer twice since its original announcement. On February 2, 2005, it announced that it was raising its initial offer of \$11.50 per share (payable in cash) to \$14.50 (payable in a combination of \$11.50 in cash and \$3.00 in Blockbuster stock). On February 11, 2005, it announced the commencement of a tender offer to purchase for cash \$225 million in debt previously issued by Hollywood.

8. Section 7A(e) provides that, during the initial waiting period, the Commission may request additional information or documentary material relevant to the proposed transaction (a "Second Request"). The effect of making such a request for additional information is to extend the waiting period for consummation of the acquisition until 30 days (10 days in the case of a cash tender offer) after the date on which the Commission receives a complete response to its request for additional information. *Id.*; 16 C.F.R. § 803.20(c). A complete response is one that either: (a) sets forth all the information and provides all the documentary material required to be submitted pursuant to the request; or (b) in the event a person is unable to provide a complete response, a detailed statement of reasons for non-compliance in accordance with 16 C.F.R. § 803.3. Section 7A(e)(2) further provides that if a proper submission is made under that Section, the thirty-day waiting period extension begins, although it may be further extended by a United States district court on application by the Commission pursuant to Section 7A(g)(2), if the acquiring person (in the case of a tender offer) has not substantially complied with the request for additional information. All submissions of additional information and documentary material must be filed where designated by the Commission or, if no designation is made, with the Commission's Pre-Merger Office in Washington, DC.

9. Blockbuster's proposed acquisition of Hollywood is a reportable transaction under Section 7A.

10. On December 28, 2004, Blockbuster filed a premerger Notification and Report Form in connection with its announced intention to launch a tender offer for the outstanding shares of Hollywood. As part of that filing, Edward B. Stead, Blockbuster's Executive Vice-President and General Counsel, certified that the filing was "true, correct, and complete."

The Commission's Second Request

11. On January 12, 2005, the Commission, pursuant to Section 7A(e)(1) of the Clayton Act, 15 U.S.C. § 18a(e)(1), and 16 C.F.R. § 803.20, issued to Blockbuster a Second Request. The first paragraph of the Commission's request informed Blockbuster that "[i]f the company believes that the required search or any other part of the Request can be narrowed in any way that is consistent with the Commission's need for documents and information, you are encouraged to discuss such questions and possible modifications with the Commission representative identified on the last page of this Request."

12. Included within this Second Request was Specification 17, which required Blockbuster to produce specific categories of data for each company store relating to, *inter alia*, each store's pricing, non-price terms, incentive programs, late fees, membership fees, discounts, and other benefits offered to customers.

13. The Second Request also contained Instruction W, which instructed Blockbuster to indicate for each question it is unable to answer fully, "why such answer is incomplete, the efforts made by the company to obtain the information, and the source from which the complete answer may be obtained." The purpose of Instruction W is to allow Blockbuster to explain why it did not provide certain information in response to the Second Request, in a way that the Commission staff reviewing the response can rely upon in assessing Blockbuster's compliance with the Second Request.

Blockbuster's Response to the Second Request

14. On February 4, 2004, Blockbuster, through its Vice-President and Senior Corporate Counsel, Judy C. Norris, certified under oath, pursuant to 16 C.F.R. § 803.6, that it

had substantially complied with the Commission's Second Request by submitting the information and materials specified in the Second Request.

15. In the course of reviewing Blockbuster's response to the Second Request, the Commission staff discovered that Blockbuster's response to the Second Request was incomplete in multiple respects. Most significant, in terms of its impact on the Commission's investigation, Blockbuster, in its response to Specification 17(a) of the Second Request, provided incorrect information relating to pricing, in the form of rental fees, at specific Blockbuster stores. As a result of a Blockbuster "programming error," more than 60,000 of the approximately 120,000 data points contained in Blockbuster's original dataset were inaccurate. The Commission's economics staff had relied on that data to try to use econometric analyses to assess the likely competitive effects of the acquisition in order to guide the Commission's decision-making process in connection with the proposed acquisition. However, all of the statistical analysis that Commission staff had performed using that pricing data was fatally flawed, and therefore useless to the Commission.

16. Commission staff identified to Blockbuster's counsel, in an oral conversation on February 16, the "discrepancies" in the data that Blockbuster had provided. Counsel for Blockbuster thereafter admitted, in an e-mail message dated February 22, 2005 that "a programming error was made in collecting the specification 17 data, so that it is inaccurate." Blockbuster counsel attached revised data responsive to specification 17(a) to that same e-mail message on February 22, 2005 - 18 days after certifying that it was in substantial compliance with the Second Request. While updating its response to now include the presumably correct

pricing data, Blockbuster did not re-certify its substantial compliance to reflect the date on which it had actually submitted accurate pricing data in response to Specification 17(a).

17. In addition to the deficiencies in response to Specification 17(a), Blockbuster failed to provide complete responses to several other Specifications of the Second Request. For example, subpart (e) of Specification 17 requires the production of data regarding "any late fees applied to late returns of rentals" for "each company store." Blockbuster's response to Specification 17(e), however, only provided data for approximately 400 of the approximately 4,600 company stores it operates in the United States. Only in a submission of late March 1, 2005, has Blockbuster provided what appears to be the complete data in response to Specification 17(e). The original data disk produced by Blockbuster contained 2.8 megabytes of data and had approximately 65,000 data rows. The disk submitted on March 1 contained 96 megabytes of data and approximately 873,000 data rows. The original data disk, therefore, was missing over 800,000 rows of responsive information.

