IN THE 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. 1:15-cv-00256-APM

FILED UNDER SEAL

DEFENDANTS' PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

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I. INTRODUCTION

A. THE PARTIES

1. Defendant Sysco Corporation ("Sysco") is a publicly traded corporation headquartered in Houston, Texas. Compl. ¶ 24.

2. Defendant US Foods, Inc. ("USF" or "US Foods") is a privately held corporation based in Rosemont, Illinois, and is a wholly owned subsidiary of Defendant USF Holding Corp., which is controlled by investment funds of Clayton, Dubilier & Rice, Inc. and KKR & Co., L.P. Compl. ¶ 26.

B. THE MERGER

3. On December 8, 2013, Sysco agreed to acquire all shares of USF in a transaction valued at $8.2 billion. The merger agreement expires on September 8, 2015. Compl. ¶ 28.

4. As a corollary to the merger agreement, Sysco and USF executed an asset purchase agreement with Performance Food Group ("PFG") to sell 11 USF distribution centers to PFG. *See generally* DX-00064, Asset Purchase Agreement. The parties also executed a Transition Services Agreement. DX-01382. These agreements obligate USF to divest these 11 strategically located distribution centers with $4.6 billion in current sales and the capacity to handle nearly $1 billion more in sales without incurring additional capital expenses; all the working capital and trucks for these distribution centers; all customers under contracts; more than 4,400 USF personnel; and use of USF "private label" products at those facilities for up to three years. *Id.*

II. PROCEDURAL HISTORY

5. By a 3-2 vote, the FTC authorized the filing of an administrative complaint in the FTC's Article I court regarding the proposed merger. That complaint, filed February 19, 2015, alleged two distinct product markets: broadline foodservice distribution (sold to "Local Customers"),

Admin. Compl. ¶¶ 30, 45; and broadline foodservice distribution sold to "National Customers," *id.* at ¶¶ 31, 34. The Commission also authorized the FTC Staff to seek a preliminary injunction in support of the Administrative Action. The Staff filed its Complaint in the instant matter that same day, Dkt. 1, seeking a preliminary injunction under section 13(b) of the FTC Act, 15 U.S.C. § 53(b). The FTC alleged the same product markets as in its administrative complaint. *See* Compl. ¶¶ 40, 44, 50.

6. At a March 4, 2015 status conference, the preliminary injunction hearing was scheduled to commence on May 5, 2015, with a seven and a half weeks for all discovery. In that period of time, approximately 14.8 million documents were produced, and 72 depositions were taken. Defendants obtained 65 new or counter declarations from industry participants, and the FTC obtained 25 new or counter declarations, in addition to the 99 that were filed with the FTC's Complaint.

7. The hearing commenced on May 5, 2015, and continued on May 6-8 and May 11-14. A total of 20 witnesses testified, either live or by video deposition, generating 2427 transcript pages. A total of 185 declarations were admitted into evidence, as well as 3554 exhibits, and 72 depositions.

III. <u>PRELIMINARY FINDINGS</u>

A. THE FTC IGNORES MARKETPLACE REALITIES

8. The evidence is overwhelming that the proposed merger is intended to capture the enormous efficiencies, in excess of $1 billion in cost savings, that will occur when Sysco and US Foods combine. *See infra* §§ IV.E; IX.E. These savings will enable the merged entity to compete more effectively, including by lowering prices, to the benefit of their customers. With the exception of a handful of suspect customer and competitor declarations procured by the FTC, speculating that prices *might* go up, there is no evidence that prices will increase as a result of the

merger. No evidence of any kind came from Sysco's or US Food's files suggesting that the merged entity intends to raise prices. Only one hearing witness even suggested that he would be forced to accept a price increase, *see infra* § VI.C.2, Appx A at § III.B; the rest testified to their options post-merger, *see generally infra* Appx A. These two facts—extraordinary efficiencies coupled with the absence of any credible evidence that prices will increase—doom the FTC's case. No merger has ever been enjoined in these circumstances.

9. Importantly, the FTC's case depends on a contrived market definition not shared by industry participants. The FTC contends that the relevant product markets consist of broadline foodservice distribution services sold to "National Customers," and broadline foodservice distribution services sold to "Local Customers." *See* Compl. ¶¶ 40, 44, 50. Using those fictitious definitions, Dr. Israel, the FTC's expert, calculated high market shares. But the record is bereft of credible evidence from industry participants suggesting that they analyze or even think of the food distribution market in this way. Indeed, the record contains overwhelming evidence from industry participants who consider Sysco and USF to have around 25% market share combined. *See infra* § VI.B. A market definition not shared by industry participants is entitled to little weight. *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962). The FTC concocted these markets with the singular purpose of calculating high market shares, seeking a presumption of illegality.

10. The FTC's case is at odds with actual industry practices. The FTC ignores that its so-called "National Customers" in *all* of the industry sectors at issue have already demonstrated that they can and do divert their business away from so-called "national" broadline distributors by purchasing on a regional basis. *See infra* § VI.E.2. This is real-world evidence of substitution out of the FTC's "National Customer" market even at current prices. *See In re R.R. Donnelley &*

Sons Co., 120 FTC 36, 78 (1995) (rejecting FTC's price discrimination market in part because "existing substitution at current (presumptively competitive) prices" demonstrated that a price increase would not be profitable). Similarly, there is real-world evidence of "National Customers" who can and do divert their business away from national broadline distributors by purchasing from alternative distribution channels—especially systems and specialty distributors. *See infra* § VI.F.1. And the evidence is simply overwhelming that the FTC's so-called "Local Customers" have a plethora of options besides national broadliners, including using regional and local broadline distributors, specialty distributors and cash-and-carry. *See infra* § VI.F.2. There is no need for economists to speculate how the FTC's and Dr. Israel's so-called "National" and "Local" customers *might* respond to a price increase. There is ample real-world evidence of what they *actually* do and will continue to do. "Antitrust theory and speculation cannot trump facts, and even Section 13(b) cases must be resolved on the basis of the record evidence relating to the market and its probable future." *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 116-17 (D.D.C. 2004).

11. The FTC has failed to establish either of its product markets, has failed to establish its geographic markets, and has failed to demonstrate any anti-competitive effects. The foodservice distribution industry, after the merger, will remain aggressively competitive. And the equities weigh in favor of the merger.

12. Appendix A summarizes the key points made by each hearing witness, organized as follows: Sysco and US Foods witnesses, "National Customer" witnesses, "Local Customer" witnesses, group purchasing organization ("GPO") witnesses, competitor witnesses, and experts.

B. THE FTC HAS FAILED TO ESTABLISH THE ELEMENTS OF ITS CASE

13. The FTC has failed to establish either of its product markets. As to "National Customers" for broadline foodservice distribution, the FTC calculated market shares by referencing internal administrative lists kept by the companies that designated certain customers as "National." *See infra* § VI.E.1. The market shares the FTC imputes to the Defendants are not shares for broadline distribution services; they are supposedly shares of the "National Customer broadline distribution market." But the FTC produced no analysis, expert or otherwise, of whether customers on those lists represent an economically meaningful segment of the market or possess the characteristics the FTC attributes to them. The evidence is clear that they do not. *See infra* §§ VI.D-E.

14. Moreover, the evidence demonstrates that "National Customers" can discipline a price increase by threatening to or actually procuring goods regionally, *see infra* § VI.E.2, or by credibly threatening to allocate or actually allocating a material portion of their demand to systems or specialty distributors, *see infra* § VI.F.1. The FTC calculates that the total sales in the FTC's "National Broadline" market are in the range of $28-34 billion, but the FTC and its expert improperly exclude relevant sales in the range of $100-plus billion. *See infra* § VI.B . By doing so, the FTC calculates fantastically high market shares. As to "Local Customers" for broadline foodservice distribution, they can, and do, substitute or credibly threaten to substitute demand for fungible products to local and regional broadliners, specialty distributors and cash-and-carry firms to discipline a price increase. *See infra* § VI.F.2.

15. Contrary to its Complaint, the FTC now appears focus on alleged harm to two types of "National Customers"— "healthcare" and "hospitality." Hearing Tr. at 30:1-8. The FTC has never alleged or attempted to prove (through expert or other testimony) that either customer

category could be a separate, relevant antitrust market. The Commission did not approve the issuance of a complaint based on these markets,they are ill-defined, there is no expert analysis or testimony that would support the issuance of preliminary injunction based just on them, *see infra* ¶¶ 233-237, and in any event the evidence is clear that customers in these segments will not be harmed, *see infra* §§ VI.G.1-4.

16. The FTC has failed to establish relevant geographic markets. The entire United States is not the relevant geographic market for "National Customers" because contracts are negotiated and prices are set regionally and locally for "National Customers," particularly for customers who purchase regionally. *See infra* § VII.B. For "Local Customers," the FTC's local geographic markets are based on an analysis that arbitrarily excludes competition from broadline distributors who already serve customers within those geographies. *See infra* § VII.C.

17. The FTC has failed to establish anti-competitive effects. "National Customers" will have numerous viable alternatives to the merged entity, including New PFG, *see infra* § IX. B, other broadline distributors, *see infra* § IX.C, and alternative distribution modes, *see infra* § VI.F.1. The FTC's "top two choices theory" and its economic analysis of potential harm are fundamentally flawed, as the model quantifying the supposed harm turns on two mistaken inputs, market shares, and margins. *See infra* § VII.B.2. For many of the FTC's local markets, Dr. Israel's methodology and arbitrary market share calculations are the only evidence of harm. *See infra* § VII.D.1. In the other local markets, the evidence overwhelmingly demonstrates that competition is robust and that "Local Customers" have myriad distribution options across multiple channels. *See infra* §§ VII.C-D. The FTC's evidence to the contrary is not credible. *See infra* § VI.C.3.

18. Aggressive competition will continue to exist in the food distribution industry and will constrain post-merger pricing. The divestiture to PFG will strengthen an already fierce competitor and add yet another nationwide distribution option for those customers that prefer a nationwide distributor. *See infra* § IX.B. Other strong competitors, like Distribution Market Advantage ("DMA"), Gordon, Reinhart, and Restaurant Depot will continue to compete with the merged entity, *see infra* § IX.C, while smaller players, like Shetakis and Shamrock, continue to expand, *see infra* § IX.D. Finally, while the harm from this merger is, at most, unlikely, the evidence demonstrates that there will be real, merger-specific efficiencies that will pass through to customers. *See infra* § IX.E.

IV. INDUSTRY BACKGROUND

A. THE FOODSERVICE DISTRIBUTION INDUSTRY IS HIGHLY COMPETITIVE WITH MANY DISTRIBUTORS SERVING DIVERSE CUSTOMERS

19. Customers are businesses that serve food to consumers "away from the home—including restaurants, school cafeterias, hotels, and hospitals." *See* FTC Mem. at 1.

20. The foodservice distribution industry in the United States has "very formidable competition." DeLaney (Sysco), Hearing Tr. at 1324:7-8. More than 16,000 companies sell and distribute food and related products to the hundreds of thousands of customers that provide food to consumers who eat outside the home. *Id.* at 1324:14-15; [redacted]

21. The competitors in the foodservice distribution industry range from broadline distributors (national, regional, and local), to specialty distributors, to systems distributors, to cash and carry and club stores. DeLaney (Sysco), Hearing Tr. at 1324:8-13; Sonnemaker (Sysco), Hearing Tr. at 1577:5-7; Schreibman (USF), Hearing Tr. at 1450:19-24; Lynch (USF), Hearing Tr. at 1701:11-17; 1730:21-1731.

22. New competitors can easily enter the industry as there are low barriers to entry. DeLaney (Sysco), Hearing Tr. at 1319:11-12 ("It's not hard to get into this industry."); *see also* DX-00272, Schreibman (USF) Dep. 74:15-17 ("That does not mean that there are high barriers to entry in our industry, in fact, very low barriers to entry."); [redacted]

23. There are hundreds of thousands of customers in this "incredibly diverse industry," Sonnemaker (Sysco), Hearing Tr. at 1559:9-12, who are "all different in some ways," DeLaney (Sysco), Hearing Tr. at 1320:24-1321:2. Foodservice distribution customers are "anyone that prepares food away from home. So restaurants, nursing homes, fast food, you know, caterers, convention centers, anyone that prepares food away from home is considered our customer." Brawner (Sysco), Hearing Tr. at 1783:14-20. Customers range from mom-and-pop shops (*e.g.*, [redacted], to nationwide fast food (*e.g.*, [redacted], and upscale dining chain restaurants (*e.g.*, [redacted], from independent guesthouses (*e.g.*, [redacted], to nationwide hotel chains [redacted]. Some are government agencies, such as the Defense Logistics Agency, which serves active military members on bases across the nation. Sonnemaker (Sysco), Hearing Tr. at 1648:5-12. Foodservice management companies (or FSMs) are large-scale aggregators that contract to supply foodservices to a wide array of locations, including, hospitals, airports, cafeterias, and

office buildings. *See* DX-01359, Bresnahan Rpt. at 20.

B. CUSTOMERS HAVE MANY OPTIONS FOR FOOD DISTRIBUTION

24. Foodservice distributors, like Sysco and USF, are intermediaries between manufacturers (also called suppliers or vendors) that produce the products and the customers that use them. Foodservice distributors provide the services that ensure that products get from manufacturers to customers, including warehousing and trucking. DeLaney (Sysco), Hearing Tr. at 1347:7-9.

25. Competitors in the foodservice distribution industry constantly evolve to keep up with changing customer demands, adjusting the number and variety of individual products (also called stock keeping units, or SKUs) they offer, the quality of their products, their product focus, delivery options, geographic reach, and marketing support. *See* PX01460, Sysco Response to VA RFP, at PX01460-004 ("inventories at Operating Companies are dynamic and will occasionally change to meet the customer's needs"). Depending on where the competitor falls along the spectra for these many characteristics, it may be labeled a broadline distributor, systems distributor, specialty distributor, or a cash-and-carry store. *See* DX-01359, Bresnahan Rpt. at 19-20.

26. Generally speaking, broadline distribution's distinguishing characteristic is that distributors carry a wider array of SKUs than distributors in competing distribution channels. DX-01359, Bresnahan Rpt. at 19. But broadline distributors vary immensely:

- Some are primarily local. For example, McDonald Wholesale is a "substantial force" in Eugene, Oregon. Sonnemaker (Sysco), Hearing Tr. at 1561:10-12. Staunton Foods, and Schenck Foods serve customers in Virginia. Brawner (Sysco), Hearing Tr. at 1803:19-21. And Orrel's, EG Forrest, and Jennette Brothers serve customers in North Carolina. *Id.* at 1801:19-25.

- Others are regional. [redacted]

[redacted]

- Even larger broadline distributors are multi-regional. [redacted]

- The largest distributors have distribution capabilities across the continental United States. [redacted]

27. Systems distributors generally service higher volume customers, and frequently those with a larger number of proprietary products. DX-01359, Bresnahan Rpt. at 19.

28. Specialty distributors "focus primarily on a specific category" of food products, Brawner (Sysco), Hearing Tr. at 1798:5-10, but offer a broader assortment of products beyond that product category, Schreibman (USF), Hearing Tr. at 1452:6-16. There are many strong local specialty distributors. Sonnemaker (Sysco), Hearing Tr. at 1562:23-1563:1. There are also national and multiregional specialty distributors, like Pro*Act, an "affiliation of produce houses across the country." *Id.* at 1584:19-23; *see also* Lynch (USF), Hearing Tr. at 1721:13-1722:25; DX-01938, Sysco and US Foods presentation, "FTC meeting," at slide 13 (Apr. 29, 2014) (listing as national specialty distributors Pro*Act, Produce Alliance, The Bruss Company, Halperns, Edward Don & Company, Wassterstrom, TriMark, Dairy Farmers of America, and

Dean Foods). Broadline foodservice distributors compete, even for nationwide accounts, with specialty distributors. Sonnemaker (Sysco), Hearing Tr. at 1585:11-20; [redacted]

29. Cash-and-carry and club stores have become serious competitors for foodservice customers. Brawner (Sysco), Hearing Tr. at 1798:20-24. Examples of these competitors are Restaurant Depot, a cash-and-carry store dedicated exclusively to servicing foodservice customers, [redacted], and Costco, a club store, [redacted]. Cash-and-carry stores carry thousands of items geared specifically to the needs of restaurants, caterers, schools, and churches. [redacted]; *see also* Schreibman (USF), Hearing Tr. at 1463:2-4 (estimating 6,000 to 6,500 SKUs in a typical Restaurant Depot warehouse). Cash-and-carry and club stores have not traditionally participated in RFPs, but Restaurant Depot recently participated in an RFP to distribute food to a California school system, and was awarded more business than Sysco or Shamrock. *Id.* at 1495:23-1497:7.

30. Although many cash-and-carry and club stores do not deliver, some do. Restaurant Depot's school system RFP required it to deliver. Schreibman (USF), Hearing Tr. at 1496:9-13. Costco offers delivery of anything in their stores to businesses in select metropolitan areas. Brawner (Sysco), Hearing Tr. at 1805:13-23; [redacted]

[redacted]

31. Restaurant Depot also offers creative distribution options to increase its market share. [redacted] Restaurant Depot's strategies have induced its customers to request lower prices from broadline distributors, like US Foods. Schreibman (USF), Hearing Tr. at 1494:16-19.

32. Many of the largest foodservice customers do not recognize any meaningful distinction between broadline and systems distribution and are indifferent between the two. Sonnemaker (Sysco), Hearing Tr. at 1582:1-13 (customers do not necessarily label themselves as systems

customers because there is "no real big distinction"); *see also* [redacted]

33. Indeed, many multi-unit restaurant customers can be serviced by either a systems or broadline distributor and many are serviced by both. For example, one chain with a nationwide footprint, Five Guys, moved from a national, sole-source contract with US Foods to a regional distribution model with some systems and some broadline. Lynch (USF), Hearing Tr.at 1701:10-1704:3; [redacted]. Systems distributors lose customers to broadline distributors. *See, e.g.*, [redacted]. And broadline distributors lose customers to systems houses. *See, e.g.*, Lynch (USF), Hearing Tr. at 1708:16-1709:1 (USF lost Krystal, a regional hamburger chain, to MBM, a systems distributor.) As a result, "systems" and "broadline" distributors often compete for the same customers. *See, e.g.*, Brawner (Sysco), Hearing Tr. at 1785:25-1786:12 (systems distributors would "love to have" Cheesecake Factory, a Sysco broadline customer).

34. "Broadline" distributors themselves do not necessarily recognize a distinction between systems and broadline. [redacted]

[redacted]

35. PFG, USF, and Sysco all blur the lines between systems and broadline. [redacted] Of Sysco's thirty-two systems customers, eleven are also broadline customers. Sonnemaker (Sysco), Hearing Tr. at 1580:15-18. USF does not distinguish between broadline and systems customers, instead serving customers out of broadline facilities that could be served by a systems distributor. Lynch (USF), Hearing Tr. at 1707:4-10.

36. The distinction between broadline and specialty distributors is likewise muddied. There may be considerable overlap between specialty distributors offering a wide variety of products

and smaller broadline distributors. *See, e.g.*, [redacted]

37. Specialty distributors often offer products outside of the product categories in which they specialize, including dry goods and janitorial goods. *See* Schreibman (USF), Hearing Tr. at 1453:6-23. It "is very typical for a specialty house [] to add product lines as their customers request it." Sonnemaker (Sysco), Hearing Tr. at 1562:5-10. As specialty companies establish relationships with their customers, "they become more aggressive and look into other [product] categories to satisfy that customer." Brawner (Sysco), Hearing Tr. at 1830:14-21. For example, Duck Delivery, a specialty produce distributor, expanded its offerings to serve all of Bellagio Pizza's foodservice needs. Sonnemaker (Sysco), Hearing Tr. at 1562:5-10; *see also* [redacted]

C. CUSTOMERS USE DISTRIBUTORS IN A VARIETY OF WAYS AND THERE IS NO ONE TYPE OF DISTRIBUTOR THAT CAN MEET THE NEEDS OF EVERY CUSTOMER

38. Similarly situated independent restaurants employ differing procurement strategies. [redacted]

[redacted]

39. Nationally-dispersed chain restaurants also employ diametrically opposed procurement strategies. [redacted]

40. In addition to the overlapping multitude of distribution channels offering customers fungible goods, customers have a number of options for how they structure their purchases. Sonnemaker (Sysco), Hearing Tr. at 1559:20-1560:6; DX-01359, Bresnahan Rpt. at 20-21.

41. Larger customers with high-volume demand frequently negotiate directly with manufacturers for the cost of the majority of products they purchase, allowing them to secure lower product costs and ensure product consistency. DeLaney (Sysco), Hearing Tr. at 1343:24-1344:6. [redacted]

42. [redacted]

[redacted]

43. Contracts negotiated directly with manufacturers often include the price for shipping the product from the manufacturer's location to a distribution center (inbound freight cost), relegating distributors to mere providers of drayage—*i.e.*, warehousing the product and trucking it to the customer. DX-01359, Bresnahan Rpt. at 19-21; *see also* DeLaney (Sysco), Hearing Tr. at 1343:24-1344:6. Under these arrangements, foodservice distributors make money only on last-mile delivery costs.

44. Some customers contract with distributors for both the procurement of goods and warehousing and delivery. Although customer contracting varies, the most common type is "cost-plus" contracting—the "cost" component referring primarily to the cost of the products themselves, and the "plus" component covering distribution costs and the margin earned by distributors. DX-01359, Bresnahan Rpt. at 20.

45. Many customers, known as "street customers," elect to purchase goods and delivery from distributors without a contract. Sonnemaker (Sysco), Hearing Tr. at 1560:7-17. Street customers typically negotiate with distributors weekly or daily on an item-by-item basis. *Id.* at 1560:12-16 ("Our sales reps have to go in and earn each case by line item every single time they go in and take an order."). Street customers are "the ongoing bread and butter of the business." *Id.* at 1560:16-17.

46. Other customers purchase their products through GPOs. GPOs themselves are not customers. [redacted] Rather, they are contracting agents—middlemen—who act on behalf of their members to negotiate lower cost of goods with manufacturers and distribution fees with

distributors. Schreibman (USF), Hearing Tr. at 1444:22-1445:5; Sonnemaker (Sysco), Hearing Tr. at 1590:10-16. More specifically, GPOs operate by aggregating the buying power of their members to obtain volume discounts from manufacturers. Schreibman (USF), Hearing Tr. at 1444:22-1445:2. In return, the GPO generally gets a fee from the manufacturer, and a fee from the distributor for the right to distribute product to a GPO member (who is the customer). *Id.* at 1444:22-1447:11. There is no direct financial relationship between the distributor and a GPO except the for fee that the distributor pays to the GPO—the GPO member generally pays the distributor directly for the cost of goods and delivery, and the distributor will receive a rebate from the manufacturer covering the difference between the GPO-negotiated price of the product and the price at which the distributor purchased it, called a "bill back". *Id.*

47. Members of GPOs join voluntarily, and the vast majority of GPOs do not require their members to purchase food products through the GPO's contracted distributors, *See* Schreibman (USF), Hearing Tr. at 1447:17-22 (GPO members can buy outside the GPO's "book of deals"); Lindahl (HPSI), Hearing Tr. at 1415:19 ("We [the GPO] don't own the customer"). Being a member of a GPO is not exclusive; members can belong to another GPO and/or can get food products from the foodservice distributor directly. *Id.* at 1413:9-19; *see also* [redacted]

48. Many GPOs leave it to members to determine which foodservice distributor or distributors will deliver the products. Lindahl (HPSI), Hearing Tr. at 1411:20-1421:1 (the customer determines which distributor to use); [redacted]

[redacted]

49. Given their immense buying power and cost structure, GPOs are exceedingly effective low-cost competitors with broadline distributors for the sourcing of products. *See* Sonnemaker (Sysco), Hearing Tr. at 1619:4-9 (there is overlap between how GPOs and Sysco and USF source their products); Schreibman (USF), Hearing Tr. at 1446:3-5 ("The GPO actually has a lower price for the product cost than we as a distributor are able to get from the manufacturing community."); [redacted]

50. [redacted]

[redacted]

51. Customers often combine strategies—and the products purchased under each—based on what best serves their unique business interest. For example, Interstate Hotels and Resorts, which arranges for food purchasing for certain of its hotels, does "a little bit of everything." Thompson (Interstate), Hearing Tr. at 204:9. Specifically, Interstate contracts with manufacturers for a substantial portion of its overall spend, and manages approximately 50 contracts with manufacturers. *Id.* at 203:22-204:3. Interstate is also a member of the Compass/Foodbuy GPO, and purchases from it. *Id.* at 204:4-7. Only then does Interstate rely on its broadline distributors (USF and PFG) "for the products that aren't met by the previous two options," *id.* at 204:7-9, as well as specialty distributors for certain items, *id.* at 216:1-6.

52. Generally, contracts are not awarded by formal RFP. Sonnemaker (Sysco), Hearing Tr. at 1595:20-22; Hausman, Hearing Tr. at 1982:10-17 (observing that only about 40% of procurement occurs in conjunction with an RFP). New contract business opportunities come about as the result of conversations foodservice distributors have with their customers to determine if the customer has any needs the distributor can fix or fill. Sonnemaker Tr. at 1595:25-1596:13.

53. Even in the event of an RFP, there are bilateral negotiations with the customer following the submission of the bid package and the foodservice distributor will alter their initial proposal in response. Sonnemaker (Sysco), Hearing Tr. at 1597:5-18; [redacted]

54. Whether in a formal RFP or not, foodservice distributors "don't know who the competition is, [] don't know what they're bidding, [and are] just making educated guesses. Hausman, Hearing Tr. at 2058:20-21. Foodservice distributors "never really know for sure" whom they are competing against. Sonnemaker (Sysco), Hearing Tr. at 1581:7-8. Because "it would be not in [the customer's] best interest most times to even share with us who potentially would be bidding on their business, . . . it's not something that you can say with any certainty who you're working with or against at any time." *Id.* at 1603:14-18; Hausman, Hearing Tr. at 1968:1-8 (noting that customers generally, and successfully, hide their preferences).

D. A CUSTOMER'S GEOGRAPHIC FOOTPRINT IS NOT DETERMINATIVE OF ITS FOOD DISTRIBUTION CHOICES

55. Sysco and USF refer internally to some customers as "national." This label does not mean that the customers require distribution services nationwide, or even across many regions; it means only that the customer and the distributor have agreed that the contract between them will be administered by staff at the corporate (or national) office as opposed to staff at local distribution centers. *See infra* § VI.E.1. PFG applies a similar "national" label to customers handled out of its corporate headquarters rather than at the local distribution level. Holm (PFG), Hearing Tr. at 826:18-20 ("[A] national account to us is an account that is managed by a person in our national account department.")

56. Whether Sysco labels a contract customer as "national" or "local" depends on where the customer's contract is administered. Sysco's "national" label is "a shorthand" for corporate multi-unit (CMU). Sonnemaker (Sysco), Hearing Tr. at 1565:22-25. CMU customers' contracts are administered by Sysco's corporate office in Houston. Brawner (Sysco), Hearing Tr. at 1783:23-1784:5. If a customer's contract is managed at the local distribution center, Sysco labels them a local contract customer (LCC). Sonnemaker (Sysco), Hearing Tr. at 1564:22-24.

57. Similarly, USF contracts can be managed either "nationally" or "locally." Lynch (USF), Hearing Tr. at 1693:2-4. For example, in its hospitality segment, 54% of USF's customers are considered "national" accounts, and 46% are considered local accounts. *Id.* at 1693:20-1694:6. For USF's regional chain restaurant customers, 75% are managed locally and 25% are managed as national accounts. *Id.* at 1701:18-21.

58. Whether a Sysco customer chooses to be a CMU or LCC is a matter of preference. DeLaney (Sysco), Hearing Tr. at 1347:23-1348:1; Brawner (Sysco), Hearing Tr. at 1784:6-17; Sonnemaker (Sysco), Hearing Tr. at 1566:14-20. "Some prefer that local touch, some prefer the national kind of support as far as getting things done." *Id.* at 1568:12-16. Some customers remain LCCs they value their relationship with the local distribution center and that local distribution center to handle them. Brawner Tr. at 1784:6-17; *see also* Sonnemaker Tr. at 1566:21-1567:1. But some customers prefer the centralized administrative support they can receive as a CMU. *Id.* at 1568:2-11.

59. The "National" label does not reflect the scope of that customer's geographic demand or footprint. For both Sysco and USF, most of their "National Customers" are not present nationwide. Lynch (USF), Hearing Tr. at 1695:1-10 (USF has "National" customers that are located in one location or region); Sonnemaker (Sysco), Hearing Tr. at 1566:3-4 ("As a matter of fact, the vast majority of [CMUs] are not national in scope"). The average Sysco CMU customer uses "about six or seven" out of seventy distribution centers. Sonnemaker Tr. at 1596:8-12; *see also* Hausman, Hearing Tr. at 1976:5-9 (37% of CMUs use five or fewer distribution centers and 55% use ten or fewer). Similarly, fifty of USF's "national" customers uses two or fewer distribution centers. Lynch Tr. at 1695:22-1696:1; *see also* Hausman Tr. at 1976:11-17 (51% of "National Customers" use five or fewer distribution centers and two-thirds use ten or fewer).

60. Conversely, many customers without the "National" label have a multi-regional or nationwide footprint. For example, Famous Dave's is a local customer with a multi-regional footprint that USF serves out of 10 distribution centers with sales in excess of $20 million. Lynch (USF), Hearing Tr. at 1694:14-25. Cinemark Theaters is an LCC that Sysco serves out of "about 25" distribution centers. Sonnemaker (Sysco), Hearing Tr. at 1566:10-13.

61. Many "National Customers" look just like customers who are not given that label. [redacted] Likewise, Southern Food Service Management and Consolidated Concepts, both FSMs, receive different classifications despite substantially similar profiles. [redacted] Put simply, the internal administrative label "National" describes the manner in which a customer's contract is administered; it does not describe the customer's geographic reach or demand profile.

62. To be sure, some "National Customers" *also* have nationwide or multi-regional geographic reach. DeLaney (Sysco), Hearing Tr. at 1348:9-11. But the mere fact that "National Customers" have multiple locations across many regions does not mean they *require* a *single* broadline distributor to service all their locations. DeLaney (Sysco), Hearing Tr. at 1401:1-11 (explaining that the few customers that need national distribution do not need to use only one distributor); Sonnemaker (Sysco), Hearing Tr. at 1572:11-13 (believing that for "not a one"

customer is regionalization not a realistic option). Of US Foods's 15 "National" sales customers served out of 35 or more distribution centers, nine use multiple broadliners. Lynch (USF), Hearing Tr. at 1777:5-1778:5.

63. To the contrary, most geographically dispersed "National Customers" prefer to source regionally, locally, or in some combination that involves multiple distributors:

- [redacted]

- [redacted] IPC recently awarded Subway's business in the Pacific Northwest to Harbor Wholesale, a local convenience store distributor. Sonnemaker (Sysco), Hearing Tr. at 1581:5-16. *See also* Lynch (USF), Hearing Tr. at 1702:17-1703:9 (noting USF could service all Subway locations "[b]ut it is the customer who decides to split its business").

- [redacted] *see also* Lynch (USF), Hearing Tr. at 1703:10-22 (Five Guys "used to have a sole source relationship with US Foods" but they "switched to using multiple distributors"). [redacted]

- Choice Hotels, a hotel chain, uses multiple distributors, including Gordon, Ben E. Keith, FSA, Reinhart, Sysco, and PFG. Lynch (USF), Hearing Tr. at 1716:3-8. Best Western, another hotel chain, likewise uses distributors on a regional basis, including Reinhart, Gordon, Ben E. Keith, and Sysco. *Id.* at 1716:9-12.

- Defense Logistics Agency (DLA) uses several distributors on a regional basis: Reinhart, USF, Nicholas & Company, Shamrock Foods, Labatt, United Food Service, Sysco, Provisions Legrand, Merchants, Pocono ProFoods, Renzi Brothers, and Hartford Provisions. Lynch (USF), Hearing Tr. at 1724:12-18.

64. Likewise, many of the hospitality and healthcare GPOs with nationwide membership, as well as FSMs with customers across the nation, provide foodservice customers with distribution options on a regional or multi-distributor basis:

- Avendra, a hospitality GPO, contracts regionally. [redacted] Its members use Sysco in Baltimore and Boston, USF in the Southeast, California, and Nevada, and DMA for the rest of the country. Sonnemaker (Sysco), Hearing Tr. at 1588:23-1589:2; Lynch (USF), Hearing Tr. at 1711:1-14.

- HPSI offers to its members nine broadline foodservice distributors that cover particular regions. Lindahl (HPSI), Hearing Tr. at 1404:3-14; [redacted] All nine broadline foodservice distributors, including Sysco, offer "pretty similar" prices. Lindahl (HPSI), Hearing Tr. at 1413:20-25. Half of HPSI's top twenty customers by dollar volume use multiple distributors. *Id.* at 1419:7-9.

- Amerinet is a major healthcare GPO with members located across the continental United States. [redacted]

- MedAssets is another major healthcare GPO with members spread across the continental United States. [redacted]

- [redacted]

- Aramark is a major FSM that uses Sysco for the majority of its foodservice distribution needs. Sonnemaker (Sysco), Hearing Tr. at 1583:24-25. But even Aramark uses specialty distributors. *Id.* at 1585:23-1586:6. And Aramark's members can opt out and use a distributor of their choice. *Id.* at 1636:19-23.

- [redacted]

- Interstate Hotels and Resorts uses a variety of purchasing strategies, including purchasing directly from manufacturers, through a GPO, from two broadline distributors, and from multitude of specialty distributors. Thompson (Interstate), Hearing Tr. at 203:20-204:9, 250:6-8, 251:9-12

65. In fact, geographically dispersed customers often compare prices between a sole-sourced distribution model and a regional distribution model, selecting the one best suited to their business. [redacted]

66. Competitors view the industry as being regional as well. [redacted]

67. As Dr. Bresnahan observed, Dr. Israel's belief that switching to multiple distributors is inefficient and prohibitively costly is an "assumption" without any underlying analysis. Bresnahan, Hearing Tr. at 2126:10-17. The cost of a customer converting to a regional distribution model is modest once the necessary internal infrastructure is established. *Id.* at

2128:1-18. Moreover, any costs associated with regionalization are offset against the benefit of having "more options" and having "more bargaining power." *Id.* at 2128:20-2129:1.

68. Numerous customers already regionalize with modest administrative burdens and costs. [redacted] Similarly, David Lindahl of HPSI testified that one employee at HPSI "handles all those contracts" for HPSI's network of nine distributors. Lindahl (HPSI), Hearing Tr. at 1405:3-11. [redacted]

69. The FTC's own witnesses undermine Dr. Israel's assumption that regionalizing a distribution network is inefficient and prohibitively expensive. [redacted] Similarly, Interstate did not require additional staff to manage its relationship with its second distributor, PFG; Jim Thompson testified that he manages it himself with only monthly contact with PFG. Thompson (Interstate), Hearing Tr. at 270:7-18; *see also id.* at 83:17-20 (testifying that he efficiently manages 50 to 60 contracts with manufacturers).

70. Sysco and USF's national footprint is not a competitive advantage. Contrary to the FTC's view of "National Customers," many prefer to be served by fewer distribution centers, which translates to higher volume per warehouse and thus lower freight costs. Sonnemaker (Sysco), Hearing Tr. at 1570:13-1571:2 (customers are trending towards using fewer distribution centers because with consolidation, the customer has inbound freight and logistical savings); *id.* at 1573:19-1574:9 (Sysco lost Red Robin, which it served out of 40 distribution centers, to DMA, which offered the chain 14 distribution centers and saved it millions of dollars in supply chain savings); [redacted] Szrom (VA), Hearing Tr. at 179:15-23 (a major weakness in Sysco's ability to distribute was that it proposed to use too many distribution centers); [redacted] Therefore, a strategy of Sysco and USF's competitors is to offer service out of fewer distribution centers. [redacted]

71. The few nationwide customers that prefer to contract with a single distributor for all or substantially all of their locations are offset by the many examples of similar customers who contract regionally. This demonstrates that sole-source distribution is a preference, not a requirement. *See infra* §§ VI.C.1, VI.E.2; *cf.* Thompson (Interstate), Hearing Tr. at 269:4-12 (even though Interstate would prefer to work with one distributor, it uses two—USF and PFG).

72. There are a number of distributors, in addition to USF and Sysco, that can cater to any preference for a sole-source distributor:

- [redacted]
- [redacted]
- [redacted]

73. Two purchasing companies, [redacted] created contingency plans in response to the merger, and determined that they could receive nationwide coverage without using Sysco and USF. [redacted]

[redacted]

E. COST EFFICIENCIES ARE THE RATIONALE FOR THE MERGER

74. The 2008 financial crisis seriously impacted the foodservice distribution industry. DeLaney (Sysco), Hearing Tr. at 1318:7-13. Even before 2008, the industry's growth had slowed from "5 to 7 percent in the '70s, '80s," *id.* at 1316:20-22, to "probably 2 to 3 percent" in the early 2000s, *id.* at 1317:7-8. With the recession, American consumers became "much more disciplined than they ever were before" with their discretionary income and changed their habits in regard to eating outside of the home. *Id.* at 1318:20-1319:1. This caused the foodservice distribution industry to "grow[] much slower than it used to, maybe 1 percent, give or take." *Id.* at 1345:10-11. Market growth, in fact, "now is flat." *Id.* at 1319:13. It also led to increased, "tremendous pressure" on distributors' gross margins. *Id.* at 1320:9-15.

75. The economic fallout of the 2008 financial crisis "made competition even more acute than it was before." DeLaney (Sysco), Hearing Tr. at 1319:7-9. The recession did not markedly affect the number of competitors in the industry. *Id.* at 1319:15. But when the same number of people compete for smaller margins in an industry with flat growth, it brought pressure on a foodservice distributor to offer lower prices and to be able to differentiate themselves from their competitors. *Id.* at 1319:15-20.

76. In order to compete and grow in a post-2008 world, Sysco has to take more costs out of the system. DeLaney (Sysco), Hearing Tr. at 1320:15-19; 1325:25-1326:10. For Sysco, "the only way to [grow] is to become more important to your customers and to understand their needs

better." *Id.* at 1326:2-4. What customers care about most post-2008 is price. Price used to be used to be "one of the top two or three things," but now is "on the top of the mind for everyone." *Id.* at 1320:2-8. The merger with USF not only allows Sysco to take costs out of the system that will lead to become a more effective competitor, and better serve its customers, *id.* at 1342:7-13; 1344:22-1345:4, but is necessary for Sysco to do so, *id.* at 1392:7-9. Sysco "can't get anywhere[] close to $600 million [in cost-savings] without the merger." *Id.* at 1399:23-24

77. In addition, the merger will provide the merged entity greater buying power to compete on par with GPOs when negotiating lower food prices with manufacturers, which will inure to the benefit of all customers. DeLaney (Sysco), Hearing Tr. at 1344:22-1345:3; *see also* Sonnemaker (Sysco), Hearing Tr. at 1591:25-1592:13.

V. APPLICABLE LEGAL STANDARDS

A. THE FTC'S BURDEN

78. When the FTC seeks to enjoin a merger, "[t]he issuance of a preliminary injunction prior to a full trial on the merits is an extraordinary and drastic remedy," because it "may prevent the transaction from ever being consummated." *FTC v. Exxon Corp.*, 636 F.2d 1336, 1343 (D.C. Cir. 1980) (quotation marks omitted); *see also Mo. Portland Cement Co. v. Cargill, Inc.*, 498 F.2d 851, 870 (2d Cir. 1974) (injunction likely "spell[s] the doom of an agreed merger"). USF will terminate the transaction if the merger is enjoined. Schreibman (USF), Hearing Tr. at 1516:10-1517:8.

79. "Given the stakes," the FTC bears a heavy burden when it requests preliminary injunctive relief. *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 116 (D.D.C. 2004); *FTC v. Foster*, No. 07-352, 2007 WL 1793441 at *51 (D.N.M. May 29, 2007) ("[T]he FTC's burden remains heavy, because the granting of any injunction by a federal court is an extraordinary and drastic remedy") (quotation marks omitted); *FTC v. Occidental Petroleum Corp.*, No. 86-900, 1986 WL 952, at

*13 (D.D.C. Apr. 29, 1986) ("The Commission's burden on a preliminary injunction motion is properly a heavy one, since, as this Circuit has recognized, the granting of preliminary injunctive relief is an extraordinary and drastic remedy, particularly in the merger and acquisition context." (quotation marks omitted)).

80. Under § 13(b) of the FTC Act, the Court must determine that an injunction is "in the public interest," after "weighing the equities and considering the Commission's likelihood of ultimate success." 15 U.S.C. § 53(b).

81. The FTC's likelihood of ultimate success is paramount: "absent a likelihood of success on the merits, equities alone will not justify an injunction." *FTC v. Arch Coal, Inc.*, 329 F. Supp. 2d 109, 116 (D.D.C. 2007).

82. To prove a likelihood of ultimate success on the merits under Section 7 of the Clayton Act, the FTC "must show a reasonable probability that the proposed transaction would substantially lessen competition in the future." *Cardinal Health*, 12 F. Supp. 2d at 45 (quotation marks omitted). The Supreme Court has explained that to satisfy this standard the FTC must show that "there is a *reasonable probability* that the merger will substantially lessen competition." *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (emphasis added); *see also FTC v. Swedish Match*, 131 F. Supp. 2d 151, 156 (D.D.C. 2000) ("[T]he Commission must show that there is a 'reasonable probability' that the challenged acquisition will substantially lessen competition/"); *FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1072 (D.D.C. 1997) (the FTC must "show that there is a 'reasonable probability' that the challenged transaction will substantially impair competition").

83. In assessing the FTC's evidence, the Court must "'exercise independent judgment'"—it cannot simply defer to the FTC. *FTC v. Weyerhaeuser Co.*, 665 F.2d 1072, 1082 (D.C. Cir

1981) (quoting H. Rep. No. 624, at 31); *Foster*, 2007 WL 1793441, at * 51 ("If Congress did not want federal courts to play some meaningful role in the injunction process, it could have given injunction power directly to the FTC.").

84. Some courts have characterized the FTC's burden under § 13(b) as being lower than that under the traditional preliminary injunction standard, but this is only because the FTC is not required to show irreparable harm. *See FTC v. Weyerhaueser, Co.*, 665 F.2d 1072, 1082; (D.C. Cir. 1981); *see also* Areeda *et al.*, Antitrust Law § 325b ("When the FTC brings suit, it is sometimes said that irreparable harm is presumed, but probable success on the merits must still be proven."). The FTC does not argue for a lower standard in proving a likelihood of success on the merits. *See also* Global Competition Review, An Interview with Deborah Feinstein (Feb. 11, 2015).

B. THE FTC MUST DEMONSTRATE A LIKELIHOOD OF SUCCESS ON THE MERITS

85. "The objective of Section 7 of the Clayton Act is to prohibit only those acquisitions that may allow the combined entities to exercise market power by raising prices and restricting the availability of a product or service to customers." *Occidental Petroleum*, 1986 WL 952, at *13.

86. "[T]he Supreme Court, echoed by the lower courts, has said repeatedly that the economic concept of competition, rather than any desire to preserve rivals as such, is the lodestar that shall guide the contemporary application of the antitrust laws," including under the Clayton Act. *Hospital Corp. of Am. v. FTC*, 807 F.2d 1381, 1386 (7th Cir. 1986).

87. To establish a likelihood of ultimate success on the merits, the FTC must demonstrate (1) a relevant product market; (2) relevant geographic markets; and (3) probable anti-competitive effects in these markets. *See, e.g.*, *United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36 49-50 (D.D.C. 2011); *Arch Coal*, 329 F. Supp. 2d at 117. Only if the FTC establishes its relevant

markets and demonstrates undue concentration is it entitled to a presumption that the merger is illegal. *See FTC v. H.J. Heinz Co.*, 246, F.3d 708, 715 (D.C. Cir. 2001). Where the FTC is not entitled to this presumption, it bears the burden of proof and persuasion to show that the merger will substantially lessen competition. *See United States v. Baker Hughes, Inc.*, 908 F.2d 981, 938 (D.C. Cir. 1990); *United States v. Oracle Corp.*, 331 F. Supp. 2d 1098, 1110 (N.D. Cal. 2004). "[A] failure of proof in any respect will mean the transaction should not be enjoined." *Arch Coal*, 329 F. Supp. 2d at 116.

88. Even if the FTC is entitled to a presumption in its favor, defendants can rebut by showing that anti-competitive effects are unlikely. *See United States v. Gen. Dynamics Corp.*, 415 U.S. 486, 498 (1974); *see also Arch Coal*, 329 F. Supp. 2d at130 ("[T]his circuit has cautioned against relying too heavily on a statistical case of market concentration alone, and that instead a broad analysis of the market to determine any effects on competition is required."). Defendants can make this showing in a number of ways. *See, e.g.*, *id.* at 158 (unilateral price increase unlikely); *United States v. Microsoft Corp.*, 253 F.3d 34, 105 (D.C. Cir. 2001) (divestiture); *Baker Hughes*, 908 F.2d at 984 (entry and repositioning of competitors); *id.* at 98 (sophisticated customers); *Heinz*, 246 F.3d at 720 (procompetitive efficiencies).

89. Injunctive relief is also improper when the equities weigh in favor of allowing the merger to proceed. *See Weyerhaeuser*, 665 F.2d at 1081.

VI. THE FTC HAS NOT DEFINED A RELEVANT PRODUCT MARKET

A. THE LEGAL STANDARD

90. A relevant product market is essential to the FTC's claim. *United States v. Marine Bancorp. Inc.*, 418 U.S. 602, 618 (1974) ("Determination of the relevant product and geographic markets is a necessary predicate to deciding whether a merger contravenes the Clayton Act.") (quotation marks omitted); *Swedish Match*, 131 F. Supp. 2d at 156.

91. "Not only is the proper definition of the relevant product market the first step in this case, it is also the key to the ultimate resolution of this type of case, since the scope of the market will necessarily impact any analysis of the anti-competitive effects of the transaction." *United States v. SunGard Data Sys., Inc.*, 172 F. Supp. 2d 172, 181 (D.D.C. 2001). *See also Arch Coal*, 329 F. Supp. 2d at 119. (a relevant product market "is necessary to identify that area of trade within which a defendant allegedly has acquired or will acquire an illegal or monopolistic or oligopolistic position"). Without a well-defined product market, "an examination of a transaction's competitive effects is without context or meaning." *FTC v. Freeman Hosp.*, 69 F.3d, 260, 268 (8th Cir. 1995).

92. Thus, "[t]he failure to properly define a relevant market may lead to the dismissal of a Section 7 claim." *FTC v. Lab. Corp. of Am.*, 2011 WL 3100372, at *17 (C.D. Cal. Feb. 22, 2011). *See also Foster*, 2007 WL 1793441, at *56 ("Only after the relevant markets have been defined is it possible to determine whether a 'substantial' lessening of competition is probable. The failure to properly define a relevant market may lead to the dismissal of a section 7 claim.").

93. Generally speaking, a well-defined product market includes all functionally similar products to which some consumers would switch if defendants imposed a small price increase. *See, e.g.*, *Arch Coal*, 329 F. Supp. 2d. at 119 ("The general question is 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." (quoting *Staples*, 970 F. Supp. at 1074) (quotation marks omitted); *id.* ("Relevant markets will generally include producers who, given product similarity, have the ability to take significant business from each other.").

94. A product market is determined through a rigorous exploration of demand, *i.e.*, "the reasonable interchangeability of use" of and the "cross-elasticity of demand" between

defendants' product and competing products. *Brown Shoe,* 370 U.S. at 325. The key question is whether a hypothetical monopolist in the alleged market profitably could impose a small but significant and non-transitory increase in price ("SSNIP"). *See, e.g.*, *Oracle*, 331 F. Supp. 2d at 1111-12; *Arch Coal*, 329 F. Supp. 2d at 120; *accord* PX06059, HMG § 4.1.1.

95. A well-defined product market "must correspond to the commercial realities of the industry and be economically significant." *See, e.g.*, *Brown Shoe*, 370 U.S. at 336-37 (quotation marks and footnote omitted); *Cardinal Health*, 12 F. Supp. 2d at 46 (same); *accord PepsiCo, Inc. v. Coca-Cola Co.*, 114 F. Supp. 2d 243, 249 (S.D.N.Y. 2000) (rejecting PepsiCo's contention "that a bundle of product (fountain syrup) and services (system distribution) utilized by certain customers comprises a separate market"). "[A]ntitrust theory and speculation cannot trump facts, and even Section 13(b) cases must be resolved on the basis of the record evidence relating to the market and its probable future." *Arch Coal*, 329 F. Supp. 2d at 117.

96. "[C]ourts should be guided by the commercial realities facing the [relevant consumer], not only by the method of product distribution." *PepsiCo*, 114 F. Supp. 2d at 251. And "[a]ny definition of a line of commerce which ignores the buyers and focuses on what the sellers do, or theoretically can do, is not meaningful." *Westman Comm'n Co. v. Hobart Int'l, Inc.*, 796 F.2d 1216, 1220 (10th Cir. 1986) (quoting *United States v. Bethlehem Steel Corp.*, 168 F. Supp. 576, 592 (S.D.N.Y. 1958)).

97. Courts reject product markets where the record shows "a spectrum of consumer choices, and active competition for those choices." *W. Parcel Exp. v. United Parcel Serv. of Am., Inc.*, 65 F. Supp. 2d 1052, 1059 (N.D. Cal. 1998), *aff'd* 190 F.3d 974 (9th Cir. 1999). *See also, e.g.*, *In re Super Premium Ice Cream Distrib. Antitrust Litig.*, 691 F. Supp. 1262, 1268 (N.D. Cal. 1988), *aff'd sub nom Haagen-Dazs v. Double Rainbow Gourmet Ice Creams, Inc.*, 895 F.2d 1417 (9th

Cir. 1990) (rejecting proposed product market of "premium ice creams" because "all grades of ice creams compete with one another for customer preference" and "the relevant market is ice cream generally"). "[T]o the extent clear breaks are difficult to identify, attempts to create defensible market boundaries are likely to be based on relatively vague product characteristics. Product characteristics that are too vague do not meet section 7's requirement that the relevant market be 'well-defined.'" *Oracle*, 331 F. Supp. 2d at 1121. Similarly, the government cannot enjoin a merger on the basis of harm to a large group of customers when the customers and products in question are extremely heterogeneous. *See, e.g.*, *SunGard*, 172 F. Supp. 2d at 193 ("The defendants' customers, as well as their computer systems, are simply too varied and too dissimilar to support any generalizations. Therefore, the central premise of the government's case-that there are 'a substantial number of customers for whom there are no competitive alternatives' has not been proven.").

98. *United States v. H&R Block*, 833 F. Supp. 2d 36 (D.D.C. 2011), is of limited utility in determining the product market here. DDIY tax preparation was a discrete product—that is, it was not divisible such that "combinations of other" products "may be a substitute," *SunGard,* 172 F. Supp. 2d at 190 n.20. By contrast, here the products are diverse and differentiated: some customers are purchasing the SKUs from the delivery company, while others are just paying for delivery, and very rarely will two customers be purchasing the same bundle of goods and services. In addition, the critical loss formula that was applied in *H&R Block*, 833 F. Supp. 2d at 63 n.17; has no applicability here because this case involves a heterogeneous (*i.e.*, asymmetric) product market. *See* Hausman, Hearing Tr. at 1958:8-11, 1960:16-17, 1964:15-17 (explaining that the formula used in *H&R Block* does not apply here "because of the heterogeneity of both distributors and of the customers"); *cf.* *H&R Block*, 833 F. Supp. 2d at 60-61 (plaintiff's expert

discussing the homogeneity of the market).

99. The government cannot enjoin a merger on the basis of harm to a large group of customers when the customers and products in question are extremely heterogeneous. *See, e.g.*, *SunGard*, 172 F. Supp. 2d at 193 ("The defendants' customers, as well as their computer systems, are simply too varied and too dissimilar to support any generalizations. Therefore, the central premise of the government's case-that there are 'a substantial number of customers for whom there are no competitive alternatives' has not been proven.").

100. Product markets predicated on a one-stop-shop distribution theory are frequently rejected—*i.e.*, courts have found that a combination of other distributors may be a substitute for one-stop shopping where customers seek a combination of goods. *See Westmann*, 796 F.2d at 1221 ("The fact that a distributor is able to satisfy all of a customer's needs at one location does not mean that it is free from competition from other types of distributors."); *accord United States v. Grinnell Corp.*, 384 U.S. 563, 572 (1966) ("We see no barrier to combining in a single market a number of different products or services where that combination reflects commercial realities."). This Court addressed precisely this issue in *SunGard*, observing that "many combinations of" products "may be a substitute for" the product in question, and distinguishing "most antitrust cases, in which the product at issue is a discrete item." 172 F. Supp. 2d at 190 n.20.

101. The relevant question is whether customers would divert enough of their demand to competitors in other channels that a SSNIP would be unprofitable. Whether a substitute channel is a comprehensive substitute is irrelevant. Similarly, where customers simultaneously allocate demand among many distribution channels in varying degrees, the proper analysis focuses on how much demand would be switched to alternate distribution channels *from* the one at issue.

See, e.g., *Staples*, 970 F. Supp. at 1070, 1073, 1077-81 (comparing sales of office supplies by superstores with all "other sellers of office supplies"); *Thurman Indus. Inc. v. Pay 'N Pak Stores, Inc.*, 875 F.2d 1369, 1376 (9th Cir. 1989) (rejecting a proposed market of products and services offered by home center stores because "other retailers" of functionally interchangeable home-improvement goods could lure consumers away from home center stores); *PepsiCo*, 114 F. Supp. 2d at 249-50 (rejecting a proposed product market of fountain syrup delivered by independent foodservice distributors because "the evidence does not show that the preference for independent foodservice distributors is so strong as to eliminate delivery through other means as an acceptable alternative").

102. Both the FTC's administrative complaint and its Complaint in this Court allege two distinct product markets in which it claims competition will be harmed: broadline foodservice distribution services sold to national customers, Compl ¶¶ 41-44; Admin. Compl ¶¶ 31-34; and broadline foodservice distribution in local markets—*i.e.*, to "Local Customers," Compl. ¶ 50; Admin. Compl. ¶ 40. *See also, e.g.*, Compl. ¶ 45 ("Defendants compete for the sale of broadline foodservice distribution services to National Customers and local customers."); Admin. Compl. ¶ 35 (same). In effect, the FTC's product markets isolate one distribution mode (broadline), and then divides that alleged product market based on a supposed distinction between "National" and "Local" Customers. The evidence does not support either of these alleged product markets.

B. ORDINARY COURSE BUSINESS DOCUMENTS FLATLY REFUTE THE FTC'S ALLEGED MARKET

103. A market definition not shared by industry participants is entitled to little weight. *Brown Shoe*, 370 U.S. 294, 325 (1962).

104. Ordinary course business documents kept by industry participants are strong evidence of market shares, because they reflect how actual competitors view the market. *See, e.g.*, *H&R*

Block, 833 F. Supp. 2d at 53-54. The Department of Justice and Federal Trade Commission Horizontal Merger Guidelines (Aug. 19, 2010) ("Horizontal Merger Guidelines" or "Merger Guidelines" or "HMG") expressly state that "[d]ocuments created in the normal course are more probative than documents created as advocacy materials in merger review. Documents describing industry conditions can be informative regarding the operation of the market and how a firm identifies and assesses its rivals, particularly when business decisions are made in reliance on the accuracy of those descriptions." PX06059, HMG § 2.2.1.

105. [redacted] *see also* Bresnahan, Hearing Tr. at 2076:9-2078:13 (explaining that "it's often true in a merger case that people in the industry will have calculated market shares in the relevant market because they think about it," noting that "several different participants in the market" calculated that the merged entity would have a market share "in the high 20s, 27 percent or something like that before the divestiture," and concluding that Dr. Israel's share calculations were therefore "unreliable").

106. And ordinary course documents created by customers are particularly important because they are direct evidence of how customers perceive their options. DX-00279, [redacted] (28% market share); DX-01505, [redacted] pie chart showing current foodservice market and post-merger

foodservice market); DX-01724, [redacted] (top 3 broadliners at 34% market share).

107. The FTC's only documents even suggesting contrary market shares are in markets they did not allege. *See* PX01008-33, [redacted] (regarding healthcare GPOs); PX09060-006, [redacted] (discussing 15 specific customers). [redacted]

C. THE PRODUCT MARKETS ALLEGED IN THE FTC'S COMPLAINT ARE BASED ON ANECDOTAL REPORTS OF CUSTOMER PREFERENCES

108. There are hundreds of thousands, if not millions, of foodservice customers in the United States. The FTC carefully selected and elicited testimony from a handful of customers primarily detailing their subjective preferences for broadline distribution and, in particular, those services provided by Sysco and USF. This testimony is irrelevant to defining a relevant product market.

109. Customer preferences cannot establish a product market because preferences shed little light on customers' ability to substitute in response to a post-merger price increase. *See Oracle*, 331 F. Supp. 3d at 1130-31 ("[T]he issue is not what [products] the customers would *like* or *prefer* . . .; the issue is what they *could* do in the event of an anti-competitive price increase."); *Arch Coal*, 329 F. Supp. 2d at 122 ("Some customers did indicate that they *prefer* 8800 Btu coal to 8400 Btu coal, but the evidence also shows that customers having that preference nonetheless can use and have used other Btu coals, and benefit from the competition between 8800 and 8400

coal."); *Global Disc. Travel Servs., LLC v. Trans World Airlines, Inc.*, 960 F. Supp. 701, 705 (S.D.N.Y. 1997) (Sotomayor J.) ("The plaintiff's argument is analogous to a contention that a consumer is 'locked into' Pepsi because she prefers the taste, or NBC because she prefers 'Friends,' 'Seinfeld,' and 'E.R.' A consumer might choose to purchase a certain product because the manufacturer has spent time and energy differentiating his or her creation from the panoply of products in the market, but at base, Pepsi is one of many sodas, and NBC is just another television network."); *accord* James A. Keyte & Kenneth B. Schwartz, *"Tally-Ho!": Upp and the 2010 Horizontal Merger Guidelines*, 77 Antitrust L. J. 587 (2011) ("courts continue to reject arguments that they should define a relevant product market based solely on consumers' preferences"); James A. Keyte, *Arch Coal and Oracle Put the Agencies On The Ropes In Proving Anti-competitive Effects*, 19 Antitrust, 79, 85 (2004) ("it is clear that the agencies may need to become less enamored with 'subjective' customer testimony and more reliant on objective market evidence—economic or otherwise—that cannot be dismissed as 'disconnected' with 'market reality'").

110. Customer testimony is helpful only if a customer witness explains why it could not switch to a competing product in response to a SSNIP. *See Oracle*, 331 F. Supp. 2d at 1131 (customer testimony was unhelpful when the witnesses did not testify to "what they would or could do or not do to avoid a price increase"); Irene K. Gotts & Daniel E. Hemli, *Just the Facts: The Role of Customer and Economic Evidence in M&A Analysis*, 13 Geo. Mason L. Rev. 1217, 1226 (2006) ("'Bare' customer claims that the removal of a competitor is likely to influence adversely prices, quality, etc., are generally unhelpful. Similarly, a customer's testimony that it would (or would not) switch to a competing product in response to a hypothetical five or ten percent price increase may not, without further explanation, be given much weight.").

111. Similarly, testimony from customers who have not explored alternative options is unhelpful in determining whether enough customers would substitute away that a SSNIP would be profitable. *Oracle*, 331 F. Supp. 2d at 1167 ("the court cannot take the self-interested testimony of five companies which chose to eliminate SAP from consideration, and from that sample draw the general conclusion that SAP does not present a competitive alternative to Oracle and PeopleSoft").

1. Customer Preferences Do Not Determine Whether Customers Could Switch To Another Supplier In Response To A Price Increase

112. Certain FTC witnesses testified to their preferences for Sysco, USF, or broadline distribution, which, even if genuinely held, does not determine whether customers *could* switch to alternative distribution channels or distributors in response to a SSNIP by the merged entity. For instance, Interstate Hotels and Resorts repeatedly stated that its preference was to use a sole-source broadline distributor, although this was not a requirement. Thompson (Interstate), Hearing Tr. at 214:11-12 ("Q: Is it fair to say that Interstate needs a broadliner? A: That would be our preference . . . ."). When asked if Interstate had ever thought about turning to a regional distribution model, Thompson responded that Insterstate had not because "again we would prefer to work with one distributor." *Id.* at 222:6-13; *see also id.* at 247:23-25 ("Q: Can you see yourself using a network of regional distributors? A: It's not my preference."). But, importantly, when asked what Interstate would do in response to a SSNIP, Thompson explained that he would consider regional distribution. *Id.* at 283:7-14 ("Q: Fair to say if Sysco and US Foods merge and the merged company comes to you at the end of this year and says your pricing is going to go up, you're going to look at your options, aren't you, sir? A: I most definitely would. Yes. Q: You'll evaluate whether you want to use regional distributors; is that right. A: I would have no choice.").

113. For every customer witness that testified in support of the FTC's case, there is a similar customer that structures its business differently, and does so successfully, demonstrating that the FTC's witnesses testified to their preferences, not needs:

- *Independent Restaurants*. While some independent restaurants, [redacted] prefer a sole-source distributor, *see* PX00486, [redacted] (98% of spend with USF), others, [redacted] mix and match broadline, specialty and cash-and-carry, comparing prices on a weekly basis, *see* DX-00190, [redacted]
- *Restaurant Chains*. While some chain restaurants, [redacted] use a sole-source broadline distributor, PX00418, [redacted] others, [redacted], prefer contracting with multiple distributors regionally. Indeed, Five Guys recently dropped USF as its sole-source national distributor, finding it advantageous to contract regionally with six distributors. Lynch (USF), Hearing Tr. at 1703:10-22.
- *Government Agencies*. [redacted]
- *Hotel Chains*. While Interstate [redacted] PX00441, [redacted] In fact, Interstate's purchasing is far more complicated than its declaration suggests. Interstate contracts directly with manufacturers, and manages approximately 50 contracts; it is a member of Compass Foodbuy, a GPO, and buys food through those contracts; and only then does it rely on a broadline "distributor for the products that aren't met by the previous two options." Thompson (Interstate), Hearing Tr. at 203:22-204:9. Interstate also purchases from specialty distributors for the perishable products with which "the broadliner struggles." *Id.* at 26:9-15.
- *GPOs*. GPOs, [redacted] *see supra* ¶¶ 46-50, utilize variants of three separate distribution models: regional distribution; distribution through multiple distributors while the GPO remains distributor neutral; and the "rare" case of sole-source distribution, *see infra* Appx. A ¶ 27 (Sonnemaker explaining GPO distribution models).

114. The FTC offered very little evidence that customers could not substitute out of its alleged product markets in response to a price increase, and the many customers that already do

substitute demonstrate that the FTC's product markets are defined too narrowly.

2. The FTC's Customer Evidence Is Unrepresentative Of The Actual Market

115. To be helpful, customer testimony must also accurately represent the plaintiff's proposed product market. *Oracle*, 331 F. Supp. 2d at 1167 ("Drawing generalized conclusions about an extremely heterogeneous customer market based upon testimony from a small sample is not only unreliable, it is nearly impossible."); *SunGard*, 172 F. Supp. 2d at 182-83 ("the striking heterogeneity of the market, particularly as reflected by the conflicting evidence relating to customer perceptions and practices, further undercuts plaintiff's product market definition"); *see also United States v. Engelhard Corp.*, 126 F.3d 1302, 1306 (11th Cir. 1997) ("No matter how many customers in each end-use industry the Government may have interviewed, those results cannot be predictive of the entire market if those customers are not representative of the market.").

116. It is even more difficult to "decipher any conclusions" from customer testimony where "customers who were interviewed by one party then changed their position when interviewed by the opposing party." *SunGard,* 172 F. Supp. 2d at 183. Based on "equivocal evidence" of this nature, a court cannot "determine whether a SSNIP would cause 'a significant number of users' to switch to alternative" products, "and as a result, plaintiff cannot sustain its burden." *Id.* at 183 (quoting *FTC v. Owens-Illinois, Inc.*, 681 F. Supp. 2d, 36 (D.D.C. 1988)).

117. The FTC has not presented customer testimony that was representative. There are hundreds of thousands of foodservice distribution customers, but the FTC made no effort to determine whether its customer witnesses accurately represent either of its product markets.

118. More specifically, the FTC's customer declarations are inherently unrepresentative in two important ways. Of the 778 customers the FTC assembled, only 25 declarants supported the

FTC's case, and only a handful of those stated that they could not substitute away from the merged entity in response to a SSNIP. *But see, e.g.*, DX-01930, [redacted] (retracting concerns after being informed about the divestiture); [redacted] (stating that [redacted] is "confident that we will continue to have multiple choices for competitive offerings" after the merger). Moreover, the FTC called two of those customers (VA, Interstate) and a GPO to testify at the hearing, none of whom testified that they would be forced to accept a price increase if the merger were consummated. *See, infra,* Appx. §§ II.A (VA), II.B (Interstate), IV.A (GPO).

119. Many customers in both of the FTC's alleged markets testified to the abundance of competitive options and their ability to substitute away from the alleged product markets in response to a SSNIP. The FTC's customer witnesses did not prove that so few customers could substitute out of the alleged product markets that a price increase would be profitable.

3. The Testimony Of FTC Witnesses Proved Unreliable, Unfounded, And Inaccurate

120. Only reliable evidence can support the plaintiff's case, even in the context of a motion for a preliminary injunction. *See FTC v. Freeman Hosp.*, 69 F.3d 260, 268 (8th Cir. 1995) (determining whether the FTC "presented sufficiently reliable evidence of likely success to warrant a preliminary injunction"); *Rosen Entm't Sys., LP v. Icon Enters. Int'l, Inc.*, 359 F. Supp. 2d 902, 904 (C.D. Cal. 2005); *see also Dickey's Barbecue Rests., Inc. v. GEM Inv. Grp. LLC*, No. 3:11-cv-2804, 2012 WL 1344352, at *1 n.* (N.D. Tex. Apr. 18, 2012) ("The court . . . has only considered evidence that it deems reliable and necessary to its ruling."). The FTC's own rules are in accord. *See* 16 C.F.R. § 3.43(b) ("unreliable evidence shall be excluded").

121. Witness testimony that is unfounded, lacks personal knowledge, or that is inaccurate is unreliable. *See Oracle*, 331 F. Supp. 2d at 1131 ("unsubstantiated customer apprehensions do

not substitute for hard evidence"); *id.* ("Although these witnesses speculated on that subject, their speculation was not backed up by serious analysis that they had themselves performed or evidence they presented."); *accord Bank Melli Iran v. Phlavi*, 58 F.3d 1406, 1412 (9th Cir. 1995) (declarations "entitled to no weight because the declarant did not have personal knowledge").

122. An affidavit (or declaration) is particularly suspect because it "can be and often is prepared by someone other than the affiant" and "is less likely to reflect fairly and accurately the affiant's own recollection or perception than is spontaneous oral testimony." *United States v. Mendel*, 578 F.2d 668, 672 (7th Cir. 1978).

123. During its 14 month investigation, the FTC interviewed around 550 market participants. *See* FTC's List of Individuals Likely To Have Discoverable Information, served by email on Feb. 23, 2015. Interviewees who gave information that did not support the FTC's view of the market, [redacted], were not asked to sign declarations. [redacted]. If an interviewee provided information that supported the FTC's theory, the FTC drafted a declaration for the interviewee to sign, *see, e.g.*, Schablein (Wintergreen), Hearing Tr. at 546:23-547:4, while facts inconvenient to the FTC's theory were left out of the declaration, [redacted]

124. Numerous FTC witnesses admitted during their depositions or at the hearing that they lacked the knowledge necessary to attest to the propositions in their declarations, that the declarations were inaccurate, or that statements core to the FTC's case were unfounded.

125. For example, Christine Szrom of the VA, who testified about the VA's Subsistence Prime Vendor ("SPV") program, plainly lacked personal knowledge for most of the key assertions in her declaration and in her hearing testimony. Despite stating that the VA achieved savings by switching from a regional to sole-source distribution model, Mr. Szrom admitted that she lacked any personal knowledge of those alleged savings, or the switch more generally, since the switch significantly predated her arrival at the VA. *See* Szrom (VA), Hearing Tr. at 163:20-164:14 (admitting lack of personal knowledge for any savings that resulted from the change). Although she testified that DMA "failed miserably" to meet the VA's requirements, [redacted] she could not articulate how DMA failed to meet those requirements—or even what those requirements might have been—because she had never evaluated a proposal by DMA, Szrom (VA), Hearing Tr. at 167:1-3. Indeed, because Ms. Szrom's sole responsibility was to determine whether prices were "fair and reasonable" during her tenure at the VA, she did not evaluate bids from any distributor for product line and availability, product quality, procurement capabilities, information systems, or customer service—in fact, she was forbidden from evaluating non-price factors. *Id.* at 176:24-181:4. Finally, although Ms. Szrom claimed that competition between Sysco and USF had inured to the VA's benefit, these benefits were wholly conjectural, since Sysco's bid was disqualified for technical reasons and was thus never brought to the negotiating table. *See, e.g.*, *id.* at 183:20-25 184:10-13; 186:16-21.

126. Numerous other FTC declarations suffered from similar defects:

- ***"National Customers."*** [redacted]

[redacted]

- ***"Local Customers."*** [redacted]

- ***Competitors.*** [redacted]

127. Hearing testimony makes abundantly clear that the declarations submitted in support of

the FTC's case are unfounded, unreliable, and inaccurate. *Compare, e.g.*, PX00411, [redacted] Accordingly, the FTC's declarations are entitled to little to no weight.

4. **The FTC's Customer Witnesses Were Generally Unaware Of The Divestiture To PFG And The Multitude of Distribution Options Available To Them**

128. Many of the FTC's declarations must also be viewed skeptically the FTC failed to inform many of these declarants of the PFG divestiture. *See, e.g.*, DX-00320, [redacted]

129. In fact, 73 of the FTC's 99 customer declarations are dated *prior to* the announcement of the divestiture on February 2, 2015.

130. Upon learning of the divestiture, a number of declarants said they no longer had reservations about the merger, including every declarant in San Diego. For instance, [redacted]

131. Other witnesses wrote off PFG as a viable competitor based on dated and incomplete information, but clarified that they would seriously consider PFG in response to a SSNIP. *See, e.g.*, Thompson (Interstate), Hearing Tr. at 225:5-9 (Interstate's information about PFG was

based on a meeting that "was several years ago"); *id.* at 246:15-16 ("Q: You'd evaluate PFG? A: I would have to look at it as an option. Yes."). Yet others learned about the many alternative distribution options available to them through their depositions. *See* DX-00288, [redacted] Some even went so far as to retract their concerns about the merger. *See* DX-01934, [redacted]

D. Dr. Israel's Opinions Should Be Disregarded Because He Failed To Do A Proper Economic Analysis And Instead Relied On Uninformative Customer Lists And Unreliable Declarations

132. Because the law requires careful application of economics to market facts, expert analysis is required to define a product market. *See, e.g.*, *Bailey v. Allgas, Inc.*, 284 F.3d 1237, 1246 (11th Cir. 2002) ("Construction of the relevant market . . . must be based on expert testimony."); *Am. Key Corp. v. Cole Nat'l Corp.*, 762 F.2d 1569, 1580 (11th Cir. 1985) ("Construction of a relevant economic market . . . cannot . . . be based upon lay opinion testimony."); *Water Craft Mgmt. LLC v. Mercury Marine*, 361 F. Supp. 2d 518, 542-44 (M.D. La. 2004) ("Courts consistently require that expert testimony adequately define the relevant geographic and product markets in antitrust cases.").

133. Where an expert's testimony is inadequate, the plaintiff's claim fails. *See Foster*, 2007 WL 1793441, at *18 (holding the FTC failed to establish a relevant geographic market where "[t]he FTC's economic expert did not endorse the relevant geographic market alleged in the FTC's complaint"); *see also Surgical Care Ctr. of Hammond, L.C. v. Hosp. Serv. Dist. No. 1 of Tangipahoa Parish*, 309 F.3d 836 (5th Cir. 2002) (plaintiff failed to establish the relevant market where expert testimony was inadequate); *Military Servs. Realty, Inc. v. Realty Consultants of Va., Ltd.*, 823 F.2d 829, 832 (4th Cir. 1987) (same).

134. Even if an expert's failure to support the alleged market does not foreclose a plaintiff's claim as a matter of law, it is still dispositive "as a practical matter" because the plaintiff will be unable to rebut the defendant's expert economists. *E.g.*, *Va. Vermiculite, Ltd. v. W.R. Grace & Co.-Conn.*, 108 F. Supp. 2d 549, 576 n.16 (W.D. Va. 2000) ("[A]s a practical matter . . . the plaintiffs' lack of any witness to testify about antitrust economics, or to rebut the defendants' economists, proves fatal."). It is virtually "impossible to prove such a complex economic question without the assistance of a qualified expert, *viz.*, an economist," *Berlyn, Inc. v. Gazette*

Newspapers, Inc., 223 F. Supp. 2d 718, 727 n.3 (D. Md. 2002). Expert testimony is particularly important where the product market's "contours are difficult to define." *Hynix Semiconductor Inc. v. Rambus Inc.*, , No. 00-20905, 2008 WL 73689, at *10 n.13 (N.D. Cal. Jan. 5, 2008).

135. To overcome inadequate expert testimony, the plaintiff's evidence must be that much more compelling. *See, e.g.*, *Drs. Steuer and Latham, P.A. v. Nat'l Med. Enters., Inc.*, 672 F. Supp. 1489, 1512 n.25 (D. S.C. 1987), *aff'd* 846 F.2d 70 (4th Cir. 1988) ("Failure to adduce expert testimony on competitive issues such as market definition augurs strongly in favor of granting summary judgment against an antitrust plaintiff.").

136. The FTC has offered Dr. Israel's opinion in support of its case. Dr. Israel was the only FTC witness who offered testimony from which the Court could attempt to calculate market shares and gauge the presumptions based on HHI. His testimony and analysis were not credible.

137. Dr. Israel did not endorse the product markets alleged by the FTC. The FTC claimed that broadline distribution services sold to "National Customers" and broadline distribution service sold to "Local Customers" are distinct product markets because the services sold to these customers are distinct. Compl. ¶ 41. In other words, the FTC alleged that although the sellers are the same (broadline distributors), different types of customers were buying different products with different attributes. *See* Bresnahan, Hearing Tr. at 2147:1-15 (explaining that even among "National Customers," the bundle of goods and services that they purchase from broadline distributors are "different products."). Without defining a product market in his declaration, D. Israel calculated market shares in the product markets alleged by the FTC. [redacted]

[redacted] which suggests that Dr. Israel started with his conclusion and worked backward.

[redacted]

139. Dr. Israel claimed at the hearing that "National Customers" and "Local Customers" could be separated under a price discrimination theory, *i.e.*, that the customers in each group were targeted customers under § 3 of the Merger Guidelines. Israel, Hearing Tr. at 908:17-909:14, 910:17-911:15. Dr. Israel's analysis is flawed and at odds with the FTC's case. Targeted-customer analysis under the Merger Guidelines applies only when "different customers [are] purchasing the same or similar products," PX06059, HMG § 3, and according to the FTC's own Complaint, the distinct bundle of goods and services that is broadline distribution sold to "National Customers" is not the "same or similar" to the separate and distinct bundle of goods and services that is broadline distribution sold to "Local Customers." Indeed, even among "National Customers" the bundle of goods and services varies so much as to constitute "different products." Bresnahan, Hearing Tr. at 2147:1-15 (explaining the distinction between price disparity and price discrimination and observing that "in the national part of [this industry], there's a different product for every customer, you know, they have different locations, they have different drop sizes, they have different lists of things they're buying, that's where they negotiate."). Simply put, this case involves differentiated, not homogenous, products.

140. Nor did Dr. Israel's analysis support his claim that "National Customers" were targeted

customers. All the experts agreed that the fundamental issue in determining whether price discrimination is possible—after, of course, it has been determined that the product is the same—is whether the customers in question have similar objectively observable characteristics that would allow a price discriminating firm to target those customers, as a group, for a price increase—*i.e.*, whether there is a common observable characteristic that stands as a proxy for inelastic demand. Hausman, Hearing Tr. at 1967:21-25 ("In order to target certain customers for price discrimination, a firm must be able to identify customers with "low price elasticity . . . [b]ecause if you try to raise the price and they're not price sensitive, they switch and you lose the profit."); Israel, Hearing Tr. at 912:1-18, 921:23-922:1 ("the grouping is really about whether these groups are treated differently, priced differently"); see also PX06059, HMG § 3 ("[T]he 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*.") (emphasis added). Dr. Hausman pointed out that common characteristics among "National Customers" are nigh impossible to observe, because those customers are smart and typically "hide their preferences." Hausman, Hearing Tr. at 1968:1-8.

141. Dr. Israel admitted that he performed no economic analysis to determine whether "National Customers" would be subject to targeting as a group. Israel, Hearing Tr. at 923:2-924:1 ("THE COURT: So just so I'm clear in my head, you didn't have, for example, a long list of customers, and you personally did not put one in one bucket and put the other in the other. Whatever the customers themselves self-identified for each category, however they labeled it and whatever the rationale was for the labeling, that's what you followed? THE WITNESS: Yes."). Instead, he uncritically relied on the parties' internal, administrative "National Customer" lists,

id. at 923:2-7, (admitting that he "strictly followed the parties' segregations" in determining which customers were "National" and which customers were "Local"), despite also testifying that "business documents [are] relatively uninformative." *Id.* at 1266:2-5. Contrary to the prescribed analysis, which requires identifying meaningful observable characteristics, Dr. Israel testified that he did not know why the "National" designation was made. Israel, Hearing Tr. at 1165:9-11. Nor did Dr. Israel perform any analysis to determine whether some or all "National Customers" possess the characteristics that the FTC alleged made these customers an economically distinct segment. *Id.* at 1177:5-8. Dr. Bresnahan debunked Dr. Israel's untested assumption that appearing on the parties' "National Customer" list denoted any vulnerability to a discriminatory price increase (*i.e.*, price inelasticity). Bresnahan, Hearing Tr. at 2146:12-16 (being on the "National Customer" list "can't be used to define a market this way"); *id.* at 2147:20-22 ("The idea that the—that the [National Broadline Customers] are all commonly vulnerable, just because they're on that list is one that I have disproved."); *id.* at 2148:19-22; *id.* at 2206:25-2207:2; *id.* at 2207:6-12.

142. Similarly, the FTC and Dr. Israel have failed to show that the parties can discriminate among firms within the "National Customer" grouping, as they have offered no observable characteristics distinguishing firms that source nationally from similarly situated firms that source regionally, *see* Bresnahan, Hearing Tr. at 2147:24-2148:22 (no way to identify customers for price increase because customers who sole source today can credibly threaten to switch to regional sourcing), to say nothing on "Nationwide Customers'" ability to credibly threaten to switch demand to other distribution channels, *see infra* §§ VI.D, VIII.B.1.

143. In short, Dr. Israel set out an economic framework, but then performed no analysis. *See* Bresnahan, Hearing Tr. at 2170:22-2171:5 ("I think he's misinterpreting the Horizontal Merger

Guidelines, he's treating them like they're a cook book, and that's not what they are. The Horizontal Merger Guidelines are a way to organize reliable economic analysis where the appropriate analysis is economic on all the different topics into a uniform frame, and so he's taken quotes from the Horizontal Merger Guidelines, but at each of those junctures, you need to do some reliable economic analysis, and I don't think he's done that.") ; *see also* Hausman, Hearing Tr. at 1969:1-15 ("all [Dr. Israel] did was to take the customer list—you know, he testified he took the customer list from Sysco and he took the customer list from USF, and whatever they named national customers, he said they could be price discriminated against, and defined a price discrimination market based on that. . . . He did no economic analysis at all, at least that I'm aware of."). Not only does Dr. Israel's work fail to pass muster under the Guidelines, it also belies the FTC's promise to the Court of a sound economic foundation justifying the distinction between "National" and "Local" customers. *Compare* Hearing Tr. at 24:18-24 ("[WEISSMAN]: And what we're saying here is there's a targeted group of customers, the national customers, under the merger guidelines test, and Dr. Israel's going to lay that all out for you. THE COURT: And you would then supply a SSNIP to the national customer group— MR. WEISSMAN: Exactly."), *with* Israel, Hearing Tr. at 1155:18-1156:7 ("Q: And you didn't do a SSNIP test, so—you didn't take a list of names, pour it into a computer that does a SSNIP, and out comes something different, other than the names the companies gave you; isn't that a fact? . . . . A: That's a—I took the list for purposes of my targeted grouping, yes."). Dr. Israel attempted no SSNIP test or other analysis that would enabled him to support a claim that "National Customers" have an observable characteristic that would make them commonly vulnerable to a price increase.

144. Dr. Hausman, author of a seminal paper on the issue, explained that for price

discrimination to be profitable, the discriminating firm must be able to determine correctly the customers' demand elasticity 64.5% of the time. Hausman, Hearing Tr. at 1968:9-14. Dr. Israel admitted he performed no such analysis, and overwhelming evidence in this case—including evidence of regionalization and customer switching—indicates that "National Customers" do not require Sysco or USF's products.

145. Dr. Israel's price discrimination market fails also as a matter of common sense. Dr. Hausman noted that he has seen price discrimination markets in the past, but that a price discrimination market in which targeted customers have lower margins than non-targeted customers "would be an all-time first, because you target people to charge them more and not to charge them less." Hausman, Hearing Tr. at 1969:22-1970:17. He pointed out that "National Customers" have lower margins than "local" customers—"exactly the opposite of what you would expect" from Dr. Israel's assertion that "National Customers" can be price discrimination targets. *Id.* at 1970:24-1971:6. Indeed, [redacted]

146. The distinction between "National" and "Local" customers affected every facet of Dr. Israel's analysis going forward—notably, he did not calculate market shares in, or evaluate, a general broadline market. Israel, Hearing Tr. at 922:12-13 ("It's really going to [a]ffect everything we say from this point forward."). It tainted his market share calculations, his analysis of harm (which relied on his market share calculations), and ultimately his conclusion that the merger would have anti-competitive effects.

147. The distinction between "National" and "Local" customers was integral to Dr. Israel's

market share calculations for "National Broadline Customers." Dr. Israel calculated market shares by dividing broadline sales to customers on the parties' "national customer list" (the numerator) by his estimation of the overall size of the "National Broadline Customer" market (the denominator), [redacted] Dr. Israel's "baseline" for the overall size of the "National Broadline Customer" market (the denominator) was [redacted], rising to only [redacted] under his most conservative analysis, [redacted] *See generally, infra* Appx. A § VI.A (analyzing weaknesses of Dr. Israel's sensitivity analyses)

148. Dr. Israel's calculation of the overall size of the "National Broadline Customer" market (the denominator), is contrary to how actual market participants view the market, and excludes most competition in the industry. Dr. Israel's "conservative" estimate of a [redacted] market pales in comparison to the testimony of US Foods' Tom Lynch, which made clear USF's "national" sales team competes for "well over $100 billion" in sales, Lynch (USF), Hearing Tr. at 1742:8-1745:1, [redacted] Indeed, overwhelming evidence by industry participants, including customers, indicate that Dr. Israel's calculation of the size of the market

was off the mark. *See infra* § VI.B. Dr. Israel, by contrast, did not cite a single business document reflecting his purported market shares, Israel, Hearing Tr. at 2391:18-2392:8.

149. Dr. Israel conceded that he had "no reason to dispute" Mr. Lynch's testimony that USF's "national customer" team competes for over $100 billion in sales. Israel, Hearing Tr. at 2366:16-17; *see also* Lynch (USF), Hearing Tr. at 1742:8-1745:1; DX-02083 (adding up the specific segments referenced by Mr. Lynch in his testimony yields a total market size of $143 billion). Dr. Israel's only attempt to harmonize Mr. Lynch's figure with his own narrower market was to speculate that "a number like this would be consistent if somebody included a lot of systems," Israel, Hearing Tr. at 2367:2-3, which fails both as a matter of logic (because it is inconsistent to include chain restaurant business won by USF, which does not have a systems division, in the parties' share of the "National Broadline" market, while excluding it from the overall market when USF loses the bid) and mathematics (because the overall systems segment size of $40 billion fails to close the gap between Dr. Israel's $34 billion total market and Mr. Lynch's $100+ billion dollar figure that Dr. Israel does not dispute, *see* DX-02016, at 3 ("Total customized")).

150. Dr. Israel and the FTC also failed to obtain the information necessary to establish the overall market size for broadline distribution sold to "National Customers," because the FTC never obtained sales data from all broadline sellers to "National Customers" nor did it obtain purchase data from "National Customers"—data that would have been necessary to accurately determine the overall size of the market. Bresnahan, Hearing Tr. at 2076:7-2077:11; Israel, Hearing Tr. at 2364:7-16. Instead, Dr. Israel relied on an RFP data set so beset with infirmities that the parties repeatedly informed the FTC that it was unreliable, s*ee infra* Appx. A ¶¶ 30-31, and [redacted]

[redacted]

151. Dr. Israel erroneously claimed also that broadline distribution constituted a relevant product market, a market that would exclude other foodservice distributors, such as specialty and system distributors. He attempted to delineate the relevant product market using aggregate diversion analysis but that analysis failed. Broadly speaking, aggregate diversion analysis contains three steps: (1) calculate the *threshold* (or critical) aggregate diversion ratio: the percentage of switchers that would need to stay within the candidate product market for a given price increase to be profitable; (2) estimate the *actual* aggregate diversion ratio: the percentage of switchers that would actually stay within the candidate product market following the price increase; and (3) compare the two: if the percentage of switchers staying within the candidate market is above the threshold level, a hypothetical monopolist would find it profitable to raise price and the candidate product market is a properly defined antitrust market. Dr. Israel's analysis failed at the first two steps, thereby making the third impossible. As Dr. Hausman made clear, Dr. Israel simply used the wrong formula in step (1) when calculating the threshold aggregate diversion ratio. Hausman, Hearing Tr. at 1964:17-22; DX-00058, Oystein Daljord et al., The SSNIP Test and Market Definition with the Aggregate Diversion Ratio: A Reply To Katz and Shapiro, 4 J. Competition L. & Econ. 263-70 (2008); DX-02251, Joseph Farrell & Carl Shapiro, Improving Critical Loss Analysis, The Antitrust Source 5, n.17 (Feb. 2008). This misstep, along with the use of an incorrect margin resulted in Dr. Israel underestimating the percentage of switching customers who would need to stay within broadline in order for broadline to be a relevant market. This is an error that would lead him to define a relevant market that was too narrow. Hausman, Hearing Tr. at 1964:7-14. Dr. Israel failed step (2) as

well, since he did not reliably estimate the actual aggregate diversion ratio and, instead, simply claimed that it was higher than the threshold level. Dr. Israel did not use any reliable evidence on substitution behavior and had no evidence of any switching that could be attributed to a change in price as required for the test. *See infra* ¶ 155, Appx. A ¶¶ 202, 243. Dr. Israel thus defined [redacted] leading to [redacted] And, as Dr. Hausman demonstrated by using the proper formula, the threshold level that the aggregate diversion ratio would have to exceed in order to define a "National" broadline market is well over 100%, a rate which Dr. Hausman termed "an impossibility." Hausman, Hearing Tr. at 1974:16-1975:9. Because the proposed market would require an aggregate diversion ratio that is impossible to achieve, Dr. Hausman concluded "that the market must be broader than the national customer market." *Id.*

152. Dr. Israel's aggregate diversion analysis, which he used to support his claim that broadline distribution is a relevant market, also used margins that are too high, because he failed to account for certain variable distribution costs. A margin is calculated by determining the difference between the total price and the total marginal costs, divided by the total price.

(Price – Marginal Cost) / Price

153. Dr. Hausman observed that Dr. Israel's margins were incorrect because Dr. Israel had omitted several significant elements of cost, thereby inflating his margin calculation. Specifically, when Dr. Israel calculated costs for an industry that more or less comprises delivery, warehousing, and selling, *he did not account for certain costs associated with delivery, warehousing, and selling*. Hausman, Hearing Tr. at 1954:21-1956:6. This significant error led "to overly narrow market definitions, upward bias market shares, and overstated harm to consumers." *Id.* at 1955:25-1956:2.

154. Like his untested segregation of "National" from "Local" customers, these two errors had cascading effects for his analysis. They justified his erroneous market shares, which in turn played an integral role in his next closest substitutes analysis and evaluation of harm. His use of the wrong margin throughout also infected his merger simulation model, as discussed below.

155. Dr. Israel's calculation of actual aggregate diversion was flawed as well; indeed, Dr. Bresnahan went so far as to say that what Dr. Israel did was not even conduct a diversion analysis at all. Bresnahan, Hearing Tr. at 2168:8-11 ("I don't think [I] see where there's diversion in there. I mean, he hasn't estimated diversion.").

156. The estimates of what Dr. Israel incorrectly calls a diversion rate are based on unreliable data. Of the 389 paragraphs in his report, [redacted] At the hearing, however, Dr. Israel spent a substantial amount of time defending his analysis, which was based on USF's Linc database for "Local Customers" and the RFP data extracted from the parties by the FTC for "National Customers." Both datasets were flawed.

157. USF's Linc database sporadically contained prospective data about business USF hoped to win and the entity that a sales representative recorded as the "main competitor" for that business. Bresnahan, Hearing Tr. at 2165:3-15. Because prospective data cannot be used to determine actual substitution, Dr. Israel metamorphosed the "main competition" field, assuming that these data reflected actual wins and losses by the "main competitor," an assumption that has no basis in fact or the record. [redacted] Overwhelming testimony and evidence demonstrated that the Linc database was unreliable and could not support the use to which Dr. Israel put it. *See, e.g.*, Bresnahan, Hearing Tr. at 2164:1-2166:15; DX-01359, [redacted] Schreibman

(USF), Hearing Tr. at 1505:5-1506:24. Indeed, Dr. Israel's claim that [redacted] of lost sales opportunities went to other broadline distributors, [redacted] is incredible on its face, and is certainly belied by the copious evidence in this case of local customers switching freely between broadline and other distribution channels.

158. The RFP data relied on by Dr. Israel were *ad hoc* responses to the FTC's request for data, and were unreliable, as the parties told the FTC at the time the data were collected. *See, e.g.*, Sonnemaker (Sysco), Hearing Tr. at 1601-10-1611:25 (explaining the process of collecting the RFP data, the numerous letters that Sysco sent to the FTC explaining that the data were flawed and not kept in the ordinary course of business, and ultimately testifying that he would not recommend anyone rely on the data); [redacted] Despite the FTC's knowledge that this data were not collected in the ordinary course of business or reliable, Dr. Israel still [redacted] although he acknowledged that [redacted] Finally, the bulk of Dr. Israel's analysis relied on FTC-composed declarations. [redacted] Because these declarations proved inaccurate, unfounded, and unreliable, Dr. Israel's analysis is unreliable as well.

E. THE FTC'S "NATIONAL BROADLINE CUSTOMER" LIST IS ARBITRARY

159. The overwhelming weight of evidence demonstrates that the FTC's proposed distinction between "National" and "Local" customers does not reflect market reality.

1. The FTC And Dr. Israel Rely Solely Upon Internal Sysco and US Foods National Customer Lists That Were Created For Administrative Reasons And Are Economically Meaningless

160. The core of the FTC's distinction between "National" and "Local" customers is defendants' internal administrative classification of some accounts as "national." Instead of using economic analysis to determine the boundaries of its product market, the FTC claims that a list of customers maintained by defendants demonstrates which customers have well-defined and substantially similar demand characteristics and which do not. Israel, Hearing Tr. at 1155:12-1156:7. But if that list does not group customers by the nature of their demand, it follows that the FTC's list of "National Customers" is not an economically meaningful product market.

161. The "National" label on which the FTC rests its case is merely an internal administrative term used to classify those customers whose accounts are managed at corporate headquarters rather than locally. Sonnemaker (Sysco), Hearing Tr. at 1347:3-1348:8. It does not classify customers by the nature of their demand. *See, e.g.*, Lynch (USF), Hearing Tr. at 1695:1-3. The arbitrariness of this distinction is demonstrated by the fact that similarly situated customers do not receive similar classifications. For example:

- *Restaurants.* [redacted]
- *FSMs.* [redacted]

162. Furthermore, customers can choose to switch from central management to local management and vice versa. [redacted] Under the FTC's logic, these customers *switch product markets* without changing the actual product (distribution services) they buy. *See* DeLaney (Sysco), Hearing Tr. at 1347:23-1348:1 ("But ultimately the customer makes the choice whether they want the sales leadership to be domiciled in a local operating company or at the corporate office.").

163. PFG makes the same administrative distinctions, separating customers that choose to maintain their contracts at the national office from those that prefer management from the local distribution centers. George Holm explained that not all "National Customers" require nationwide distribution. Holm (PFG), Hearing Tr. at 826:16-22; 827:14-828:8. Indeed, it would make little sense for PFG to classify its customers as "National" based on the geographic extent of their demand, given that PFG currently does very little distribution in the western half of the United States. *Id.*

164. In short, the FTC has taken a list maintained by defendants and claimed that the customers on that list represent an economically meaningful segment of the market. But that list cannot bear the weight the FTC and its expert put on it.

2. The Companies On Sysco's And USF's National Customer Lists Bear Little Resemblance To The FTC's Criteria For Customers Who Supposedly Require National Broadline Distribution Services

165. The FTC's distinction between "National" and "Local" customers fails for another reason—it does not accurately describe market behavior. Indeed, the evidence demonstrated that regional distribution is an attractive distribution model for even the largest "National Customers," which is real-world evidence of substitution out of the FTC's "National Customer"

market even at current prices:

- The Defense Logistics Agency, for instance, breaks the nation into 42 regions, and is serviced by at least 12 different distributors nationwide. *See* DX-00250, Defense Logistics Agency, CONUS Regions.