18. Timely submission of the pricing information required by Specification 17(a) and 17(e) is critical to the Commission's economic analysis of the potential competitive effects of Blockbuster's proposed acquisition. The type of econometric analyses that the Commission's staff have applied in this investigation are complex, and require substantial Commission resources. The accurate pricing data that Blockbuster did not provide until February 22 is highly probative information to that analysis. The result of Blockbuster's failure to provide the accurate data, combined with its theory that its initial submission constituted substantial compliance, would be to reduce, by over half, the statutory period that Congress has provided to the Commission to use the information it is entitled to obtain from Blockbuster.

19. During the time that the Commission would have had if Blockbuster's submission of data in response to Specification 17(a) and 17(e) had been timely, the Commission would be able to conduct the complex economic analyses that would help inform its decision making in connection with Blockbuster's proposed acquisition of Hollywood. Because of Blockbuster's serious errors, however, the Commission has not yet had a sufficient opportunity to complete these analyses.

The Commission's Two Notices of Deficiencies

20. After reviewing Blockbuster's response to the Second Request, Commission staff notified Blockbuster's counsel in two letters, both dated February 24, 2005, of the numerous deficiencies, including Blockbuster's failure to comply with Specification 17(a) and 17(e), that had been identified in the Second Request. Each of those letters clearly states that it constitutes a notice of deficiency under 16 C.F.R. 803.10(c)(2), and that therefore the statutory waiting periods specified in 16 C.F.R. §§ 803.10(b)(2)(i) has not begun.

Blockbuster's Response to the Two Notices

21. In response to the Commission's letters, Blockbuster counsel delivered to the Commission on February 28 a letter challenging the Commission's position that Blockbuster was not in substantial compliance with the Second Request. With respect to its untimely response to Specification 17(a), for example, Blockbuster took the position that the Commission had not been prejudiced by its failure to provide store pricing data on a timely basis, stating that it "defies imagination that the staff has been so impeded in the investigation that a court should find that Blockbuster was not in substantial compliance with its original February 4 response."

22. Blockbuster on March 2, 2005, filed an appeal with the Commission's General Counsel, pursuant to Section 2.20 of the Commission's Rules of Practice, 16 C.F.R. § 2.20, of the notices of deficiency that Blockbuster had received from the Commission's representatives. In its March 3, 2005 response to that appeal, the Commission's General Counsel stated that Blockbuster was not in substantial compliance at least until it had corrected its failures to submit accurate data.

Blockbuster Has Not Complied With Its Legal Obligations

23. By failing to provide complete and accurate information responsive to Commission Specification 17 (as well as other Specifications), Blockbuster has not complied with the premerger reporting obligations set out in Section 7A(e)(2) and 16 C.F.R. § 803.20.

24. Section 7A(g)(2) of the Clayton Act provides that if any person fails substantially to comply with the notification requirement of Section 7A(a) or any request for the submission of additional information or documentary material pursuant to Section 7A(e)(1), a United States district court, upon application of the Commission, "shall extend the waiting period ... until there has been substantial compliance." Section 7A(g)(2) further provides that, upon application, the district court "may order compliance" and "may grant such other equitable relief as the court in its discretion determines necessary or appropriate."

25. As noted above, Blockbuster has refused to recertify both its original Notification and Report Form and its substantial compliance with the Second Request. Moreover, counsel for Blockbuster has refused even to acknowledge the deficient character of its certification.

26. Blockbuster has stated in the press, and has stated to the Commission, its intention to effect its proposed acquisition of Hollywood as soon as possible, indicating that unless the

Commission takes action by mid-March Blockbuster will go ahead with its acquisition and force the Commission to bring suit to stop the transaction. This timing is based on Blockbuster's February 4 certification which, if unchallenged, would result in a termination of the statutory waiting period on March 7, 2005.

27. Thus, unless enjoined by this Court, Blockbuster may acquire Hollywood as early as March 8, 2005. Accordingly, a temporary restraining order and an injunction enjoining consummation are necessary to ensure compliance with the requirements of Section 7A of the Clayton Act and to give the Commission and its staff the time provided by Congress for evaluation of the proposed acquisition.

WHEREFORE, the Commission prays for an order:

- a. Enjoining Blockbuster from acquiring, directly or indirectly, any interest in Hollywood until Blockbuster has conducted a thorough search for responsive material and recertified its original Notification and Report Form, provided all responsive information sought by the Commission in the Second Request, recertified its substantial compliance with the Commission's Second Request, and complied with the statutory waiting period required by Section 7A of the Clayton Act; and
- b. Awarding such other relief as this Court shall deem just and appropriate.

Respectfully Submitted,

John D. Graubert (D.C. Bar No. 370670)
Acting General Counsel

Susan Creighton, Director
Bureau of Competition

A handwritten signature in black ink, appearing to read "Michael Bloom", written over a horizontal line.

Michael Bloom
Director of Litigation

Michael H. Knight
Assistant Director

Bureau of Competition
Federal Trade Commission
600 Pennsylvania Avenue, N.W.
Washington, DC 20580
(202) 326-2475