- [redacted] contracts separately with each of the 58 distribution centers that service it. [redacted]

- [redacted] an FSM, divides its purchases across 70 regions to [redacted]

- [redacted] recently dropped USF as its sole, nationwide distributor and moved to regional distribution using six distributors, but just over half as many distribution centers. [redacted]

- [redacted] splits its network into five regions and uses multiple distributors in each. Indeed, [redacted] currently uses 11 distributors. [redacted]

166. Dr. Bresnahan's analysis confirmed that many of the FTC's "National Customers" could turn to regional distributors in response to a SSNIP. Only [redacted] of Sysco "National Customers" and [redacted] of USF "National Customers" use more than [redacted] distribution centers, while [redacted] and [redacted] of Sysco and USF "National Customers" use [redacted] or fewer distribution centers, [redacted] meaning regional distributors like Ben E. Keith, Reinhart, or Cash-WA would likely be able to handle the business of many of these customers alone.

167. [redacted] the chief executive of large broadline distributor [redacted] testified that term "national broad-line customer" is oxymoronic because the broad-line business is

inherently local. DX-00264, [redacted] And [redacted] would never use the term "national broad-line customer" while he "was in leadership" because he is not aware of any customers that fit this description. *Id.* [redacted] offered as one example of how broadline competition is inherently local the difference between Rochester, New York and Wilkes-Barre, Pennsylvania.

[redacted]

168. [redacted] in order to be effective with broad-line customers, a food distributor must therefore know the customer's business at the local level. DX-00264, [redacted]

169. Other competitors view the industry regionally too. *See* DX-00299, [redacted]

[redacted]

170. Since customers exhibit a wide variety of characteristics, there are some—but not many—nationwide customers who prefer to contract with a single, nationwide or geographically dispersed distributor. But the many examples of similar customers who contract regionally demonstrate that sole-source distribution is not a requirement for these customers—it is, again, a mere preference. *See, e.g.*, Thompson (Interstate), Hearing Tr. at 247:23-25 ("It's not my preference [to use regional distribution]."); DX-00265, [redacted]

171. Given the reality of regional distribution for even the largest "National Customers," the FTC's claim that "National Customers" require "a broadline distributor with national distribution capabilities" is false. FTC Mem. at 20. Customers prefer fewer distribution centers—not more—since fewer distribution centers means higher volume per warehouse and thus lower freight costs from manufacturer to warehouse. *See supra* ¶ 70.

172. For substantially similar reasons, the abstract characteristics that the FTC says defines "National Customers" do not fit. The FTC asserts that, due to "geographic dispersion,"

"National Customers" "typically" require: a single contract; a single point of contact; product consistency; a single ordering platform; a single technology platform for transaction and other reporting; and consistent pricing and terms *across all customer locations*. FTC's Response No. 2 to Defendants' First Set of Interrogatories.

173. Even assuming the presence of some set of factors that customers "typically" require could provide the specificity necessary to delineate a well-defined antitrust product market, point for point, these factors do not support a "National Customer" market in which USF and Sysco are head and shoulders above the rest.

a. **Geographic Dispersion**

174. The foundational premise of the FTC's definition is flawed, as geographic dispersion of "National Customers" is not uniform, but instead exists along a spectrum. Many of the FTC's "National Customers" are not geographically dispersed, and a single local or regional distributor could easily satisfy their demand—[redacted] Given that the size of "National Customers" varies immensely, finding requirement common across all "National Customers" is a tall order—and one the FTC has not met.

175. Many healthcare GPOs use a regional model for their members. For example, Mr. Lindahl of HPSI testified that HPSI awards contracts on a state-by-state basis. Lindahl (HPSI), Hearing Tr. at 1405:24-1406:3; *see also* [redacted] HPSI contracts with leading regional distributors in the geographies in which those distributors have a strong presence. For example, FSA, with which HPSI contracts, "is a strong competitor in the Northwest United States." Lindahl (HPSI), Hearing Tr. at 1407:13-15. Gordon Foodservice ("GFS") is a "strong food distributor" in Michigan and surrounding areas. *Id.* at 1407:16. Martin Brothers is "a very strong regional broadline food distributor in the state of

Iowa." *Id.* at 1408:7-12. Shamrock is a "big player in Arizona as far a healthcare is concerned." *Id.* at 1409:14-19.

[redacted]

b. **Single Contract Across All Locations**

179. Almost all customers, large and small, use alternative distribution channels for some portion of their demand. *See* Szrom (VA), Hearing Tr. at 100:3-8 (purchasing from small business, disabled-veteran owned business, and specialty for produce, bakery, and dairy); DX-00270, [redacted] Customers already deal with multiple points of contact. *See* DX-00270, [redacted]

180. With regard to individual distributors, the evidence demonstrates that a substantial

number of customers do not value a single contract across all locations of any given distributor; indeed, any customer that contracts with multiple broadline distributors does not accord this characteristics the primacy the FTC does. These customers include [redacted] (showing contracts with 12 "prime vendors" and 137 specialty distributors), all of whom either negotiate multiple contracts across regions or allow members to choose among the many negotiated contracts available to them.

181. For the many companies that source regionally, it is simply not true that a single point of contact across all purchases, or even all broadline purchases, is a valued attribute. Many of the FTC's customers with a nationwide footprint do not require or even want a single point of contact. *See, e.g.*, DX-01359, Bresnahan Rpt. at 40-41, Exhs. 6-7 (demonstrating regional footprint of so-called "National Customers"). For most distribution-related issues, the contact is between the customer and the local distribution center, not the "National" contact. DX-00289, [redacted]

c. **Product Consistency**

182. By and large, product consistency is not within the control of a distributor; it is controlled by the manufacturer. DX-01359, Bresnahan Rpt. at 73. A primary way that "customers that value consistency achieve it is through direct negotiation with manufacturers to create proprietary products, *i.e.*, products that are unique to the customer and frequently branded as such." *Id.*; *see also* Szrom (VA), Hearing Tr. at 93:18-94:6 (for the VA's "most highly critical items required throughout all hospitals that need to be standardized" the VA enters deviated pricing agreements with manufacturers); *id.* at 138:24-139:5 (same). Thus, [redacted] of the products

purchased by "National Customers" who use 10 or more distribution centers are either nationally branded or proprietary. DX-01359, Bresnahan Rpt. at 73. While customers could seek consistency through the nationwide use of private-label products, these products are not consistently available, suggesting that consistency, at least in the sense the FTC uses the term, is not a priority for "National Customers." *Id.* at 74 (only 2.8% of private-label SKUs were available in at least 80% of Sysco distribution centers, and only 5.5% of private-label SKUs were available in at least 80% of USF distribution centers).

183. Most "National Customers" have no need for product consistency across multiple locations. *See, e.g.*, DX-00265, [redacted] Indeed, some "National Customers" choose to source regionally because they want the best products available *in that region*, prizing quality over consistency.

184. Even where a large customer does want product consistency across various geographies, this can be accomplished across multiple distributors. *See* DX-00320, [redacted]

d. **Single Ordering and Technology Platforms**

185. The many customers that purchase regionally demonstrate that a single ordering platform is not a priority. And for those customers that do value a single ordering platform, DMA offers a single ordering platform across the country without sole-source distribution. *See* DX-00236, [redacted]

186. Moreover, customers do not need a broadline distributor to provide a single technology platform. Many customers turn to third-party platforms, *see* DX-00308, [redacted]

[redacted] and some, [redacted] have developed their own proprietary software to accomplish the same function, DX-00279, [redacted] In short, this is not a characteristic that makes broadline distribution unique or valuable.

e. **Consistent Pricing and Terms**

187. As with volume purchasing, consistent pricing and terms for products is controlled more by manufacturers than distributors, and does not apply to GPOs. For non-GPOs that do not negotiate with manufacturers, consistent pricing and terms is often not an important characteristic, as these customers compare prices nationally and regionally to find the *cheapest* distribution option. Similarly, while Sysco and USF may offer consistency in pricing, it comes at a cost. Many customers prefer regional distributors with fewer distribution centers, which generally leads to lower inbound freight costs. *See* Schreibman (USF), Hearing Tr. at 1503:11-15 ("So the rationale is the larger more sophisticated customers want to disaggregate all the cost of getting the product from the manufacturer to them, and what they understand is one of the material costs is what's called inbound freight.").

188. Even for customers that use one broadliner for multiple geographies, prices are not centrally determined; [redacted] Schreibman testified that "customers like Sonic and Subway, they will bid their business regionally, and as a result we will bid their business regionally…and

the price will be different based on that geography." Schreibman (USF), Hearing Tr. at 1528:21-25. Even SPV-4, the contract awarding all of the VA's broadline distribution to one distributor, has prices that "vary across the country if they're not deviated prices," and did not "for a particular category have one set of prices across the nation." Szrom (VA), Hearing Tr. at 184:21-185:8. [redacted]

189. Real-world examples demonstrate how regional pricing actually benefits many so-called "National Customers." [redacted] And even if some "National Customers" could not purchase regionally, the FTC has not demonstrated that these customers

are so numerous that a price increase on *all* "National Customers," including those who do contract regionally, would be profitable.

F. THE FTC IMPROPERLY EXCLUDES COMPETITION PROVIDED BY NON-BROADLINE COMPETITORS FROM BOTH OF THE PRODUCT MARKETS ALLEGED IN ITS COMPLAINT

190. The FTC contends that various distribution channels are not in the relevant market because customers cannot satisfy all their foodservice distribution needs through that channel, and that broadline distribution should be compared to other channels separately and individually. These arguments ignore customers' ability to allocate purchases freely across multiple distribution channels simultaneously, allowing them to defeat a SSNIP without allocating *all* of their purchases to a single alternative distribution channel. *See, e.g.*, Thompson (Interstate), Hearing Tr. at 252:3-25 (Interstate uses numerous specialty distributors and USF "work[s] hard to get all of [that] business"); Hoffman (Upstream Brewing), Hearing Tr. at 346:25-347:3, 361:17-19 (50% of spend is with specialty purveyors and, for example, the bulk of produce orders "swing[] back and forth between US Foods" and a specialty distributor); DX-00191,

[redacted]

[redacted]

191. Where customers can allocate demand for fungible goods across multiple distribution channels, the fact that a competitor distribution channel is not a perfect substitute is irrelevant.

[redacted]

192. The relevant question is whether customers could divert a material portion of their demand *from* broadline to competitors in other channels such that a SSNIP would be unprofitable. PX06059, HMG § 4.1.3 ("The hypothetical monopolist's incentive to raise prices depends . . . on the extent to which customers would likely substitute *away from* the products in

the candidate market in response to" a SSNIP (emphasis added)); *id.* ("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." (emphasis added)). *See* DX-01359, Bresnahan Rpt. at 9 ("If enough buyers included within a proposed relevant market can substitute *out* of it by buying from suppliers who are outside the defined market, the relevant market is defined too narrowly."); DX-01355, Hausman Rpt. ¶ 26 (When the hypothetical monopolist increases its price, its profits increase on customers who continue to purchase its product, but it loses the previous profits on customers who discontinue their purchases."); DX-01359, Bresnahan Rpt. at 121 ("But a buyer does not need to switch all purchases to another supplier to discipline a price increase. If a customer switches some of its purchases from, for example, a broadline distributor to a specialty distributor in response to a price increase at the broadline distributor, that loss of sales will certainly make the price increase less profitable and could make the price increase unprofitable. Distributors do not have to lose all a customer's business to want to avoid losing a substantial share of its business."). [redacted]

[redacted]

1. **The Merged Company Could Not Profitably Raise Prices To So-Called "National Customers"**

194. The FTC has not carried its burden to demonstrate that broadline distribution services

sold to "National Customers" is a relevant product market because actual evidence of substitution across distribution channels demonstrates that a SSNIP in the FTC's "national broadline" market would not be profitable.

a. **"National Customers" Divide Their Demand Across Multiple Distributors And Multiple Channels**

195. The FTC's market definition did not account for the fact that "National Customers" frequently divide their demand across multiple distributors and multiple channels, and thus could divert revenue away from Sysco in the event of a price increase. *See, e.g.*, Thompson (Interstate), Hearing Tr. at 203:20-204:9, 251:4-11 (purchasing directly from manufacturers, GPOs, two broadline distributors, and a multitude of specialty distributors); DX-00320, [redacted]

b. **Systems and Broadline Distribution Are Functionally Interchangeable For Many "National Customers"**

196. For many "National Customers" broadline and systems distribution are functionally interchangeable, as demonstrated by the fact that similarly situated "National Customers" take divergent approaches to their use. *See generally* DX-01359, Bresnahan Rpt. at 82-86. [redacted] And many "National Customers" do not recognize a meaningful distinction between broadline and systems distribution. [redacted]

[redacted]

197. The industry also does not recognize a "National Broadline Customer." USF does not have a separate systems distribution business, and serves so-called "systems customers" and "broadline customers" out of the same distribution centers.

198. Dr. Bresnahan demonstrated the wide variation in the extent to which "National Customers" use broadline and systems. DX-01359, Bresnahan Rpt. at 82-85. If these product were complements, rather than substitutes, the ship-to locations from broadline and systems would overlap—*i.e.*, a single customer location would receive "systems goods" from a systems distributor and "broadline goods" from a broadline distributor. *Id.* at 84. But this is not the case, which confirms that "National Customers" are using systems and broadline as substitutes, not complements. *Id.*

199. On a more general level, the FTC's distinction between systems and broadline customers fails. [redacted] If this distinction were

meaningful, similarly situated customers would be similarly classified—but they are not.

c. **Specialty Distributors Constrain Broadline Pricing**

200. The evidence also demonstrated that specialty distribution also constrains broadline pricing. *See* Thompson (Interstate), Hearing Tr. at 251:3-252:10 (Interstate uses specialty distributors for produce, meat, and fish, all business for which USF competes). Many "National Customers" allocate substantial portions of their overall spend to specialty distribution:

[redacted]

201. Real-world examples demonstrate how specialty distribution disciplines broadline pricing.

[redacted]. At the hearing, David Schreibman testified that US Foods directly competes with specialty distributors, which compete against US Foods "by having a broader array of products within their expertise," and by using staple products as loss leaders. Schreibman (USF), Hearing Tr. at 1452:5-16. US Foods lowers its prices to compete with specialty distributors. *Id.*at 1452:17-22. Likewise, James Thompson of Interstate acknowledged that USF competes fiercely with specialty distributors, and that Interstate's spend with specialty distributors represented lost revenue to USF. Thompson (Interstate), Hearing Tr. at 251:9-16 (while Interstate uses specialty distributors for produce, US Foods "would love to sell produce to my hotels."); *id.* at 252:3-10 ("Q. And US Foods would like all of your meat business, wouldn't they? A. They work hard to get all of our meat business. Q. . . . US Foods competes with specialty retailers in an effort to get all of your meat business; right? A: That's correct."); *id.* at 252:15-17; *id.* at 252:15-17 ("Q. Do they compete with your specialty seafood distributors to get the seafood business of your hotels? A: I would say that they do."); Lynch (USF), Hearing Tr. at 1709:25-1710:25 (US Foods had to lower its prices to compete with specialty distributors for two large customers, Fogo de Chao and Tavistock).

202. Specialty distributors are capable of winning large parts of broadliner business; customers can use their large contract items to discipline broadliners. *See, e.g.*, DeLaney (Sysco), Hearing Tr. at 1350:10-1351:22 (in response to any anti-competitive conduct, customers could give away certain markets or certain product line to competitors). Sonnemaker (Sysco), Hearing Tr. at 1585:3-20. Likewise, Inland Seafood won Aramark's frozen catfish contract away from Sysco. *Id.* at 1586:3-15 (referring to DX-00546). Pro*Act, a group of more than 50 produce distributors, has taken large chunks of business away from Sysco—recently, $40 million in business from Compass, a large nationwide customer. *Id.* at 1584:7-1585:2 (referring to DX-01015).

203. Assuming there exists a "National Customer" market, the FTC fails to offer economic analysis demonstrating that it is limited solely to broadline distribution, and erroneously excludes systems and specialty distribution from it.

2. The Merged Company Could Not Profitably Raise Prices To So-Called "Local Customers"

204. The FTC has failed to carry its burden to demonstrate that broadline distribution sold to "Local Customers" is a relevant product market, because competition for "Local Customers" is fierce across distribution channels and, like the FTC's "national broadline market," actual evidence of switching demonstrates that a SSNIP in this market would not be profitable. *See generally* DX-01359, Bresnahan Rpt. at 107-113.

205. Competitors state that competition between all distribution channels is robust in local markets. [redacted]

[redacted]

206. "Local Customers" testify that they could allocate a material portion of their demand away from the combined entity in response to a SSNIP, even if it means having to purchase from a number of "small guys." [redacted]

[redacted]

207. The FTC has not provided any economic analysis demonstrating that a SSNIP in its "Local Customer" broadline market would be profitable, and real-world evidence demonstrates that the FTC has erroneously excluded specialty and cash and carry distributors.

a. Local Customers Frequently Use Multiple Distributors And Distribution Channels, Which Can Discipline A Price Increase By The Merged Entity

208. "Local Customers" frequently use multiple distributors. Industry organization research indicates that the typical independent customer uses 12 different distributors. [redacted] Hoffman (Upstream Brewing), Hearing Tr. at 355:23-360:56 (Upstream

[redacted] *see also* Brawner (Sysco), Hearing Tr. at 1664:23-1665:3 ("Q. Now, in your experience, Mr. Brawner, do customers use a single foodservice distributor? A. You know, we wish they would. It's —it's—no, they don't. There's just so many options and so many competitors and so many specialty companies that provide specialty products in certain categories."); Hearing Tr. at 1737:18-19 (video testimony of Hodges (Elmo's Diner) Dep. at 29:18-32:9) (referring to DX-01894 (testimony and exhibit concerning Elmo's Diner's purchases from US Foods, Orrell's, Sysco, Sam's Club, EG Forrest, and Performance/IFH)); [redacted]

209. In determining an optimal distribution mix, "Local Customers" regularly compare prices across distribution channels and distributors, switching between them on a weekly basis depending on which distributor offers the best price and product. *See, e.g.*, Hoffman (Upstream Brewing), Hearing Tr. at 361:10-19 (comparing prices between specialty and USF on a weekly basis and switching purchases back and forth); [redacted]

[redacted]

210. "Local Customers," including many of the FTC's declarants, testified that switching purchases between distribution channels is not difficult. *See* Hoffman (Upstream Brewing), Hearing Tr. at 361:17-19 (purchases "swing[] back and forth between US Foods" and a specialty distributor); [redacted]

[redacted]

b. **Competition Is Fierce Among Broadline Distributors Serving "Local Customers"**

212. Broadline distributors have wide-ranging product offerings that enable them to service

"Local Customers. Brawner (Sysco), Hearing Tr. at 1792:16-22 ("Q. In you experience, do these competitors have the products that enable them to compete with Sysco for your customers? A. Oh, absolutely. They're all broadliners, so they all carry all the categories of products to be identified as a broadliner."); [redacted]

213. Broadline distributors, such as Pate Dawson, Merchants Foodservice, and Cheney Brothers, compete aggressively for "Local Customers" by offering various incentives, including upfront money, rebates, and trips. Brawner (Sysco), Hearing Tr. at 1793:13-1794:14. *See also id.* at 1795:4-1796:11 (discussing DX-02237; Sysco ultimately granted an Internal Request for Incentive to counter PFG's offer to "Local Customer" in South Carolina).

214. Broadline distributors also compete for each other's employees. Brawner (Sysco), Hearing Tr. at 1804:5-11 ("[O]ver the last six to nine months, we've lost over 21 sales associates to PFG, and few to Gordon"); Holm (PFG), Hearing Tr. at 811:16-182:1 (PFG's recent salesmen hires in South Carolina and Georgia primarily have come from Sysco and USF, and those salesmen have "done a good job" bringing their customers with them to PFG).

215. This competition has led "Local Customers" to switch their business from one broadline distributor to another, [redacted]

[redacted]

c. **Specialty Distributors Are Highly Competitive For "Local Customers," And The Threat Of Switching Business To Specialty Distributors Will Discipline A Price Increase**

216. Other "Local Customers" prefer specialty distribution to comparable broadline offerings, since specialty distributors often source locally and support local producers. [redacted] *see also* Schablein (Wintergreen), Hearing Tr. at 529:24-530:8 ("[T]here's a lot of market to table situations so we also try to use some local farms in order to get some product just to support that . . . . [T]he folks in charge of the food decisions, if you will, certainly feel that the best route to go for both fresh food and fresh produce is some of these specialty providers."); Brawner (Sysco), Hearing Tr. at 1799:13-19 (Using specialty providers for all or a majority of one's purchases, "it's kind of a trend in the industry . . . . it's called farm-to-plate, and it's where a lot of these chefs now are utilizing local, local seafood, local produce, local beef, local poultry, and that's somewhat their marketing strategy."); [redacted]

217. Certain "Local Customers" will even use specialty distributors for all or a majority of their foodservice distribution needs. Brawner (Sysco), Hearing Tr. at 1799:19-1800:5 ("There's a restaurant in Columbia called Terra . . . . his strategy is farm-to-plate, and he buys the majority of his product from specialty companies, from local farmers, from—you know, it's basically all local."); [redacted]

[redacted]

218. Specialty distributors compete directly with broadline distributors enabling "Local Customers" to leverage the competition for better pricing. In fact, the FTC's Omaha hearing witness admitted that he buys from specialty distributors instead of buying the same product from a broadline distributor. Hoffman (Upstream Brewing), Hearing Tr. at 360:2-5. This was true for: (1) steaks, *id.* at 356:1-2; (2) produce, *id.* at 357:18-358:3; (3) seafood, *id.* at 356:21-25; (4) chicken, *id.* at 358:21-23, (5) pastries, *id.* at 358:4-11; and (6) coffee, *id.* at 358:14-15. Mr. Hoffman even admitted to comparing US Foods' produce prices against a specialty distributor's and alternating his orders between the two. *Id.* at 361:10-18. Finally, Mr. Hoffman agreed that "for seafood[,] there are certain products where [Upstream] can get better pricing from the specialty distributors than [Upstream] can from US Foods." *Id.* at 361:1-6.

219. Specialty distributors also offer signing bonuses and upfront incentives to customers to take business away from broadline distributors. Brawner (Sysco), Hearing Tr. at 1794:20-22.

220. Specialty distributors also offer products beyond their primary specialties, including dry groceries, such as flour, cooking oil, and tin foil. *See* Brawner (Sysco), Hearing Tr. at 1798:11-18, (Limehouse Produce in Charleston, South Carolina is now selling dairy products and Inland Seafood, a strategic seafood company, has branched into beef and poultry.); Sonnemaker

(Sysco), Hearing Tr. at 1561:25-1562:2 ("And Duck Delivery started in produce, but moves into more and more product lines, which is very typical for a specialty house . . . .").

221. Nearly every broadline distributor views specialty distributors as direct competitors within the food distribution market. [redacted]

[redacted]

222. Customers also view specialty distributors as direct competitors (and thus price constraints) to broadline distribution. *See* Hoffman (Upstream Brewing), Hearing Tr. at 362:12-20 (would consider switching from Sysco to specialty distributor in response to a price increase); [redacted]

d. **Cash And Carry And Club Stores Are An Important Competitive Alternative That Can Discipline Price Increases To "Local Customers"**

223. In addition to specialty distribution, cash-and-carry and club stores are an important competitive alternative for "Local Customers." *See, e.g.*, Brawner (Sysco), Hearing Tr. at 1798:20-24 (cash-and-carry store "have had an impact and have become competitors seriously with a lot of our customers."); Hodges (Elmo's), Hearing Tr. at 1859:18-19, [redacted]

[redacted]

224. Self-distribution is a meaningful option for local customers as demonstrated by the many customers who make frequent trips to cash and carry stores. *See, e.g.*, Brawner (Sysco), Hearing Tr. at 1799:3-9 (discussing a customer in Columbia, South Carolina who "buys at least 80 to 90 percent of the products he serves in his restaurant from Sam's Club"); [redacted]

225. While cash-and-carry firms historically have not delivered, their delivery capabilities are expanding, allowing them to take even more business from broadline distributors. Restaurant Depot's win in a California school system RFP was conditioned on its ability to deliver. Schreibman (USF), Hearing Tr. at 1496:9-22. Costco offers delivery of anything in their stores to businesses in select metropolitan areas. Brawner (Sysco), Hearing Tr. at 1804:25-1805:25 (discussing Costco's delivery abilities and DX-05027, a photograph of a Costco truck that says "We Deliver"); [redacted]

[redacted]

226. Restaurant Depot, a cash-and-carry firm devoted solely to restaurant business, [redacted] offers creative distribution options as a means of increasing market share. It currently has a test program where it reimburses customers the cost of the lease of their vehicle if the customer hits certain spending thresholds, [redacted] and its "Keep it Kool" program offers both trucks and refrigeration options to allow customers to transport perishable items up to three hours away, [redacted] Third-party distributors, also called jobbers, shop at Restaurant Depot and redeliver food and food-related products to restaurants and other customers. [redacted] Restaurant Depot offers these third-party distributors volume purchasing discounts. [redacted] Restaurant Depot's strategies have induced consumers to request lower prices from broadline distributors, like US Foods. Schreibman (USF), Hearing Tr. at 1494:16-19.

227. Many "Local Customers" are optimistic that their cash-and carry options will expand. [redacted]

[redacted]

228. "Local Customers" can and do use the threat of diverting purchases to cash-and-carry and club stores to obtain lower prices from broadline distributors. [redacted]

[redacted]

230. Distributors regard cash-and-carry and club stores as strong competitors. [redacted]

[redacted]

[redacted]

232. The opening of a cash-and-carry or club store causes broadline distributors to lose sales, and broadline distributors now conduct price checks on cash and carry and club offerings. *See, e.g.*, Schreibman (USF), Hearing Tr. at 1457:23-1458:14 ("we looked at the three months before and the three months after in proximity to the Restaurant Depot, and what you can see is they have a significant negative impact to our volume when they open up a Restaurant Depot");

[redacted]

G. THE FTC CANNOT GERRYMANDER A PRODUCT MARKET BASED ON CERTAIN CUSTOMERS WITHIN ITS "NATIONAL CUSTOMER" PRODUCT MARKET

233. The FTC's Complaint alleged that broadline distribution services sold to "National Customers"—which included, but was not "limited to" GPOs, FSMs, and hotel and restaurant chains—constituted a relevant product market. *See, e.g.*, Compl. ¶ 41. By contrast, at the hearing, the FTC suggested that broadline distribution services sold to "limited" types of "National Customers," namely, "healthcare customers" and "hospitality customers," could potentially be "further submarkets." Hearing Tr. at 29:16-30:8 ("Will you be asking me to make a determination as to those submarkets? Mr. Weissman: Yes."). This allegation is contrary to the FTC's complaint, the FTC's briefing, which alleged that "National Customers across all classes" would experience anti-competitive effects as a result of the merger, FTC Mem. at 30, and the FTC's own expert, whose "opinion is that that group of customers ['National Customers'] will suffer harm as a whole." Israel, Hearing Tr. at 2381:8-22.

234. The FTC has offered no definition of these possible, newly-minted "submarkets." It is unclear whether the FTC intends for a any product market of broadline services sold to "healthcare customers" to be limited to healthcare GPOs (who are not customers for distribution services, *see supra* ¶¶ 46-50). The healthcare segment of the market is far larger than just GPOs. [redacted] *see also* Sonnemaker (Sysco), Hearing Tr. at 1649:5-8 ("Q: If somebody hypothetically had 50-percent of the healthcare GPOs, does that mean they have 50-percent of the healthcare provide[r] business in the United States? A: Absolutely not."). The same is true if the FTC were now to allege a product market of broadline services sold to "hospitality customers." It is unclear whether the FTC would intend

that "hospitality customers" be limited to hotel chains, or whether this market would also include hotel purchasing organizations, like HSM, and hospitality GPOs like Avendra. The FTC cannot establish anti-competitive effects in a "well-defined" product market when it has not alleged or defined what that product market is. *Brown Shoe*, 370 U.S. 294.

235. The FTC's theory of harm for these customers is also new. The FTC alleged and argued that Sysco and USF were customers' top two choices and thus the elimination of competition between them would permit the merged entity to raise prices on all "National Customers." *See* FTC Mem. at 28-30 (alleging anti-competitive effects for "National Customers across all classes"). Any new theory of harm would appear to need to be that the merged entity will be able to price discriminate against "healthcare customers" and "hospitality customers" as compared to other "National Customers." *See, e.g.*, Israel, Hearing Tr. at 911:22-913:6.

236. Any attempt by the FTC to inject new product markets and theories of harm after the close of discovery is untimely, improper and prejudicial. *See, e.g.*, *Queen City Pizza, Inc. v. Domino's Pizza, Inc.*, 124 F.3d 430, 444 (3d Cir. 1997) ("Plaintiffs have a duty to make the district court aware that they intend to rely on a particular relevant market theory."). The FTC spent over a year investigating this merger, and the parties labored diligently under an aggressive discovery schedule to litigate the case that was alleged by the FTC. Fundamental fairness dictates that this bait-and-switch approach by the government be rejected.

237. It is also doubtful that the FTC's litigation staff possesses the authority to seek to enjoin a merger on the basis of product markets or submarkets not alleged in the administrative complaint voted out by the FTC Commissioners. By a narrow 3-2 margin, and after more than a year of investigation, the Commissioners—just barely—allowed the FTC to move forward with their administrative case against Defendants on the basis of the allegations described in the FTC's

administrative complaint and parallel Complaint. The Commission may authorize its attorneys to "bring suit" in federal court to preliminarily enjoin a merger if a preliminary injunction would aid the FTC's Article I tribunal in effectively adjudicating the FTC's administrative complaint. *See* 15 U.S.C. § 53(b)(2). Since the FTC's administrative complaint does not allege harm in any such product "submarkets," Hearing Tr. at 29:16-30:8, and since the Commission—which voted out the Complaint—did not find reason to believe that this merger violated the antitrust laws based on the FTC's recently-purported "submarkets," there is no authorization for this Court to consider these allegations.

238. Were the Court to consider product markets not alleged in the FTC's complaints, the FTC would not be entitled to any presumption in its favor, since it has not provided expert analysis of, or calculated market shares in, any markets other than those alleged in its Complaint. *See, e.g.*, *Heinz*, 246 F.3d at 725. Indeed, its expert analysis is to the contrary, since Dr. Israel's theory was that "National Customers" "will suffer harm as a whole," Israel, Hearing Tr. at 2381:8-20, and Dr. Israel "did not assess [harm to] specific customers," *id.* at 2381:25-2382.

239. The only economic analysis of Defendants' market power over nationwide customers was provided by Defendants' expert, Dr. Hausman. *See* Hausman, Hearing Tr. at 1971:17-1974:14 (discussing his econometric study); DX-01353, Hausman Rpt. ¶¶ 119-24 ("My econometric results confirm that large customers (those served out of a high number of OpCos) have credible competitive alternatives in addition to Sysco and USF."). Dr. Hausman demonstrated that even for customers using more than 35 distribution centers, Sysco and USF were unable to earn high margins, meaning those customers did not have elastic demand for Defendants' products despite the fact that Sysco and USF were the only companies with nationwide distribution centers. Hausman, Hearing Tr. at 1972:5-23; DX-01353, Hausman Rpt.

[redacted] Dr. Hausman also explained that these lower margins were not caused by competition between the two because "there's a lot of economic theory, including a paper by a—a Nobel Prize winner that discusses—when you only have two people competing, you expect higher prices because they recognize that they only have one competitor and they don't beat each other's brains out." Hausman, Hearing Tr. at 1973:11-15.

1. **Restaurant Chains Will Not Be Harmed**

240. [redacted]

241. The FTC has all but conceded that restaurant chains will not be harmed by the merger. *See* Hearing Tr. at 18:5-10 ("And the fact that certain fast food restaurants and quick service restaurants that may be included in national customers, that they can and sometimes do use systems distribution, tells us very little to nothing about all the other broadline distributor customers we have[.]"); *see also* Israel, Hearing Tr. at 2348 101:2-11 (restaurants may have "options"), and did not call a restaurant chain customer to testify at the hearing.

242. [redacted] They can threaten to divert a material portion of demand to systems distributors, as acknowledged by the FTC in its opening. *See* Hearing Tr. at 18:5-10. Or they can threaten to divert a material portion of their overall demand to specialty distributors. [redacted]

[redacted] To the extent a nationwide restaurant chain prefers a sole-source agreement for broadline distribution, it can choose from Sysco, New PFG, DMA, or MUG/Unipro.

2. FSMs Will Not Be Harmed

243. Much like restaurant chains, the FTC now appears less interested in FSMs, *see* Hearing Tr. at 39:1-5 (focusing on "hospitality customers" and "healthcare customers" specifically), despite the fact that they are "[t]he next largest segment" within the FTC's "National Customer" market. *See* Sonnemaker (Sysco), Hearing Tr. at 1579:5-1580:2. The FTC did not call a FSM witness to testify at the hearing.

244. [redacted]

245. Both Sodexo and Compass procure food regionally. *See, e.g.*, Sonnemaker (Sysco), Hearing Tr. at 1572:15-17. [redacted]

[redacted]

246. Aramark, the third largest FSM, has remained neutral in this litigation. However, it already permits small-scale regionalization, *see* Sonnemaker (Sysco), Hearing Tr. at 1583:20-1584:2, 1636:9-23, and could regionalize further, *id.* at 101:12-14, or turn to other distribution modes, *id.* at 1585:23-1586:2, to defeat a price increase. [redacted]

3. **"Healthcare Customers" Will Not Be Harmed**

247. [redacted] *see also* Sonnemaker (Sysco), Hearing Tr. at 1649:5-8 ("Q: If somebody hypothetically had 50-percent of the healthcare GPOs, does that mean they have 50-percent of the healthcare provide[r] business in the United States? A: Absolutely not.").

248. [redacted] Customers are businesses that serve food to consumers "away from the home—including restaurants, school cafeterias, hotels, and hospitals," FTC Mem. at 1; *see also supra* ¶ 19. Hospitals, acute care facilities, assisted living facilities, and nursing homes are all customers. They receive food from broadline

distributors and prepare it for consumers. *See, e.g.*, Ralph (Premier), Hearing Tr. at 379:6 (referring to GPO members as "the end customer").

249. GPOs, by contrast, "don't buy or sell food," *see* Ralph (Premier), Hearing Tr. at 378:11-20; *compare* Brawner (Sysco), Hearing Tr. at 1783:16-20 (foodservice customers are "anyone that prepares food away from home"). GPOs negotiate contracts with manufacturers and distributors on behalf of their members, receiving a fee from manufacturers whenever a member makes a purchase through a GPO-negotiated contract, *and* a fee from the distributor every time the distributor delivers that product, *see supra* ¶ 46. The only direct financial relationship that exists between a GPO and a distributor is the administrative fee that *the distributor pays the GPO*. *Id.* Thus, it does not make sense to ask whether the combined entity could raise prices to GPOs: GPOs do not purchase anything from distributors.

250. GPO members will benefit from this merger. One of the primary benefits of this merger will be the merged entity's increased purchasing power, which will allow it to compete on par with GPOs when negotiating lower cost of goods directly with manufacturers. *See* Sonnemaker (Sysco), Hearing Tr. at 1591:25-1592:13 (GPOs "could be concerned because, number one, our buying power is going to drive our cost from our manufacturers down and that will allow us to provide a better cost to our customers."); [redacted] These reduced prices will increase competition for GPO members, who are not required to buy off GPO-negotiated contracts, and who will be able to choose to purchase similarly priced goods through either a GPO or Sysco. Indeed, to the extent this direct competition between Sysco and GPOs diminishes the value proposition of a GPO, it will inure to the benefit of GPO members, as

GPOs will be forced to offer their members *more* competitive pricing to retain their business and thus earn administrative fees. *See* Sonnemaker (Sysco), Hearing Tr. at 1412:20-1413:2 (offering lower priced products than GPOs would be "cutting the GPO out"). It is no wonder that some of the most vociferous critics of this merger have been GPOs.

251. This merger will increase what is already significant competition between GPOs and distributors on the cost-of-goods side of the equation. *See, e.g.*, Ralph (Premier), Hearing Tr. at 433:13-435:14 (discussing competition between GPOs and distributors). Thus, the only way that the merged entity could raise prices on GPO members would be to raise distribution prices. [redacted] But there is no evidence that the merged entity would or could do that. *See* Lindahl (HPSI), Hearing Tr. at 1413:18-25 (HPSI's nine broadline distributors compete on distribution pricing and their distribution pricing is "pretty similar").

252. There will be considerable *downward* pressure on distribution prices post-merger. Sysco will have a powerful incentive to lower distribution fees charged to customers sourcing goods through it in order to lure customers away from GPOs. In so doing, Sysco will be able to keep a greater share of the revenue, since it will no longer have to pay the administrative fee that it pays to the GPO when it delivers product to GPO members. *See* Schreibman (USF), Hearing Tr. at 1447:20-22 (the GPO does not receive a fee from the distributor when its members by outside the GPO); *accord* Sonnemaker (Sysco), Hearing Tr. at 1592:20-25 ("Q: But if you had a better deal on catfish or any other product, [a GPO member] could buy it through you; am I right? A: That's correct. Q: And in that instance the GPO would not get its cut or would not get its administrative fee? A: That's right.").

253. GPOs will have every incentive to negotiate lower distribution fees with other distributors. Because the merged entity will now offer competitive cost of goods, the primary way GPOs can remain competitive for customer business (and therefore earn administrative fees) will be to negotiate with other distributors for *lower* distribution costs.

254. For most GPOs, the ability to negotiate lower distribution fees for their members is already part of their business model. GPOs are organized in three ways. First, GPOs may offer overlapping regional awards to multiple distributors. *See* Sonnemaker (Sysco), Hearing Tr. at 1590:21-1591:3 (referencing HPSI and Amerinet); *see also* Lindahl (HPSI), Hearing Tr. at 1405:24-1406:3; [redacted] Second, GPOs may be distributor neutral, which means their members can choose from multiple distribution contracts and the GPO is indifferent as to which contract the GPO member selects. *See* Sonnemaker (Sysco), Hearing Tr. at 1591:4-14 (referencing UHF Navigators and MedAssets); [redacted] Both models offer GPO members "options," Lindahl (HPSI), Hearing Tr. at 1415:25; [redacted] and both models foster competition between distributors, which benefits GPO members. *See* Lindahl (HPSI), Hearing Tr. at 1412:2-7 ("[Y]ou used the term 'distributor neutral.' Does that create competition between the distributors for your members? A: It does, it does, yes. Q: Does that competition benefit your members? A: Yes, it does."). [redacted]

[redacted] In short, GPOs will have every incentive to, and will be able to, play distributors off each other to secure lower distribution costs for GPO members and thus retain their administrative fees as those members continue to purchase through the GPO.

255. This essentially leaves the "rare" cases of GPOs that have "sole source agreement[s] with one distributor." Sonnemaker (Sysco), Hearing Tr. at 1591:15-17. To the extent the merged entity can offer GPO members cost-competitive goods, these GPOs will either lose revenues to Sysco or other GPOs, since members are not obligated to purchase through them, *see* Ralph (Premier), Hearing Tr. at 425:24-426:1, or have to find a way to secure lower distribution costs to induce its current members to continue to purchase through their contracts. And, as the evidence has shown, the way to do that is by harnessing competition among distributors through a regional or distributor-neutral distribution model, *see* Lindahl (HPSI), Hearing Tr. at 1427:2-7, [redacted] In the post-merger world, whether or not customers purchase through a GPO with a sole-source distribution agreement, they will have options, while GPOs will be under intense pressure to offer lower prices than the merged entity.

256. Current GPO members—*i.e.*, foodservice customers—will not be harmed by this merger.

If anything, this merger will *increase* competition for their business, driving down prices.

4. "Hospitality Customers" Will Not Be Harmed

257. The FTC's expert agrees that "hospitality customers," like restaurant chains, will have "options" post-merger. *See* Israel, Hearing Tr. at 2348:2-11 ("I spent a fair amount of time in my direct testimony—and I think Dr. Bresnahan agreed—that restaurants and hotels aren't really—aren't representative of the overall set of purchasers, right? . . . Secondly, [hotels and restaurants are] a group that, you know, is a small percentage of total sales, and as we talked about, is not representative of the overall group, may have some different options."). Dr. Bresnahan similarly agrees that restaurants and hospitality customers will continue to enjoy many options post-merger. *See* Bresnahan, Hearing Tr. at 2117:3-2119:4 (demonstrating substitution by hotel away from the Defendants).

258. Most of the FTC's "hospitality customers," which, again it is unclear whether the FTC intends "hospitality customers" be limited to hotel chains, or whether this market would also include hotel purchasing organizations, do not serve food to consumers outside the home. Hotel owners and ownership groups, however,—the real customers who directly serve consumers of food products—currently have a wealth of options to meet their foodservice distribution needs. Hotel owners can purchase through branded-hotel purchasing organizations, like Starwood and Hilton Supply Management (HSM), which are essentially GPOs that specialize in servicing branded hotels. [redacted] As with GPO members, hotel owners are not required to purchase through these purchasing organizations. [redacted]

some portion of their foodservice purchasing; the other 20% "has relationships with other procurement organizations"); [redacted] Hotel owners can purchase through generalist hospitality GPOs like Avendra. *See* Thompson (Interstate), Hearing Tr. at 200:13-22. They can "procure their food independently" from broadline or other distributors. [redacted] They can contract with hotel management companies, like Interstate, that manage foodservice needs for branded hotels upon request (Interstate is like an FSM for hotels). *See* Thompson Tr. at 199:2-200:4. Or they can mix and match—in the end, even the FTC's own "hospitality customer" witness agrees that "an owner does have some choices." *Id.* at 200:21-22.

259. Hotel owners will benefit from this merger. They already benefit from the competition between the FTC's "hospitality customers." *See* Thompson (Interstate), Hearing Tr. at 250:14-15 (Interstate competes with Avendra); [redacted] And the merged entity's increased purchasing power will offer yet another option for hotel owners looking to create an optimal distribution mix.

260. The FTC's "hospitality customers" also have multiple options to maintain their profitability post-merger. These entities contract with manufacturers (or with GPOs who in turn

contract with manufacturers) to secure low pricing and product consistency—in product categories where that is important—for the vast majority of their goods. [redacted] Thompson (Interstate), Hearing Tr. at 203:20-204:9 (purchasing directly from manufacturers and through Compass, and then purchasing from its two broadline distributors and specialty distributors "for the products that aren't met by the previous two options."); [redacted] In so doing, these organizations efficiently manage many separate contracts. *See, e.g.*, Thompson (Interstate), Hearing Tr. at 204:17-20 (managing 50 to 60). Hotel purchasing organizations also commit significant spend to specialty distributors. *See id.* at 217:1-3 ("we actually do run a pretty significant regional produce program"). [redacted]

261. These purchasing organizations, like hospitality GPOs, are already purchasing regionally or could do so to defeat a price increase. *See* Sonnemaker (Sysco), Hearing Tr. at 1572:11-13 ("Q: All right. Do you have any customer for whom you believe regionalization is not a realistic option, sir? A: No, not a one."). [redacted]

Similarly, although the FTC's own witness from Interstate Hotels expressed a "preference" for

USF, Thompson (Interstate), Hearing Tr. at 247:23-25 (contracting regionally "is not my preference"), Interstate already uses PFG on a limited basis, *id.* at 204:21-205:5, and "most definitely would" evaluate alternative distributors if the merged entity raised prices, *id.* at 283:7-11, including regional distribution, *id.* at 283:12-14. [redacted]

262. Hotel purchasing organizations, like Interstate, that "would prefer to work with one distributor," Thompson (Interstate), Hearing Tr. at 222:6-14, have strong options: (1) New-PFG, *id.* at 281:10-13, 283:15-17; (2) DMA, *id.* at 271:13-19, 281:14-18, and (3) MUG/Unipro.

263. [redacted]

VII. <u>THE FTC HAS NOT PROPERLY DEFINED A RELEVANT GEOGRAPHIC MARKET</u>

264. The FTC alleges two geographic markets: the United States, for alleged "National Customers," and "Local Markets," for alleged "Local customers of broadline services." Compl.

¶¶ 45 (introductory paragraph), 46-49 (defining United States as geographic market for "National Customers"); 50-55 (explaining rationale for definition of local markets); Appx. A (listing specific alleged local geographic markets).

A. THE LEGAL STANDARD

265. In a Section 7 case, "[t]he FTC bears the burden of proof and persuasion in defining the relevant market." *FTC v. CCC Holdings Inc.*, 605 F.Supp.2d 26, 37 (D.D.C. 2009).

266. To establish a relevant geographic market, "the FTC must present evidence on the critical question of *where* consumers [in the product market] could practicably turn for alternative services should the merger be consummated and prices become anti-competitive." *FTC v. Tenet Health Care Corp.*, 186 F.3d 1045, 1052 (8th Cir. 1999) (emphasis added). "The relevant geographic market in which to examine the effects of a merger is 'the region in which the seller operates, and to which the purchaser can practicably turn for supplies.'" *Arch Coal*, 329 F. Supp. 2d at 116 (quoting *Cardinal Health*, 12 F. Supp. 2d at 49).

267. Markets must be drawn broadly enough to include all goods that "compete on substantial parity" with the goods that will allegedly become anti-competitive due to the merger. *Lantec, Inc. v. Novell, Inc.*, 306 F.3d 1003, 1026-27 (10th Cir. 2002) (citations and internal quotations omitted). *See also E.I. du Pont de Nemours & Co. v. Kolon Indus., Inc.*, 637 F.3d 435, 442-43 (4th Cir. 2011) (geographic market must be defined in relation to "commercial realities," specifically, "factors bearing upon where customers might realistically look to buy the product"); *Funeral Consumers Alliance, Inc. v. Serv. Corp. Int'l*, No. H-05-3394, 2008 WL 7356272, at *10 (S.D. Tex. Nov. 24, 2008) (plaintiffs failed to allege a nationwide geographic market for casket sales where "[t]he evidence clearly demonstrates that casket prices vary across geographic markets and even within the same funeral chain").

B. THE UNITED STATES IS NOT A RELEVANT GEOGRAPHIC MARKET FOR "NATIONAL CUSTOMERS"

268. "The FTC alleges that the United States constitutes the relevant geographic market because "Defendants, other broadline distributors, customers, and other industry participants recognize the existence of a national market for broadline foodservice distribution services." Compl. ¶¶ 47-48. But "National Customers" contract regionally or even locally for foodservices, and prices vary across regional and local geographic markets in response to regional and local competition and customer demands, which bars the finding of a nationwide geographic market. This reality also underscores the fact that the FTC's use of an economically meaningless administrative label applied to heterogeneous customers was erroneous.

1. "National Customer" Is An Administrative, Not Economically Significant, Distinction

269. As described at length, the label "National Customers" is an administrative distinction made by some distributors, not a substantive distinction about customer needs. *See, e.g.*, *supra* § VI.E.1. Customers, regardless of size, can choose whether they would like to be managed under a "National" or "Local" contract. *See supra* ¶¶ 58.

270. [redacted] However, several customers under the "National Customer" label use a large number of distribution centers; while some "National Customers" use far fewer. *See* Sonnemaker (Sysco), Hearing Tr. at 1565:22-1566:4 ("the vast majority of [Sysco's 300 CMU customers] are not national in scope"). On average, a Sysco CMU customer uses only six or seven OpCos, *id.* at 1569:8-12, while 60 of the 300 Sysco CMU customers use only one OpCo. *Id.* at 1565:10-16.

271. Likewise, many "National Customers" purchase from multiple distributors, particularly for different geographies. [redacted]

2. There Are No Indicia Of A True Nationwide Geographic Market, Such As Nationwide Pricing

272. To find a nationwide market for "National" foodservice customers, the FTC must show that "prices within different parts of the continental United States[] tend towards uniformity" or that "changes in the price of the product in one area will affect prices in another area." *See Marathon Oil Co. v. Mobil Corp.*, 530 F. Supp. 315, 321-22 (N.D. Ohio 1981); *cf. Grinnell*, 384 U.S. at 575 (finding a nationwide market for security systems where prices and rates were set centrally).

273. Even for customers that use one broadliner for multiple geographies, prices are not centrally determined; rather, customers contract with broadliners in a manner where cost is "determined on a distribution center basis." [redacted] Schreibman stated at the hearing that "customers like Sonic and Subway, they will bid their business regionally, and as a result we will

bid their business regionally…and the price will be different based on that geography." Schreibman (USF), Hearing Tr. at 1528:18-25. Even SPV-4, the VA contract awarding all of the VA's broadline distribution to one distributor, have prices that "vary across the country if they're not deviated prices," and did not "for a particular category have one set of prices across the nation." Szrom (VA), Hearing Tr. at 184:21-185:8. Likewise, with 11 Reinhart distribution centers, IPC negotiated 11 different prices in each of its geographies. Baker (IPC), Hearing Tr. at 1916:19-20 (video testimony of Dep. 18:5-15). [redacted]

274. And as described *supra* ¶¶ 179-181, customers maintain points of contact with the local distribution entity, rather than the central entity. [redacted]

C. THE FTC'S LOCAL MARKETS ARE ARBITRARILY DRAWN AND FAIL BECAUSE THEY IMPROPERLY EXCLUDE COMPETITOR SUPPLIERS ALREADY SERVING THOSE MARKETS

275. The FTC's local geographic markets assume that broadline distributors would not serve customers located farther than 100 miles from a distribution center. Compl. ¶ 51.

276. But distributors can and do service customers greater than 100 miles away from a distribution center. *See* Brawner (Sysco), Hearing Tr. at 1784:20-1785:5 (Sysco Columbia

services customers in Knoxville (260 miles), and Murfreesboro, Tennessee (over 400 miles));

[redacted]

277. The existence of distributors servicing local customers over a long distance also undercuts Dr. Israel's methodology for defining local markets. [redacted]

[redacted]

278. At the hearing, Dr. Bresnahan demonstrated that Dr. Israel's local geographic markets analysis was erroneous. Dr. Bresnahan began with a case study of Omaha. He observed that, because Dr. Israel lacked sales data in Omaha, he assumed that competitors would drive "no further in his baseline than Sysco or USF drives 75 percent of the time in that local area." Bresnahan, Hearing Tr. at 2156:10-12. But "if the firms you're interested in are in town," he explained, "how far they drive is not a good indicat[o]r of whether folks will drive in from out of town to compete. But anyway, that's what he does." *Id.* at 2156:14-18. Instead of relying on assumptions about driving distances for in-town distributors, Dr. Bresnahan used the zip code data provided by Cash-Wa to the FTC, applying the national/local distinction that Dr. Israel articulated. *Id.* at 2156:19-25. He demonstrated that Dr. Israel's analysis dramatically understated competition in the local overlap areas, thereby dramatically overstating market shares of the parties. *Id.* at 2157:8-13; *id.* at 2158:10-22 (noting that Dr. Israel declined to use this zip code data, and used zip code data only from the parties). In sum, Dr. Bresnahan emphasized "that the assumption that the out of town competitors won't drive any further than the folks in town is false. I mean, here it's sort of extremely false." *Id.* at 2159:2-5; *see also id.* at 2159:10-12 (referencing an example from Chicago which showed the same problem with Dr. Israel's methodology); *id.* at 2212:2-18 (discussing Chicago example to show that Dr. Israel's draw methodology is arbitrary).

279. Dr. Israel's draw areas demonstrate only the distances Sysco or USF are currently driving to service particular markets; they do not denote any limitation on how far competitors do or

would drive to service those markets. Dr. Israel's own data demonstrates the point. [redacted]

280. Sysco and USF drive much farther than the draw areas as a matter of assigned geography. The *assigned* geography for the Sysco Columbia distribution center includes locations over 150 miles away, including Hilton Head and Myrtle Beach, South Carolina. Brawner (Sysco), Hearing Tr. at 1787:6-1788:3. [redacted] Further, assigned geographies do not limit distribution distances. The Sysco Columbia distribution center services customers over 200 miles away in neighboring states beyond the OpCo's assigned geography. Brawner (Sysco), Hearing Tr. at 1788:4-18.

281. Because Sysco and USF draw areas are not the same in most local markets, the distances Dr. Israel assumes that a competitor would drive differ depending on which company is

servicing that customer. [redacted]

282. Competitors already drive farther than Sysco or USF do, and would drive even farther to undercut a Sysco price increase, and thus Dr. Israel's draw areas understate competitor market shares. [redacted]

283. Numerous competitors testified to delivering goods to distances far greater than Dr. Israel's draw areas. [redacted]

284. Moreover, "Local Customers," including FTC declarants, testified that the distance between them and a distribution center was not a material issue. [redacted]

285. Dr. Israel's overlap area calculations are not factually correct. [redacted]

[redacted]

286. [redacted]

[redacted]

VIII. THE FTC CANNOT DEMONSTRATE ANTI-COMPETITIVE EFFECTS

287. The FTC alleges that the merger will create "extraordinarily high market shares," which trigger a "presumption that the merger will substantially lessen competition." FTC Mem. at 23. But the FTC's market share calculations spring from faulty market definitions and cannot support a presumption of illegality.

288. Stripped of this presumption, the FTC appears to rely on two theories to establish that the merger will harm consumers. First, for both "National" and "Local Customers," the FTC posits a unilateral effects theory in which Sysco and USF allegedly are the closest substitutes for many customers and thus, for these customers, elimination of rivalry between the two will reduce competition substantially. *See* FTC Mem. 27-34. Second, the FTC apparently now alleges that the merged entity will be able to target certain customers and charge them higher prices. These theories fail as to both "National" and "Local Customers."

A. THE LEGAL STANDARD FOR DEMONSTRATING ANTI-COMPETITIVE EFFECTS

289. In order to prove targeted price discrimination, the FTC must show that a hypothetical monopolist can identify consumers with inelastic demand ("targeted customers"), that the hypothetical monopolist can actually charge higher prices to only those consumers with inelastic demand, and that the targeted customers cannot defeat the price increase through arbitrage. *In re R.R. Donnelley & Sons Co.*, 120 FTC 36, 51 (1995).

290. In order to prove unilateral anti-competitive effects, the FTC must show that the Defendants compete in a differentiated market, that the Defendants' products are customers' top two choices, and that it is unlikely that other firms (existing or new) will reposition themselves to offer close substitutes. *Oracle*, 331 F. Supp. 2d at 1117–18.

B. "NATIONAL CUSTOMERS" WILL NOT BE ADVERSELY IMPACTED BY THE PROPOSED MERGER

1. Dr. Israel Has Failed To Identify A Group Of Particular Customers That The Merged Company Could Target For Price Discrimination

291. Dr. Israel claims that the merger will allow the merged company to exploit "National Customers" by charging them, on a discriminatory basis, higher prices. *See* Israel, Hearing Tr. at 910:16-915:14. But Dr. Israel fails to show that "National Customers" exhibit *any* meaningful common characteristics, much less those that indicate inelastic demand. The only "characteristic" he could point to for these customers is the administrative classification given to them by Sysco and US Foods. *Id.* at 1165:7-13. In addition, even if he could show a set of such characteristics, he could not demonstrate that the merged company could successfully charge higher prices, because "National Customers" can and will find lower prices elsewhere.

a. **There Are No Economically Meaningful Common Characteristics Among "National Customers"**

292. So-called "National Customers" do not exhibit common characteristics indicating inelastic demand for broadline services. The FTC lists several characteristics that it claims "National Customers" "typically" require, including: a single contract; a single point of contact; product consistency; a single ordering platform; and a single technology platform for transactions and other reporting across all customer locations. Compl. ¶ 42; FTC's Response No. 2 to Defendants' First Set of Interrogatories. But none of these characteristics is common to "National Customers." *See supra* § VI.E.2.

293. That Sysco or USF designates a customer as "National" (or "CMU") is likewise economically meaningless. *See, infra*, at § VI.E.1.

b. **Even If Sysco And USF Could Distinguish "National Customers," They Could Not Do So On A Characteristic That Indicates Inelastic Demand**

294. To the extent that certain "National Customers" have some inelastic demand for a broadline distributor with nationwide reach, the FTC has not tied that demand to any observable characteristic that would allow a distributor to identify and target "National Customers" for price discrimination. None of the characteristics of "National Customers" described by the FTC correlate to inelastic demand. *See* Thompson (Interstate), Hearing Tr. at 214:11-13 ("Q. Is it fair to say that Interstate needs a broadliner? A. That would be our preference, yes, it is fair to say, yeah."), 247:23-25 ("Q. Can you see yourself using a network of regional distributors? A. It's not my preference."), 248:11-14 ("And would you—can you see yourself contracting with a GPO for your foodservice distribution needs? A. That is not the option we'd want to go to if we could avoid it."), 269:4-6 ("Q. You mentioned a couple of times today that Interstate has a preference for one distributor; right? A. That's correct.").

295. "National Customers" as a group do not exhibit inelastic demand for services that only Sysco and USF can offer, because they can substitute a variety of other services. Many of the FTC's "National Customers" rely on distributors to provide only a drayage function. They procure foodservice products by negotiating directly with manufacturers and use distributors to warehouse and deliver those products to their locations. Schreibman (USF), Hearing Tr. at 1443:19-1444:15 ("Q. So when you're supplying the customer for a national chain account, the product price is what they have—is what they have contracted with the manufacturer, and then added to that is your drayage or distribution cost? A. That's exactly right."); [redacted]

296. The vast majority of the FTC's "National Customers" rely on distributors simply to provide a drayage function. They procure foodservice products by negotiating directly with their suppliers and rely on distributors to warehouse and deliver those product to their locations. [redacted]

[redacted]

297. The merged entity's size does not hinder "National Customers'" ability to substitute. In fact, many of the largest foodservice customers seek to use fewer distribution centers and frequently divide their business up locally or regionally. *See* Schreibman (USF), Hearing Tr. at 1503:11-23 ("So the rationale is the larger more sophisticated customers want to disaggregate all the cost of getting the product from the manufacturer to them . . . . And by putting more of their restaurants into fewer of our distribution centers, we can bring what's known as truckload quantities or larger quantities into our distribution center, thereby reducing the cost per case of moving the product ."); [redacted]

[redacted]

298. Even the VA admits that it would prefer to use fewer distribution centers; in fact, one of the reasons it disqualified Sysco from an RFP was because Sysco proposed using too many OpCos. *See* Szrom (VA), Hearing Tr. at 179:15-180:3 ("Q: And the major weakness on capability to perform nationwide was because Sysco was proposing to use too many warehouses; is that right? A: . . . yes, that would have been a weakness at that point in time. Q. And so one of the things that you might have evaluated—might have negotiated with Sysco, had you ever negated [sic] with Sysco, would be to reduce the number of warehouses that they were using to service the VA's business? A: In possible areas, yes.").

299. For customers that have not moved toward fewer distribution centers and do not break up business by region, a plethora of other price-constraining choices remain. [redacted]

2. **Sysco And USF Are Not Uniquely Close Competitors**

300. The FTC maintains that Sysco and USF are uniquely close competitors, and therefore

their merger will eliminate vital competition from the foodservice distribution market. FTC Mem. at 5. The FTC fails to present adequate proof that Sysco and USF are uniquely close competitors to each other.

a. **Dr. Israel's Auction Model**

301. [redacted]

302. Dr. Israel's model purports to calculate harm based on the effect of the merger on the value the second-choice bidder will offer the customer, with the idea being that if the merger removes one of the top two choices, the old number three choice will become the new number two. Israel, Hearing Tr. at 1250:23-1251:8. As Dr. Israel admitted at trial, his RFP dataset contains no systematic information on who finished second or third: there are no ordinal rankings. *Id.* at 1251:15-20. Dr. Israel conceded that it is market share that is used to determine the bidders' rankings in the auction model, *id.*, and even to determine how often each distributor wins the simulated auction, *Id.* at 2384:24-2385:10 ("I assume the winning probability is the market share, yes."). Thus, Dr. Israel's auction model provides no independent information on the likely merger effects; it simply bootstraps into the "effects" analysis Dr. Israel's unreliable "national broadline customer" "market shares."

b. The FTC Fails To Show That Sysco And USF Are Each Other's Closest Competitor

303. [redacted] As Dr. Bresnahan testified, the appropriate way to measure whether two firms are each other's closest competitors is to average the amount of sales lost by each party to the other. Bresnahan, Hearing Tr. at 2141:6-14 ("I think to think about whether they're really important head-to-head competitors for one another, you want to average these two things . . . head-to-head competitors is sort of a, you know, bilateral concept, back and forth concept"). It is not enough to merely cherry pick a single measure of switching in one direction, as Dr. Israel did with revenues switching from Sysco to USF. Israel, Hearing Tr. at 2382:2-17.

304. [redacted] These percentages of lost sales to one another are insufficient to find Sysco and USF are each other's closest competitors for "National Broadline" customers. They also roughly correspond to the multitude of ordinary course documents reporting the parties' combined market share at anywhere from 25 to 30%. Bresnahan, Hearing Tr. at 2141:6-14 ("[Y]ou want to

average these two things . . . and . . . you're going to get a number that's sort of like their national shares of overall foodservice, even a quarter or something[.]").

305. Contrary to Dr. Israel's claim, Israel, Hearing Tr. at 2352:7-12, Dr. Bresnahan's analysis was robust. *See* Bresnahan, Hearing Tr. at 2209:23-2210:1 (discussing DX-01610 and DX-01611, showing that accounting for Dr. Israel's criticisms changes the results trivially; Dr. Israel did not dispute this methodology or these results). [redacted]

306. The three largest customers lost by Sysco during this period did not move all their locations from Sysco to USF. [redacted] And removing these three customers, who Dr. Israel acknowledges could switch to systems distribution, from the analysis drops the percentage of Sysco revenue that went to USF [redacted] Moreover, many other large customers lost by Sysco moved the majority of their locations to competitors other than USF [redacted] This switching demonstrates that "National Customers" divide demand among multiple distributors or distribution modes, and do not view Sysco and USF as uniquely attractive options.

307. Additionally, Dr. Israel's theory of harm rests on an assumption that customers

principally engage in RFPs and that Sysco and USF's frequent meetings at those RFPs indicate that they are close competitors. Hausman, Hearing Tr. at 1982:9-17; [redacted] This does not fit the reality of the industry, which, for the most part, does not conduct procurement via RFPs. [redacted]

308. Actual procurement only rarely occurs through RFP; most of the time, it is done via informal, fluid bilateral negotiations, in which the customer is able to leverage its many distribution choices against Sysco or USF to achieve favorable pricing. *See* Thompson (Interstate), Hearing Tr. at 226:8-14 ("Q: [W]hen was the last request for proposal that Interstate put out for broadline distribution? A: The last actual request for proposal was before my tenure as vice-president. Q: And can you give us an approximate time? A: Well, it would be approximately nine years ago."); [redacted]

309. Many "National Customers" have forced Sysco and USF to lower their prices through negotiation, or have used negotiation to replace Sysco or USF. [redacted]

310. Even where RFPs actually occur, they are almost always a mere prelude to bilateral negotiation in which terms are materially changed and negotiation-specific pressures carry the day. [redacted]

311. The Veterans Administration, which received bids from only Sysco and USF in its most recent RFP, negotiated bilaterally with both companies during the RFP process. Szrom (VA), Hearing Tr. at 136:6-13 ("Q: Without getting into confidential details about the offers, were there

negotiations between the VA and Sysco over any of the terms of their proposal? A: Yes, there was. Q: And again, without getting into any confidential details, were there any negotiations between the VA and US Foods over the terms of their proposal? A: Yes, there was."). These negotiations lasted over eight months. *Id.* at 93:5-7 ("The RFP was issued in 2011. We did eight months of negotiations, and the award happened in—I believe, May 1st of 2012 . . .").

312. Moreover, the VA did not actually negotiate lower *prices* when it dealt with Sysco and USF; it merely negotiated *terms*. Szrom (VA), Hearing Tr. at 181:23-182:3 ("Q. In fact, there were never any negotiations on price with Sysco; is that correct? A: That's correct. Q: And there were never any negotiations on price with US Foods, correct? A: That's correct."). In fact, contrary to the FTC's contention that customers play Sysco and USF off of each other to obtain lower prices, the VA neither negotiated price nor *even mentioned* to Sysco or USF that there was competition for the VA's business. *See id* at 180:18-20 ("Q: In other words, you don't let the bidders know who the other bidders that are participating are, correct? A: No.").

313. Interstate did not use Sysco in its price negotiations with USF—negotiations in which it felt like it achieved favorable results. Thompson (Interstate), Hearing Tr. at 268:5-14 ("Q: To be clear, sir. You felt like you achieved favorable results . . . [i]n that renegotiation with US Foods? A: I did. Q: And to achieve those favorable results, you didn't rely on any proposal from Sysco or anyone else to get leverage on better rates with US Foods; correct? A: That's correct.").

314. The FTC hypothesizes that Sysco and USF exert duopoly power over "National Customers." *See* FTC Mem. at 25. But profit margins for these customers are low, demonstrating in fact the opposite. *See* DX-01353, Hausman Rpt. ¶¶ 125-26 ("An economist would expect infra-normal profits [if Defendants exerted duopoly power], yet this is not what is observed in practice.").

315. Even if RFP data were an accurate proxy for competition in the industry, Dr. Israel's RFP data set is of suspect integrity. Dr. Israel used only Sysco and USF records to determine that the companies were each other's closest competitors, creating a data set that was "obviously . . . not a complete record[,]" Israel, Hearing Tr. at 1084:2, and included instances in which RFP participants (and occasionally winners) were reported inaccurately, *id.* at 1086:12-1087:14 ("They might just not have as good of records of th[ose] opportunit[ies]."); *see also id.* at 1089:10-18 ("The Court: So when the data showed that they didn't win, you had to use some subjective assessment of how they would have treated the customer if they had one? [Dr. Israel]: Yes. I mean, that's example, yeah. I mean, if you think about—I mean, ultimately for the purposes of the RFPs, the net effect, if someone ends up on the other side of the line, it'd be one more or one less RFPs in my observation. I'm just doing the best to have the best sample of national RFPs that I can.").

c. Many "National Customers" Do Not Consider Sysco And USF To Be The Other's Closest Competitor In The Foodservice Distribution Market

316. Some "National Customers" have testified that neither Sysco nor USF are their top two choices for foodservice distribution. [redacted] And where "National Customers" conduct formal RFPs, often Sysco and USF are not the top bidders. [redacted] Occasionally, they do not even show up. [redacted]

317. Other "National Customers" have shown that while *one* of its top two choices may be Sysco or USF, the *other* is not. [redacted]

[redacted] *accord* Thompson (Interstate), Hearing Tr. at 258:24-259:21 ("Q: This is the analysis that your consultant prepared for Interstate after comparing Avendra, Sysco and US Foods; is that right? A. That's correct. . . . Q: And they suggested you could save $3.5 million over the next lowest bid? A: That's what it says. Yes. Q: And do you recall who the next lowest bid was? A: Sysco, to my knowledge. Q: So in the financial results, Avendra came out number one, Sysco, number two, and then was US Foods number three? A: That's correct.").

318. The Veterans Administration ultimately excluded Sysco entirely from its most recent RFP. While the VA compared Sysco's prices to USF's "to ensure fair and reasonable pricing could be established," it did not consider Sysco to be one of its top two choices. Szrom (VA), Hearing Tr. at 91:25-92:4 ("A. [W]hen the technical evaluation portion was completed, we evaluated price. Due to Sysco no longer being within the competitive range at that time, we still utilized their prices to compare to U.S. Foods' proposed prices to ensure fair and reasonable pricing could be established."); *id.* at 134:17-23 ("Q: Okay. Was there any evaluation of price as part of the SPV-4 evaluation? A: Well, price is always evaluated, and SPV-4 because Sysco was taken out of the competitive range prior to any type of price negotiations. Their prices were still utilized to determine fair and reasonable pricing on behalf of the other vendor, which was US Foods."); *id.* at 186:1-2 ("Based on the price analysis there was a 30 percent difference between Sysco and US Foods[.]").

319. While the VA's witness stated that the VA compared USF's prices to Sysco's, the comparison was not a meaningful price check. By the VA's own admission, "Sysco's offer was still substantially higher than US Foods." Szrom (VA), Hearing Tr. at 156:1-2.

320. Some "National Customers" that maintain that Sysco and USF are their top two choices tend not to pit the two against each other. Interstate, a current USF customer, maintains that only Sysco and USF could serve its nationwide broadline needs. Thompson (Interstate), Hearing Tr. at 221:9-14. Yet during Interstate's last RFP, it also considered using Avendra, a GPO. *Id.* at 227:2-6 ("Q: [W]ho . . . based upon what you've just described did Interstate look at during that RFP back in 2005? A: In 2005, we looked at—we looked at Sysco, Avendra was a bit of an option, and then US Foods."). And Interstate's Senior Vice President of Procurement has not discussed foodservice distribution with Sysco for *five years*. *Id.* at 225:22-226:1 ("Q: And have you ever had occasion to meet with Sysco representatives about foodservice distribution for your hotels? A: Approximately five years ago . . .").

321. Interstate claims that it regularly threatens to switch to Sysco in order to keep USF's prices in check. Thompson (Interstate), Hearing Tr. at 233:23-234:7 ("Q: . . . Can you remember an explicit, explicit threat where you said, I'm going to go to Sysco unless you cut me a better deal? A: You know what, I say that a lot, unfortunately. But, you know, I think it—is it in jest sometimes, but yeah, I have said that. Q: So is it fair to say that or to what extent do you play US Foods and Sysco off each other in your ordinary course of business? A: I have, and I do frequently, yes."). But these cannot be credible threats: a USF representative, dubbed "Mr. US Foods," is based *in Interstate's offices* and attends Interstate staff meetings. *Id.* at 231:11-232:18 (emphasis added). Sysco has no such representation at Interstate.

322. And completely ignored by the FTC and its expert Dr. Israel is the competitive tension between FSMs and GPOs for the ultimate customer which has resulted in US Foods getting little, and in the case of Aramark, no FSM business. Lynch (USF), Hearing Tr. at 1737:8-1739:12.

[redacted]

[redacted]

C. THE FOUR LOCAL MARKETS EMPHASIZED BY THE FTC ARE AND WILL REMAIN COMPETITIVE

323. To establish anti-competitive effects in a differentiated product market, as here, the FTC must establish that competitor offerings (*i.e.*, other broadline distributors) are "sufficiently different from the products offered by the merging firms that a merger would make a small but significant and non-transitory price increase profitable for the merging firm." *CCC*, 605 F. Supp. 2d at 68 (citing *Oracle*, 331 F. Supp. 2d at 1117-18).

324. The FTC has not established that the products offered by other broadline distributors are sufficiently different from those offered by USF and Sysco that a price increase by the merged entity would be profitable. Indeed, the features that allegedly distinguish Sysco and USF are meaningless to local customers. The fact that Sysco and USF offer geographically dispersed distribution centers, a single point of contact, a single ordering platform and consistent pricing and terms across multiple distribution centers is immaterial to a local restaurant in Raleigh, North Carolina. A street customer in Raleigh does not care whether Sysco has distribution centers in 69 other cities. The only point of contact and the ordering system it cares about is the one its local sales representative provides, and it is typically buying for one location and does not need consistent pricing or products. And many local customers have been shown to switch distributors frequently based on prevailing prices. *See supra* ¶¶ 209-10. The FTC has not identified any characteristics that would make Sysco and US Foods each other's closest competitors in local markets. Nor has the FTC explained how other broadline distributors are

sufficiently different that a price increase would be profitable for the merged firm.

325. At the hearing and in its briefing, the FTC focused on only four local markets: Omaha, NE; Columbia/Charleston, SC; Raleigh/Durham, NC; and Southwest Virginia. For each of those markets, evidence and customer testimony show that competition is fierce, that customers have myriad distribution options across multiple channels, and that the merged entity will not be able to raise price or reduce service.

1. **Omaha**

326. The FTC's claim that the merged entity will have a 90% market share in Omaha, Compl. Appx. A, is directly contradicted by information the FTC received during its investigation of the merger. *See* DX-01359, Bresnahan Rpt. Exh. 41.

327. [redacted]

328. In addition, US Foods estimated its market share among independent restaurants in Omaha at 5.7%. Schreibman (USF), Hearing Tr. at 1513:25-1514:10.

329. [redacted]

330. [redacted]

[redacted]

331. Specialty distributors also compete directly with Sysco and US Foods in Omaha. [redacted] In fact, Mr. Hoffman of Upstream Brewing admitted that he buys from specialty distributors instead of buying the same product from a broadline distributor, and that he compares pricing between specialty and broadline distributors including for steaks, produce, and seafood, and that "there are certain products where [Upstream] can get better pricing from the specialty distributors than [Upstream] can from US Foods." Hoffman (Upstream Brewing), Hearing Tr. at 361:1-19.

332. [redacted]

333. Additional Omaha customers confirmed that other competitors will provide a credible threat to leverage against the merged entity.

- [redacted]
- [redacted]

334. The FTC's claim that viable broadline distributor options do not exist in Omaha is based

on local customer declarants who repeatedly acknowledge that their opinions rely on significantly outdated information. *See e.g.*, Hoffman (Upstream Brewing), Hearing Tr. at 352:11-13; [redacted]

335. The FTC's own customer witness from Omaha at the hearing, Mr. Hoffman of Upstream Brewing, admitted that he has "not looked at Reinhart since at least 2006 and maybe even earlier," Hoffman (Upstream Brewing), Hearing Tr. at 352:11-13, that he "ha[s]n't looked at Cash-WA since at least 2006 and possibly earlier," *id.* at 352:14-16, and that he has no "direct current knowledge" about the product offerings of Reinhart or Cash-Wa, *id.* at 353:18-354:10.

2. Columbia/Charleston

336. There are numerous broadliners in the Columbia/Charleston market competing with US Foods and Sysco, including Merchants, Gordon Foodservice ("Gordon"), Performance Foodservice ("PFG"), Cheney Brothers, Reinhart, and Pate Dawson. *See, e.g.*, Brawner (Sysco), Hearing Tr. at 1789:23-1793:6 ; [redacted]

337. Additionally, there are numerous specialty distributors who compete with US Foods and Sysco for market share including Limehouse Produce, Inland Seafood, and Senn Brothers. *See, e.g.*, Brawner (Sysco), Hearing Tr. at 1798:8-19; [redacted]

[redacted]

338. Customers generally use a multitude of specialty and broadline providers in addition to US Foods and Sysco. Customers state:

- [redacted]
- [redacted]

339. If the merged entity were to raise prices or reduce service levels, customers could easily switch to an alternative broadline distributor. Customers state:

- [redacted]
- [redacted]

340. Most of the FTC's declarants who suggested that Sysco and US Foods were their only options admittedly had not explored the options available to them in Columbia/Charleston and were unaware of the products, prices, and services of the other broadline distributors in the Columbia/Charleston market. [redacted]

[redacted]

341. US Foods' own estimates of the local broadline market shares in Columbia are significantly lower than the estimates reported by the FTC's expert. [redacted]

3. **Raleigh/Durham**

342. Numerous broadline distributors compete with US Foods and Sysco in the Raleigh-Durham market, including Gordon Food Service, Pate Dawson, PFG, Orrell's, EG Forrest and Reinhart. *See* Brawner (Sysco), Hearing Tr. at 1801:2-1802:5; [redacted]

343. Many customers in the Raleigh-Durham area currently use these distributors for significant portions of their foodservice spending. [redacted]

344. PFG is a strong competitor in the Raleigh-Durham market. [redacted]

[redacted]

345. Pate Dawson is also a strong competitor in the Raleigh-Durham market. [redacted]

346. If the merged entity were to raise prices, customers could easily switch to an alternative broadline distributor. Customers state:

- [redacted]
- [redacted]
- [redacted]

347. Customers and competitors have noted that broadline competition in the Raleigh-Durham area is currently increasing, particularly with the announced opening of a Gordon Foodservice distribution center in nearby Charlotte. [redacted]

348. Many customers also use specialty distributors for a large portion of their business, and

stated that both US Foods and Sysco compete with the specialty distributors on pricing, product quality and breadth. [redacted]

349. Other customers use cash and carry for significant portions of their purchases because Sam's Club, BJ's and Costco offer better pricing than broadliners. [redacted]

350. Cash & carry competitor Restaurant Depot is expanding its presence in Raleigh. [redacted] Current broadline customers plan to use Restaurant Depot and are "enthusiastic" about the nearby opening. [redacted]

351. Most of the FTC's declarants who suggested that Sysco and US Foods were their only options admittedly had not explored the options available to them in Raleigh and had not even spoken to or reached out to many of Raleigh-Durham's broadline distributors in recent years, if ever. [redacted]

[redacted]

352. Raleigh customers—including the FTC's declarants, [redacted]—stated that they believe the merged company may offer lower prices and improved service, as it takes advantage of an expanded, streamlined distribution network and increased purchasing power with manufacturers. Customers state:

- [redacted]
- [redacted]

353. US Foods's own estimates of the local broadline market shares in Raleigh are significantly lower than those reported by the FTC's expert. [redacted]

4. **Southwest Virginia**

354. Numerous broadline distributors compete with US Foods and Sysco in the Southwest Virginia market, including PFG, Reinhart, Pate Dawson, Gordon, Saval Foods, FoodPRO, Buzz Food Service, Orrell's, Ferraro Foods, Staunton Foods, Schenk Foods, Richmond Restaurant

Service, and Layman Distributing. *See, e.g.*, Brawner (Sysco), Hearing Tr. at 1802:14-1803:21; [redacted]

355. US Foods' Roanoke division (which services the region) has a market share for sales to independent restaurants of only 16.2%. Schreibman (USF), Hearing Tr. at 1513:5-7; [redacted]

356. [redacted]

[redacted]

357. Reinhart and Pate Dawson are also strong competitors servicing Southwest Virginia. [redacted]

358. There are also scores of strong specialty players that earn sizeable chunks of business from Southwest Virginia customers, including True World Foods, Sam Rust Seafood, Steve Connolly Seafood, Honolulu Fish Company, Merchants Grocery Company, Wholesome Foods, Cavalier Produce, Roanoke Fruit and Produce, Standard Produce, Produce Source Partners, Pet Dairy, Polyface Farm, Howard Spangler, and Discount Paper Products. *See, e.g.*, Schablein (Wintergreen), Hearing Tr. at 552:21-553:24; [redacted]

359. Specialty distributors compete directly with Sysco and US Foods. For instance, Mr. Schablein, one of the FTC's witnesses, chooses to purchase produce and fresh seafood from specialty distributors even though he could purchase those products from Sysco, Schablein (Wintergreen), Hearing Tr. at 529:15-530:8, and uses 20%-25% of his restaurant's total foodservice spend with specialty distributors, *Id.* at 532:5-13 [redacted]

360. Southwest Virginia customers also take advantage of numerous club and cash-and-carry stores including Costco, Walmart, and Sam's Club. [redacted]

361. Club and cash-and-carry stores compete directly with Sysco and US Foods and exert significant pricing pressure throughout the area. [redacted]

362. Southwest Virginia customers—including FTC declarants—have said they would not hesitate to move part or all of their business to broadline, specialty, and cash & carry and club competitors if they became dissatisfied with Sysco's prices or service following the merger:

- [redacted]
- [redacted]

[redacted]

- [redacted]

363. The FTC's suggestions that customers in Southwest Virginia would not have alternative distributors in the case of the merger is not supported by the testimony the FTC offered because the FTC's witnesses have not explored whether alternative distributors exist. For instance, Mr. Schablein acknowledged that he has not looked into the prices or distribution capabilities of Pate Dawson, Reinhart, or other distributors servicing the area. Schablein (Wintergreen), Hearing Tr. at 549:7-551:6. Mr. Schablein's restaurant received a bid from PFG, but he never saw the bid and was not involved in negotiations with PFG. *Id.* at 551:7-552:1. An FTC declarant admitted his business with PFG had increased since he signed his declaration, [redacted] is currently conducting a price review of PFG, among others, [redacted]

D. THERE IS NO EVIDENCE THAT COMPETITION WILL BE ADVERSELY AFFECTED IN THE REMAINDER OF THE FTC'S 32 ENUMERATED LOCAL MARKETS

1. The FTC Submitted No Evidence For Many Local Markets

364. The FTC submitted no customer declarations or testimony for the alleged Kansas City, MO/KS, Philadelphia, PA, Chicago, IL, Memphis, TN, Washington/Baltimore, DC/MD, Bloomington, IN, Minneapolis, MN, Central Pennsylvania, Tampa, FL, Orlando, FL, Fargo, ND, Cleveland, OH, Birmingham, AL, Pittsburg, PA, Atlanta, GA, Salt Lake City, UT, Saint Louis, MO, Jackson, MS, Rochester, NY, Lubbock, TX, Milwaukee WI, and Albany, NY markets. As

to these markets, the only evidence of anti-competitive effect is Dr. Israel's draw areas, which have been shown to be meaningless. *See supra* § VII.C.

2. The FTC's Local Market Submissions Ignore Divestitures To PFG

365. In seven of the FTC's identified markets, the merger will not create any increase in concentration, because the only overlapping US Foods facility will be divested to PFG. DX-01359. Bresnahan Rpt. at 152. These markets include San Diego; San Francisco, Minneapolis, Kansas City (MO); Las Vegas, Cleveland, and Salt Lake City. *Id.* at 154 n.342.

366. The FTC's local market evidence submitted for Las Vegas, San Diego, and San Francisco ignores the divestitures of the US Foods' distribution centers to PFG in those areas. All but one of the declarations submitted by the FTC predate the February 2, 2015 divestiture announcement. [redacted] The single declarant who signed his declaration after the announcement was unaware of the divestiture when signing his declaration. [redacted]

367. Upon learning of the proposed divestiture, customers recognized that their declarations were inapplicable and stated that they would consider switching to PFG in the event of a price increase or drop in service levels by a merged Sysco. [redacted]

[redacted]

3. Charlotte, Los Angeles, and Pensacola

368. The FTC submitted little evidence with respect to its claims for the alleged Charlotte, Los Angeles, and Pensacola markets. The evidence that is before the Court shows competition in these areas to be robust.

369. In Charlotte, Sysco and US Foods compete with multiple other broadliners. [redacted]

370. Gordon Food Service is also growing in Charlotte through the opening of a 300,000 square-foot distribution center in Kannapolis, North Carolina, DX-01409, "Gordon Food Service Announces Expansion into North Carolina," at 1-2 (Oct. 27, 2014), located less than thirty miles from Charlotte. [redacted]

371. In Los Angeles, PFG is acquiring US Foods' distribution center in Corona, California through the divestiture. The divested Corona facility is 30 miles from the US Foods' Los Angeles facility, presently distributes to the farthest points of the Los Angeles facility's existing footprint, and can serve all zip codes served by the LA facility. DX-01939, Sysco/US Foods Presentation, "FTC Meeting," at SY003-000244.

372. Sysco and US Foods compete with numerous other broadliners in Los Angeles. Shamrock describes itself as "one of the top 10 foodservice distributors nationally," and entered

the market in 2012 by opening a distribution center in Eastvale, California, which is less than 50 miles from Los Angeles. DX-01834, "Shamrock Opens Fourth Distribution Center," (Feb. 20, 2012). Shamrock serves "restaurants, health care facilities, military bases, schools, hotels and other foodservice operations." *Id.* [redacted]

373. In Pensacola, Sysco and US Foods compete with a variety of broadline distributors. [redacted]

IX. THE FOOD DISTRIBUTION INDUSTRY IS AND WILL REMAIN COMPETITIVE POST-MERGER

A. THE LEGAL STANDARD FOR REBUTTING A PRESUMPTION OF ANTI-COMPETITIVE EFFECTS

374. Only if the FTC establishes its relevant markets and demonstrates undue concentration is it entitled to a presumption that the merger is illegal. *Heinz*, 246 F.3d at 715. Where the FTC is not entitled to this presumption, it must establish likely anti-competitive effects from the merger. *See, e.g.*, *H&R Block*, 833 F. Supp. 2d at 49-50. "[A] failure of proof in any respect will mean the transaction should not be enjoined." *Arch Coal*, 329 F. Supp. 2d at 116.

375. Defendants can rebut any showing of anti-competitive effects the FTC might make, since

"a broad analysis of the market to determine any effects on competition is required." *Arch Coal*, 329 F. Supp. 2d at 130; *see also United States v. Gen. Dynamics Corp.*, 415 U.S. 486, 498 (1974). Defendants can make this showing in a number of ways. *See, e.g.*, *Arch Coal*, 329 F. Supp. 2d at 158 (unilateral price increase unlikely); *Baker Hughes*, 908 F.2d at 984 (entry and repositioning of competitors); *id.* at 98 (sophisticated customers); *Heinz*, 246 F.3d at 720 (procompetitive efficiencies); *cf. Microsoft*, 253 F.3d at 105 (divestiture).

376. Where "non-merging firms [are] able to reposition their products to offer close substitutes for the products offered by the merging firms," the likelihood of anti-competitive effects if further diminished. PX06059, HMG § 6.1; *see also CCC Holdings*, 605 F. Supp. 2d at 57 ("The ability and willingness of current competitors to expand their foothold in the market and/or reposition greatly reduces the anti-competitive effects of a merger, and is essentially equivalent to new entry.").

B. PFG WILL BE A STRONG COMPETITOR FOR CUSTOMERS SEEKING DISTRIBUTION NATIONWIDE

377. The touchstone of merger analysis is "future competitiveness." *Baker Hughes*, 908 F.2d at 986. Divestiture has long been considered the "most important of antitrust remedies" to blunt any anti-competitive effects likely to flow from a merger. *Microsoft*, 253 F.3d at 105 (quoting *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 331 (1961)). Therefore, the merger's effect on competition cannot be analyzed without reference to the divestiture to PFG and its additional plans for immediate expansion.

378. The proper inquiry is whether the entity buying the divested assets will be able to replace the competitive intensity of the acquired firm in the market, not whether it will replicate the footprint or market share of the acquired firm. *See* Antitrust Division, U.S. Dep't of Justice, Policy Guide to Merger Remedies at 5 (Oct. 2004) (divestiture's effectiveness is guided by

whether the transaction "replace[s] the competitive intensity lost as a result of the merger rather than focusing narrowly on returning to premerger [market share] levels").

379. [redacted]

380. [redacted]

381. In the context of this case, operational *efficiency*, not size, is determinative of PFG's ability to compete. *See, e.g.*, *United States v. Syufy Enters.*, 903 F.2d 659, 670-71 (9th Cir. 1990) ("[W]hile size no doubt provides significant business advantages, it can also have very substantial drawbacks, such as increased management costs and other diseconomies of scale.").

[redacted]

[redacted]

382. [redacted]

383. PFG is the third largest foodservice distributor in the United States. [redacted]

384. PFG is highly regarded by customers. [redacted]

[redacted]

385. Even with its current footprint, PFG regularly competes with Sysco and USF for all types of customers, and wins. [redacted]

386. [redacted] PFG also serves several customers who changed from systems

distribution to broadline distribution. Holm (PFG), Hearing Tr. at 574:11-25 ("We have secured business in our broadline that was in a [systems] environment fairly recently, and I would think that pricing did have something to do with that."), *id.* at 575:14-24 ("We have had customers change from a systems environment of a competitor to a broadline."); [redacted]

387. PFG is confident that GPOs and customers will increase their business with PFG post-merger. [redacted]

[redacted]

388. [redacted]

389. To the extent the declarations obtained by the FTC expressed reservations regarding the availability of alternative distributors with a nationwide presence, it is important to note that an overwhelming number of FTC declarations were signed prior to the PFG divestiture announcement. Of the 99 FTC declarations in the record, 73 were signed prior to the announcement of the divestiture. [redacted]

390. [redacted]

391. [redacted]

[redacted]

392. The FTC's concerns are also inapt because PFG will be well-positioned to *bid* on Day One. [redacted]

393. Other competitors have similarly explained that they could serve customers nationwide with significantly less than the number of distribution centers currently operated by USF. [redacted]

[redacted]

394. The FTC's "bigger-is-better" theory also overlooks the fact that an *optimized* and *efficient* network is more important than a big network. 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. *See supra* ¶¶ 70 (customers prefer being served from fewer distribution centers); *infra* Appx. A ¶ 183 (Mr. Holm discussing inbound efficiencies). For example, to deliver to Zaxby's, a restaurant customer, PFG drives past some of its own distribution centers; the longer drive proves cheaper for the customer. Holm (PFG), Hearing Tr. at 852:20-853:4; *see also* DX-06107, "Inbound Efficiencies in Effect."

395. [redacted]

[redacted] The use of shuttle yards is cost-efficient and common; USF uses shuttling for 27% of its distribution. Schreibman (USF), Hearing Tr. at 1501:19-1503:1. [redacted] And Mr. Holm explained that shuttle service can actually increase efficiencies. Holm Tr. at 850:23-851:21.

396. [redacted]

397. PFG's product cost will not be a disadvantage. Customers with a nationwide footprint purchase the majority of their goods directly from manufacturers, and so distributors do not control the cost of goods for the majority of purchases. *See supra* ¶¶ 41-42. [redacted]

[redacted]

398. The FTC's fallback position is that acquisition and expansion are hard, and that PFG could fail in its endeavor. [redacted] The FTC's position is inconsistent with its implicit assumption that Sysco will seamlessly integrate all 42 USF distribution centers, a far taller task than that facing PFG.

399. PFG has a demonstrated history of successful acquisition and expansion, and is well-positioned to succeed here. First, Mr. Holm, who will be overseeing the acquisition of the 11 divested distribution centers as well as the additional foldouts and expansions, has over 38 years of experience in the food distribution industry and has worked for both USF and Sysco in the past. [redacted] 847:3, 841:17-24 (while at Sysco, Mr. Holm never "went three years without doing an addition"); Holm (PFG), Hearing Tr. at 562:23-25. In addition, Mr. Holm successfully oversaw the acquisition of PFG by Vistar, a transaction that involved 20 broadline distribution centers and 8 systems distribution centers—nearly 2.5 times the number of distribution centers to be integrated through the divestiture here. *Id.* at 567:2-19. Furthermore, PFG acquired IFH in 2012, substantially expanding its presence in the Carolinas. [redacted]

C. THE CURRENT ROBUST COMPETITION PROVIDED BY OTHER BROADLINERS AND OTHER DISTRIBUTION CHANNELS WILL CONTINUE AND GROW

400. In addition to PFG, a wealth of food service distributors compete with Sysco and USF, and many of those distributors do not expect the merger to reduce competition. Many customers feel the same way; they view the food service distribution industry as highly competitive, and do

not believe that a Sysco-USF merger will change that attribute.

1. Distribution Market Advantage (DMA)

401. [redacted]

402. [redacted]

403. [redacted]

[redacted]

404. [redacted]

405. [redacted]

406. [redacted]

407. [redacted]

408. [redacted]

409. [redacted]

410. [redacted]

2. **Pate Dawson**

411. [redacted]

412. [redacted]

3. **Restaurant Depot**

414. Restaurant Depot is a one-stop "cash-and-carry broadline foodservice wholesaler." DX-00167, Restaurant Depot Official Information Video; [redacted]

415. [redacted]

416. [redacted]

[redacted]

417. [redacted]

418. [redacted]

419. [redacted]

4. **Other Distributors Compete Fiercely With Sysco And USF**

420. Many other distributors compete with Sysco and USF for customers on every level. [redacted]

[redacted]

421. US Foods has lost national sales to numerous competitors, including DMA, PFG, Gordons, HPC, MUG/Unipro, Ben E. Keith, Maines, and MBM. US Foods lost [redacted] to DMA. DX-01911; DX-00389; DX-00445; DX-01911; DX-01143; DX-00837; DX-01152; DX-01162; DX-01164. US Foods also lost [redacted] to Gordons. DX-00412; DX-01171. Additionally, US Foods has lost a St Louis Franchise of [redacted] to PFG. DX-00379; DX-00820; DX-01098; DX-01099; DX-02188. US Foods has lost [redacted] to both PFG and Maines. DX-00379. US Foods has lost the New England zone of [redacted] to HPC. *See* DX-01590. US Foods lost [redacted] to MUG, DX-00045, as well as Krystals to MBM, Lynch (USF), Hearing Tr. at 1708:16-21, and Slim Chickens to Ben E. Keith, Lynch (USF), Hearing Tr. at 1701:22-1702:7. In 2015, US Foods lost [redacted] to a number of regional and systems distributors including Willow Run, FSA/SSA, I Supply, CDI, and BEK. DX-01373, [redacted]

422. Distributors compete with Sysco in each region. In Portland, Oregon, for example, Sysco has battled daily for customers with FSA, a regional broadline distributor, as well as with Pacific Seafood, a specialty seafood distributor, McDonald Wholesale, a local broadline distributor, cash and carry firms, and Duck Delivery, a specialty produce distributor. Sonnemaker (Sysco), Hearing Tr. at 1561:5-1562:21. [redacted] sees itself as second in market share to Sysco in

certain markets, above US Foods. [redacted]

423. Distributors already compete with Sysco and USF on price. [redacted] In fact, prices in the food service distribution industry are highly competitive across the board, such that [redacted] If a distributor prices its product too high, customers [redacted]

424. Mr. Sonnemaker testified emphatically that, should the companies merge, Sysco could "[a]bsolutely not" target customers for higher prices, Sonnemaker, (Sysco), Hearing Tr. at 1577:15-19, because there are multiple capable distributors in every market, *id.* at 1577:21-22, and because "[t]he business is just too competitive to think that," *id.* at 1577:22-23. Mr. Sonnemaker explained that customers "are too well educated" and understand the business too well to accept a price increase. *Id.* at 1577:23-25. He testified that a price increase post-merger "wouldn't be justified, and our customers, if we did that, they would move very quickly to another distributor." *Id.* at 1614:8-14.

425. Many distributors see an opportunity to expand operations in light of the merger. *See* DX-00260, [redacted] Indeed, some distributors have been expanding steadily across the country for years, and continue to do so. [redacted]

426. [redacted] Ralph (Premier), Hearing Tr. at 429:6-432:2 (while the witness refused to admit that Premier competed with distributors, she did admit that Premier has bid on the same contracts as distributors and lost); *id.* at 434:24-435:11 ("Q: Dartmouth is not the only college or university that you've lost a bid to PFG, for example, to; is that right? A: No."); *see also supra* ¶¶ 251-53 (discussing competition between GPOs and Sysco post-merger).

427. GPOs take both business and revenue from broadline distributors. Ralph (Premier), Hearing Tr. at 423:5-426:9 (Premier takes a percentage of every dollar its members spend through its contracts, and USF pays a fee for everything it distributes under contract with Premier); [redacted]

[redacted] The majority of the distribution industry anticipates increased competition from GPOs. [redacted]

D. THE ENTRY OF NEW COMPETITION AND THE REPOSITIONING OF EXISTING COMPETITORS WILL KEEP THE INDUSTRY COMPETITIVE

428. Growth through expansion or acquisition is common in this industry. There are no substantial barriers to entry that might prevent entry and repositioning—there are no technological, legal, or regulatory barriers, and this is not a business involving a scarce good. [redacted] ("In any local market, anyone with a truck will be able to distribute to a street operator because there are low barriers to entry in this industry.").

1. Growth By Expansion

429. Many successful companies that were once small shops are now successful competitors with Sysco and USF. [redacted]

[redacted] are testaments to the fact that scrappy competitors can thrive in this industry.

430. Many small distributors have expanded to regional and super-regional prominence. [redacted]

431. For example, Maines started as a candy company that sold nickel candy to local grocers. DX-01617, Maines Website Printouts at 9. After expanding into the foodservice business in the 1970s, Maines opened its second distribution center in 1987 and introduced a new distribution center in New York in 1999. *Id.* The largest growth in Maines' history took place in 2000 when four new distribution centers were opened in Oxford, Massachusetts; Oakwood Village, Ohio;

Farmingdale, New York; and Conklin, New York to serve over 1,700 Burger King restaurants. *Id.* at 10. Today, Maines claims to be the largest foodservice distributor in the Burger King System. *Id.* [redacted]

432. There are many examples of competitors successfully expanding existing facilities.

- **Reinhart:** [redacted]
- **Ben E. Keith**: [redacted]
- **FSA**: [redacted]
- **Shamrock**: [redacted]
- **Shetakis**: [redacted]
- **Nicholas & Co**.: [redacted]

433. A number of competitors, [redacted] have expansion plans underway. [redacted]

[redacted]

434. [redacted]

435. Competitors testified that the merger will present them with opportunities to expand their customer base.

- [redacted]
- [redacted]

[redacted]

- [redacted]
- [redacted]
- [redacted]
- [redacted]
- [redacted]

2. **Growth By Acquisition**

436. There are also numerous examples of growth by acquisition. [redacted]

437. [redacted] for instance, acquired two [redacted] distribution centers [redacted] in part to win [redacted] business from USF. [redacted]

438. [redacted] has successfully acquired six or seven distribution

centers [redacted]

439. [redacted] initially began servicing customers in [redacted] through the acquisition of [redacted], and it has continued to acquire other distributors including [redacted] in the last several years. [redacted]

440. [redacted] and expanded the facility to include both specialty and broadline, doubling the size of the distribution center in short time. [redacted] The acquisition and expansion extended [redacted] reach to [redacted]

E. THE MERGER CREATES CONSIDERABLE EFFICIENCIES THAT BENEFIT CUSTOMERS

441. The merger will result in lower prices, better service, and increased potential for innovation, the benefits of which will in large part pass through to the merged entity's customers. [redacted] These benefits are often referred to as synergies or efficiencies. DX-01359, Bresnahan Rpt. at 156.

442. The merger will generate [redacted] in annual cost savings and operational synergies. [redacted]

[redacted]

443. Even when discounted substantially for unforeseen integration complications, possible customer loss, and the divestiture, the merged company's efficiencies are expected to generate over [redacted] in savings. [redacted] Of those, Dr. Hausman has identified more than [redacted] as merger-specific, variable cost savings. [redacted]

444. Dr. Hausman's estimate far exceeds the efficiencies projections accepted as pro-competitive in similar cases. *See Arch Coal*, 329 F. Supp. 2d at 122–23 ($35-50 million); *FTC v. Butterworth Health Corp.*, 946 F. Supp. 1285, 1301 (W.D. Mich. 1996) (over $100 million). Indeed, this is one of the largest (and most verifiable) efficiency amounts ever presented in a Clayton Act case.

445. Efficiencies figures are more likely to be reliable if they are consistent with figures presented to a company's board of directors. *See Staples*, 970 F. Supp. at 1090 (rejecting defendants' efficiencies figures at preliminary injunction hearing because it was different from figure cited to board of directors).

1. **Calculation And Methodology**

446. Sysco and USF reported a risk-adjusted efficiencies estimate of over [redacted] to their shareholders and their Boards of Directors in November 2014—months before this litigation

began—and employees and managers are now responsible for delivering the [redacted] in cost savings. PX06155, Sysco Presentation, "US Foods Merger Update, Board of Directors Meeting," MCK2-SYS-0027503-58 at MCK2-SYS-0027529 (Nov. 17, 2014).

447. Employees will be evaluated and, in some instances, compensated based on the merged entity's ability to meet its efficiencies projections. [redacted] The efficiencies target is thus the product of meticulous analysis and planning, not mere speculation or litigation posturing. Wood (McKinsey), Hearing Tr. at 1901:20-1902:2; *see infra* Appx. A ¶¶ 84-86. The efficiencies target was calculated over the course of eight months by a large team of subject matter experts, including many experts from the independent consulting firm McKinsey & Company. Wood (McKinsey), Hearing Tr. at 1865:25-1867:2 (over 100 McKinsey personnel and over 170 Sysco-USF personnel worked full time for the better part of a year to determine efficiencies); *id.* 1901:22-1902:1 ("we spent an inordinate amount of time doing very detailed rigorous analytics, and it involved the subject matter experts who knew this stuff.").

448. 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. Wood (McKinsey), Hearing Tr. at 1865:3-24, 1868:15-1869:8, 1902:5-25. The scale and rigor of McKinsey's work cost Sysco roughly [redacted] dollars. DX-00262, Wood (McKinsey) Dep. 43:6-10; DeLaney (Sysco), Hearing Tr. at 1334:16-24.

449. The resulting efficiencies calculation was intended to be conservative and achievable in the near term. Wood (McKinsey), Hearing Tr. at 1868:15-1869:1, 1877:25-1878:20, 1889:10-

18; [redacted]

2. Merger-Specific, Variable Cost Savings

450. Of the cost savings quantified by McKinsey, Dr. Hausman identified more than [redacted] as both merger-specific and variable. Hausman, Hearing Tr. at 1992:22-23; DX-01353, Hausman Rpt. Errata, Exh. C. Mr. Gokhale, testifying for the FTC, confirmed that he followed a similar process to the one undertaken by Dr. Hausman in the three cases where Mr. Gokhale performed a more full-blown analysis of merger efficiencies, starting with the company's estimate of the cost savings resulting from the merger and then identifying merger-specific cost savings. Gokhale, Hearing Tr. at 2289:13-21. Although fixed costs can also lead to lower prices, economists typically focus on variable cost synergies because they lead to lower prices in the short run. Hausman, Hearing Tr. at 1992:22-23. Dr. Hausman found:

[redacted]

451. These cost-saving opportunities do not simply flow from the merger; they would be unlikely to be accomplished, if not impossible to accomplish, in the absence of a merger. *See* [redacted]

452. The merger's efficiencies track two general themes—increased volume and the elimination of overlap between Sysco and USF. Wood (McKinsey), Hearing Tr. at

1990:16-1901:19. Both of these themes rest on premises that cannot exist without the merger.

453. **Merchandising.** The merged company will be able to realize significant cost savings by combining their purchasing volume and different sets of SKUs to achieve incremental category management synergies. Wood (McKinsey), Hearing Tr. at 1881:20-1882:6 ("Q: [T]hese are category management savings that arise because the two companies are proposing to combine or this would simply be an extension of Sysco's current efforts, that category management? A: No. these are clearly incremental because of the combined volume and the new opportunity to reduce the SKU assortment to a more optimal assortment."); [redacted]

454. Category management is a process by which Sysco researches customers' preferences and trending items, builds a sourcing strategy to eliminate redundant SKUs and drive more volume through preferred individual SKUs, and then negotiates for cost savings on the increased volume of retained SKU sets. Wood (McKinsey), Hearing Tr. at 1881:7-19. By eliminating SKUs that serve essentially the same purpose, Sysco can increase its purchase volume on the remaining SKUs without affecting customers' choices. [redacted]

455. The merchandising integration team spent months determining the incremental savings that would result from the combined purchasing volume of the two companies. Wood (McKinsey), Hearing Tr. at 1890:5-9. Early in the process, when the integration team's information-sharing capabilities were limited, it conducted a formulaic mathematical exercise as a straw man for its later, better-informed analysis. *Id.* at 1885:20-1887:8. Once the integration

team had access to more complete information, it found that the straw man math was inaccurate the majority of the time and rejected its results for 138 out of 204 categories. Gokhale, Hearing Tr. at 2310:20-2311:1.

456. After the parties were cleared to share information regarding prior category management savings, the integration team reviewed a wealth of information on the supply market and on individual suppliers, Wood (McKinsey), Hearing Tr. at 1887:9-1888:2, and concluded that a 50% increase in Sysco's product volume would generate 1.25% savings on the companies' combined addressable spend. *Id.* at 1889:10-18. This is a conservative estimate; indeed, it is "on the low end" of what McKinsey normally achieves for its clients on similar assignments. *Id.*

457. **Operations: Distribution.** Distribution refers to the process of moving goods from distribution centers to customer locations. Wood (McKinsey), Hearing Tr. at 1870:12-17. One of the core distribution efficiency mechanisms is network optimization, or the process of consolidating and rationalizing the number of distribution centers. *Id.* at 1871:1-16.

458. Sysco and USF already optimize their individual networks. Wood (McKinsey), Hearing Tr. at 1876:17; 1877:1-7. But because the companies built their networks through acquisition, the networks are not *optimal*. *Id.* at 1876:17. By combining their networks, the companies can realize new optimization opportunities including the consolidation of facilities and the realignment of customers between facilities. [redacted] In addition, where Sysco and USF now use separate routes to deliver separate orders to a single customer, the merged company will need only one route, with a fuller truck, to deliver the same products to the same customer. [redacted]

459. **Operations: Supply Chain.** Supply chain concerns the process of obtaining products from suppliers. Wood (McKinsey), Hearing Tr. at 1891:19-24. Supply chain savings stem from switching the merged company to the best third-party freight rates, *id.* at 1892:7-1893:5, increasing the volume it can offer to third-party carriers, *id.* at 1893:7-21, increasing its ability to dictate terms on inbound freight, *id.* at 1893:22-1894:19, and maximizing backhaul, or the ability to have outbound trucks "swing by" suppliers to pick up inbound freight that a third party would normally deliver, *id.* at 1894:22-1895:8. These savings are achievable because of the larger overall freight spend of the combined company as well as increased network density. [redacted]

460. **Operations: Enterprise Asset Management.** Enterprise asset management savings flow largely from indirect sourcing, which is the acquisition of "goods and services that the company uses in the course of their business as opposed to what they sell to customers." Wood (McKinsey), Hearing Tr. at 1895:12-15. Because neither Sysco nor USF have previously analyzed indirect sourcing savings and did not have a factual basis to discuss incremental savings opportunities, McKinsey calculated what each of the two companies could achieve on their own and then what they could achieve by combining. *Id.* at 1895:19-1896:15. Only the amount attributable to the combined purchasing volume of the two companies was included as a merger-specific, variable cost saving. *Id.* at 1895:19-1896:15 ("the full value of what we calculated is five times this number.").

461. **Field Sales.** Field sales synergies stem from optimizing the merged company's number of field sales associates. Wood (McKinsey), Hearing Tr. at 1896:16-1897:12. Field sales employees will see their non-sales responsibilities reduced, allowing them to focus more on selling. *Id.* at 1897:23-1898:9. The merged company will also be able to consolidate its

customer-facing representation, based on the consolidation of Sysco and USF customers. *Id.* at 1897:8-12; DX-01355, Hausman Rpt. ¶ 153. And because the company will be able to consolidate its sales force, it will be able to reduce the number of individual managers as well. Wood (McKinsey), Hearing Tr. at 1899:22-1900:6.

3. Efficiencies Will Pass Through To Customers

462. The merger will reduce the costs incurred by the merged company when it purchases and distributes food, which will in turn reduce the prices customers pay for those products and services. [redacted] DX-03159, Bresnahan Rpt. at 156-61.

463. The combined entity's cost reductions will pass through to customers at high rates, particularly street and other "Local Customers." Historically Sysco and USF have "passed on" [redacted] of their savings in some high-volume product categories and roughly [redacted] of their savings for other products. *See* DX-03159, Bresnahan Rpt. 159-60; [redacted] These past practices are instructive and suggest that similar savings will pass through to customers as a result of this merger. [redacted]

464. The merged company's increased buying power with suppliers will create value that will pass through to customers. [redacted]

[redacted] Sysco and USF competitors have conceded as much. [redacted]

465. The merged company's ability to optimize its distribution network will enhance its customer service in highly competitive local markets and allow it to deliver goods at lower cost. [redacted]

466. The merged company's ability to reduce its marginal cost of goods will result in lower prices for end consumers. *See* DX-01359, Bresnahan Rpt. at 156 [redacted]

467. The merged company's ability to offer lower prices will increase competition between the merged company and other market participants, including broadline distributors, systems distributors, GPOs, and specialty distributors, by forcing them to improve their pricing for the same services. [redacted]

[redacted]

468. Many Sysco and USF customers anticipate generally that the merger's efficiencies will pass through to them. [redacted]

469. Taken together, the cost savings for consumers, increased competition among distributors, and lower costs for suppliers and distributors weigh heavily in favor of the merger.

X. THE EQUITIES WEIGH IN FAVOR OF THE PROPOSED MERGER

470. Public equities, or those that inure to the benefit of consumers, weigh in favor of the merger. These benefits include the merger-specific efficiencies that will pass through to food service distribution customers, as well as improvements to the industry generally.

471. The merger will generate substantial efficiencies for the benefit of consumers throughout the country. Denying injunctive relief will ensure that those efficiencies can be realized quickly. By contrast, granting an injunction will doom the merger, ensuring that its benefits are never realized.

472. If the FTC obtains a preliminary injunction, the merging parties and their customers will be harmed. Sysco and US Foods will abandon the merger and consumers will be deprived of its benefits. *See* Schreibman (USF), Hearing Tr. at 1516:10-1517:8.

473. Even if the FTC reviews the merger in a so called "fast-track" proceeding, the merger will inevitably wither. Indeed, no merger has ever survived a fast-track proceeding, much less the Commission's full-scale Part III administrative review. Substantial mergers simply cannot weather the "glacial pace of an FTC administrative proceeding." *Lab. Corp*, 2011 WL 3100372, at *22 (quotation omitted). None ever has, despite the FTC's institution of so-called "fast-track" proceedings in 2009. *Id.*

474. Issuing an injunction would deprive consumers of the considerable benefits of the merger. Denying an injunction would enhance competition in multiple significant respects.

475. The equities require denying the FTC's request for injunctive relief.

XI. CONCLUSION

476. The FTC's request for an injunction should be denied.

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Respectfully submitted,

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APPENDIX A: KEY HEARING TESTIMONY BY WITNESS

I. SYSCO AND US FOODS WITNESSES

A. WILLIAM DELANEY (SYSCO)

1. Bill DeLaney is the President and CEO of Sysco Corporation. DeLaney (Sysco), Hearing Tr. at 1313:2-3 (May 11, 2015). He has worked at Sysco for 26 years and has held positions including: (1) Assistant Treasurer of Sysco Corporation; (2) Vice President and Treasurer of Sysco Corporation; (3) CFO of the Syracuse Operating Company; (4) President of the Charlotte Operating Company; and (5) President and CEO of Sysco Corporation. *Id.* at 1313:2-20.

2. Mr. DeLaney testified to the long history of Sysco, detailing its evolution from a small, family-owned company into a $46 billion company that currently serves nearly 400,000 customers. DeLaney (Sysco), Hearing Tr. at 1314:1-1317:11, 1320:24-1321:9. Sysco has grown organically and through acquisitions. *Id.* at 1317:12-1318:6.

3. The food distribution industry grew, particularly from the 1970s through the early 1990s, DeLaney (Sysco), Hearing Tr. at 1316:15-18. But the 2008 financial crisis changed the foodservice industry, as consumers became much more disciplined in how they spent their discretionary income, it directly impacted foodservice distributors customers, placing customers under pressure and bringing lower growth and increased competition *Id.* at 1318:7-1319:20 ("[The financial crisis has] made competition even more acute than it was before."); *see also id.* at 1320:9-20 ("[O]ur gross margin has been under tremendous pressure."). Price has become the first, or a close second, priority for all of Sysco's customers. *Id.* at 1319:21-1320:8 ("You still need to provide the service. You still need to have the right people, but price is on the top of the mind for everyone.").

4. Nearly 16,000 firms compete in the foodservice industry, and new firms can enter with ease. DeLaney (Sysco), Hearing Tr. at 1319:7-12. Mr. DeLaney explained that these market

realities have made it even more important for Sysco to reduce costs to remain competitive. *Id.* at 13:9-20 ("[W]e have to continue to even accelerate taking costs out of our business. . . because that's the only way we can really continue to compete at the level we want to compete. . .").

5. As a recognition of this imperative, in FY2013, Sysco established a plan to take $600 million out of its costs over a three-year period, ending in FY2015. DeLaney (Sysco), Hearing Tr. at 1321:10-22. These initiatives will conclude in FY2016. *Id.*

6. Mr. DeLaney explained that, according to publicly available Technomics data, foodservice is a $240 billion industry and has 16,500 competitors. DeLaney (Sysco), Hearing Tr. at 1323:21-22, 1324:14-19. Mr. DeLaney confirmed that, after the merger, Sysco and USF will control "about 25 percent before the . . . PFG divestiture." *Id.* at 1324:23-1325:6.

7. DeLaney testified that he recommended that Sysco acquire USF because the best way to grow the company "is to become more important to your customers and to understand their needs better and do everything we can to compete. And as we just talked about at the top of that list is to find ways to take costs out of the . . . system." DeLaney (Sysco), Hearing Tr. at 1325:20-1326:10. From the very beginning of its merger talks with USF, Sysco focused on cost savings and synergies. *Id.* at 1327:14-1328:4. Even before initiating the merger, Sysco engaged McKinsey & Co. to estimate cost savings. *Id.* at 1328:21-1329:4. Sysco presented these preliminary cost savings estimates to its Board in November 2013. *Id.* at 1329:10-1330:16.

8. Sysco expects to achieve cost savings that stretch across multiple areas, including "merchandising, sales and marketing, supply chain, et cetera." DeLaney (Sysco), Hearing Tr. at 1330:20-22. Within these cost savings calculations, Mr. DeLaney noted that Sysco tempered its estimates based on the likely scenario that it would lose business to its many competitors during the transition period. *Id.* at 1331:18-1332:1. Sysco expects to lose customers because "there's

going to be some disruption, especially early days as we go along, and that will give competitors an opportunity to swoop in and use that as an excuse to take business. It's already begun to happen. The other reason . . . is that most customers talk to a lot of suppliers, and they buy from multiple suppliers." *Id.* 1332:2-17. Sysco expects to lose "2 billion in sales." *Id.* at 1341:1-7.

9. After the transaction was approved, Sysco put together a more extensive team to evaluate cost savings for the merged company. DeLaney (Sysco), Hearing Tr. at 1333:21-1334:12. This work continues today. *Id.* at 1334:13-15. Sysco has invested "at least $200 million" to identify and plan for these cost savings. *Id.* at 1334:16-24. Some of the efficiencies for which Sysco has planned include:

- **Merchandising Savings**: "[T]he easiest way to understand what merchandising savings are, are leveraging the volume of the combined entities in a way that you couldn't separately to create cost savings on product purchases." *Id.* at 1337:7-10.

- **Supply Chain and Distribution Savings**: "[Y]ou look at how we deliver goods to customers and how we route trucks in a given day, say, here in the Baltimore/DC area, how could we more efficiently do these routes." *Id.* at 1337:16-1338:5.

- **Sales and Marketing Savings**: "Sales and marketing is a combination of over time enhancing some of the business solutions and some of the sales support that we provide our customers but also doing that in a more efficient way with less people with people that are maybe stronger than some of the people that we have individually." *Id.* at 1338:6-14.

- **Corporate Function Savings**: "Corporate function is essentially looking at the [G&A] side of the business of both corporate headquarters and in the field. US has a regional structure. We're moving toward that. So, it's—there's quite a bit of overlap there, which over two or three years there's an opportunity to reduce head count there as well." *Id.* at 1338:15-21.

10. Mr. DeLaney testified that his team is "signed up to produce at least $600 million in cost savings." DeLaney (Sysco), Hearing Tr. at 1339:6-1340:2. This $600 million is in <u>annual</u> savings and is what Sysco believes it can do "at a minimum." *Id.* at 1339:22-1340:8, 1342:14-16; *see also* 1340:18-19 ("Q: And you have high confidence you can do this? A: I do."). These savings will be fully realized in three to four years. *Id.* at 1342:17-20. And these savings will

not only benefit Sysco; they will be passed onto customers. *Id.* at 1341:18-20. During cross examination, Mr. DeLaney affirmed that these savings are merger-specific, stating: "We can't get anywheres [sic] close to $600 million without the merger." *Id.* at 1399:18-24.

11. Mr. DeLaney explained that this transaction is not about buying more distribution centers. DeLaney (Sysco), Hearing Tr. at 1342:22-1343:10. Rather, the transaction's value comes from "creat[ing] great returns by improving service to [Sysco's] customers." *Id.* at 1343:12-23. Mr. DeLaney testified that Sysco's increased buying power will allow it to better compete with volume aggregators, such as GPOs, to negotiate better prices with food manufacturers and drive down costs for customers. *Id.* at 1343:24-1345:4.

12. Mr. DeLaney does not believe that there is a national distribution monopoly that needs to be remedied. DeLaney (Sysco), Hearing Tr. at 1345:6-1346:6. But Sysco recognized that the FTC was concerned about national distribution, so to facilitate the merger and alleviate any concerns, Sysco agreed to divest some of its assets. *Id.* Sysco contacted multiple distributors but ultimately decided to divest distribution centers to PFG. *Id.* Sysco considers PFG a "strong competitor today," led by an "able executive." *Id.* at 1346:3-18

13. Mr. DeLaney testified that Sysco's CMU list—from which the FTC derived its national market definition— provides only an administrative convenience, noting that "ultimately the customer makes the choice whether they want the sales leadership to be domiciled in a local operating company or at the corporate office." DeLaney (Sysco), Hearing Tr. at 1345:6-1346:6. Mr. DeLaney confirmed that "not every company on the CMU list is national in the way the term would be understood generally." *Id.* at 1348:4-8. He explained that "this is a local business. All of our customers are delivered [to] . . . out of warehouses on trucks, on our trucks, from local operating companies." *Id.* at 1347:3-9.

14. Mr. DeLaney testified that customers such as Subway, Compass, Sodexo, which "really do need service all over the United States," can and do regionalize. DeLaney (Sysco), Hearing Tr. at 1348:9-25. Mr. DeLaney testified that Sysco would "pay the price" if it tried to target these customers for a price increase. *Id.* at 1349:4:14. When asked to step into the shoes of a Sysco customer, Mr. DeLaney stated that if Sysco tried to raise its prices, he would have many options "to replace some or all of Sysco's business." *Id.* at 1349:17-1350:15. Mr. DeLaney said he would contact Mr. Holm at PFG in addition to "a lot of large regionals . . . the Gordons, the Ben E. Keiths, and the Reinharts, because . . . the reality of this business is I probably don't have to do anything to get Sysco's business. I probably just have to threaten the business." *Id.* at 1350:16-1351:4.

15. Mr. DeLaney confirmed that the "National" customers for which the FTC claims Sysco and USF are the only options are "lower margin customers." DeLaney (Sysco), Hearing Tr. at 1354:18-1355:1. Mr. DeLaney attributes this to "the volume that they have the leverage in their negotiations and to the fact that they—you know, they negotiate, as we said earlier, a lot of their volume directly with the suppliers on a product." *Id.* at 1355:2-8. Sysco earns "a modest markup on cost . . . for warehousing and delivering their goods." *Id.*

16. Mr. DeLaney described a post-merger world that looks very similar to the extremely competitive pre-merger world. DeLaney (Sysco), Hearing Tr. at 1355:9-1356:8.

17. Mr. DeLaney testified that companies with different business models compete with Sysco all the time, including systems, DeLaney (Sysco), Hearing Tr. at 1324:11-13, specialty, *id.* at 1351:9-22, and cash and carry, *id.* at 1352:8-25.

18. Finally, Mr. DeLaney clarified that the statistics in the 2013 Food Network tracking results were the product of a marketing/advertising study, entirely unmoored from reliable

market share data. DeLaney (Sysco), Hearing Tr. at 1383:5-1387:10 ("[T]he nature of this work was more about our branding work. This was not work we did to assess market share or market opportunity.").

B. SCOTT SONNEMAKER (SYSCO)

19. Scott Sonnemaker is the Senior Vice President of Sales for Sysco Corporation. Sonnemaker (Sysco), Hearing Tr. at 1557:8. Mr. Sonnemaker has extensive experience in the foodservice distribution industry. He worked at Sysco's Portland, Oregon distribution center, and currently works at corporate headquarters, where he is responsible for corporate-multi unit customers, among other things, *id.* at 1558:4-17.

20. Mr. Sonnemaker provided background on this "incredibly diverse industry," explaining that Sysco serves customers "across the gamut," including "mom and pop operations," stadiums, hotels, hospitals, restaurants, and educational facilities, to name a few. Sonnemaker (Sysco), Hearing Tr. at 1559:9-19 ("We're the biggest industry with small business."). Given this diversity, customer procurement strategies vary considerably. *Id.* at 1559:20-1560:6. Smaller customers may shop around between multiple distributors, while larger customers may contract directly with manufacturers, GPOs, a distributor, or "all of the above." *Id.*

21. Mr. Sonnemaker explained how Sysco classifies and views its customers. The simplest distinction, he testified, was between contract customers and non-contract customers (known as "street customers"). Sonnemaker (Sysco), Hearing Tr. at 1560:7-17. Street customers are the "bread and butter" of Sysco's business, *id.* at 1560:16-17, and Sysco "sales reps are in competing every day for ever line item . . . with every possible avenue . . . that foodservice products will be brought to market," *id.* at 1561:2-5. Mr. Sonnemaker recounted that when he ran the distribution center in Portland, Oregon, he battled daily with: Pacific Seafood, a specialty seafood distributor; FSA, a regional broadline distributor; McDonald Wholesale, a local broadline

distributor; cash-and-carry firms; and Duck Delivery, a specialty produce distributor that has added "more and more product lines, which is very typical for a specialty house," and which competed with Sysco for customers as large as Compass. *Id.* at 1561:5-1562:21.

22. Mr. Sonnemaker testified that Sysco has two main types of contract customers: LCC, or local contract customers, Sonnemaker (Sysco), Hearing Tr. at 1563:8-25, and CMU, or corporate-multi unit customers, *id.* at 1566:14-20. The driving force behind this distinction is "customer preference" as to whether their contract is managed by the local operating company, in the case of an LCC, or corporate headquarters, in the case of a CMU. *Id.* at 1566:16-20 ("LCC allows the customer, the customer preference really drives us because that lead house concept allows the restaurant or the customer to be very close in proximity to the folks that they feel like are handling their business."); *id.* at 1568:12-16 ("Now again, that's a preference. Some prefer that local touch, some prefer the national kind of support as far as getting things done. So it's something that we allow the customer really to push or to really work on their preferences."). Hence, an LCC customer could include "a multistate group of restaurants," or a single location, depending on the customer's preference. *Id.* at 1563:12-18; *see also id.* at 1566:5-13 (discussing Shari's, an LCC which services its 100 locations from seven or 8 distribution centers, and Cinemark, an LCC serviced out of about 25 distribution centers). And customers may switch back and forth, depending on what works best for them. *See id.* at 1568:20-1569:7 (discussing Black Bear Diner and Culver's which switched between designations). Sysco does not have different sales formulae for different customers—as Mr. Sonnemaker explained, the model is "[g]ood service, right price, right products." *Id.* at 1623:19-21.

23. Approximately 300 accounts make up Sysco's CMU customer list. Sonnemaker (Sysco), Hearing Tr. at 1565:10-16. Mr. Sonnemaker emphasized that although CMU customers are

called "national customers" "as kind of a short hand" internally at Sysco, this label "certainly doesn't mean" that these customers "are national in scope at all." *Id.* at 1565:22-1566:4. "As a matter of fact," he explained, "the vast majority of them are not national in scope." *Id.* Rather, CMU customers are a diverse group, ranging from very small operations (60 of the approximately 300 CMUs use one operating company, and many others "have three or four locations or less," *id.* at 1565:12-16), to very large businesses spanning the entire United States, *id.* at 1571:13-17. The average CMU customer uses about six or seven operating companies. *Id.* at 1569:8-12.

24. With respect to Sysco's largest customers, Mr. Sonnemaker testified that he did not have a single customer for whom regionalization would not be a realistic option—"not a one." Sonnemaker (Sysco.), Hearing Tr. at 1572:11-13. Indeed, Mr. Sonnemaker explained that many of Sysco's larger customers already regionalize, including Compass, Sodexo, Wendy's, and Subway. *Id.* at 1572:14-19.

25. Sysco faces robust competition for these larger CMU customers. Over his 20 years at Sysco, Mr. Sonnemaker testified that his biggest disappointments in terms of losing customers have been Red Robin, which Sysco lost to DMA, and Culver's, which Sysco lost to FSA and Gordon. Sonnemaker (Sysco), Hearing Tr. at 1573:7-1574:23. And in just the last two fiscal years, Sysco has lost 10 CMU accounts entirely. *Id.* at 1576:11-17. Out of these ten, only two and one-third went to USF (because USF split one customer's business with other distributors). DX-05016. One customer elected self-distribution and the rest went to DMA, PFG, Gordon Foodservice, FSA, and SSA. Sonnemaker (Sysco), Hearing Tr. at X 1575:12-1576:10. Mr. Sonnemaker testified that he did not consider USF to be Sysco's closest competitor for these customers. *Id.* at 1576:24:1577:14.

26. From a management perspective, Sysco divides CMU customers into four groups, or "verticals," Sonnemaker (Sysco), Hearing Tr. at 1579:5-8: chain restaurants; FSMs; travel and leisure; and healthcare, military, education, and retail.

- *Chain Restaurants*. By revenue, the largest of these groups is chain restaurants, which is "significantly bigger that the" other three. *Id.* at 1579:10-13. Mr. Sonnemaker observed that Sysco competes vigorously with systems distributors and other broadline distributors for this business. *Id.* at 1580:6-11. He explained that chain restaurants are served from both broadline and systems facilities, and of the 32 customers served from Sysco's systems facilities, 11 were shared accounts (with its broadline facilities), including Texas Roadhouse Grill and Panda Express, among others. *Id.* at 1580:6-21. Customers served from systems distribution facilities do not label themselves as systems customers; instead, Mr. Sonnemaker testified, they recognize that "there's no real big distinction," they simply want lower inbound freight costs. *Id.* at 1581:17-1582:13.

- *FSMs*. Mr. Sonnemaker testified that FSMs are the "next largest segment." *Id.* at 1579:18-21. Even the largest among these customers award their business regionally, including Compass and Sodexo. *Id.* at 1583:20-1584:2. Aramark, one of the three largest FSMs, currently has the ability to "move certain markets to someone else per their contract," and could regionalize further if it chose. *Id.* at 1588:12-14; [redacted] Mr. Sonnemaker noted that some Aramark members are served by Gordon Foodservice in the Midwest. Sonnemaker (Sysco), Hearing Tr. at 1636:21-23. Mr. Sonnemaker noted also that Sysco competes vigorously with specialty distributors for FSM business. He recounted that Sysco recently lost $40 million of Compass business to PROACT, a consortium of specialty produce distributors, *id.* at 1584:7-19; DX-01015, and lost Aramark's catfish business in the Southeast to Inland Seafood, Sonnemaker (Sysco), Hearing Tr. at 1586:3-15; DX-00546. These types of losses to specialty distributors happen, Mr. Sonnemaker explained, "with regularity"—Sysco is "always in competition" with specialty distributors for "product lines." Sonnemaker (Sysco), Hearing Tr. at 1585:9-14.

- *Travel and Leisure*. Within Sysco's travel and leisure segment are hotel chains, like Hilton, and GPOs, like Avendra, that service hotel chains. *Id.* at 1588:17-24. Mr. Sonnemaker testified that Avendra contracts regionally, with DMA securing the majority of those regions, USF with "several," and Sysco servicing only two. *Id.* at 1588:24-1589:2. Hilton used to award its business regionally, but in the last few years, it created a Joint Venture Program with Sysco. *Id.* at 1589:4-15. Even within that JVP, should service slip or if there are "any other issues," Hilton's franchises could "move their distribution back to another distributor" as individual hotels did when Sysco had service problems in the Denver market. *Id.*

- *Healthcare, Military, Education, and Retail.* Mr. Sonnemaker testified that the healthcare business is "highly fragmented" and "very local in nature" due to the fact that most hospitals and nursing chains, who are the end-customers, are located in a single area. *Id.* at 1589:20-24. In fact, Mr. Sonnemaker observed that healthcare customers tend to act "more like a local contract customer." *Id.* at 1590:2-6. Healthcare GPOs are another major portion of this business segment. *Id.* at 1590:7-8. Mr. Sonnemaker explained that while Sysco was successful in securing business from healthcare GPOs, that achievement by no means reflected Sysco's overall success in the healthcare provider market, as a substantial portion of healthcare spending occurs outside GPOs. *Id.* at 1649:5-1650:3.

27. Mr. Sonnemaker explained the three primary ways in which healthcare GPOs structure their business. First, some GPOs, like HPSI and Amerinet, award business regionally. Sonnemaker (Sysco), Hearing Tr. at 1590:21-1591:3. Second, some GPOs, like UHF Navigator and MedAssets, are distributor neutral, meaning they secure contracts with multiple distributors and are indifferent as to through which distributor a member purchases. *Id.* at 1591:4-14. Third, some GPOs, like Premier, use a sole-source distributor, although this arrangement is "rare." *Id.* at 1598:16-18. But even Premier awards regionally. *Id.* at 1634:16-24.

28. Mr. Sonnemaker testified that some GPOs may be concerned about the merger because the merged entity's buying power and synergies would allow it to compete more effectively with GPOs, which, in turn, would "diminish the value proposition of a GPO." Sonnemaker (Sysco), Hearing Tr. at 1591:25-1592:13. With respect to Premier and sole-source GPOs, Mr. Sonnemaker opined that they might "feel like there will be increased competition because of [Sysco's] current relationships with several other healthcare GPOs," *id.* at 107:2-4, but that they "certainly have the options," including regionalizing, becoming distributor neutral, or using PFG or DMA, *id.* at 1593:19-1594:7.

29. RFPs are an uncommon occurrence for CMU customers, Mr. Sonnemaker explained, and when they do occur, they are not formal auction-type RFPs—they more akin to bilateral negotiations. Sonnemaker (Sysco), Hearing Tr. at 1596:20-1597:3 ("on the core business, CMU business, it's really not a pure RFP process, it's usually a conversation that starts with a meeting and it will—to determine if there's a need, and it kind of goes from there"); *id.* at 110:5-18 (explaining that formal bids do not happen "that frequently" and that they are frequently followed by bilateral negotiations). For example, Mr. Sonnemaker explained that the University of California RFP, in which PFG won the Northern California business, was "kind of an informal RFP approach because there was so much give and take, there was not a blind opening of this bid." *Id.* at 1599:7-21; DX-01168. When asked how many formal RFPs Sysco responds to each year, Mr. Sonnemaker estimated two or three, with Premier's 2014 regional RFP being one of them. Sonnemaker (Sysco), Hearing Tr. at 1598:5-22 ("it's just not that common, it's usually a bilateral negotiation").

30. Mr. Sonnemaker clarified how the FTC obtained the RFP data on which Dr. Israel ultimately based a number of his conclusions. He testified that the FTC asked for and required Sysco to produce RFP data using the format the FTC provided. Sonnemaker (Sysco), Hearing Tr. at 1600:18-1601:6; [redacted] In other words, without the RFP "data," there could be no certification, and without the certification, the transaction could not conclude. Sonnemaker (Sysco), Hearing Tr. at 1605:7-13. This was despite the fact that Sysco does not keep an RFP database in its ordinary course of business. *Id.* at 1601:7-17; [redacted] Mr. Sonnemaker noted the many instances in which Sysco objected to the

process of compiling this data because it could not construct the requested data "with any reasonable accuracy." Sonnemaker (Sysco), Hearing Tr. at 1603:3-18 ("We share your wish that there was a reliable database of bidding activity in this industry, but unfortunately neither we nor Sysco can simply fabricate one by wishing.") (quoting DX-05024 at 3); Sonnemaker (Sysco), Hearing Tr. at 1603:19-1604:2 ("As stated on the call, the end result of all this work would be an unreliable dataset at best given that Sysco loses 20 to 25 percent of its sales force per year. The limits of human memory for those salespeople that have stayed during the relevant period, and the fact that customers control the universe of information relating to bidding on their business.") (quoting DX-05024 at 4). Mr. Sonnemaker explained that the data ultimately submitted to the FTC were inaccurate because customers generally do not inform Sysco which other competitors are bidding on an RFP. Sonnemaker (Sysco), Hearing Tr. at 1603:14-18; *id.* at 1604:14-20. When Sysco ultimately responded to the FTC's request, its attorneys sent a letter to the FTC explaining that it could not "verify the veracity of the shared information," that the information was "not maintained in the ordinary course of business," and that Sysco did not "have the information or knowledge required to provide a complete and accurate to response" to the FTC. *Id.* at 1620:13-20; DX-01556, at 2. In fact, when Sysco submitted this information to the FTC, it compared its RFP data to USF's and, finding substantial inconsistencies, informed the FTC that these inconsistencies serve "to demonstrate how unreliable much of the requested information might be." Sonnemaker (Sysco), Hearing Tr. at 1607:21-1608:5; DX-01556, at 3.

31. Mr. Sonnemaker testified that the RFP data submitted to the FTC did not contain information about customers' second and third choices—it only listed winning bidders. Sonnemaker (Sysco), Hearing Tr. at 1611:2-25. In short, Mr. Sonnemaker would not recommend that anybody rely on the RFP data for business decisions or analysis. *Id.*

32. Mr. Sonnemaker explained that, by and large, Sysco does not offer consistent products nationwide. Sonnemaker (Sysco), Hearing Tr. at 1569:13-22. Sysco aims to carry "a group of core products" across its locations, but for the remainder of its offerings—even its private-label products—Sysco will not "have the exact same product in every box." *Id.* at 1569:15-25. And, he explained, the "easiest way to get consistent products for those customers that really want that is obviously just to" purchase directly from the manufacturer. *Id.* at 1570:4-12.

33. Mr. Sonnemaker testified that the recent trend is for customers to prefer service from fewer distribution centers, because that diminishes inbound freight costs, which can outweigh the associated increase in outbound freight costs. Sonnemaker (Sysco), Hearing Tr. at 1570:12-1571:2.

34. Mr. Sonnemaker was emphatic that, should the companies merge, Sysco could not target customers for higher prices, Sonnemaker (Sysco), Hearing Tr. at 1577:15-19 ("Absolutely not."), because there are multiple capable distributors in every market, *id.* at 1577:21-22, and because "[t]he business is just too competitive," *id.* at 1577:21-23. Specifically, Mr. Sonnemaker explained that customers "are too well educated" and understand the business too well to accept a price increase. *Id.* at 1577:23-25. Mr. Sonnemaker readily acknowledged that Sysco and USF have the broadest footprint of any of their competitors, *id.* at 1578:10-12, but explained that the merged entity would be unable to raise prices, even to nationwide customers because "foodservice is local." *Id.* at 1578:13-16 ("It's about that facility competing against other folks in that facility."); *see also id.* at 1572:11-13 (regionalization is a realistic option for all nationwide customers). And Mr. Sonnemaker was "adamant[]" that many street customers prefer local distributors who source local products and are part of the local community—success is "not about whether [Sysco's] the biggest." *Id.* at 1579:1-4.

35. In sum, Mr. Sonnemaker testified:

> [T]here [is] just too much competition [to raise prices], and frankly, our customers are also extremely educated in this business, and—and customers move between other [competitors]. There is a lot of pricing pressure at all times in every segment of our business. And [a price increase] wouldn't be justified, and our customers, if we did that, they would move very quickly to another distributor.

Id. at 1614:8-14.

C. DAVID SCHREIBMAN (USF)

36. David Schreibman is the Executive Vice President of Strategy for USF. Schreibman (USF), Hearing Tr. at 1442:1-3. Mr. Schreibman's responsibilities include: all USF merger and acquisition activity; competitive intelligence, which involves understanding the markets in which USF competes; operational strategies; and CHEF'STORE, USF's cash and carry segment. *Id*. at 1442:8-18.

37. Mr. Schreibman explained USF's business for both "Local" and "National" Customers. For service to independent restaurant operators (known as "street" distribution), USF purchases products from manufacturers, stores them in its warehouses, and resells them to customers. Schreibman (USF), Hearing Tr. at 1443:2-13. Street customers pay a single price, which includes the cost of the product and the cost of delivery. *Id.* at 1443:14-18. He explained that USF sells to street on a product-by-product, week-by-week basis. *Id.* at 1452:17-22. National customers usually negotiate their prices directly with manufacturers. *Id.* at 1443:19-1447:3. These customers negotiate separately with USF to determine the markup or per-case fee for distribution. *Id.* at 1444:4-15.

38. Mr. Schreibman testified that GPOs compete with USF. He explained that, instead of purchasing through USF, GPOs contract directly with manufacturers on behalf of their members, creating a menu of products at lower cost than USF can offer. The price that the GPO members

pay is the price that the GPO negotiates directly with manufacturers. Schreibman (USF), Hearing Tr. at 1558:8-19. GPOs have lower product volume than USF, but can obtain better prices from manufacturers. *Id.* at 1445:25-1446:10. GPOs collect administrative fees from manufacturers and distributors whenever the distributor delivers product to a GPO member. *Id.* at 1446:21-1448:6.

39. USF estimates that the food away from home market in which it competes had $250 billion in sales in 2014, and that USF had a 9% share of that market. Schreibman (USF), Hearing Tr. at 1449:9-11; 1450:3-10; [redacted]

40. GPOs do not actually pay distributors. The distributor purchases the product from the manufacturer and receives a rebate or "bill back" from the manufacturer when the product is delivered that covers the difference between the GPO-negotiated price and the price the distributor pays the manufacturer. Schreibman (USF), Hearing Tr. at 1446:6-20 (explaining that if a GPO has negotiated an $18 per-case rate for a product that usually costs $20, US Foods purchases the product at $20 and is issued a $2 rebate by the manufacturer). Separately, the GPO negotiates with the distributor for the distribution fee that the GPO member will pay the distributor; GPO members pay that fee to the distributor directly. *Id.* at 1446:6-1448:6. Thus, the only exchange of money between the GPO and distributor is the administrative fee that the distributor pays the GPO for the "privilege" of delivering product to GPO members. *Id.* at 1446:25.

41. Mr. Schreibman testified that distribution to independent restaurants is highly competitive. There are approximately 16,500 distributors serving independent restaurants. Schreibman (USF), Hearing Tr. at 1442:1-3. USF estimates that its share of this customer segment is 9% ($6.4 billion out of $70 billion). *Id.* at 1442:3-10; DX-02118, US Foods Market Update at 5 (February 24, 2014). On average, independent restaurants purchase from twelve distributors. Schreibman (USF), Hearing Tr. at 1451:16-20. Mr. Schreibman explained that USF competes directly with specialty distributors for sales to independent restaurants. Specialty distributors "hav[e] a greater array of products within their expertise," and use products offered by USF as "loss leaders," or products sold at a loss to attract customers. *Id.* at 1452:1-16. USF lowers its prices to compete with specialty distributors. *Id.*at 1452:17-1453:5. *See id.* at 1453:6-23. Ethnic specialty distributors also compete directly with USF, and can act "as a broadliner" within their specialty. *Id.* at 1454:8-15.

42. Mr. Schreibman testified that USF competes with cash and carry firms, which are a "major competitive threat." Schreibman (USF), Hearing Tr. at 1455:5-10. Mr. Schreibman observed that Restaurant Depot is a particularly strong competitor, and views it as "a leader in a highly fragmented and competitive market." *Id.* at 1460:21-1461:4. Mr. Schreibman testified that Restaurant Depot carries approximately 6,000 to 6,500 SKUs in its warehouses, which is comparable to the number of SKUs USF carries in about ten of its distribution centers, including its distribution center in Omaha, Nebraska, *id.* at 1463:2-8, and that Restaurant Depot "stores" are typically 60,000 to 70,000-foot warehouses "that look just like [USF's warehouses]," *id.* at 1501:16-18.

43. Mr. Schreibman testified that customers substitute between cash and carry and broadline distribution in local markets, explaining that USF loses significant volume of sales when

Restaurant Depot opens a new facility. Schreibman (USF), Hearing Tr. at 1457:23 1458:14. Mr. Schreibman pointed out that Restaurant Depot maintains a cost advantage over USF, because it receives superior prices from manufacturers. *Id.* at 1458:15-1459:18. Mr. Schreibman testified that, to compete with cash and carry firms, USF frequently has to lower its prices. *Id.* at 152:23-153:4. Indeed, he noted that Restaurant Depot explicitly targets customers of broadline distributors by comparing its prices to those of broadline distributors, even asking customers to provide invoices from their distributor, Schreibman (USF), Hearing Tr. at 1498:3-9; [redacted] and providing delivery options for high-volume customers. *Id.* at 5:7-8:23. Like Restaurant Depot, USF competes with club stores, Schreibman (USF), Hearing Tr. at 1456:4-12; 1499:3-5, and lowers its prices to compete, *id.* at 1499:6-8.

44. Mr. Schreibman testified that USF tracks customers who shop at its CHEF'STORE, and finds that customers in every segment, including GPO members, healthcare, hospitality, and education shop in the cash-and-carry format. Schreibman (USF), Hearing Tr. at 1498:3-9.

45. Mr. Schreibman testified that distributors with fewer distribution centers can and do compete effectively against USF. In fact, USF has lost customers that preferred to be served by fewer distribution centers. Schreibman (USF), Hearing Tr. at 1503:2-23. Using fewer distribution centers reduces the cost per case of transporting product from the manufacturer to a distribution center (the "inbound freight") cost—a cost that the customer pays to the manfacturer. *Id.* Mr. Schreibman testified that shuttle yards reduce the cost of distributing to customers located further away from a distribution center. He stated that "[t]wenty-seven percent of [USF's] total distribution is by shuttle yard[.]" *Id.* at 1502:15.

46. Mr. Schreibman explained that USF's Linc database is unreliable and "very inaccurate." Schreibman (USF), Hearing Tr. at 1506:3. He testified that USF's territory managers (or sales representatives) "would not get their paycheck until they filled out Linc," and thus would "put fake information in just to complete the exercise." *Id.* at 1506:8-17. USF never relied on Linc to determine "what the competition was in any given market." *Id.* at 1506:4-6. USF replaced Linc with SalesForce.com, citing various issues. *Id.* at 1505:10-23.

47. Mr. Schreibman testified that the analysis conducted by Shapard (and relied upon by Dr. Israel to calculate market shares), evaluated USF's market *penetration*, not its market shares—*i.e.*, the percentage of customers that used USF and not the percentage of total spend that went to USF . Schreibman (USF), Hearing Tr. at 1512:11-21. USF engaged CHD, an outside consultant, to estimate the total size of the purchases made by all independent restaurant customers in each local market and USF's sales as a percentage of those purchases. *Id.* at 1507:25-22:6. USF's estimates of market share in local markets as discussed above are significantly lower than the "market penetration" figures relied on by Dr. Israel in his report. *Id.* at 1512:22-1514:3; DX-07003, "USF Market Shares," at 1.

48. Mr. Schreibman explained that the merger was necessary to allow both Sysco and USF to decrease their cost of goods, because "by definition synergies require two parties, and the scale of US Foods merging with Sysco would allow [them] to take out more cost than [USF] could do as a standalone entity." Schreibman (USF), Hearing Tr. at 1555:6-14.

49. Finally, Mr. Schreibman testified that if the court preliminarily enjoins the merger, USF will terminate the transaction in September 2015 because the uncertainty over its future has adversely affected the company. Schreibman (USF), Hearing Tr. at 1516:10-1517:8

D. THOMAS LYNCH (USF)

50. Thomas Lynch is the senior vice president of national sales at USF. Lynch (USF), Hearing Tr. at 1692:5-7.

51. Mr. Lynch testified that USF's "National" sales customers are those whose contracts are managed at the corporate level. "National" does not mean that a customer is served by only one broadline distributor, or that it has a single contract across all of its locations, a single point of contact, product consistency across all of its locations, or a single technology platform. Lynch (USF), Hearing Tr. at 1692:11-22. There is no hard-and-fast rule governing whether USF customers are managed nationally or locally. For instance, some customers with footprints across multiple regions of the country, such as Famous Dave's—to which USF has more than $20 million in sales across 10 separate distribution centers—are locally managed. *Id.* at 1694:7-25. Other customers are nationally managed "even though their locations are limited to one region of the country," "one state" or even to "one distribution center." *Id.* at 1695:1-10. 50 of USF's 210 national sales customers are serviced by only one or two distribution centers, and only 15 are serviced by more than 35 distribution centers. *Id.* at 1695:22-1696:13; DX-02151. Of those 15, 9 use multiple broadline distributors. Lynch (USF), Hearing Tr. at 1777:5-1778:5.

52. Mr. Lynch testified that his national sales team competes for "well over $100 billion" of potential national sales, Lynch (USF), Hearing Tr. at 1744:24-1745:1; [redacted] from customers in the chain restaurant, healthcare, hospitality, education, government, and retail segments, *id.* at 1742:8-1744:15. Mr. Lynch has never used an estimate of potential sales to "National" customers, nor seen such an estimate limited to around $30 billion, as claimed by Dr. Israel. *Id.* at 1742:2-5.

53. Mr. Lynch testified that "USF has many national sales customers where USF is not the only broadliner [servicing the customer] across all of the customers' locations." Lynch (USF), Hearing Tr. at 1692:21-1693:1. For instance, Applebee's and IHOP (national chain restaurants), Avendra (a hospitality GPO), MedAssets (a healthcare GPO), the Defense Logistics Agency (a government agency), and Sodexo (a contract feeder or foodservice management company) are all serviced by multiple broadliners in addition to USF. *Id.* at 1749:20-1750:1. Because the customers use multiple broadliners, they do not have a single broadliner contract, single broadliner price and terms, a single broadliner point of contact, or a single broadliner technology platform. *Id.* at 1749:20-1750:2-10; DX-07009, "Plaintiffs' 'National Broadline Customers.'"

54. Mr. Lynch testified that MedAssets members are serviced by PFG, several DMA members, and Sysco. Lynch (USF), Hearing Tr. at 1696:21-1697:11. Similarly, Amerinet, another healthcare GPO, gives the majority of its business to Reinhart, Gordon, FSA, and Sysco. *Id.* at 1697:19-1698:1; [redacted] DMA members Reinhart, Gordon, and FSA contract with Amerinet in their individual capacities, not through DMA, meaning that Amerinet is sourcing regionally. Lynch (USF), Hearing Tr. at 1698:24-1699:1.

55. Avendra, USF's largest hospitality customer, is also serviced by various members of DMA. Lynch (USF), Hearing Tr. at 1711:1-14; [redacted] DMA is USF's "primary competition" for Avendra's business, Lynch (USF), Hearing Tr. at 1711:12-14, and USF's ordinary course documents show that DMA is a "bigger threat" than Sysco to take Avendra's business. *Id.* at 1711:15-1712:2; [redacted]

56. Mr. Lynch testified that DLA is serviced by Reinhart, Shamrock, Nicholas, Hartford Provisions, and multiple other broadliners to which DLA has awarded regional bids. Lynch (USF), Hearing Tr. at 1724:3-18; [redacted] He explained that the Veterans Administration ("VA"), which has been a USF customer for 20 years, told USF in its last renewal that it was also considering a "multi source" model like the one used by DLA, *id.* at 1726:22-25, 1727:17-17, and that USF believed it was competing for the VA's business against DMA members and PFG, as well as Sysco. *Id.* at 1726:14-1727:23. Mr. Lynch noted that VA Hospitals also make purchases from other broadliners such as PFG, Ben. E. Keith, and Sysco. *Id.* at 1728:1-21; [redacted]

57. Mr. Lynch explained that "National Customers" may use multiple broadline distributors to "reduce costs." Lynch (USF), Hearing Tr. at 1702:22-1703:9, 1707:20-1708:3 (referencing Subway, IHOP, and Applebees). In fact, Five Guys—which has almost 700 restaurants across the country—left USF as its sole-source distributor for a "a regional supply chain model" in order to "reduce costs," *id.* at 1703:14-22, 1705:15-1706:6; [redacted] representing USF's "single largest loss over the last several years," Lynch (USF), Hearing Tr. at 1705:9-14. *See also id.* at 1704:7-13 (USF was Hooters' sole-source distributor until it left for DMA).

58. Although USF does not have a systems distribution division, Mr. Lynch explained that USF competes systems (or customs) distributors. Mr. Lynch noted that IHOP and Applebees are serviced by both USF and Maines, a systems distributor, Lynch (USF), Hearing Tr. at 1708:4-15, that USF won the McAllister's Deli business from MBM, a systems distributor, before losing it (along with its $80 million annual revenue) to Merchants, a broadliner, *id.* at 1704:16-1705:8,

and that USF recently lost the Krystal's business to MBM, *id.* at 1708:16-1709:1. Similarly, Mr. Lynch observed that Five Guys is now serviced by a collection of both broadline and systems distributors. *Id.* at 1705:15-1707:5; [redacted]

59. Mr. Lynch testified that USF regularly competes with specialty distributors. For instance, USF's "pricing proposals to Avendra take into account expected competition from specialty distributors." Lynch (USF), Hearing Tr. at 1715:11-22, and Avendra is serviced by numerous specialty distributors for products that USF could distribute, including seafood, meat, poultry, produce, and cheese products. *id.* at 1712:7-1713:20, 1715:4-10; [redacted] Likewise, USF has lost $20 to $30 million in produce business with Foodbuy (which offers procurement services to various GPOs) to specialty distributors, Lynch (USF), Hearing Tr. at 1721:3-1723:1, and is currently showing Foodbuy its "capability within the produce area" to try to "win [the business] back from the specialty distributors and have it [on USF's] trucks." *Id.* at 1722:3-21. And he noted that DLA is serviced by a variety of specialty distributors which were awarded regional bids by DLA, against which USF has "los[t] those product categories" in various regions. Lynch (USF), Hearing Tr. at 1725:20-1726:13; [redacted]

60. Mr. Lynch further explained that healthcare customers use specialty distributors for product categories which USF would like to supply, and USF must respond to those specialty distributors' prices in order to compete. Lynch (USF), Hearing Tr. at 1723:18-1724:2. Similarly, USF has "had to lower its price[s] to national sales restaurants to compete against specialty distributors." Lynch (USF), Hearing Tr. at 1709:16-18. USF had to "increase the amount of investment behind certain cuts of meat in order to get the[] franchisees back to buying

off of the [USF] . . . contract." *Id.* at 1709:19-1710:8. Mr. Lynch also acknowledged that lowering prices was "necessary to even get in the game" with Tavistock, and compete against its specialty distributors. Lynch (USF), Hearing Tr. at 1710:10-25 [redacted]

61. Mr. Lynch testified that USF competes with GPOs for national sales customers. For instance, Avendra was USF's "lead competitor" for Starwood , Lynch (USF), Hearing Tr. at 1717:13-24, and USF's pricing proposal to Starwood was targeted "to keep [Starwood] as [USF's] customer, as opposed to having them through a GPO," like Avendra. *Id.* at 1718:7-12.

62. Mr. Lynch testified that USF competes with manufacturers for national sales customers. For instance, Premier, USF's largest customer, has a "rotating calendar of where they put out different categories [of products] to compete." Lynch (USF), Hearing Tr. at 1729:5-9, 1731:20-45:8. "US Foods competes to sell its private-label product[s]" to Premier with "the nationally-branded manufacturers," *id.* at 1731:8-13, and Premier generally makes a "dual source" award, so that its members have the option to buy a branded product or a USF private label product. *Id.* at 1731:20-1732:8.

63. Mr. Lynch testified about USF's unique relationship with Premier. Until recently, USF was Premier's only broadline distributor, but in 2014, Premier negotiated a carveout giving it the right "to use regional distributors to cover . . . ten states." Lynch (USF), Hearing Tr. at 1732:25-1733:10. Mr. Lynch observed that if Premier implemented its single-state carveout model in the rest of the country, "US Foods could lose approximately 40 to 45 percent of [Premier's] business." *Id.* at 1734:19-1735:3. In fact, Premier has told USF that PFG, Gordon, Ben E. Keith, and Reinhart are "serious competitors" to USF. *Id.* at 1735:16-24. Following the merger

announcement, Premier told its members and USF that it would not be reliant on the merged entity. Premier said:

> The value [its members] receive through the Premier program today is primarily due to the strength of our manufacturer agreements and *will continue with whatever distribution solution we choose*;
>
> Distribution is only one component of [Premier's] program. Premier has a very extensive CMA portfolio and value-added services. *All of the significant distributors in the US are competing to be Premier's distributor(s) of our program*;
>
> *Most of our CMA programs are with branded manufacturers and will not change regardless of what happens with distribution.* For those CMAs that are within US Foods' private label, the foodservice committee is working to ensure we have branded alternatives.

Id. at 1735:25-1736:22; DX-01723, "Frequently asked questions concerning the Sysco acquisition of US Foods," USF3-00013086-88 at USF3-00013086-87 (emphasis added). Finally, Mr. Lynch noted that, although its contract with Premier requires Premier members to purchase 80% of their spend through USF, USF does not check for compliance.

64. Mr. Lynch explained that the merger presents concerns for USF's continued business with Premier. Premier has told USF that it is concerned about doing business with Sysco "because of Sysco's relationship with the three the largest contract feeders," which are Premier's competitors and against which USF has helped Premier compete. Lynch (USF), Hearing Tr. at 1737:8-10, 1739:13-1740:23; [redacted] Conversely, the three largest contract feeders have told USF that "US Foods' relationship with Premier is a negative consideration for them in whether to do business with US Foods," Lynch (USF), Hearing Tr. at 1738:6-1739:12, and USF does relatively little business with these FSMs—an estimated 10% of Compass's total spend, an estimated 1%-3% of Sodexo's total spend, and no business with Aramark, *id.* at 1738:6-1739:8.

65. Mr. Lynch testified that "National Customers" whose business will be split between PFG

and post-merger Sysco will have an easier transition than if all the customer's business remained at post-merger Sysco. A customer whose service changes as part of the merger integration from a USF location to a Sysco location would "experience a completely different set of products available at that distribution center . . . . a different IT platform of how they'd have to order . . . . [and] most likely there would be different people talking to them and managing their business." Lynch (USF), Hearing Tr. at 1747:22-1748:7. On the other hand, the divestiture will present little disruption for customers who move from USF to PFG: "[T]he transition to PFG should be seamless, because [customers are] going to have the same driver delivering [their] groceries, the same items . . . in stock . . . the same technology [platform] . . . [and] the same people talking to [the customers] at the local level." *Id.* at 1747:12-21. In addition, national sales customers who have contracts with manufacturers have already negotiated the price of their goods as delivered to a distribution center, so PFG will not be at any disadvantage on cost of goods sold to national sales customers because, for those customers, "the price is secured already." *Id.* at 1745:21-1746:8.

66. Mr. Lynch explained that some of USF serves some "National Customers" from distribution centers that are hundreds of miles away. For instance, Interstate's locations in Boise, Idaho are serviced by USF's distribution center in Salt Lake City, Utah, which is about 345 miles away. Lynch (USF), Hearing Tr. at 1719:5-18; DX-07007 at 3. Approximately 35 Interstate hotels are more than 100 miles from the USF distribution facility servicing the hotel location. DX-07007 at 3.

67. USF does not have a database that tracks its bids or the wins and losses or its competitors for any such bids. Lynch (USF), Hearing Tr. at 1755:2-17.

68. Mr. Lynch testified that if the merger occurs, national sales customers "will continue to use or threaten to use distributors other than Sysco," Lynch (USF), Hearing Tr. at 1749:9-13, and "this would be more than sufficient to defeat any price increase by Sysco, if it even tried to do one," *id.* at 1749:17-19.

E. MIKE BRAWNER (SYSCO)

69. Mike Brawner is Sysco's market president for the Mid-Atlantic region and the acting president of Sysco Atlanta. Brawner (Sysco), Hearing Tr. at 1657:2-9. As a regional market president, Mr. Brawner oversees eight "OpCos," or distribution centers, including Eastern Maryland, Baltimore, Virginia (Harrisonburg, VA), Hampton Roads, Raleigh, Charlotte, Columbia, and Atlanta. *Id.* at 1659:5-14. He is responsible for customer relationships in his market. *Id.* at 1660:10-16.

70. Mr. Brawner testified that "CMU" (corporate multi-unit) is an administrative designation of customers managed by Sysco's corporate sales team and that the decision to be designated a CMU customer is entirely based on "customer preference." Brawner (Sysco), Hearing Tr. at 1661:21-1662:17. If a customer prefers to maintain a relationship with a local OpCo, that customer will not opt for CMU designation; if a customer prefers to deal with the corporate office, that customer will opt for CMU designation. *Id.* CMU designation does not depend on a customer having national locations or locations across the country. *Id.* at 1663:17-20.

71. Mr. Brawner testified that systems distributors, including MBM, Golden State Foods, and CDI, compete for some of Sysco's largest customers. Brawner (Sysco), Hearing Tr. at 1663:25-1664:22 (stating that systems distributors would particularly "love to have" Cheesecake Factory, Jimmy John's, and Quizno's).

72. Mr. Brawner testified that customers generally do not use a single foodservice distributor, but instead divide their demand among many distributors. Brawner (Sysco), Hearing Tr. at

1664:23-1665:5 ("There's just so many options and so many competitors and so many specialty companies that provide specialty products in certain categories, and it's -- it's a challenge, and our sales team is constantly challenged to -- for the share of wallet in an account.").

73. Mr. Brawner testified that Sysco Columbia's assigned geography includes markets over 150 miles away from the OpCo. Brawner (Sysco), Hearing Tr. at 1665:6-1666:3. Mr. Brawner testified that Sysco Columbia OpCo services customers over 200 miles away, in neighboring states beyond the OpCo's assigned geography, and that the mid-Atlantic OpCos are willing to do "whatever it takes to take care of that customer." *Id.* at 1666:4-1665:19.

74. Mr. Brawner testified Sysco competes in the Columbia, South Carolina market with a number of other distributors, many of which do not have a facility within Sysco Columbia's geographic footprint, but nevertheless come in to that footprint and compete with Sysco. Brawner (Sysco), Hearing Tr. at 1667:23-1668:15.

75. Distributors of all types—broadline, regional, specialty—offer significant upfront incentives to Columbia market customers as a way to compete against each other and against Sysco. Brawner (Sysco), Hearing Tr. at 1671:13-1674:15. Sysco has lost business to all of these types of distributors, as well as cash and carry, and local specialty distributors serving customers offering "farm-to-plate" concepts. *Id.* at 1674:16-1678:1.

76. Mr. Brawner testified that Sysco faces stiff competition also in the Raleigh, North Carolina market. As with Columbia, Sysco serves customers outside the Raleigh geographic footprint from its regional OpCo. Brawner (Sysco), Hearing Tr. at 1678:16-1679:1.

77. Sysco sees competition from a number of distributors in the Raleigh market, including broadline distributors PFG, Merchants, Reinhart, Orrell's, EG Forrest, Pate Dawson, and systems distributors Golden State, and MBM. Brawner (Sysco), Hearing Tr. at 1679:2-1680:5.

78. The geographic footprint of Sysco's Virginia OpCo, located in Harrisonburg, includes Richmond, Roanoke, and communities in southwestern Virginia. Brawner (Sysco), Hearing Tr. at 1680:6-13.

79. Sysco Virginia faces competition from distributors located both inside Virginia and those with facilities in neighboring states, including Reinhart, Buzz Food, Saval Food, FoodPRO, Gordon, Ferraro, PFG, Orrell's, Staunton Foods, and Schenk Foods. Brawner (Sysco), Hearing Tr. at 1680:14-1681:21. Customers in the Virginia market regularly threaten to switch business away to competitors, even over amounts as low as $5. *Id.* at 1682:10-24.

80. Mr. Brawner testified that even cash-and-carry stores like Costco have started to deliver in Atlanta, adding yet another competitor to the distribution landscape. Brawner (Sysco), Hearing Tr. at 1682:25-1683:23.

81. Sysco does not just lose business to competitors in the mid-Atlantic region; it loses personnel, as well. Brawner (Sysco), Hearing Tr. at 1683:24-1684:11 ("We just in the last 60 days, I lost—or the Sysco Columbia OpCo lost two of our top ten salespeople to PFG, and we also lost an account exec within that 60-day window to PFG. And I'd say over the last six to nine months, we've lost over 21 sales associates to PFG, and a few to Gordon.").

82. Mr. Brawner testified that, despite the FTC's exclusive presentation of documents showing competition between Sysco and USF, Sysco received requests for incentives based on offers from a wide swath of competitors. Brawner (Sysco), Hearing Tr. at 1706:21-1707:1. When reviewing several RFIs from customers based on offers from USF, Mr. Brawner cautioned: "I would state that, you know, if we're going to look at [the RFIs], let's look at all of them. Let's don't, you know, just pull out the ones that are US-based, because there's . . . all kinds of requests for incentives against all competitors." *Id.* at 1705:6-10.

F. CARTER WOOD (MCKINSEY - CONSULTANT TO SYSCO)

83. Carter Wood is a Director at McKinsey & Company and the head of McKinsey's Organization Practice. Wood (McKinsey), Hearing Tr. at.1739:9-14. McKinsey's Organization Practice routinely works on post-merger management, change management, and organization design. *Id.* at 1739:15-17. Mr. Wood personally has worked on four mergers, including mergers in the food and transportation industries. *Id.* at 1739:23-1740:2. Prior to leading the Organization practice, Mr. Wood led McKinsey's purchasing and supply management practice. *Id.* at 1739:18-22.

84. Sysco hired Mr. Wood and McKinsey in the fall of 2013 to conduct due diligence on the synergies—or cost savings—that would result from bringing Sysco and US Foods together. Wood (McKinsey), Hearing Tr. at 1741:12-23. To conduct a "first pass" analysis, McKinsey evaluated all available Sysco and US Foods data in a pre-merger data room. *Id.* at 1741:19-1742:3. McKinsey used the data to establish an initial fact base and baseline for the integrated company's cost structure. *Id.* at 1742:9-12. It then interviewed Sysco and US Foods executives to identify and assess cost savings opportunities as a result of the merger. *Id.* at 1742:4-8. The McKinsey due diligence analysis revealed "very significant synergies" as a result of "putting the two companies together." *Id.* at 1742:9-12; [redacted] The Sysco board of directors considered and relied on McKinsey's conclusions when evaluating and ultimately approving the merger with US Foods. Wood (McKinsey), Hearing Tr. at 1731:13-21.

85. Following the announcement of the merger in December 2013, McKinsey undertook a comprehensive analysis of the cost savings "that would arise from the" merger and began to plan for the integration of the two companies. Wood (McKinsey), Hearing Tr. at 1742:22-1743:12.

Its work involved over 100 McKinsey consultants, *id.* at 1743:25-1744:2, 170 full-time Sysco and US Foods employees, *id.* at 1744:25-1745:2, and lasted twelve months, with the most intensive analysis occurring between January and September 2014, *id.* at 1731:10-14. Collectively, McKinsey dedicated tens of thousands of hours to and created tens of thousands of documents during the course of its efficiencies work. *Id.* at 1747:2-8.

86. In total, McKinsey and the business integration teams calculated over $1 billion in annual cost savings. Wood (McKinsey), Hearing Tr. at 1747:9-13; [redacted] The estimated cost savings come from a number of post-merger opportunities and include savings in distribution, merchandising, supply chain, enterprise asset management, and sales, among others. DX-05026 (trial demonstrative).

87. The estimated cost savings that will result from the merger are verifiable and substantiated given the (1) the tens of thousands of hours identifying, analyzing, and testing savings opportunities; (2) the requirement that Sysco and US Foods employees deliver the estimated cost savings after the merger closes; and (3) the "unprecedented" level of planning to ensure the combined company can capture every saving opportunity. Wood (McKinsey), Hearing Tr. at 1779:20-1780:25 ("So as one example, I mentioned there's 132 distribution facilities in the new company prior to any divestitures. Each of those 132 facilities has a detailed plan for every week of the year for the first year post-integration about exactly what's going to happen to that distribution facility. By the way, many of them are quite different from another because it depends on what's the order of shutting down facilities or consolidating things. But each one has a very detailed plan. And sitting behind those plans about what's going to happen are playbooks. So, for example, the playbook I mentioned on how to combine distribution

facilities. There's a playbook on how to go out and combine customers, et cetera, et cetera. So I would say a reasonable unprecedented amount of very detailed planning.").

88. *Distribution*: The distribution business team created a detailed five-year plan for capturing network optimization savings. Wood (McKinsey), Hearing Tr. at 1755:25-1756:8. It also updated and modified Sysco's existing manual regarding how to integrate new distribution centers—from customer transfers to IT requirements—to reflect the merger with US Foods. *Id.* at 1756:9-20. While the network optimization savings could be captured faster, Sysco and US Foods sought to pace the changes over five years for the sake of prudence. *Id.* at 1755:25-1756:8. The distribution business team also sought to account for issues that cannot reliably be modeled, including stretch distribution, by reducing its gross network optimization savings estimates by 25 percent. *Id.* at 1756:21-1757:14.

89. The estimated cost savings from route consolidation are $4 million. DX-05026 at 2 (trial demonstrative). Mr. Wood testified that the $4 million estimate is very conservative because (1) it only reflects savings attributable to overlapping customers that, after aggregating their Sysco and US Foods purchases, purchase most of those products from either Sysco or US Foods; and (2) the distribution team actually calculated a number four times as large during its modeling. Wood (McKinsey), Hearing Tr. at 1758:1-24.

90. *Merchandising*. [redacted] Mr. Wood testified about two illustrative examples of merchandising savings: end-to-end category management and interim savings levers (best cost and terms, enhance terms, consolidate suppliers). Wood (McKinsey), Hearing Tr. at 1768:18-1769:12; DX-05026 at 3 (trial demonstratives). End-to-end category management refers to the process by which companies determine which food products customers

value, and then aggregate their product supply around those items in order to achieve lower costs from the suppliers. Wood (McKinsey), Hearing Tr. at 1759:5-19, 1760:9-1761:8. For example, Sysco carries over 1,000 separate French fry items. *Id.* at 1760:16-19. Some of those items represent variations that customers care about—for example, sweet potato fries versus plain fries—while many do not, like 7/16th width French fries versus 9/16th width French fries. *Id.* at 1760:9-1761:8. Category management allows a company to aggregate volume in, for example, the 9/16th width French fries to achieve bulk savings from suppliers. *Id.*

91. Mr. Wood also testified that category management does not reduce choice for consumers. Wood (McKinsey), Hearing Tr. at 1761:9-21. He explained that category management need not result in eliminating any products from a company's product assortment, only buying more of those products that really matter to consumers. *Id.* Smaller quantities of other product varieties can remain in company warehouses. *Id.*

92. [redacted]

93. *Enterprise Asset Management.* [redacted] Mr. Wood testified about $21 million in indirect sourcing savings attributable to the merger. Wood (McKinsey), Hearing Tr. at 1773:9-15; *see also* DX-05026 at 5. Indirect sourcing is the process of purchasing goods and services for use by the company and not for resale to customers. Wood (McKinsey), Hearing Tr. at 1773:9-15. Mr. Wood explained that the EAM business team actually calculated a total of $103 million in indirect sourcing savings, but determined that a smaller savings amount of $21 million

specifically was attributable to the merger. *Id.* at 1773:21-1774:15; [redacted] It did so because neither Sysco nor US Foods had sophisticated experience with indirect sourcing and, as a result, there was no way for the EAM business team to determine what savings were possible as a result of combined volume of the two companies without first determining what the companies could do on their own. *Id.* at 1773:21-1774:15.

94. *Field Sales.* [redacted] After the merger, the combined company will need only one sales representative to call on a joint customer, allowing it to reduce the number of sales representatives employed by the combined company. Wood (McKinsey), Hearing Tr. at 1775:2-12. Natural attrition of sales representatives will reduce headcount to the appropriate level; no sales representatives will be fired. *Id.* at 1775:14-22. The merger will also improve productivity through changes to the combined company's sales coverage model, which results in $42 million in annual savings within five years of the merger. *Id.* at 1775:25-1776:9; DX-05026 at 6. This savings opportunity requires new technology and new employees to free marketing associates from administrative tasks like order entry. Wood (McKinsey), Hearing Tr. at 1775:25-1776:9. Sysco has attempted to make these productivity changes in the past, but failed. *Id.* at 1776:12-1777:6. Mr. Wood testified that the merger represents a transformational event that will unlock the company's ability to make large-scale changes across its 7,000-person sales force. *Id.*

II. <u>"NATIONAL CUSTOMER" WITNESSES</u>

A. CHRISTINE SZROM (VA)

95. Christine Szrom was called by the FTC to bolster its claim that there are "National Customers" that require national broadline services. Ms. Szrom lacked personal knowledge for most of the key assertions in her declaration.

96. Ms. Szrom is a Department of Veterans Affairs employee who worked as the senior contract specialist for the Subsistence Prime Vendor Program ("SPV") from 2010 to 2013. Szrom (VA), Hearing Tr. at 85:12-86:3. During this time, Ms. Szrom administered the food procurement program for the Department of Veterans Affairs, which uses one foodservice distributor for all products except baked goods, dairy, and produce VA medical centers, veteran canteen services, Army medical centers, and several Naval hospitals. *Id.* at 89:14-23. The VA is not a typical foodservice customer because of "administrative restraints" that require it to review and evaluate its foodservice distributors formally, *id.* at 97:2-7. Ms. Szrom stated that regulations prohibit the VA from contracting with a GPO, *id.* at 173:14-19, or an FSM, 173:14-19. The VA's foodservice contract amounts to around $225 million per year. *Id.* at 185:16-18.

97. Ms. Szrom had no responsibility for the VA's foodservice distribution contracting until June 2010, during the pendency of SPV-3, and accordingly did not have any role in the planning or negotiation of SPV-1, -2, or -3 contracts. Szrom (VA), Hearing Tr. at 150:21-161:12 ("Q. Now, SPV-1, which you talked about a little bit today, that was in place from 1996 to September of 2001? A. That's correct. Q. And that was before you were at the VA? A. That's correct. Q. And so you were not involved with SPV-1 at all; is that correct? A. Correct."), 162:24-25 ("Q. And you weren't involved at all with SPV-2, correct? A. Correct."), 166:6-13 ("Q. Is it fair to say that you were involved in the administration of SPV-3, but not its planning or negotiation? A. That's correct. Q. And you can't tell us who the bidders were for SPV-3, can you? A. I wasn't there for that, no. Q. And you were not involved in evaluating those bids? A. No, I was not.").

98. Because Ms. Szrom did not know about the specifics of the bidding process for SPV-1, including which distributors were involved with SPV-1 or the number of people at the VA who

were involved in administering SPV-1, Szrom (VA), Hearing Tr. at 162:1-19, Ms. Szrom could not know whether the VA had in fact achieved any savings by using a single broadline distributor as opposed to five different distributors, a fact to which she admitted at the hearing. *Compare* [redacted] *with* Szrom (VA), Hearing Tr. at 163:20-164:14 (admitting lack of personal knowledge for any savings that resulted from the change to SPV-2); *id.* at 165:2-6 ("Q. And so you don't have any personal knowledge of any underlying evaluation through which the VA determined that using a single broadline distributor was the most cost effective; is that correct? A. I was not part of that evaluation, no."). Nor could she quantify or describe the savings achieved by going to one broadline distributor; as she stated, she was not involved in evaluating those bids. *Id.* at:164:11-14. [redacted] Ms. Szrom could not articulate whether or how DMA had failed to meet requirements, or even what requirements DMA had failed to meet. This was because she had never evaluated a single proposal by DMA, ever. Szrom (VA), Hearing Tr. at 167:1-3. ¶

99. As the contracting officer for SPV-4, Ms. Szrom conducted "market research" that consisted of reading articles and doing Internet searches, contacting US Foods and Sysco, and posting a Request For Information on a website. Szrom (VA), Hearing Tr. at 167:13-168:7. Though her market research yielded a list of possible distribution options including DMA, PFG, Premier, CMARK, and Unipro, Ms. Szrom did not reach out to any of these companies. *Id.* at 170:3-171:1. She thus lacked a basis to conclude that any of these distributors lacked "the depth and breadth of the product line and the ability to meet special medical needs" to service the VA.

Id. at 149:8-13. For example, Ms. Szrom had never analyzed PFG beyond looking at its website, and had no information on PFG's product line offerings, pricing, private label products, whether PFG could cover all of the VA facilities that US Foods covers today, or whether PFG had experience in serving large acute care hospitals. *Id.* at 189:18-190:21. Nor did Ms. Szrom discuss foodservice distribution with other government agencies, such as the Defense Logistics Agency, even though Ms. Szrom reviewed the DLA's model of bidding out 42 separate regions across the United States. *Id.* at 171:11-20.

100. While both Sysco and US Foods submitted proposals for SPV-4, the VA eliminated Sysco before the price negotiations stage because Sysco's proposal took exception to the VA's terms and conditions, and was thus excluded from further participation. Szrom (VA), Hearing Tr. at 181:6-183:16. As a result, the VA did not negotiate price terms with Sysco or US Foods. *Id.* at 183:20-25; 184:10-13 ("Q. So in the entire months of negotiation between the VA and separately Sysco and US Foods, there were no price negotiations, correct? A. Correct."). Instead, Ms. Szrom merely evaluated US Foods' pricing proposal against Sysco's initial proposal, to analyze whether US Foods's proposed pricing was fair and reasonable. *Id.* at 184:1-7. US Foods was never told that there was a second bidder, *id.* at 185:9-12, and neither US Foods or Sysco changed the prices in its initial RFP proposal during the entire bidding process. *Id.* at 184:5-17. [redacted] she was comparing US Foods's pricing to Sysco's pricing in a bid that was never brought to the negotiating table. Szrom (VA), Hearing Tr. at 184:4-9. [redacted]

[redacted] was based on an "assumed" difference in pricing between US Foods and Sysco—an assumption "based on no negotiations because Sysco wasn't—we didn't negotiate with Sysco for price." Szrom (VA), Hearing Tr. at 186:16-21. (When asked about how the $4 million and [redacted] million figure could be reconciled, Ms. Szrom was unsure, and stated that "I'd have to look at the declaration to see if we base that on market basket or something else." *Id.* at 187:22-188:2.)

101. The contract awarded to US Foods reflected product pricing and delivery markups that varied across the VA's 23 regions (VISNs). Szrom (VA), Hearing Tr. at 184:21-185:8.

102. Ms. Szrom lacked the specialization or basis to comment on different competitors' breadth of product offerings and non-price factors. In evaluating bids for SPV-4, Ms. Szrom was not allowed to participate in the evaluation of non-price factors, such as the technical evaluation, Szrom (VA), Hearing Tr. at 176:13-23, product line and availability, 176:24-177:1, product quality, 177:2-4, procurement capabilities, 177:5-7, information systems, 177:8-10, customer service, 177:11-13, or evaluation of the offerors, 177:17-178:7. Ms. Szrom was only charged with evaluating whether US Food's proposed prices were fair and reasonable. *Id.* at 184:1-4.

103. In a debriefing memo the VA informed Sysco that one of its major weaknesses was its "capability to perform nationwide," which reflected Sysco's plan to use *too many* distribution centers. Szrom (VA), Hearing Tr. at 179:15-180:8.

B. JAMES THOMPSON (INTERSTATE HOTELS)

104. James Thompson was called by the FTC in support of its claim that hotel chains are an example of "National Customers" that require national broadline services. His testimony did not support this assertion.

105. Mr. Thompson is the senior vice president of procurement for Interstate Hotels and Resorts, a hotel management company that manages approximately 350 branded hotels in the

continental United States. Thompson (Interstate), Hearing Tr. at 198:14-19; 199:4-8. Interstate does not manage food distribution at all the hotels that it operates; it only manages foodservice distribution if the hotel owner requests or requires it. *Id.* at 199:24-200:4; 250:9-11. Mr. Thompson explained that Interstate-managed hotels that do not use Interstate to manage foodservice distribution, "have a choice. Some ownership groups work with different companies . . . like Avendra," a hospitality GPO, and others, like Hilton-branded hotels, offer their own procurement programs. *Id.* at 200:16-201:4.

106. For properties where Interstate manages foodservice distribution, the distribution model is complex—as Mr. Thompson explained, "we're doing a little bit of everything." Thompson (Interstate), Hearing Tr. at 204:9. Interstate contracts directly with manufacturers for a variety of goods, from bottled water to meats; managing approximately 50 to 60 separate contracts. *Id.* at 203:23-204:20. Interstate is also a member Foodbuy/Compass, a GPO, that permits them to purchase at GPO-negotiated prices. *Id.* at 204:4-6. Although Compass is capable of managing distribution, Interstate prefers to manage its own contracts. *Id.* at 206:10-14. For some products "that aren't met by the previous two options," Interstate purchases from either USF or PFG, its two broadline distributors. *Id.* at 204:7-8, 205:2-3. Interstate also uses multiple specialty distributors and "run[s] a pretty significant regional produce program." *Id.* at 217:2-3; 251:9-252:25. Despite this complex operation, Interstate only employs two individuals to manage foodservice distribution. *Id.* at 203:7-17.

107. Mr. Thompson acknowledged that USF competes fiercely with specialty distributors for this business, and that Interstate's spend with specialty distributors represented lost revenue to USF. Thompson (Interstate), Hearing Tr. at 251:14-16 ("Q: And US Foods would like [to] sell produce to your hotels; right? A: They would love to sell produce to my hotels."); *id.* at 252:3-5

("Q: And US Foods would like all of your meat business, wouldn't they? A: They work hard to get all of our meat business. . . . US Foods competes with specialty retailers in an effort to get all of your meat business; right? A: That's correct."); *id.* at 232:15-17 ("Q: Do they compete with your specialty seafood distributors to get the seafood business of your hotels? A: I would say that they do."). Mr. Thompson further explained that Interstate tries to purchase as much product as it can through its direct contracts with manufacturers because Interstate "feel[s] that's the best option." *Id.* at 212:23-213:3. If Interstate were to switch distributors, it would work with the new distributor to ensure that those contracts would be transferred, and that it would continue to negotiate directly from manufacturers for many of its products. *Id.* at 275:3-18.

108. For those purchases not made from manufacturers, Compass, or specialty distributors, it is Interstate's "preference" to use a broadline distributor. Thompson (Interstate), Hearing Tr. at 214:11-12 ("Q: Is it fair to say that Interstate needs a broadliner? A: That would be our preference, yes[.]").

109. Mr. Thompson also explained that product consistency was driven by contracting directly with manufacturers, and that USF was not integral in maintaining product consistency across locations. Interstate manages a wide range of hotels, with different foodservice distribution needs, Thompson (Interstate), Hearing Tr. at 253:9-21, across a number of different hotel brands, including Hilton, Marriot, and Hyatt. *Id.* at 253:23-25. Although each of those hotel brands have different requirements, Mr. Thompson explained that a variety of distributors could easily satisfy them. *Id.* at 254:7-9. Indeed, Mr. Thompson clarified that there is "[n]o way" that all product offerings across his hotels were consistent, and that there was only "a limited number" of products that were used across the whole Interstate system. *Id.* at 274:11-16. With respect to private-label products, Interstate does not purchase any unique goods that it could not get

elsewhere. *Id.* at 276:11-14.

110. Mr. Thompson's knowledge of the industry and the options available to Interstate was limited and dated. Mr. Thompson acknowledged that he became vice-president of procurement in 2004 or 2005 and that he did not work in foodservice distribution prior to that date. Thompson (Interstate), Hearing Tr. at 253:13-20. In fact, Mr. Thompson was not vice-president of procurement and was "not involved in" the RFP that took place nine years ago. [redacted] *Id.* at 255:16-25; [redacted] In fact, Mr. Thompson's limited knowledge regarding this RFP was so egregious that the FTC objected to any questioning about the process on the basis of lack of foundation. [redacted] Thompson (Interstate), Hearing Tr. at 260:7-9 ("Mr. Weissman: Objection, Your Honor. This lacks foundation. He said this is 2003. He didn't take on his position until 2006.").

111. Interstate has not issued an RFP in "approximately nine years," Thompson (Interstate), Hearing Tr. at 226:14, during the course of which Interstate reviewed three companies, Avendra (a hospitality GPO), Sysco, and USF. *Id.* at 256:9-11. Avendra actually offered the lowest-priced bid and, at $3.5 million less than the next lowest bid inclusive of distribution costs, *id.* at 259:14-16, 260:24-261:1, was recommended as the best option, *id.* at 259:14-22. Despite the fact that USF was the third rated option, Interstate elected to stay with USF for reasons unknown to Mr. Thompson. *Id.* at 256:14-24; 262:19-24; 263:4-11.

112. Interstate does not play Sysco and USF off of each other to obtain more favorable pricing. Interstate has not evaluated Sysco's options in "[a]pproximately five years." Thompson (Interstate), Hearing Tr. at 225:22-226:1. When renegotiating Interstate's contract with USF five years ago, Mr. Thompson did not receive a price proposal from Sysco or any other company, *id.*

at 265:3-7, never made any reference to prices offered by other distributors, *id.* at 266:11-16, and never threatened to move his business elsewhere to receive better pricing, *id.* at 267:14-25. *See also id.* at 268:11-14 ("Q: And to achieve those favorable results, you didn't rely on any proposal from Sysco or anyone else to get leverage on better rates with US Foods; correct? A: That's correct."). In fact, Mr. Thompson testified that he was not able to compare the prices he received from USF against other pricing in the market. He testified that he could "get a feel for what the distribution costs" are when Interstate acquired another hotel, but that "there's so much stuff that goes on in the background, [that he] would never really know which one is better than the other." *Id.* at 238:19-23.

113. Interstate also has not investigated PFG as a comprehensive distribution option since a meeting held "several years ago," Thompson (Interstate), Hearing Tr. at 225:5-8; *id.* at 246:11-12 ("I'm speaking not knowing all the facts here."), although Mr. Thompson was aware that the pricing PFG currently offers is competitive with USF pricing, *id.* at 273:4-6, and is satisfied with PFG's current service, *id.* at 276:18-20. Mr. Thompson explained that the basis of his knowledge of post-divestiture PFG was that he was asked by the FTC to compare PFG's post-divestiture geographic reach, and that he spent only an hour comparing the USF distribution map with PFG's. *Id.* at 241:22-242:25. Mr. Thompson was unaware of PFG's expansion plans or its service levels in various areas. *Id.* at 280:15-281:9.

114. Nor has Interstate evaluated other options like DMA, Thompson (Interstate), Hearing Tr. at 269:24-270:3, Gordon, *id.* at 282:4-5, Reinhart, *id.* at 282:6-7, Shamrock, *id.* at 282:11-13, MUG, *id.* at 282:14-16, systems distributors, *id.* at 283:1-3, or any other GPO since the RFP nine years ago, *id.* at 282:22-25.

115. Similarly, Interstate has never analyzed contracting regionally because it "would prefer to

work with one distributor." Thompson (Interstate), Hearing Tr. at 222:6-14; *id.* at 247:25 (contracting regionally "is not my preference"). Mr. Thompson explained that he has never evaluated whether managing multiple distributors would require additional staffing, or whether contracting regionally could be cheap enough to offset any additional staff costs, *id.* at 269:15-23, although Interstate currently manages two broadline distributors and 50 to 60 contracts with manufacturers.

116. Despite his current preference for USF, Mr. Thompson agreed that Interstate "most definitely would" evaluate alternative distributors if the merged entity raised prices. Thompson (Interstate), Hearing Tr. at 283:7-11. Specifically, he testified that Interstate would consider regional distribution, *id.* at 283:12-14, PFG, *id.* at 281:10-13, 283:15-17, and DMA, *id.* at 271:16-19 ("I have to look at the option. I can't say no to anything."); *id.* at 281:14-18.

117. Although Thompson testified that he believed that competition between Sysco and USF had kept prices down, he admitted that "[i]t absolutely is an assumption," that Sysco and USF have never competed for his business, and that he has no personal knowledge of competition between Sysco and USF leading to lower prices. Thompson (Interstate), Hearing Tr. at 283:20-284:6.

C. PHILLIP KEISER (CULVER'S)

118. The Defendants played a clip of deposition testimony by Phillip Keiser at the hearing, to illustrate customer switching from Sysco or USF to another broadline distributor.

119. Phillip Keiser is the president and chief operating officer of Culver Franchising System, Inc. ("Culver's"), a quick service restaurant chain with over 500 locations. Keiser (Culver's) Dep. 8:21-22, 9:2-5, 12:17-12:22, 13:8-11. Mr. Keiser has been with Culver's for almost 20 years. *Id.* at 9:6-7.

120. Culver's currently uses Gordon in collaboration with Services Group of America ("SGA") as its food service distributors. Keiser (Culver's) Dep. 16:19-23. Prior to 2004, Culver's used Sysco as its food service distributor. *Id.* at 17:7-19. In 2004, Culver's transitioned a portion of its business to Gordon, in part, due to Gordon's better ability to service certain of Culver's restaurants in the Midwest, and, in part, as a strategic plan to split up Culver's business among more than one food distributor. *Id.* at 33:3-34:15.

121. In 2013, Culver's put out an RFP for its food service business beginning in June 2014. Keiser (Culver's) Dep. 37:14-18. In response to the RFP, Sysco, and Gordon, in combination with SGA, submitted bids. *Id.* at 80:10-18. [redacted] Culver's spoke with US Foods about participating in the RFP but US Foods did not submit a bid. *Id.* at 80:14-18, 141:10-13. Ultimately, Culver's awarded the business to Gordon. *Id.* at 87:12-13.

122. Mr. Keiser has no concerns that the merger of Sysco and US Foods will hinder Culver's business or limit Culver's food services distribution options. Keiser (Culver's) Dep. 94:4-13.

D. ROBERT BAKER (IPC)

123. Robert Baker is the Director of Distribution at Independent Purchasing Cooperative ("IPC"), a franchisee-owned purchasing cooperative for Subway restaurants. Baker (IPC) Dep. 7:22-8:1; 10:9-21. Mr. Baker has been in the food service distribution industry for over forty years, including twenty-eight years working with Martin Brower Company, the food distribution company for McDonald's, and eight years at IPC. *Id.* at 8:5-20.

124. IPC employs a regionalized distribution strategy and "manage[s its] network" of Subway restaurants across the United States by dividing the country into eight regions. Baker (IPC) Dep. 14:3-14; 30:2-4. Each region is "managed by an employee who lives in th[at] zone." *Id.* at 14:11-12. In 2010, IPC sourced its food distribution from fifty-eight different distribution

centers across its eight different regions. *Id.* at 14:15-18; [redacted] Since then, "Subway has grown rather rapidly over the years," Baker (IPC), Dep. 14:23-25, adding over 4,000 restaurants in the last five years alone. *Id.* at 30:9-12. By 2015, IPC's number of distribution centers had grown to sixty-four. [redacted] *see also* Baker (IPC), Dep. 30:5-12. Mr. Baker explained that "each of [IPC's] distributors is contracted to perform business within a geographic territory" and each contract "includes responsibility for [the distributor] to perform … service[s] for any restaurant that would open up within that same geographic territory through the course of the contract." Baker (IPC) Dep. 16:16-17:4.

125. IPC maintains individual contracts for each distribution center. Mr. Baker explained that this arrangement "allows for some flexibility" and "allows for pricing variation." Baker (IPC) Dep. 17:18-18:5. This means that, for example, in 2010 when IPC worked with eleven different Reinhart distribution centers, IPC had eleven different contracts with Reinhart, each possibly with different prices, at the time. *Id.* at 18:5-15.

126. In 2010, IPC worked with twenty-two different food service distributors. Baker (IPC) Dep.19:3-15. Reinhart is currently IPC's largest distributor in terms of the number of Subways serviced. *Id.* at 30:13-16. After Reinhart, PFG and Sysco are IPC's third and fourth largest distributors, respectively. *Id.* at 30:13-22.

127. Despite the number of food service distributors that IPC uses, IPC is able to maintain product consistency because "distributors do not impact product consistency other than through their handling." Baker (IPC) Dep. 24:25-25:1. As Mr. Baker explained, distributors cannot "impact the formula or the specifications of the product," which are dictated by IPC to the suppliers with whom they contract. *Id.* at 25:1-15.

128. IPC relies on a third-party data management company, iTrade, to compile and organize the invoice, purchasing, and service performance metrics data from its 58 distribution centers and 22 distributors. Baker (IPC) Dep. 28:11-29:18. Each distributor is required to provide information to iTrade, which then compiles that information into one "reporting structure" that IPC can "use . . . across the country." *Id* at 29:2-6; *see also id.* at 151:12-14 ("We use iTrade to roll up invoice information from across our system, and present it to us in a consistent format."). iTrade allows IPC to view one set of uniform reports and performance metrics across all of IPC's distribution centers. *Id.* at 29:12-18.

129. IPC renews contracts with incumbent distributors "90-plus percent of the time" rather than entering a RFP processes. Baker (IPC) Dep. 43:8-12. IPC has relationships across the country—"[e]very zip code is covered"—and IPC "look[s] to these relationships as ones that will last." *Id.* at 42:12-14. For that reason, IPC "do[esn't] perform an RFP every single time a contract is up for renewal." *Id.* at 42:14-16. Instead, about six months before a contract is due for renewal, IPC will go to the incumbent to assure themselves that the service is adequate and the relationship is satisfactory. *Id.* at 42:17-22. If that is the case, IPC will enter into bilateral negotiations with the incumbent on renewed pricing. *Id.* at 42:22-43:4.

130. Mr. Baker described the Jacksonville, Florida RFP—which Cheney Brothers won—in some detail. In the Jacksonville RFP, IPC invited the incumbent, Reinhart, Sysco, Merchants Food Service, and Cheney Brothers to bid. Baker (IPC) Dep .49:12-17. US Foods was invited but declined due to a lack of capacity. *Id.* In the invitation letters, each distributor was asked to determine a distribution fee based on detailed restaurant information, a territory map, information about incentives, and buying metrics that IPC provided. *Id.* at 49:18-50:15; [redacted] When asked to rank the bids based on financial

information, Mr. Baker provided the following list: "Merchants, No. 1; Cheney, No. 2; Sysco, No. 3; Reinhart, No. 4." Baker (IPC) Dep. 62:23-63:2. Ultimately, IPC choose Cheney Brothers to win the Jacksonville, Florida RFP. Cheney Brothers, a former "distributor of the year," was a "current partner" of IPC's "down in South Florida, so [IPC] had a lot of familiarity with them." *Id.* at 63:9-12. Cheney Brothers "offered [IPC] the best combination of service, stability and price," so IPC recommended that Subway franchisees select Cheney Brothers. *Id.* at 63:21-25. They did. *Id.* at 70:21-23.

131. When the Sysco-USF merger was announced, IPC performed a contingency plan to ensure that each region was covered "in the event [IPC] los[t] or f[ell] out of favor in a [distributor] relationship somewhere across the country." Baker (IPC) Dep. 80:5-17. IPC was satisfied that it was covered nationwide. *Id.* at 81:6-10 ("[W]e tried to identify two distributors, obviously with the caveat that Sysco couldn't back up US Foods, and vice versa, and we were successful in doing that."). Prior to the merger, it was common for Sysco to back-up a US Foods and vice versa. IPC wanted to "reidentify candidates" post-merger "that could potentially take on [IPC's] business in every market" in case there were issues with the merged company. *Id.* at 80:13-25; 82:7-11. In addition to finding sufficient back-ups post-merger, IPC also identified a number of potential distributors with whom they were previously unfamiliar. *Id.* at 87:5-88:15. Mr. Baker disclosed that IPC was "excited" about the "many companies that were interested [in IPC's business] and were capable" of handling IPC's account. *Id.* In all, IPC identified "39 new non-Subway companies in the U.S." *Id.* at 93:5-94:6; [redacted]

132. Mr. Baker stated that IPC has "no reason to object" to Sysco and US Foods merging. Baker (IPC) Dep. at 81:18-21. In fact, IPC is interested in the "potential for efficiencies that

would come in a merged company." *Id.* at 81:24-82:2. [redacted] When asked what IPC would do if a merged Sysco and US Foods came to them with a five percent across-the-board increase, Mr. Baker said his reaction would be to "say no." Baker (IPC) Dep. at 112:9-12. If the merged company did not lower the price, IPC would simply "go to RFP." *Id.* at 113:4-6.

III. "LOCAL CUSTOMER" WITNESSES

A. DAN SCHABLEIN (WINTERGREEN RESORTS)

133. Dan Schablein was called by the FTC to bolster its claim that "National Customers" require Sysco or USF. Mr. Schablein's testimony did not support that assertion.

134. Dan Schablein is the controller for Wintergreen Resort, a four-seasons resort located in the Blue Ridge Mountains in Virginia. Schablein (Wintergreen Resort), Hearing Tr. at 525:7-8; 525:24-526:4. Wintergreen operates four restaurants that are open year-round, three seasonal restaurants, and a convenience store. *Id.* at 526:10-20; 527:10-18.

135. Wintergreen currently uses Sysco as its primary broadline distributor. Schablein (Wintergreen Resort), Hearing Tr. at 527:19-25. Wintergreen's most recent contract with Sysco began in late 2011, *id.* at 538:17-19, and expired in late 2014. *Id.* at 543:24. However, terms of this contract were replaced in practice, when Wintergreen was acquired by James Justice, who also owns Greenbrier Resort, which had a contract with Sysco. *Id.* at 547:13-548:8. Greenbrier's terms remain in place today, although Mr. Schablein failed to disclose this fact in his declaration. *Id.* at 548:6-12.

136. In addition to Sysco, Wintergreen purchases food from multiple specialty distributors as well as local farms. Schablein (Wintergreen Resort), Hearing Tr. at 529:18-530:1; Schablein

[redacted] Its purchases from specialty providers account for 20-25% of Wintergreen's total foodservice spend. Schablein (Wintergreen), Hearing Tr. at 532:5-7. For certain products, Wintergreen believes that specialty distributors are the "best route to go" and are "much better to serve [Wintergreen's] customers" than broadline distributors. *Id.* at 530:6-7. For example, Wintergreen purchases produce from specialty distributors Standard Produce and Cavalier produce, even though Wintergreen could purchase its produce from Sysco, because Wintergreen prefers to use local providers. *Id.* at 553:6-14. Similarly, Wintergreen currently purchases fresh seafood from Steve Connolly and Sam Rust rather than Sysco. *Id.* at 554:5-7.

137. Mr. Schablein's testimony showed he is not involved in and has no knowledge of Wintergreen's food purchasing decisions. For example, Mr. Schablein admitted that he does not "pretend to be a food expert," is not involved in deciding what kind of food products to buy, Schablein (Wintergreen Resort), Hearing Tr. at 530:17-21, and that the Wintergreen employees who are responsible for determining where to buy products do not discuss their decisions with Mr. Schablein or report their decisions to him. *Id.* Mr. Schablein does not review the product selections of *any* distributors, including those of US Foods and Sysco. *Id.* at 546:6-10. He is not familiar with the quality of the products available through Sysco, *id.* at 546:11-13, does not have regular contact with Wintergreen's Sysco representative, and does not even know his representative's name. *Id.* at 547:5-9.

138. Mr. Schablein's testimony that Wintergreen has no alternatives to US Foods and Sysco lacks credibility because Mr. Schablein has done no work to identify or investigate alternative distribution options. For example, he has failed to look into the prices, distribution capabilities, and ordering processes of Pate Dawson, Reinhart, H.T. Hackney, or Dan Valley Foods. Schablein (Wintergreen Resort), Hearing Tr. at 549:7-551:6 ("Q. In fact, you don't review

product selections al all; right? A. Yes, that's not my job."); [redacted]. Moreover, he has not been involved in looking for alternative broadliners to Sysco or US Foods. Schablein (Wintergreen), Hearing Tr. at 549:4-6.

139. [redacted]—one of which took place over fifteen years ago, Schablein (Wintergreen Resort), Hearing Tr. at 551:13-15—and neither of which were attended by Mr. Schablein. *Id.* at 551:11-12. Mr. Schablein acknowledged that Wintergreen had received a bid from PFG, but claimed that PFG's offer was not competitive. *Id.* at 551:16-19. However, Mr. Schablein conceded that he did not know in what way PFG's offer was not competitive, since he was not involved in negotiations with PFG, and never saw PFG's bid. *Id.* at 551:19-552:3; [redacted] Mr. Schablein did not know if Wintergreen asked PFG to meet Sysco's or US Foods' bid. Schablein (Wintergreen), Hearing Tr. at 552:2-4. Mr. Schablein is not aware of any products Wintergreen has purchased from Sysco that PFG could not provide at the same price. *Id.* at 552:15-17; [redacted].

140. Mr. Schablein could not point to any direct evidence of price competition between Sysco and US Foods because Wintergreen's policy is not to ask US Foods or Sysco to meet each-others' bids. Schablein (Wintergreen Resort), Hearing Tr. at 555:19-23.

B. GARY HOFFMAN (UPSTREAM BREWING CO.)

141. Gary Hoffman was called by the FTC in support of the claim that there are "local" customers that require Sysco or USF. His testimony did not support that assertion.

142. Gary Hoffman is the corporate executive chef and the managing partner of Upstream Brewing Company LLC ("Upstream"), Hoffman (Upstream), Hearing Tr. at 323:5-13, which has

two restaurants in the Omaha area serving a wide variety of items, such as steaks, seafood, and salads, *id.* at 323:16-25, 325:15-20. . Since 1999, Hoffman has been in charge of purchasing Upstream's food products and selecting its foodservice distributors. *Id.* at 324:10-20. Upstream spends approximately $3 million on food annually, making it the second largest purchaser of food products in "most of Eastern Nebraska." *Id.* at 7:24-8:1, 19:10-11. *Id.* at 325:24-326:1, 337:10-11. Of Upstream's "$3 million in purchases [Upstream] spend[s] about 50 percent with specialty [distributors] and 50 percent with US Foods." *Id.* at 346:25-347:3. [redacted]

143. Mr. Hoffman chooses to use specialty distributors for many products that Upstream could buy, and sometimes does buy, from US Foods. For instance, Upstream purchases steaks from Omaha Steaks, from farmers, and also from US Foods. Hoffman (Upstream), Hearing Tr. at 356:1-7. The "bulk of [Upstream's] produce orders swings back and forth between US Foods and Loffredo," *id.* at 361:17-19, Upstream's "principal specialty produce distributor," *id.* at 358:1-3, as well as local farmers, *id.* at 357:24-25. US Foods offers seafood, *id.* at 359:18-24, but Upstream purchases seafood from Connolly Seafood, Ocean Beauty, and Jacobson Fish, *id.* at 356:21-357:13. US Foods offers chicken, *id.* at 358:24-25, but Upstream purchases some chicken from boutique farmers, *id.* at 358:21-23. US Foods offers coffees and teas, *id.* at 358:12-17, but Upstream purchases coffee from Hill of Beans, *id.* at 358:14-15, and tea from LaRue, *id.* at 358:12-13. Upstream purchases pastries from vendors in New York and San Francisco, *id.* at 358:4-11, and other products from Olafsson, 358:18-20, and Omega Chemical, *id.* at 359:1-2, some of which are also available from US Foods, *id.* at 359:6-17.

144. The specialty distributors and US Foods compete vigorously on price and quality for

Upstream's business. Mr. Hoffman has "had discussions with [his US Foods sales representative] Ms. Pete about her trying to sell [Upstream] more steaks than [Upstream] currently purchases from [US Foods]," Hoffman (Upstream), Hearing Tr. at 356:13-26, and Mr. Hoffman has told Ms. Pete "what price range [US Foods] would need to be in, based on the prices [Upstream is] getting from Omaha Steaks," *id.* at 356:17-20.

145. Mr. Hoffman believes that "for seafood there are certain products where [Upstream] can get better pricing from the specialty distributors than [Upstream] can from US Foods." Hoffman (Upstream), Hearing Tr. at 361:1-6. For instance, for Copper River Run salmon, Mr. Hoffman's "first concern" is that Upstream "would probably get better pricing going straight to [specialty distributors] than [Upstream would] through US Foods." *Id.* at 368:7-23. He therefore chooses to purchases salmon from Ocean Beauty for reasons of "cost efficein[cy] and quality." *Id.* at 361:7-9. Similarly, Mr. Hoffman chooses to purchase seafood from Connolly "to get the best quality product at the best price." *Id.* at 328:14-17. Mr. Hoffman has "had discussions with Ms. Pete about purchasing more of [Upstream's] seafood from . . . US Foods rather than Connolly and Ocean Beauty," *id.* at 360:18-21, and has generally told Ms. Pete the price ranges that Upstream receives from its specialty distributors, *id.* at 360:22-25.

146. For produce, Mr. Hoffman compares prices from Loffredo and US Foods "weekly," Hoffman (Upstream), Hearing Tr. at 361:10-12, and has told Ms. Pete "on occasion that US Foods['] prices are higher for some items than some of the prices [Upstream] can get from Loffredo," *id.* at 361:13-16. "[I]n determining whether to buy from Loffredo or US Foods, [Mr. Hoffman] watch[es] the market and the prices that [Upstream] is offered." *Id.* at 361:20-23. If Sysco were to raise prices following the merger, and Loffredo had product available, Mr. Hoffman would consider Loffredo "an option to purchase more of [Upstream's] produce needs."

Id. at 362:5-20.

147. Many of the products purchased by Upstream are delivered from well outside the Omaha area. For instance, Connolly Seafood (which is in Boston) and Ocean Beauty deliver to Upstream by air freight. Hoffman (Upstream), Hearing Tr. at 330:12-13, 357:3-8.

148. When Mr. Hoffman first brought Upstream's business to US Foods, from FSA, US Foods did not carry all of the products for which Upstream had manufacturer contracts. Hoffman (Upstream), Hearing Tr. at 334:7-12; 345:10-18. Ms. Pete, who had been Mr. Hoffman's sales representative at FSA, left to join US Foods, *id.* at 344:19-345:5, and "in order to keep [Upstream] as a customer . . . when she moved from one company to another" she and US Foods came to an agreement with the manufacturers "to carry those products that [Upstream] had under contract with the manufacturer[s]" that US Foods did not previously stock. *Id.* at 345:14-21.

149. Mr. Hoffman's knowledge of the industry and options available to Upstream is limited and dated. In fact, Mr. Hoffman does not even consider Cash-Wa and Reinhart to be broadline distributors. Hoffman (Upstream), Hearing Tr. at 335:8-12; 335:23-336:1. Mr. Hoffman has heard that the FSA facility that used to service Upstream is now operated by Reinhart, *id.* at 345:6-9, but has "not looked at Reinhart since at least 2006 and maybe earlier," *id.* at 352:11-13. Mr. Hoffman also "ha[s]n't looked at Cash-Wa since at least 2006 and possibly earlier." *Id.* at 352:14-16. "[I]t may actually be 2002, the last time [Mr. Hoffman] looked at the product list of either Cash-Wa or Reinhart." *Id.* at 352:17-19. Mr. Hoffman has "no direct current knowledge about the current product offerings" of Cash-Wa or Reinhart. *Id.* at 353:19-354:10.

150. Upstream has not considered Sysco to be an alternative to US Foods for Upstream's business. While one of Upstream's restaurants makes "some very limited purchases from Sysco," Hoffman (Upstream), Hearing Tr. at 355:1-4, the chef at that restaurant "doesn't give

Sysco a lot of orders as a result of the fact that . . . Sysco's service is [not] to his liking," *id.* at 355:12-15. Mr. Hoffman believes that "in [Upstream's] area of Omaha, Sysco couldn't hit a service window [] to save their lives," *id.* at 355:19-22. Sysco has never called on Upstream to pitch its business, *id.* at 350:15-351:10, Mr. Hoffman "ha[s]n't looked at a Sysco product guide since approximately 2006," *id.* at 354:13-15, and has "not spoken to a Sysco sales rep since approximately 2010," *id.* at 354:16-18. "It's been at least eight years since [Upstream] had a request to Sysco to provide [Upstream] a bid." *Id.* at 346:9-11. (Mr. Hoffman admitted that [redacted] *id.* at 346:12-14). In the last eight years, when Upstream's contracts with US Foods have been up for renewal, Hoffman has negotiated only with US Foods; not Sysco. *Id.* at 348:20-349:5.

C. [redacted]

151. [redacted]

152. [redacted]

153. [redacted]

154. [redacted]

155. [redacted]

156. [redacted]

IV. GPO WITNESSES

A. JOAN RALPH (PREMIER)

157. Joan Ralph was called by the FTC in support of its contention that GPOs require a single national broadline distributor. Her testimony did not support that assertion.

158. Ms. Ralph is the vice president of Continuum Care services at Premier, a publicly-traded national group purchasing organization. Ralph (Premier), Hearing Tr. at 371:5-372:2. Premier negotiates contracts for products and distribution on behalf of its members. *Id.* at 418:5-9 ("You don't take possession of goods or services, right? A. No."). Unlike many other GPOs, Premier historically has offered distribution through only one nationwide distributor: USF. *Id.* at 432:18-433:3. Premier receives a percentage of all foodservice purchases that its members make through its contracts, and it receives an "administrative fee" from USF for every delivery USF makes under those contracts. *Id.* at 423:15-424:23. [redacted]

[redacted]

159. Ms. Ralph's testimony shows that under the FTC's definitions in this case, Premier is not a *customer* but rather an intermediary: The GPO itself never possesses the product—it is simply a contracting agent. *Compare* Ralph (Premier), Hearing Tr. at 377:20-23 ("We have no trucks. We have no food. We don't buy and sell food. We are not in that -- that supply chain of the actual movement of the product, nor in the financial supply chain. We do not buy and sell food.") *and id.* at 418:5-9 ("Q: As Your Honor pointed out, you don't actually buy the products, you enter into contracts on behalf of your members? A: We negotiate the contracts for them. Q: You don't take possession of goods or services, right? A: No.") *with* FTC Mem. at 1 (describing "customers" as the "hundreds of thousands of venues across the country where food is served away from home—including restaurants, school cafeterias, hotels, and hospitals"). Premier's members, on the other hand, *are* customers. *See* Ralph Tr. at 379:6 (referring to GPO members as "the end customer"); *id.* at 417:8-24 (listing various Premier members, all of whom serve food to people outside the home).

160. Premier already bids the same contracts that broadline foodservice distributors bid, Ralph (Premier), Hearing Tr. at 113:2-13, [redacted] While Ms. Ralph refused to say explicitly that Premier competes with distributors, she admitted that Premier has won and lost several contracts on which it bid against distributors. Ralph (Premier), Hearing Tr. at 434:24-435:11 ("Q: Dartmouth is not the only college or university that you've lost a bid to PFG, for example, to; is that right?").

161. Ms. Ralph testified that Premier considered moving some of its business to regional distribution, both before and after the Sysco-USF merger was announced. Ralph (Premier),

Hearing Tr. at 398:21-399:4; [redacted]

162. [redacted]

163. Ms. Ralph's testimony demonstrates that if Sysco and USF merge, Premier's prices will not rise. [redacted]

164. Ms. Ralph acknowledged several characteristics that are unique to Premier that make it a poor representative example of customers that require national broadline service. [redacted]

[redacted]

B. DAVID LINDAHL (HPSI)

165. David Lindahl is a managing director of HPSI, a national group purchasing organization ("GPO") that primarily provides food and medical supplies to senior living facilities across the nation. Lindahl (HPSI), Hearing Tr. at 1405:1-11. HPSI has approximately 13,000 members, *id.* at 1403:18-19, 60 percent of which purchase food and foodservice distribution through HPSI. *Id.* at 1404:18-21. HPSI is a family-owned business, founded in 1964, and Mr. Lindahl has been involved in that business for nearly his entire adult life, since 1979. *Id.* at 1403:20-1404:4. In his current position as a managing director, Mr. Lindahl oversees all sales and contract management, *id.* at 1403:5-6, which includes reviewing and approving—in conjunction with HPSI's in-house counsel—all of HPSI's foodservice distribution contracts. *Id.* at 1425:9-25.

166. HPSI uses multiple distributors, awarding contracts state-by-state, Lindahl (HPSI), Hearing Tr. at 1406:24-99:3, and contracting for at least two distributors in each geographical area, *see* DX-01454, to provide choice to HPSI members. Lindahl (HPSI), Hearing Tr. at 1415:11-1416:1. HPSI contracts with leading regional distributors in the geographies in which those distributors are dominant. For example, FSA, with which HPSI contracts, "is a strong competitor in the Northwest United States." *Id.* at 1407:13-14. Gordon Foodservice ("GFS") is

a "strong food distributor" in Michigan and surrounding areas. *Id.* at 1480:23-25. Martin Brothers is "a very strong regional broadline food distributor in the state of Iowa." *Id.* at 1408:11-12. Shamrock is a "big player in Arizona as far a healthcare is concerned." *Id.* at 1409:16-19. And Newport Farms, a smaller distributor in Southern California, "pretty much own[s] the market out there with the smaller nursing homes." *Id.* at 1417:23-24.

167. HPSI's territory awards are not fixed, and HPSI has grown its relationships with regional distributors who in turn helped HPSI grow its business. Lindahl (HPSI), Hearing Tr. at 1406:4-6. For example, HPSI has grown its relationship with FSA over time, expanding into several other states beyond Washington where the company is headquartered. *Id.* at 1406:7-12. GFS is another example of a distributor with which HPSI has expanded its territory award over time. *Id.* at 1408:1-6. HPSI currently contracts with 9 broadline foodservice distributors: Sysco, US Foods, GFS, Martin Brothers, Feesers, PFG, HFM, Newport Farms, and Shamrock. *Id.* at 1409:10-14, 1416:24-1417:3.

168. Within this multiple distributor model, HPSI stays "distributor neutral"—that is, HPSI will allow distributors within its network to compete for member business currently being serviced by other distributors within HPSI's network. Lindahl (HPSI), Hearing Tr. at 1411:10-23. This practice creates competition among distributors for HPSI member business, which ultimately benefits HPSI customers. *Id.* at 1416:2-7. Distributors within the HPSI network compete on multiple fronts: price, *id.* at 1412:17-18, service levels, *id.* at 1414:1-2, and value-added offerings such as healthcare expertise, *id.* at 1414:3-5. Shamrock, for example, was chosen to become an HPSI distributor in part because of its healthcare expertise. As Mr. Lindahl recalled, "we had some meetings [with Shamrock] and came to find out that where Sysco has

one or two healthcare experts in their OpCo there in Arizona and US Foods has six, these guys [Shamrock] have eight people, salespeople just dedicated to healthcare . . . ." *Id.* at 1410:1-4.

169. Distributors other than US Foods and Sysco have a considerable sales presence among HPSI's members. [redacted] These rankings generally hold true for HPSI's entire membership (not just the top members reflected in DX-01458). Lindahl (HPSI), Hearing Tr. at 1424:20-25.

170. Mr. Lindahl further testified that HPSI contracts with specialty distributors to provide its members products like produce, janitorial supplies, and meat. Lindahl (HPSI), Hearing Tr. at 1414:8-13. With respect to janitorial supplies, Mr. Lindahl testified that specialty janitorial providers are frequently preferred by members over identical offerings from broadliners since "it's one thing to buy the chemicals to clean the floor; it's another thing to know how to use the chemicals on the floor, and [specialty distributors] provide more training and that type of stuff with the janitorial products than a broadline food distributor." *Id.* at 1414:23-1415:2.

171. Further competition is seen by the fact that HPSI members are not required to obtain their distribution services through HPSI. Members can purchase directly through distributors and even other GPOs. Lindahl (HPSI), Hearing Tr. at 1413:9-19.

172. HPSI has contracts with all of the distributors it uses, and when these contracts near their expiration, HPSI typically engages in bilateral renegotiation with the distributors individually. Lindahl (HPSI), Hearing Tr. at 1419:20-1420:7.

173. HPSI is not concerned that the merger between Sysco and US Foods will result in a price increase to its members. As Mr. Lindahl explained, "if there was a large price increase, our customers would go elsewhere. . . . They live and breathe by their budgets, and if pricing started going through the roof, they'd go somewhere else." Lindahl (HPSI), Hearing Tr. at 1420:18-21. Mr. Lindahl further explained that HPSI would "look for another regional" if necessary to provide suitable alternative distributors if prices from the merged entity increased. *Id.* at 1422:1-2. If a post-merger Sysco increased prices by 5% without adequate justification, HPSI would react by "let[ting] our customers know that they're going to get a pretty good price increase and a lot of them would probably start looking at other options." *Id.* at 1422:23-25. HPSI would further assist its customers in looking at those other options. *Id.* at 1423:1-3.

174. As for HPSI's geographical coverage by distributors post-merger, Mr. Lindahl testified that HPSI reviewed the proposed divestiture and "felt that it would work well for us." Lindahl (HPSI), Hearing Tr. at 1420:16-18. Mr. Lindahl anticipates that HPSI would add PFG as a distributor to the states where a US Foods divestiture is scheduled to occur. *Id.* at 1420:13-1421:1. Mr. Lindahl is not concerned about the level of service PFG would provide since, "any time you acquire a business, they're not going to want to lose those customers, so we think that the service levels might even step up." *Id.* at 1421:6-9. In addition, Mr. Lindahl testified that PFG would be price competitive since, "[w]e see them competitive where we use them now." *Id.* at 1421:10-13. Moreover, Mr. Lindahl agrees that "taking into account the PFG

divestitures, [HPSI] would have options throughout the United States for [its] members in the event of a merger." *Id.* at 1422:3-6.

V. COMPETITOR WITNESS

A. GEORGE HOLM (PFG)

175. George Holm was called by the FTC in support of its contention that PFG would not offer adequate competition to the merged Sysco-US Foods entity. Mr. Holm's testimony did not support that assertion.

176. Mr. Holm is the President and CEO of PFG. Holm (PFG), Hearing Tr. at 562:6-11. [redacted]

177. [redacted] PFG also serves several customers who changed from systems distribution to broadline distribution. Holm (PFG), Hearing Tr. at 574:21-23 ("We have secured business in our broadline that was in a [systems] environment fairly recently, and I would think that pricing did have something to do with that."); *id.* at 575:19-20 ("We have had customers change from a systems environment of a competitor to a broadline.").

178. [redacted]

[redacted]

179. [redacted]

[redacted]

180. [redacted]

181. [redacted]

182. [redacted]

[redacted]

183. [redacted] Trucks with an "LTL load or less-than-truckload" have a "significantly higher price" than full truckloads for the inbound costs (*i.e.*, the cost per case is higher for less-than-truckload quantities). Holm (PFG), Hearing Tr. at 851:2-12; *see also* DX-06106 (trial demonstrative). [redacted] even if the trucks have to "drive more miles" from a distribution center to the customer, *id.* at 851:14-21. [redacted]

184. [redacted]

[redacted] Although PFG has 11 broadline distribution centers in that area, because it is "more favorable economics for Zaxby's," PFG has "consolidate[d] that volume into five distribution centers as opposed to 11 distribution centers." Holm (PFG), Hearing Tr. at 852:5-17. This has led to increased savings on inbound freight. *Id.*

185. At the hearing, Mr. Holm also described how, through shuttling, PFG is currently able to serve more locations from further away and thus optimize its number of distribution centers. [redacted]

186. [redacted]

[redacted]

187. The divestiture package ensures not only that PFG is ready to compete at any level but also that it will be able to compete immediately. [redacted]

188. Mr. Holm was emphatic that PFG would be a cost-competitive option for so-called "National Customers," which he defined as specific customers with a national footprint that generally prefer a single distributor; specifically the "eight large ones": Compass, Aramark, Sodexo, Premier, Novation, Avendra, Hilton, and Starwood. Holm (PFG), Hearing Tr. at 828:12-829:23. He clarified that he was referring to the business of those eight customers when he signed the FTC's declaration. *Id.*

189. [redacted]

190. [redacted]

191. [redacted]

192. [redacted]

[redacted]

VI. **EXPERT WITNESSES**

A. **MARK ISRAEL (FTC)**

193. Dr. Mark Israel, an economist, testified on behalf of the FTC about a range of subjects. Dr. Israel was the only FTC witness who offered testimony from which the Court could possibly calculate market shares or gauge the relevant presumptions of harm based on HHI. His testimony and analysis were not credible.

194. Dr. Israel did not endorse the product markets advanced by the FTC. The FTC alleged that broadline distribution services sold to "National Customers" and broadline distribution service sold to "Local Customers" are distinct product markets because the services sold to those two sets of customers are unique. DX-00158, Compl. ¶¶ 41-44. In other words, the FTC alleged that although the sellers are the same (broadline distributors), different types of customers were buying different products with different attributes.

195. Dr. Israel concluded, however, that broadline distribution services to *all* customers was the relevant product market, a position at odds with the FTC's case. According to Dr. Israel, "National" and "Local" customers are "targeted customers" under § 3 of the Merger Guidelines. Israel, Hearing Tr. at 910:16-911:17. [redacted] And, according to the FTC's own complaint, the distinct bundle of goods and services that constitute broadline distribution sold to "National Customers" is not the "same or similar" product as the distinct bundle of goods and services that constitute broadline distribution sold to "Local Customers." DX-00158, Compl. ¶¶ 41-44. More

fundamentally, even within the "National Customer" grouping, customers purchase highly differentiated products, so it would be impossible to attribute price differentials to discrimination rather than to varying product characteristics. *See* Israel, Hearing Tr. at 1146:20-1152:15; *see also* Bresnahan, Hearing Tr. at 2147:15 (explaining that "National Customers" purchase "different products").

196. Dr. Israel also treats "National Customers" as a group vulnerable to price discrimination without ever making the necessary showing that there are "general, objective criteria by which buyers with relatively inelastic demand for the services of the merged firm can be identified." *In re R.R. Donnelley & Sons Co.*, 120 F.T.C. 36, 141 (1995); [redacted] Dr. Israel never testified or explained that "National Customers" as a group were treated or priced differently, other than the fact that they were labeled as "national" by the parties. In fact, Dr. Israel predicated his analysis on the fact that that *all* customers' prices were "individually negotiated"—not that "National Customers" as a group were treated similarly. *See* Israel, Hearing Tr. at 912:9-17. [redacted] As Dr. Hausman explained, it "would be an all-time first" for there to be a price discrimination market where the targeted customers have lower margins "because you target people to charge them more and not to change them less." Hausman, Hearing Tr. at 1969:22-1970:17.

197. Dr. Israel performed no economic analysis to justify separating "National" from "Local"

Customers. Israel, Hearing Tr. at 922:23-923:25 ("THE COURT: So just so I'm clear in my head, you didn't have, for example, a long list of customers, and you personally did not put one in one bucket and put the other in the other. Whatever the customers themselves self-identified for each category, however they labeled it and whatever the rationale was for the labeling, that's what you followed? THE WITNESS: Yes."). Instead, he "strictly followed the parties' segregations"—here, the parties' administrative customer lists—in determining which customers were "National" and which customers were "Local." *Id.* at 923:2. Dr. Israel's reliance on these lists fails to meet the requirements of the Merger Guidelines and belies the FTC's promise of an economic foundation. *Compare* Hearing Tr. at 24:18-24 ("And what we're saying here is there's a targeted group of customers, the national customers, under the merger guidelines test, and Dr. Israel's going to lay that all out for you. THE COURT: And you would then supply a SSNIP to the national customer group -- MR. WEISSMAN: Exactly.") *with* Israel, Hearing Tr. at 1155:18-1156:7 ("Q: And you didn't do a SSNIP test, so -- you didn't take a list of names, pour it into a computer that does a SSNIP, and out comes something different, other than the names the companies gave you; isn't that a fact? . . . . A: That's a -- I took the list for purposes of my targeted grouping, yes.").

198. [redacted] He simply cribbed the "national" distinction from the parties' administrative lists despite his belief that "business documents [are] relatively uninformative on the specifics of antitrust market definition, because they are almost never written with that in mind." *Id.* at 1266:3-5. And Dr. Israel failed to determine whether the customers contained on those administrative lists satisfied the characteristics that the FTC

alleged made them an economically distinct segment. *Id.* at 1176:5-14; 1177:6-8.

199. This distinction—between "National" and "Local" customers—affected every facet of his analysis. Israel, Hearing Tr. at 922:12-13 ("It's really going to [a]ffect everything we say from this point forward.").

200. According to Dr. Israel, the "most useful" part of his analysis was his empirical work. Israel, Hearing Tr. at 989:16. That work, however, fails to support the conclusions Dr. Israel puts forward.

201. The Merger Guidelines prescribes what is known as the hypothetical monopolist test, which asks whether a hypothetical monopolist in the candidate market could impose a small but significant non-transitory price increase (a SSNIP)—in practice, a 5% price increase. [redacted] He instead performed an aggregative diversion analysis. As employed by Dr. Israel, aggregative diversion analysis considers whether customers would substitute to alternative broadline distributors if the merged entity raised its prices—*i.e.*, "what percentage of those lost sales would go to other broadliners." Israel, Hearing Tr. at 927:13-928:18. Aggregate diversion analysis involves three steps. The first step is to calculate the threshold (or critical) aggregate diversion ratio: the percentage of switchers that would need to stay within the hypothetical monopolist's' product market for a price increase to be profitable. Here, Dr. Israel's analysis suffers from two errors.

- First, Dr. Israel used the wrong formula. Economists use two separate formulae depending on whether they are evaluating "symmetric" markets with similar suppliers and customers or "asymmetric" markets with differentiated suppliers and customers. *See* Hausman, Hearing Tr. at 1957:23-17; 1964:35. A symmetric market assumes a uniform, across-the-board price increase for all products; an asymmetric market assumes a price increase for one product because such an increase is more likely to be profitable in an asymmetric market with differentiated products. *Id.* at 1959:2-7 ("when you have different types of customers and different types of firms, the hypothetical monopolist might well find it profitable to raise prices on only one product, but since the customers in all are different, it might not find it profitable to raise prices on all products because of heterogeneity"); [redacted] Dr. Israel used the formula for symmetric markets when it is clear that he evaluated an asymmetric market by analyzing what would happen if one broadliner raised prices, not whether all broadline distributors would raise prices. *See* Israel, Hearing Tr. at 1007:20-23 ("[W]hat we're saying is this broadliner raises his price. If as much of the diversion goes to other broadliners as goes elsewhere, then we've passed the test . . . ."); [redacted] As Dr. Hausman explained, this is the formulation used when considering asymmetric markets. Hausman, Hearing Tr. at 1959:7-11 ("[T]he question is: If Sysco or a hypothetical monopolist were to impose a 5 percent SSNIP, what percentage of sales loss . . . would be recaptured by other broadline distributors versus nonbroadline distributors?"). Although Dr. Israel cited to the formula used in *H&R Block*, Israel, Hearing Tr. at 1017:22-1018:1, 2213:16-22, that case is inapposite because, unlike the differentiated market here, *H&R Block* dealt with "products [that] all provide[d] a fundamentally similar service and a similar user experience for the consumer," making the symmetric formula appropriate. *United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36, 61 (D.D.C. 2011). As the Court noted during opening statements, foodservice distribution is "not tax preparation services, there's not a single unique good that is sold across a number of different types of customers." Hearing Tr. at 64:18-20.

- Second, even assuming Dr. Israel used the right formula, he used the wrong margin. [redacted] He changed his story at trial, claiming that the omitted costs were not really marginal. Israel, Hearing Tr. at 2340:2-11 ("warehousing costs, selling costs . . . wouldn't be a marginal cost."). Dr. Israel new position at trial was that economists should not even try to determine marginal costs and should instead rely on whatever margins are used in the companies' SEC filings, Israel, Hearing Tr. at 2340:12-17, [redacted] Dr. Israel also inexplicably referred for the first time at trial to using a margin of 10 percent, Israel, Hearing Tr. at 1005:15, a figure entirely disconnected from anything presented in his reports or reported by the companies. His changing story cannot obscure his failure to use the right margin.

- As demonstrated by Dr. Hausman, *see infra* Appx. A ¶ 268, using the correct formula and margin results in a threshold diversion ratio over 100%, which means the market must be defined more broadly (*i.e.*, must include other distribution channels). Dr. Israel disagreed with Dr. Hausman about the correct diversion test and the proper margin, but agreed that if Dr. Hausman is correct about those two points, then the market definition must be changed: Israel, Hearing Tr. at 2341:21-23 ("Either one of them alone wouldn't be enough to do it; only by using the [Hausman] test and the [Hausman] margin do you get to this other market definition.").

202. Dr. Israel next testified that he used USF's Linc data to calculate actual aggregate diversion for "Local Customers" and RFP data submitted by the parties in response to specification 16 of the FTC's second request to calculate aggregate diversion for "National Customers." Israel, Hearing Tr. at 1008:21-110:7. Both data sets are unreliable and not suited for the purpose for which they were used.

- *Linc data.* [redacted] USF did not rely on these data for any course-of-business analysis, and the database was of such limited utility to USF that it discontinued use of it entirely as of November 2014. Schreibman (USF), Hearing Tr. at 1505:10-13 [redacted] Finally, as explained by Dr. Bresnahan, given that Dr. Israel used a prospective data base incompletely cataloguing business opportunities USF hoped to win, Dr. Bresnahan concluded that Dr. Israel had not calculated actual diversion (*i.e.*, real-world switching) at all. *See* Bresnahan, Hearing Tr. at 2168:8-11 ("I don't think [I] see where there's diversion in there. I mean, he hasn't estimated diversion.").

- *RFP Data.* [redacted] While the broader RFP dataset suffers from many reliability problems of its own, the decision to use a much smaller sample for this analysis—even though Dr. Israel relied on the broader set of data for other analyses—was never explained. The data also was not kept in the ordinary course of business, was reconstructed "based on imperfect memories" by the parties at the FTC's request, was based on highly imperfect and unverifiable information regarding competing bidders, and contained numerous inconsistencies between Sysco and USF submissions that highlighted the data's unreliability. *See supra* Appx. A ¶¶ 30-31 (Mr. Sonnemaker explaining the process by which the FTC collected this data, and the numerous instances in which Sysco informed the FTC that the data was not collected in the ordinary course of business and unreliable); [redacted]

203. Because he failed adequately to demonstrate either the critical aggregate diversion ratio or the actual aggregate diversion ratio, Dr. Israel was unable to provide a meaningful comparison of the two to determine whether the hypothetical monopolist test was satisfied.

204. Turning to geographic markets, Dr. Israel testified that the relevant geographic markets are nationwide for "National Customers," Israel, Hearing Tr. at 1018:6-10, and are limited to certain "draw areas" for "Local Customers," *id.* at 1024:7-1030:3. The majority of Dr. Israel's testimony focused on his methodology for defining local markets, which proceeded as follows. He first identified Sysco and USF distribution centers near each other and drew circles around them to capture where those distribution centers made a majority (75% by revenue) of their sales (the draw areas). *Id.* at 1024:23-1025:4, 1025:19-1026:2. He then identified customers who were located in the area where the circles overlapped. *Id.* at 1026:3-11. Finally, to determine which competitors to include in his market share calculations, he used only those competitors who were as close or closer than Sysco or USF were to their farthest customer within the draw area. *Id.* at 1028:1-10. In other words, Dr. Israel's methodology assumed that no competitor would drive farther than Sysco or USF does today to serve a customer in the overlap area. This assumption is unfounded, [redacted] Dr. Israel could have verified his draw area methodology

(although he would have found it incorrect) had he tested his circles against the zip code-level sales data available in numerous locales. He chose not do so, routinely ignoring competitor sales in his so-called local markets as reflected in the data collected by FTC. Israel, Hearing Tr. at 1071:15-1073:10.

205. [redacted] Dr. Israel's contention is belied by the absence of numerous national customers who source foodservice distribution regionally from the constructed RFP dataset used in his baseline market share calculations. *Id.* at 1253:8-12. [redacted]

206. Dr. Israel claimed that getting the same answer when analyzing an issue in different ways validated and confirmed the correctness of his results. Israel, Hearing Tr. at 2333:23-2334:7 ("what I really stress in my work and with the team is that I come with the analysis of the merger from a variety of points of view and make sure that those – that variety of points of view consistently leads to the same conclusion."). He specifically cited his market share sensitivity analyses as the prime example of following this approach in his empirical work. *Id.* at 2334:17-21. Taking a closer look at the "National Customer" market share sensitivity analyses reveals the hollowness of Dr. Israel's claims. Genuinely testing the validity of the shares would involve making substantial changes to the overall size of the market (the denominator) and checking if

the shares remained similar. [redacted] and the most conservative (inclusive) sensitivity expanded that market to only $ 34 billion, Israel, Hearing Tr. at 2364:17-22, DX-06112, Backup to Dr. Israel's Report. To the extent that Dr. Israel's market share calculation "consistently leads to the same conclusion," Israel, Hearing Tr. at 2333:23-2334:7, it is because he consistently uses the same (incorrect and untested) assumptions.

207. For instance, Dr. Israel acknowledged that he left out $30 billion in systems distribution in the sensitivity analysis purporting to account for systems sales, Israel, Hearing Tr. at 1259:19-1260:14, and $38 billion in broadline sales even in his most "conservative" sensitivity estimation, *id.* at 1265:7-19. Nowhere did Dr. Israel purport to run any sensitivities testing his decision to exclude specialty distributors, which are heavily used by many "national" customers [redacted]

208. The sensitivities assume the conclusion (that the market is correctly defined), and only make small incremental changes to the calculation by varying which sales from the very limited set of broadline distributor CID respondents to count in the denominator. [redacted]

209. [redacted]

[redacted]

210. Dr. Israel's sensitivity analyses fail both to test the fundamental assumptions upon which he bases his market shares and to accurately capture the foodservice distribution purchases of "National Broadline Customers.: They therefore do nothing to validate Dr. Israel's market shares or the conclusions that he draws from them.

211. More fundamentally, as discussed by Professor Bresnahan, Dr. Israel's national shares fail to capture the competitive landscape faced by a customer using regional procurement. For example, if a customer is purchasing in Ohio, Sysco and USF shares in California and Oregon are completely irrelevant, while the presence of Ohio distributors with few existing "National

Customer" sales who are not captured in Dr. Israel's national shares may be key in providing a competitive constraint.

212. Dr. Israel's erroneous market share calculations infected the remainder of his analysis, including his conclusion that the merger would in fact harm customers and that efficiencies were unlikely to be passed through. In terms of harm to "National Customers," Dr. Israel testified that the harm generated by the merger would be the loss of a customer's second best alternative. Israel, Hearing Tr. at 1076:3-10. Dr. Israel performed a qualitative analysis of the incomplete and unreliable RFP data mentioned above, concluding that Sysco and USF are each other's closest substitutes. *Id.* But Dr. Israel's RFP database is biased in favor of finding close competition between Sysco and USF and does not accurately reflect competitive dynamics. Dr. Israel constructed the RFP database from Sysco's and USF's documents and information, purposefully excluding bidding opportunities submitted to the FTC and/or the parties by third party distributors. Israel, Hearing Tr. at 2343:15-2344:5. [redacted] Furthermore, although Dr. Israel does not believe the parties had any incentive to bias their Specification 16 responses to the FTC, on which he based his RFP database, Israel, Hearing Tr. at 2346:19-21, Dr. Israel included only a subset of the parties' reported bidding opportunities in his RFP database. [redacted]

[redacted]

213. Despite the absence of all bids for which neither Sysco nor USF competed, Dr. Israel proceeded to rely on this constructed RFP database to determine the market shares of Sysco and USF in his alleged "National Broadline Customer" market. Israel, Hearing Tr. at 2334:17-19. And despite omitting numerous bids that included one party but not the other, Dr. Israel also relied on this database to determine that Sysco and USF are each other's closest competitors for "National Broadline Customers." *Id.* at 2342:19-22. This is another example of Dr. Israel appearing to have reached a conclusion first and working backward to create supporting analyses.

214. Professor Bresnahan's analysis of actual switching behavior, *infra* Appx. A ¶ 231, shows that Dr. Israel's reliance on the artificially constructed RFP dataset produces highly inaccurate results that do not match customers' real-world behavior.

215. [redacted] These two inputs are wrong.

216. With respect to "Local Customers," Dr. Israel conducted an entry event study to determine whether the price impact of the merger, Israel, Hearing Tr. at 1095:22-1096:25

(describing an entry event study), although an exit event study would have been of far greater utility, since a firm's exist is similar to a merger in which one of the merging parties ceases to exist as a competitor. In any event, Dr. Israel's entry event study does not lead to reliable conclusions regarding unilateral effects in local markets; as explained in connection with Dr. Hausman's testimony, Dr. Israel's study failed two reliability tests. *See infra* Appx. A ¶ 291. And as shown by Dr. Bresnahan, entry by other competitors has a greater effect on USF's prices than entry by Sysco, confirming that the two merging parties are not each other's closest competitors, at least in that market. Bresnahan, Hearing Tr. at 2160:6-2161:9.

217. [redacted]

218. Finally, Dr. Israel testified that merger-specific efficiencies would not offset his claimed

harms. [redacted]

B. RAJIV GOKHALE (FTC)

219. Mr. Rajiv B. Gokhale is an executive vice president at Compass Lexecon. Gokhale, Hearing Tr. at 2252:21-24. He has no doctoral degree. *Id.* at 2253:3-9; 2331:1-5. He has never before testified at trial regarding merger-related efficiencies and he has filed only one report discussing merger-related efficiencies. *Id.* at 2331:6-11. Mr. Gokhale has never filed a report regarding efficiencies in the foodservice distribution industry, or even the food industry more generally. *Id.* at 2331:12-20. He can remember three instances in which he evaluated cost-savings estimates "related to merger-specific cost efficiencies." *Id.* at 2254:5-16. The Court admitted him as an expert in financial economics. *Id.* at 2254:21-24.

220. Mr. Gokhale testified that his previous experience in calculating merger-specific efficiencies came in the airline industry, the oil industry, and the bath products industry.

Gokhale, Hearing Tr. at 2288:16-2289:1.

221. In his previous work with merger efficiencies, Mr. Gokhale used the merging parties' efficiencies calculations to "conduct some analysis of what [he] might consider merger specific." Gokhale, Hearing Tr. at 2289:9-21. In one case, Mr. Gokhale had a series of phone calls with company employees, *id.* at 2293:16-20; in another, two days of meetings, *id.* at 2293:21-24; and in the third, a trip to a company plant to speak to people there, *id.* at 2293:25-2295:25. In each, Mr. Gokhale relied on information from the merging companies and requested additional information to the extent he needed it to determine merger-specific efficiencies. *Id.* at 2287:25-2288:8, 2292:23-2293:15.

222. Mr. Gokhale testified that in this case he did not have enough information to assess whether any of the claimed efficiencies were merger-specific. Gokhale, Hearing Tr. at 2298:9-15. [redacted]

223. Mr. Gokhale admitted that his report on merger-specific efficiencies included a "Materials Considered" list that contained no more than 3,000 documents. Gokhale, Hearing Tr. at 2299:17-2300:7. He accepted also that McKinsey & Company, a "well-regarded firm," was a third-party consultant in this matter and produced over 100,000 documents to the FTC regarding efficiencies. *Id.* at 2300:8-2301:5.

224. [redacted] Mr. Gokhale acknowledged that there are analyst reports that are optimistic about Sysco's and US Foods' chances of achieving significant efficiencies as a result of their merger,

but that he did not include a single analyst report on his "Materials Considered" list. Gokhale, Hearing Tr. at 2327:16-2329:24.

225. Mr. Gokhale acknowledged that part of his efficiencies analysis—specifically the analysis regarding category management—related to two separate sets of efficiencies calculations performed by McKinsey, Sysco, and US Foods: one that occurred during the first weeks of work, when the companies legally could not share relevant information, dubbed the "math" step; and another which took stock of market dynamics surrounding the two companies and every individual product category, dubbed the "business judgment" step. Gokhale, Hearing Tr. at 2301:16-2303:22.

226. When asked if he considered any factors that may have affected the business judgment step to determine why estimated savings might have changed, Mr. Gokhale did not answer, stating instead that the business judgment step "is really opaque." Gokhale, Hearing Tr. at 2311:2-22. After considering one such example—Sysco and USF will be able to combine their dishwashing detergent volume to achieve greater scale post-merger—Mr. Gokhale admitted that "if you have higher scale you may be able to extract some better cost profile." *Id.* at 2311:23-2314:1.

227. Mr. Gokhale was not present for the testimony of Defendants' efficiencies witness, Mr. Carter Wood, nor did he read the entirety of Mr. Wood's testimony. Gokhale, Hearing Tr. at 2319:6-13.

C. TIMOTHY BRESNAHAN (DEFENDANTS)

228. Timothy Bresnahan, one of Defendants' economic experts, testified about the flaws of the analytic methods and data underlying the FTC's market definitions and allegations of future harm.

229. Dr. Bresnahan is a professor of economics at Stanford University. Bresnahan, Hearing

Tr. at 2062:3-4. He is a leader in the field of competition and industrial organization, specializing in competition in particular industries. *Id.* at 2062:5-12. He has authored the *Industrial Organization Handbook* chapter on econometric methods for industries with market power, and served on the National Bureau of Economic Research's industrial organization steering committee until he was appointed to the Bureau's Board. *Id.* at 2062:13-20. Much of his work focuses on testing whether business data and business models are "reliable for the economic inference [businesses are] trying to draw." *Id.* at 2062:21-2063:2.

230. In 1999 and 2000, Dr. Bresnahan served as the chief economist in the Department of Justice's Antitrust Division; as explained by Dr. Bresnahan: "the chief economist is half of the discussion of whether it's a good idea to try and block this merger, whether that's in the interest of the American consumer." *Id.* at 2063:16-2064:11.

231. Based on his analysis of market data, Dr. Bresnahan reached three conclusions. First, "there is no reliable evidence that there's a harm to competition" in "so-called broadline customers markets. . . . [I]f you look at the reliable available economic [data], it shows that there won't be a harm to the competitive interests of those national broadline customers." Bresnahan, Hearing Tr. at 2066:3-9. Specifically, Dr. Bresnahan's switching analysis is direct evidence of substitution from Sysco and USF to *other* distributors at current prices, which not only defeats the FTC's alleged markets, it also rebuts the idea that Sysco and USF are each other's "next closest substitute." *Id.* Second, Dr. Bresnahan concluded that for the 32 local geographic markets alleged by the FTC, "reliable economic evidence about the competitive circumstances serving the ['Local' broadline customers]" shows that "they won't be harmed by the merger." *Id.* at 2066:10-1. Last, he opined that Dr. Israel's "market definition in the broadline market without a national or local modifier" was also incorrect. *Id.* at 2066:16-17.

232. Dr. Bresnahan voiced numerous critiques of Dr. Israel's calculation of market shares for the "National Customer" market, which were at the heart of the FTC's case, largely because Dr. Israel relied on those shares in his quantification of harm. Bresnahan, Hearing Tr. at 2067:19-21. The first critique was that Dr. Israel's share calculations for the "National Customer" market were significantly overstated because "national broadline customers can and do buy regionally, and so the national shares don't measure the competitive alternatives available to them." *Id.* at 2068:10-15. For all "National Customers" that contract regionally, and for the many "National Customers" only located in one region, Dr. Israel "overcount[ed] the competitive importance of Sysco and USF" by counting the merging parties' shares across the entire United States. *Id.* at 2071:8-15. For a "National Customer" in one region or a nationwide "National Customer" that bids regionally, like Amerinet, the fact that USF and Sysco have capacity across the country is not "part of the competitive pressure that's holding down prices at [the regional] purchase," and thus Dr. Israel's model overstated "the importance of Sysco and USF." *Id.* at 2073:11-19.

233. Dr. Bresnahan next faulted Dr. Israel for calculating market shares dramatically different than represented by industry participants. Drawing on his experience, Dr. Bresnahan explained that "it's often true in a merger case that people in the industry will have calculated market shares in the relevant market because they think about it." Bresnahan, Hearing Tr. at 2076:9-12. Indeed, in this case, "several different participants in the market" calculated that the merged entity would have a market share "in the high 20s, 27 percent or something like that before the divestiture." *Id.* at 2078:6-13. Dr. Israel's calculations, which varied dramatically from these industry numbers, were therefore likely "unreliable." *Id.* at 2077:16-18.

234. Dr. Bresnahan testified that Dr. Israel's underlying data were biased, reflecting his own subjective judgment, and were not reliable. Specifically, Dr. Bresnahan explained that Dr.

Israel's RFP data, which he treated as if it were a score-sheet of bidding outcomes kept by the parties in the ordinary course of business, were unreliable because they were constructed by Dr. Israel based on "Dr. Israel's sense" and Dr. Israel "had to put a lot of his judgment into it." Bresnahan, Hearing Tr. at 2078:25-2079:9. Similarly, Dr. Bresnahan concluded that the data underlying Dr. Israel's auction model were flawed because they were not kept in the ordinary course of business, were compiled only to comply with the FTC's request, and because "the parties were explicit with the [FTC] that the parties deemed that evidence as unreliable and incomplete." *Id.* at 2048:11-17; *accord* Sonnemaker (Sysco) Tr. X 1604:3-1605:13. Moreover, as Dr. Bresnahan observed, Dr. Israel admitted that he "exercised case-by-case judgment" to augment what the parties had given him." Bresnahan, Hearing Tr. at 2108:18-2109:2.

235. As explained by Dr. Bresnahan, the bottom line was that Dr. Israel did not "have an appropriate denominator" to calculate market shares because he used unreliable RFP data. Bresnahan, Hearing Tr. at 2111:4-15. Then he used those shares, which were infected by the tainted RFP data, to quantify harm. *Id.* at 2111:13-17. Thus, Dr. Israel's inextricably-intertwined estimates of national shares and competitive harm to "National Customers" were unreliable. *Id.* at 2111:18-23.

236. Dr. Bresnahan explained that the FTC's analysis of substitution, which is "central to the question of whether there is harm to competition in the so called national broadline customer market" was flawed. Bresnahan, Hearing Tr. at 2112:4-9. According to Dr. Bresnahan, the FTC's willful blindness in the data it requested precluded any reliable calculation of the overall sales by market participants and "the effort to do it with RFP data has also failed." *Id.* at 2112:10-15. Instead, Dr. Bresnahan took what reliable data was available to him to demonstrate that customers "choose away from Sysco and USF all the time," a methodology that differed

from Dr. Israel's in that Dr. Bresnahan directly analyzed data to determine substitution while Dr. Israel relied on market shares. *Id.* at 2112:16-25. Dr. Bresnahan's analysis compared detailed transaction data kept by the parties about their customers to an independent data source that systematically collects data about the industry. *Id.* at 2113:4-19. Using these data, Dr. Bresnahan showed substantial substitution away from the two parties for "National Customers." *Id.* at 2114:15-2116:22. Then Dr. Bresnahan demonstrated statistically that "National Customers" of the parties (namely, hotels and restaurants, because that was the data available) were "substituting away from the defendants in a systematic way." *Id.* at 2117:3-2119:12; *see also id.* at 2120:25-2121:8 (discussing his methodology). This methodology actually understated the degree to which customers used distributors other than Sysco and USF because "a customer that wasn't using either of them, that wouldn't be accounted for." *Id.* at 2123:18-20 (the Court speaking). For restaurant chains, Dr. Bresnahan analyzed switching by revenue using available data and reached similar conclusions. *See id.* at 2130:18-2135:4. Dr. Bresnahan also performed a similar analysis for Amerinet, a GPO, and Kaiser Permanente, a nationwide hospital chain, *id.* at 2123:25-2124:13, but the data set available to him for the switching analysis was generally limited to hotels and restaurants, *id.* at 2122:9-11; *id.* at 2207:21-23 (the FTC failed to gather location data for GPO members). Dr. Bresnahan corroborated his switching analysis by evaluating whether, when a customer switched, it switched to another competitor or closed a location. *Id.* at 2136:13-23.

237. Dr. Bresnahan found that when a "National Customer" leaves USF, it switches to Sysco only 15 percent of the time, Bresnahan, Hearing Tr. at 2139:6-12, and when a "National Customer" leaves Sysco, it switches to USF 39 percent of the time (or 57 percent based on revenue), *id.* at 2139:13-17. Dr. Bresnahan then demonstrated that these numbers corresponded

fairly neatly with industry calculations of market shares. If you average the 15 and the 39, "you're going to get a number that's sort of like their national shares of overall foodservice, even a quarter or something." *Id.* at 2141:6-14. Dr. Bresnahan concluded that he used "much more reliable data" than Dr. Israel and got "a very different picture of substitution. I'm seeing a lot of substitution to third parties." *Id.* at 2142:23-25. Although Dr. Israel testified that Dr. Bresnahan's switching analysis was flawed, *see* Israel, Hearing Tr. at 2352:7-12, Dr. Bresnahan's sensitivity analyses show that Dr. Israel's critiques are without merit, *see* Bresnahan, Hearing Tr. at 2210:23-2210:11 (discussing DX-01610 and DX-01611). Dr. Israel did not dispute the methodology and the conclusion of Dr. Bresnahan's sensitivity analyses. Moreover, contrary to Dr. Israel's claim that Dr. Bresnahan's switching analysis evaluated only a small fraction of total sales, Israel, Hearing Tr. at 2348:16–19, [redacted]

238. Dr. Bresnahan explained that Dr. Israel's claim that large customers require a primary distributor was mistaken because "[h]e's confusing switching enough business to defeat a price increase or threatening to switch enough business to negotiate away from a price increase with switching a hundred percent of your business." Bresnahan, Hearing Tr. at 2125:20-2126:9; *see also* 2129:12-2130:6 (a customer does not have to switch all of its purchases to credibly threaten harm to a distributor). With respect to the costs associated with using multiple distributors, Dr. Bresnahan observed that Dr. Israel performed no analysis and that "that was an assumption on his part." *Id.* at 2126:10-17. In fact, Dr. Bresnahan explained that the primary cost would be the switch to regionalizing, and once that was in place, the cost of running a regional model would

be quite modest. *Id.* at 2128:1-18. And the cost of regionalization would have to be weighed against the benefit of having "more options" and having "more bargaining power." *Id.* at 2128:20-2129:1.

239. Dr. Bresnahan refuted Dr. Israel's price discrimination theory, which was that the "merged firm could target everyone that's on the CMU list or the national list." Bresnahan, Hearing Tr. at 2143:20-24. Fundamentally, Dr. Israel's theory was incorrect because customers purchasing different bundles of goods and services were purchasing "different products" and price discrimination requires that all relevant customers are purchasing the same product. *Id.* at 2147:1-15. Dr. Bresnahan also explained that, although being on the parties' national customer list was an observable characteristic, it was not one in the relevant sense, because it did not reflect inelastic demand. *Id.* at 2146:12-16 (being on the national customer list "can't be used to define a market this way"); *id.* at 2147:20-22 ("The idea that the -- that the [National Broadline Customers] are all commonly vulnerable, just because they're on that list is one that I have disproved."); *id.* at 2148:19-22 (the "national" customer list does not identify which customers can multisource and which cannot); *id.* at 2206:25-2207:2 ("One is ['National Customers'] are very heterogeneous and some of them -- the boundary between them and other forms of contract is administrative rather than economic."). Dr. Bresnahan clarified that he looked "with some care at the CMU customers to see if they are, as a group, suitable for price discrimination by a distributor with a big footprint and they're not. You know, many of them are regional, many of them are regionalized. So that -- being on that list isn't a good indicat[o]r of their demand elasticity for a large distributor, you know widespread distributors' services." *Id.* at 2207:6-12.

240. Dr. Bresnahan also demonstrated the flaws in Dr. Israel's analysis of local markets. He testified about his switching study for "Local Customers" based on the parties' own transactional

data, and explained that, when "Local Customers" switch away from Sysco, they only switch to USF 11% of the time, and when they switch away from USF, they only switch to Sysco 15% of the time. Bresnahan, Hearing Tr. at 2163:3-23 (weighted by revenues, only 20% of switches were to the other party); *see also id.* at 2164:1-21 (observing that Dr. Israel did not use the data for a similar analysis). In short, "the switching over time in these local markets is not primarily between these two competitors, it's mostly the third parties." *Id.* at 2163:23-25. Dr. Bresnahan also testified to his study of local customer purchasing behavior with respect to an exemplar item—fresh chicken sold to "Local Customers" in San Diego—and how that demonstrated that broadline distribution sold to "Local Customers" was not a relevant product market. Specifically, Dr. Bresnahan demonstrated that local customer demand is divisible—that is, they can substitute among distribution channels for any item they purchase, including fresh chicken. *Id.* at 2162:2-25; *see also id.* at 2205:25–2206:9 ("Q. And Dr. Israel maintains that defendants have 100-hundred percent of broadline in San Diego. Isn't that what he shows in one of his charts? A. Yes. Q. So those customers not buying from Sysco or USF in San Diego may be buying specialty or cash-and-carry fresh chicken? A. Possibly.").

241. Dr. Bresnahan was critical of Dr. Israel's reliance on the Linc database, which was a "prospecting database" used when "sales reps are hoping to get an account," not to "assess the competitive strength of competitors." Bresnahan, Hearing Tr. at 2165:3-15. Indeed, USF did not require its territory managers to fill out the main competition field, one of the hundreds of fields in the Linc database and one of the fields on which Dr. Israel relied to construct local competition statistics. *Id.* at 2165:3-15; [redacted]

64% [of the entries in the database] are missing the data on main competition on which Dr. Israel relies."). Moreover, Dr. Bresnahan noted that "USF didn't use [the Linc data] to track competition" and has now replaced the database. Bresnahan, Hearing Tr. at 2166:1-4. Dr. Bresnahan observed that Dr. Israel could have used the parties' transaction data to analyze local competition and substitution, like he did, but Dr. Israel failed to do so. *Id.* at 2164:1-14.

242. Dr. Bresnahan was critical of Dr. Israel's aggregate diversion analysis for both "National" and "Local" customers because he used the Linc data and the RFP data "as if they were won/lost records, but they're not. And he hasn't got anything that's about responses to price increases here at all." Bresnahan, Hearing Tr. at 2168:4-7. Dr. Bresnahan would not even call what Dr. Israel did a diversion analysis because he did not "see where there's diversion in there. I mean, he hasn't estimated diversion." *Id.* at 2168:8-11.

243. Dr. Bresnahan demonstrated that Dr. Israel's local geographic markets analysis was erroneous. Dr. Bresnahan began with a case study of Omaha. He observed that, because Dr. Israel lacked sales data in Omaha, he assumed that competitors would drive "no further in his baseline than Sysco or USF drives 75 percent of the time in that local area." Bresnahan, Hearing Tr. at 2156:10-12. But "if the firms you're interested in are in town," Dr. Bresnahan explained, "how far they drive is not a good indicat[o]r of whether folks will drive in from out of town to compete. But anyway, that's what he does." *Id.* at 2156:14-18. Instead of relying on assumptions about driving distances for in-town distributors, Dr. Bresnahan used the zip code data provided by Cash-Wa to the FTC, applying the national/local distinction that Dr. Israel articulated. *Id.* at 2156:19-25. He demonstrated that Dr. Israel's analysis dramatically understated competition in the local overlap areas, thereby dramatically understating Cash -Wa's market share. *Id.* at 2157:8-13; *id.* at 2158:10-22 (noting that Dr. Israel declined to use this zip

code data, and used zip code data only from the parties). In sum, Dr. Bresnahan emphasized "that the assumption that the out of town competitors won't drive any further than the folks in town is false. I mean, here it's sort of extremely false." *Id.* at 2159:2-5; *see also id.* at 2159:10-12 (referencing an example from Chicago which showed the same thing); *id.* at 2212:9-18 (discussing Chicago example to show that Dr. Israel's draw area methodology is arbitrary); [redacted]

244. Dr. Bresnahan also rebutted Dr. Israel's interpretation of his Sysco entry study. As Dr. Bresnahan explained: "Dr. Israel looked at Sysco's entry into markets where USF already was and said prices fall. I don't see the antitrust salience of that. That establishes that Sysco and USF are competitors, and I agree with that, everybody agrees with that." Bresnahan, Hearing Tr. at 2160:9-19. Applying Dr. Israel's own methods to Shamrock's entry into Los Angeles, Dr. Bresnahan found that "Shamrock is a much more effective competitor against USF as measured by the price impact of their entry, which is not a crazy metric, than is Sysco[.]" *Id.* at 2160:20-25. Thus, "if you actually did the right thing, which was comparative, you'd reverse his conclusion. It's not Sysco and USF are particularly close competitors, they're actually not particularly close competitors in this locale." *Id.* at 2168:1-6.

245. Fundamentally, Dr. Israel's market shares, which Dr. Bresnahan demonstrated to be erroneous, were "a critical input into [Dr. Israel's] calculations in the model" for unilateral effects. Bresnahan, Hearing Tr. at 2149:9-12. Because Dr. Israel did not have a database

ordinally listing the place in which a competitor finished in any particular RFP bid, he relied on market shares to determine unilateral effects. *Id.* at 2149:15-16 ("He may know who won, but he doesn't know who was second and who was third. So to replace that critical information to do an auction kind of analysis, who was second, who was third, what did they bid . . . . [h]e uses the shares.").

246. Dr. Bresnahan echoed Dr. Hausman's observation that both Dr. Israel's critical loss analysis and his harm analysis were wrong because both relied on the parties' margins and he failed to include variable distribution costs in calculating the margin. Bresnahan, Hearing Tr. at 2150:7-12.

247. Dr. Bresnahan tested Dr. Israel's hypothesis that the merged entity would not pass efficiency gains through to the consumer against actual efficiency gains in the recent past and found that, when Sysco realized efficiency cost savings through its category management program, "a lot of that was passed through to their customers." Bresnahan, Hearing Tr. at 2150:22-2151:6. Dr. Bresnahan explained that these conclusions applied to both "Local" and "National Customers" because there were not "market conditions . . . related to pass-through [that] were radically different in those two" markets. *Id.* at 2184:10-16. [redacted]

248. Finally, Dr. Bresnahan explained how Dr. Israel's analysis was not internally tested, consistent with the scientific method, or consistent with the Horizontal Merger Guidelines. Contrary to Dr. Israel's claims, Dr. Bresnahan testified that Dr. Israel's sensitivity tests did not actually test the assumptions he made. Bresnahan, Hearing Tr. at 2170:8-12. Dr. Brensahan testified that Dr. Israel's approach was inconsistent with the scientific method. *Id.* at 2170:15-17 ("Q. And in your view is Dr. Israel's approach consistent with the scientific method? A. No,

we've come to so many places where there are comparatively reliable data you could use to check the predictions, he hasn't. I have, the predictions have failed."). And Dr. Bresnahan testified that Dr. Israel's approach was inconsistent with the Merger Guidelines, as Dr. Bresnahan applied them when he was Assistant Attorney General for Economics. *Id.* at 2170:18-2171:5. As Dr. Bresnahan told it: "I think he's misinterpreting the Horizontal Merger Guidelines, he's treating them like they're a cook book, and that's not what they are. The Horizontal Merger Guidelines are a way to organize reliable economic analysis where the appropriate analysis is economic on all the different topics into a uniform frame, and so he's taken quotes from the Horizontal Merger Guidelines, but at each of those junctures, you need to do some reliable economic analysis, and I don't think he's done that." *Id.*

D. JERRY HAUSMAN (DEFENDANTS)

249. Dr. Jerry Hausman is the John and Jennie S. MacDonald Professor of Economics at the Massachusetts Institute of Technology, where he has taught for over forty years. Hausman, Hearing Tr. at 1945:4-17. He teaches courses on firm and consumer behavior, competition, and econometrics. *Id.* at 1945:10-15. He is the co-inventor of the first merger simulation model, *id.* 6:3-6, and has testified in six previous antitrust cases, *id.* at 1947:2-3. The Court admitted him without objection as an expert in microeconomics, industrial organization, and econometrics. *Id.* at 1947:22-8:1.

250. Dr. Hausman testified that the economic analysis of a merger's potential anti-competitive effects is a three-step process: beginning with market definition, followed by an assessment of likely competitive effects within that market, and concluding with an evaluation of efficiencies. Hausman, Hearing Tr. at 1948:5-22; 10:9-19. Notably, Dr. Hausman testified that the FTC's expert, Dr. Israel, improperly defined the relevant market and overstated the anti-competitive effects of the merger by miscalculating the parties' margins.

251. Dr. Hausman agrees with Dr. Israel that "the relevant margin for antitrust analysis is price minus marginal cost." Hausman, Hearing Tr. at 1953:6-9. In other words, the margin (in percentage) is:

(Price – Marginal Cost) / Price

252. Dr. Hausman pointed out that accurate margins "demonstrate that this is a very competitive industry." Hausman, Hearing Tr. at 1952:20-24. Dr. Hausman testified also that margins "are critical inputs into what Dr. Israel does, both for market definition and for his auction model." *Id.*; [redacted]

253. Dr. Hausman highlighted that Dr. Israel stated different margin numbers in his testimony and in his report. Hausman, Hearing Tr. at 1953:14-17 ("He testified—I actually used margin of 10%. And his calculations in his report . . . were significantly higher than the 10 percent that he used."). The margin number in Dr. Israel's testimony (10%) was not based on any calculations. *Id.* at 1953:17-19. Dr. Hausman testified that the margin numbers in Dr. Israel's testimony and in his report were too high. *Id. at* 1953:23-1954:8.

254. Dr. Hausman observed that the margins in Dr. Israel's expert report were incorrect because Dr. Israel had omitted several significant elements of marginal cost, thereby inflating the numerator in his margin calculations. *See* Hausman, Hearing Tr. at 1954:21-1956:6. Specifically, when Dr. Israel calculated costs for an industry that more or less comprises delivery, warehousing, and selling, he did not account for certain variable costs associated with delivery, warehousing, and selling. *Id.* at 1954:21-24.

255. Dr. Hausman calculated the correct margins for Sysco's and USF's broadline customers and "national broadline customers," respectively. *See* Hausman, Hearing Tr. at 1955:4-24. The

correct margin calculations are as follows:

	Broadline		"National Broadline"	
	Sysco	USF	Sysco	USF
Total Sales	100%	100%	100%	100%
ACOGs + Earned Income	(81.4%)	(82.9%)	(86.3%)	(85.8%)
Delivery	(3.9%)	(3.5%)	(3.1%)	(5.2%)
Warehouse	(1.9%)	(1.8%)	(2.1%)	(1.8%)
Selling	(3.7%)	(3.2%)	(0.7%)	(0.8%)
Margin	**9.09%**	**8.69%**	**7.82%**	**6.29%**

See id.; DX-05028, Hausman Slide Deck, at 5.

256. Dr. Hausman testified that Dr. Israel's margin for broadline customers was about 50% higher than the correct number. *See* Hausman, Hearing Tr. at 1955:9-10. Dr. Hausman also testified that Dr. Israel's margin for "national broadline customers" was about 70 percent higher than the correct number. *See id.* 15:23-24. Dr. Hausman cautioned that "incorrect margins will lead to overly narrow market definitions, upward bias market shares, and overstated harm to consumers." *Id.* at 1955:25-1956:2; *see also id.* at 1954:12-14 ("[H]e continues to use those margins in his auction model, and that's going to lead to upward bias calculation of potential harm).

257. Markets can be defined in reference to a SSNIP—that is, a market's boundaries depend on marginal customers, or those who would switch away from a product in the relevant market if that product became more expensive. Hausman, Hearing Tr. at 1949:18-1950:1. Dr. Hausman used Budweiser beer as an example; if the price of a six-pack of Budweiser went up fifty cents, the people who would switch to Coors and Miller are the marginal customers; the people who would keep buying Budweiser are inframarginal customers. *Id.* at 1951:16-1952:6. If, by charging and extra fifty cents for a six-pack, Budweiser would actually make less money (because marginal customers would buy a different beer), Budweiser will not charge that extra

fifty cents. *Id.* The ultimate question for market definition is whether there are "sufficiently great number of marginal customers that will switch" when the hypothetical monopolist raises price. *Id.* at 1948:23-1949:4, 1949:18-1950:1.

258. Dr. Hausman agreed with Dr. Israel that critical loss analysis is an application of the SSNIP test under the Merger Guidelines. Hausman, Hearing Tr. at 1957:12-15. However, when performing the critical loss analysis, Dr. Israel used the inappropriate formula, *id.* at 1961:14-15, and applied the wrong margin to that formula, *id.* at 1952:12-14 (Dr. Israel did not use the proper margin); *id.* at 1952:20-24 (the margin for broadline customers was a critical input to Dr. Israel's critical loss analysis and thus an essential determinant of Dr. Israel's market definition), thus defining the relevant market too narrowly, *id.* at 1955:25-1956:1,1963:5-8. Dr. Hausman testified that Dr. Israel also erred by failing to conduct a SSNIP test on "National" or "Local" customer markets, *id.* at 1966:5-9, and by espousing a targeted price discrimination theory that fails on its face, *id.* at 1966:24-1967:.

259. Dr. Hausman testified that Dr. Israel erred by miscalculating critical loss. *See* Hausman, Hearing Tr. at 1963:5-8 ("[U]sing the Critical Loss Test, . . . the bottom line is his defined market, product market, for broadline foodservice distribution is too narrow."). Critical loss is the highest percentage of sales that a hypothetical monopolist can lose in response to a given price increase without making that price increase unprofitable. *See* PX09516,Michael Katz & Carl Shapiro, *Critical Loss: Let's Tell the Whole Story*, ANTITRUST, Spring 2003, at 53(explaining that "if a 10 percent price increase would cause the hypothetical monopolist's profits to be higher than their pre-merger level, then the profit maximizing price increase is at least 5 percent").

260. Dr. Hausman explained that there are two models for calculating critical loss:

Katz/Shapiro and Farrell/Shapiro. Hausman, Hearing Tr. at 1957:14-1958:11. Both of these models employ the "aggregate diversion ratio," which measures the percentage of sales that would switch to other broadline distributors (as opposed to non-broadline distributors) following a price increase by a hypothetical monopolist. *See id.* at 1959:7-11.

261. Katz/Shapiro is the appropriate critical loss model for markets characterized by heterogeneous suppliers or customers. Hausman, Hearing Tr. at 1957:23-25; *id.* at 1974:3-5 (Katz/Shapiro applies to markets where suppliers and customers are "asymmetric"). In this case, the Katz/Shapiro test would approximate the percentage of a hypothetical monopolist's sales that would be lost to other broadline distributors if a monopolist started charging customers more for a particular product. *Id.* at 1958:19-1959:23.

262. Drs. Hausman and Israel agree that Katz/Shapiro is the appropriate critical loss model for this case. Hausman, Hearing Tr. at 1958:12-17 ("I agree with Dr. Israel that Katz/Shapiro should be used because I think that you do have different costs, different mix of customers. And, in fact, he emphasized that you have different types of suppliers and different types of customers, you know, that they're quite heterogeneous, and I agree with him."); Israel, Hearing Tr. at 2335:24-2336:3.

263. Farrell/Shapiro is the appropriate critical loss model for markets characterized by homogeneous suppliers and customers. Hausman, Hearing Tr. at 1958:8-11; *id.* at 1964:15-17 (Farrell/Shapiro applies to markets where suppliers and customers are "symmetric"). In such markets, a hypothetical monopolist raises the prices of all the products in the candidate market, leading to an all-product uniform SSNIP test. DX-02251, Joseph Farrell & Carl Shapiro, Improving Critical Loss Analysis, ANTITRUST SOURCE, Feb. 2008, at 5 n.17. Farrell/Shapiro does not fit the circumstances of this case "because of the heterogeneity of both distributors and

of the customers." *Id.* at 1960:16-17.

264. Dr. Hausman testified that the proper formula for calculating a diversion ratio in the Katz/Shapiro model—the model that best fits the facts of this case—is:

$$\text{Estimated Aggregate Diversion Ratio} > \frac{10\%\ \text{Price Increase}}{\text{Percentage Margin}}$$

Hausman, Hearing Tr. at 1962:12-15; DX-05028, at 11. The economics literature supports Dr. Hausman's testimony. *See* DX-00058, Oystein Daljord, Lars Sorgard, and Oyvind Thomassen, *The SSNIP Test and Market Definition with the Aggregate Diversion Ratio: A Reply to Katz and Shapiro*, 4 J. COMPETITION L. & ECON. 263-270 (2008); DX-02251, Joseph Farrell & Carl Shapiro, Improving Critical Loss Analysis, ANTITRUST SOURCE, Feb. 2008, at 5 n.17.

265. Dr. Hausman testified that the proper formula for calculating a diversion ratio in the Farrell/Shapiro model—a model not suited to the facts of this case—is:

$$Estimated\ Aggregate\ Diversion\ Ratio > \frac{10\%\ Price\ Increase}{10\%\ Price\ Increase + Percentage\ Margin}$$

Hausman, Hearing Tr. at 1961:25-1962:10; DX-05028, at 11. The economics literature supports Dr. Hausman's testimony. *See* DX-02251, Joseph Farrell & Carl Shapiro, *Improving Critical Loss Analysis*, ANTITRUST SOURCE, Feb. 2008, at 5.

266. Dr. Hausman testified that Dr. Israel used Farrell/Shapiro formula to calculate a critical aggregate diversion ratio, not the proper Katz/Shapiro formula. Hausman, Hearing Tr. at 1964:17-22. This misstep resulted in a critical diversion ratio that is too low. *Id.* at 24:7-14.

267. An artificially low critical aggregate diversion ratio can lead to a market definition that is too narrow. DX-00058, Oystein Daljord, Lars Sorgard, and Oyvind Thomassen, *The SSNIP Test and Market Definition with the Aggregate Diversion Ratio: A Reply to Katz and Shapiro*, 4 J.

COMPETITION L. & ECON. 263, 270 (2008); *see also* Hausman, Hearing Tr. at 1965:23-1966:3 ("Q: [S]o what you're saying is he misapplied—he used the wrong formula and he ended up excluding things from the relevant markets that shouldn't have been excluded. That's what we're saying here? A: That's what I'm saying, yes.").

268. Dr. Hausman testified that even assuming Dr. Israel's margin for broadline customers were correct, using the proper Katz/Shapiro formula to calculate a diversion ratio would show that "a market for broadline foodservice distribution, which was [Israel's] product market, is too narrow." Hausman, Hearing Tr. at 1962:12-21. Dr. Hausman explained that, under the proper formula, the actual aggregate diversion ratio for a broadline foodservice distribution product market had to "be greater than or equal to 1"; aggregate diversion ratio, however, cannot "be greater than 1 by definition." *Id.* at 1962:15-23. Neither can aggregate diversion ratio be equal to 100 percent, because "some of the business goes to systems, [and] some of the business goes to specialty." *Id.* at 1962:23-1963:2. Dr. Hausman testified that the critical loss analysis shows that the proper product market definition requires the inclusion of other types of products. *See id.* at 1963:11-12 ("You certainly need to include other things, and the most obvious candidates are specialty, systems and so on.").

269. Dr. Hausman testified that Dr. Israel performed a SSNIP test only for the general "broadline product market," and thus did not perform a SSNIP test for "National" or "Local" customers. Hausman, Hearing Tr. at 1966:5-9.

270. Dr. Hausman testified that the market definitions for "National" and "Local" customers are too narrow. Hausman, Hearing Tr. at 1966:10-23.

271. Dr. Hausman considered Dr. Israel's alleged market comprising "National" broadline customers and, using the proper Katz/Shapiro formula, found that the estimated aggregate

diversion ratio would have to be higher than 100% for this alleged market to pass the SSNIP test, a ratio that Dr. Hausman termed "an impossibility." Hausman, Hearing Tr. at 1974:16-1975:9; [redacted] Because diversion ratios cannot be greater than 100 percent, Dr. Hausman concluded "that the market must be broader than the national customer market." Hausman Tr. at 1975:2-5; DX-05028, Slide Deck, at 15.

272. Dr. Hausman testified that the market definition must be wider, in light of data showing that most foodservice customers use fewer than ten distribution centers. Hausman, Hearing Tr. at 1976:2-1977:3 ("it seems to me the market definition, which excludes, for instance, many regional and local distributors, is incorrect because certainly if I am only using one OpCo and I'm in Boston, I can use local people, I can use regional people, I have a whole host of people I can use.").

273. Dr. Hausman testified that Dr. Israel invoked a targeted price discrimination theory, Hausman, Hearing Tr. at 1966:24-1967:1, but that he failed to show that there was any danger of post-merger price discrimination in this case, *id.* at 1978:15-1979:6.

274. Dr. Hausman testified that in order to target certain customers for price discrimination, a firm must be able to identify customers with "low price elasticity . . . [b]ecause if you try to raise the price and they're not price sensitive, they switch and you lose the profit. So if they stay you get the 5 percent, but if they switch you lose the whole margin." Hausman, Hearing Tr. at 1967:21-25. Large customers—like some of the FTC's so-called "National" customers in this case—are smart and typically "hide their preferences." *Id.* at 1968:1-8.

275. Dr. Hausman pointed out that Dr. Israel did no analytical work to show how the merged company would or could identify customers with low price elasticity. Hausman, Hearing Tr. at

1968:15-25. Instead, "all [Dr. Israel] did was to take the customer list—you know, he testified he took the customer list from Sysco and he took the customer list from USF, and whatever they named national customers, he said they could be price discriminated against, and defined a price discrimination market based on that. . . . He did no economic analysis at all, at least that I'm aware of." *Id.* at 1969:1-15.

276. Dr. Hausman has seen price discrimination markets in the past, but a price discrimination market in which targeted customers have lower margins than non-targeted customers "would be an all-time first, because you target people to charge them more and not to charge them less." Hausman, Hearing Tr. at 1969:22-1970:17. "National Customers" have lower margins than "local" customers—"exactly the opposite of what you would expect" from Dr. Israel's assertion that "National Customers" can be targeted for price discrimination. *Id.* at 1970:24-1971:6.

277. Dr. Hausman's own econometric analysis suggests that Sysco and USF do not see "National Customers" as targets for price discrimination, and are unlikely to do so post-merger. *See* Hausman, Hearing Tr. at 1971:17-1972:23. Dr. Hausman's econometric model analyzes how Sysco's and USF's profitability on a customer varies with the number of OpCos the customer uses. *Id.* at 1972:5-6. Dr. Hausman found that Sysco's and USF's profitability "never increases at all" "on a statistical basis" for customers using 5 or more OpCos. *Id.* at 1972:7-9. Indeed, Sysco's and USF's profitability on customers using 70 OpCos is "actually a little bit lower than" their profitability on customers using around 25 OpCos (which is the number of OpCos PFG operates), despite that according to Dr. Israel's price discrimination theory, customers using more than 25 OpCos "are the people that you would expect would end up paying higher because they'd have fewer choices." *Id.* at 1972:11-20. Essentially, Dr. Hausman's model shows that customers using more OpCos than others are not targets for price

discrimination. *See id.* at 1971:17-1972:23 Dr. Hausman testified that larger customers likely obtain low prices because they are sophisticated power buyers and can credibly threaten to move their business to alternative distribution if the merged entity raises prices. *Id.* at 1973:18-1974:14.

278. Dr. Hausman testified that direct competition between Sysco and USF probably does not produce low prices for large customers, because if direct competition were truly so fierce, local customers would be able to pit the two companies against each other to obtain lower prices, as well. Hausman, Hearing Tr. at 1972:24-1973:10. But they cannot, "for local customers the margins are over double, or approximately double, what they are for national customers. So if [Sysco and USF] were beating [each other's] brains out for national customers, they should also be beating [each other's] brains out for local customers, and we don't see that." *Id.* at 1973:6-10; *see also id.* at 2033:9-2036:10 (discussing an industry analysis from the Cleveland Research Company, stating "what these people are saying is somehow Sysco and US Foods is [sic] beating their brains out in national but not in local markets. And what I'm saying is, no, in national markets it's because you have power buyers and you don't in local markets.").

279. Dr. Hausman assessed potential anti-competitive effects of the merger in several ways. He analyzed and critiqued Dr. Israel's auction model and its conclusions of harm, evaluated the effect of USF's divestiture to PFG, and opined as to the merger's probable efficiencies. Dr. Hausman, after cautioning that in his experience "as an inventor of merger simulation models, the secret is those models always lead to a . . . predicted price increase," concluded that the merger could lead to a price increase "of significantly less than 1 percent, which in my view is de minimis." Hausman, Hearing Tr. at 1997:1-21 (using Merger Guidelines § 6.1 in reaching the conclusion).

280. Dr. Hausman testified that, overall, the merged company will continue to face stiff competition, despite having more distribution centers than its competitors. Hausman, Hearing Tr. at 2047:19-2048:23.

281. Dr. Hausman testified that Dr. Israel performed a "qualitative analysis" of the merger's potential anti-competitive effects, and "used an auction model to try to quantify it." Hausman, Hearing Tr. at 1978:5-9. Neither the qualitative analysis nor the auction model fit this case.

282. Dr. Hausman testified that Dr. Israel's auction model is "absolutely not" an appropriate model for the foodservice distribution industry. Hausman, Hearing Tr. at 1979:7-8.

283. Dr. Israel's "auction model assumes each bidder observes the bids of its competitors. That's not true here. . . . [I]t's much closer to a sealed bid auction. The bidder, the customer is not going to tell you what the competitor's bid is. In fact, he's always going [to] imply, depending on [how] truthful he is, that the other bidders are offering him a heck of a good price and you've got to beat it. I mean, you know, that's how the world works." Hausman, Hearing Tr. at 1979:10-19.

284. Dr. Hausman testified that the auction model is inappropriate because foodservice distributors do not bid on a fixed quantity like a picture of Brett Favre in his Packers uniform or a plot of land, as they would in a true auction. Hausman, Hearing Tr. at 1979:20-1980:4. In fact, distributors often lack specific information on the business they seek. Dr. Hausman observed that "many customers don't put out any requirements at all. Those that do are usually between 70 and 80 percent. So it's not a fixed quantity because those customers can still go to specialty people or other people to fulfill part of their requirements." *Id.*

285. Dr. Hausman testified that the auction model is inappropriate because it does not account for the bilateral negotiations that occur as part of nearly every transaction in the foodservice

distribution industry. Hausman, Hearing Tr. at 1980:5-20. Dr. Hausman observed that in both this case and in previous cases, "[w]hen you have big companies . . . they say, . . . you could well be the winner, but it's time to sharpen your pencils. . . . [A]nd that's how you close." *Id.* at 1980:9-14.

286. Dr. Hausman testified that, unlike the foodservice distribution industry, auctions provide no incumbency advantage. Hausman, Hearing Tr. at 1980:20-21. He stated that the incumbency advantage in this case leads to several contracts never reaching an auction format; instead, the incumbent simply "make[s] a new deal" or allows its contract with the customer to renew automatically. *Id.* at 1981:1-6.

287. Addressing Dr. Israel's qualitative analysis of anti-competitive effects, Dr. Hausman testified that "[Dr. Israel's] model is based on RFPs, and . . . only 40 percent of contracts are signed with RFPs, the other 60 percent are signed either through bilateral negotiations or just renewal. So his model doesn't apply to over half of the contracts. And even when there is an RFP there's always by lateral [sic] negotiations afterwards, and his model doesn't take into account bilateral negotiations." Hausman, Hearing Tr. at 1982:10-17. For this reason, Dr. Israel's model failed to show that Sysco and USF were customers' top two distributor choices: that is, because he based his "top two" conclusion on market shares derived from a model that omitted over half of the business in the market, his results reflect "upward bias estimates of merger harm." *Id.* at 1981:7-13.

288. Dr. Hausman testified also that the RFP data that Dr. Israel used was "a self-selected sample. . . . there was testimony how a lot of that is just recollection of people, but it's not a random sample. It's a biased [sic] sample, so I have severe doubts, as an econometrician, what weight you should put on that." Hausman, Hearing Tr. at 2009:23-2010:6; *see also id.* at

2011:6-9 ("I've done many mergers, probably 50 to 100 in my lifetime, and when you have these and salesmen start saying this is what I remember, it's just not objective."). And when the FTC showed Dr. Hausman PX03055, an email purporting to show incentive information from one distributor being used to bargain with another distributor, Dr. Hausman stated that the writer, who mentioned both Sysco and DMA, was "making an educated guess that [the incentive is] from Sysco, but nobody knows, it could be from DMA, and he's inferring[.] . . . [M]y point is, is that you just don't know when you're bargaining. It could be DMA; it could be Sysco." *Id.* at 2019:21-2020:2; *see also id.* at 2058:20-21 ("You don't know what the competition is, you don't know what they're bidding, you're just making an educated guess.").

289. Consistent with his report, Dr. Hausman testified that GPOs "are part customers and part competitors of the distributors[.]" Hausman, Hearing Tr. at 2028:25-2029:1.

290. Dr. Hausman testified that he and Dr. Israel disagreed as to the type of analysis needed to assess anti-competitive effects in local markets. Dr. Israel performed an entry analysis, assessing the effects of competitor's foray into a market, and Dr. Hausman performed an exit analysis, assessing the effects of a competitor's withdrawal from a market. Hausman, Hearing Tr. at 1982:18-19. Dr. Hausman stated that Dr. Israel's foundation for choosing an entry analysis was flawed. *Id.* at 1985:18-1986:8 ("Dr. Israel testified the other day that he thinks, based on an academic paper, that entry studies are better than exit studies, but if you look at that paper, they're talking about closing down supermarkets. . . . But it wasn't as if USF was pulling out of the market here, you know, they were still going to deliver into that market, just from other places. So that is very different. . . . Supermarkets are not the same as food distribution, so I think using that basis is incorrect.")

291. Dr. Hausman testified that with respect to local markets, Dr. Israel performed an

inaccurate entry analysis in order to determine anti-competitive effects. Hausman, Hearing Tr. at 1982:1-5. Dr. Israel used a regression model to examine Sysco's entry into two local markets: Riverside, California and Long Island, New York. Dr. Hausman stated that Dr. Israel's regression suffered from two statistical deficiencies. First, his analysis combined the two test markets; Dr. Hausman testified that this violates the F test, a statistical test used to determine how well a regression model fits a given data set. *Id.* at 1983:3-11. Dr. Israel's model fails also the Hausman test, another statistical test that approximates the fit between a model and a set of data. *Id.* at 1983:13-1984:15 (Q: . . . [Y]ou would not make any inferences, as a professional economist, about his entry analysis? A: Well, even more so, [I'm] Hausman of the Hausman test, I certainly wouldn't do it."). Dr. Israel did not contest that his entry analysis failed both the F test and the Hausman test.

292. Dr. Hausman performed an exit analysis addressing USF's June 2012 exit from the Paducah, Kentucky market. Hausman, Hearing Tr. at 1984:17-20. His analysis, which featured multiple iterations based on different dates, showed that USF's exit had no anti-competitive effect on the market. *Id.* at 1985:6-12.

293. Dr. Hausman testified that while USF and Sysco certainly compete, the effects of their merger cannot be determined by simply using aggregate market shares. Hausman, Hearing Tr. at 1986:9-1987:2; *see also id.* at 2005:11-16 (stating that PFG will operate as a constraint on the merged company's prices post-merger). Rather, it is important to segment customers and to evaluate other competitors in the market, even if Sysco and USF truly are each other's closest competitors. *Id.*

294. Dr. Hausman testified that Dr. Israel inaccurately assessed the potential economic effects of USF's divestiture of eleven distribution centers to PFG. Hausman, Hearing Tr. at 1988:1-18

("[H]e looked at market effects, but I think, again, he has problems because he has the wrong margins again, and it's also based, in my view, on incorrect shares.").

295. Dr. Hausman testified that the potential economic effects of the divestiture were likely pro-competitive, highlighting the fact that a number of other distributors believed they could be competitive with even fewer distribution centers than PFG planned to receive, Hausman, Hearing Tr. at 1989:5-22, and that PFG stated in court that it planned to spend $1.5 billion on expansion, *id.* at 1990:1-5 ("if you're going to spend a billion-and-a-half dollars, you expect to be able to succeed or you don't spend the money."). Dr. Hausman highlighted also that PFG is growing faster than either Sysco or USF, and that it is "blacked [sic] by Blackstone, which is one of the most successful and sophisticated investment firms." *Id.* at 1991:5-1992:4.

296. Dr. Hausman highlighted also PFG's business acumen, stating that "[t]hey're sophisticated, Blackstone's behind them, so even if it takes four to five years, that doesn't mean it takes them four to five years to be competitive. They're competitive off the bat, it just takes four to five years to become big enough. . . . [T]hese people are not babes in the woods. If they're going to invest money in seven or nine new things, it's because four to five years they're willing to wait and become profitable. That's the idea." Hausman, Hearing Tr. at 2048:13-23.

297. Dr. Hausman testified that, contrary to Dr. Israel's claim that PFG would be at a cost disadvantage to the merged company, PFG would in fact be able to decrease its inbound freight costs as a result of the divestiture. Hausman, Hearing Tr. at 1990:9-16. He stated also that PFG's cost of goods sold is similar to USF's, and that PFG's membership with UniPro gives it "even more purchasing power." *Id.* at 1990:17-25. Dr. Hausman testified also that PFG has lower operating costs than USF. *Id.* at 1990:22-24.

298. Dr. Hausman testified that his initial efficiencies calculation resulted in approximately $1

billion in annual cost savings and synergies. Hausman, Hearing Tr. at 1992:15-21 ("And the present discounted value of that, using Sysco's cost of capital, is over $7 billion, so that's a really big saving."). After restricting his estimate to variable costs and filtering out synergies not specific to the merger, Dr. Hausman calculated approximately $500 million in efficiencies. *Id.* at 1992:22-1993:10.

299. Dr. Hausman stated that Mr. Gokhale calculated a lower merger-specific efficiencies figure because he presumed that the merging companies were "leaving a lot of money on the table" by not pursuing savings unilaterally. Hausman, Hearing Tr. at 1993:14-1994:4. Dr. Hausman disagreed with this presumption, explaining that it the parties could have attained the efficiencies without the merger, it would be irrational for them not to have done so, implying that the efficiencies were in fact merger-specific. *Id.* at 1993:25-1994:1 ("[E]conomists don't usually think people leave large amounts of money on the table.").

300. Dr. Hausman testified that Dr. Israel incorrectly predicted the amount of efficiencies that would pass through to the merged company's customers. Dr. Hausman attributed this error to the fact that Dr. Israel's prediction necessarily implicated his auction model, which was itself inaccurate. Hausman, Hearing Tr. at 1994:17-1995:2.

301. Dr. Hausman predicted pass-through by reviewing the amount of category management-based savings that Sysco and USF currently pass through to their customers in the form of lower prices; he found those amounts to be 64% and 69%, respectively. Hausman, Hearing Tr. at 1995:3-13 ("[L]awyers I know often find this difficult to understand, but when you lower prices you sell more."). Dr. Hausman noted also that increasing competition from other distributors would force the merged company to pass savings through to its customers. *Id.* at 1995:21-25.