

## 3 Takeaways From FTC's Victory In Sysco Merger Challenge

By **Melissa Lipman**

*Law360, New York (June 29, 2015, 10:00 PM ET)* -- The Federal Trade Commission's victory last week convincing a D.C. federal judge to block Sysco Corp. and US Foods Inc.'s \$3.5 billion merger underscores the value of internal documents, backs the government's bid to use customers to define a national product market and offers guidance about why a proposed divestiture plan may not save the day.

After spending nearly two weeks hearing testimony about the deal, U.S. District Judge Amit P. Mehta granted the FTC's request for a preliminary injunction on June 23 blocking the tie-up between the nation's two largest broadline food distributors despite a proposal to sell 11 distribution centers to the companies' next largest rival, Performance Food Group Co.

When Judge Mehta released his full opinion Friday, he explained that he was ultimately persuaded by the FTC's narrower market definition and ultimately didn't believe even an expanded PFG could act as a real restraint on the companies after the merger.

Sysco pulled the plug on the deal Monday, but the company's chief legal officer suggested the lesson the company had taken from the decision was that another deal might still be a possibility for the distributor as long as US Foods is out in the market. But the ruling is also rife with lessons for all kinds of companies, regardless of their industry.

Here are three key takeaways from the decision:

### **The Best Arguments in the World Can't Save You From Bad Documents**

It's hardly a surprise at this point that internal documents matter in antitrust probes. So-called hot documents — like the ones in the U.S. Department of Justice's Bazaarvoice Inc. case talking about taking out the competition — have long caught the attention of antitrust enforcer and courts alike.

But Judge Mehta's constant discussion of all the times where the parties' own documents undercut their arguments is a reminder that internal documents need not be colorful to cause problems when it comes to selling a merger.

"It's true [Sysco and US Foods] didn't have any 'antitrust porn' in their files, but they did have very clear statements about how they ... viewed each other," Goodwin Procter LLP antitrust co-chair Andrea Murino said, referring to the kind of notorious materials in the Bazaarvoice case. "I've got to imagine that \$300 million breakup fee was negotiated in light of that reality."

And the case is proof that when the documents the companies created before they were trying to get a deal through support the antitrust enforcer's arguments, all the economic experts in the world may not be able to save the deal.

"While expert testimony is necessary and important in merger cases, a party can run into trouble when experts' views are at odds with contemporaneous business records and ... in this case a substantial volume of third party testimony or declarations," Mayer Brown LLP's Adam Hudes said. "I think any courtroom lawyer has likely experienced that persuasive nature of contemporaneous documents. They're very difficult to run from."

And companies trying to find a fix to get a transaction through the agencies should consider the opinion a warning.

Judge Mehta cited a presentation PFG made opposing the deal in January 2014 — while represented by different antitrust counsel before it began negotiating a divestiture package with Sysco — as further support for the way the FTC's economic expert analyzed local markets.

He likewise pointed to PFG internal documents from later that year after negotiations had begun to show that even the divestiture buyer thought it had to pick up more distribution centers to be a realistic competitor after Sysco and US Foods merged.

While the limited number of sizable rivals in the market meant that Sysco and US Foods likely had no option but to negotiate a remedy with a company that had criticized the deal by the time they began talks, the judge's repeated references to PFG's documents point toward the value in coming to the FTC with a "fix-it first" remedy proposal.

"If you find yourself in a situation like Sysco where you've clearly conceded you need to do something ... I think you might find yourself in that boat where you need to consider how to structure a remedy with a remedy partner that clearly resolves all the FTC's concerns and at a point in time when the remedy partner can be an asset to you instead of a liability," Murino said.

### **The Judge Endorsed a National Product Market Based on the Companies' Customers**

In challenging the Sysco merger, the FTC argued that the relevant market was not just broadline distribution — in which Sysco and others offer a wide range of products to many different kinds of customers — versus other kinds of food distribution, but that there was also a market for national broadline distribution.

And Judge Mehta ultimately agreed that the deal would harm national customers, pointing to those customers' own purchasing habits despite the defendants' claim that such evidence pointed to customer preference, not a separate market.

"While this has come up in other contexts and may come up again, I don't think there have been too many court cases that basically took a market that wasn't undeniably national, as some are, and found that there was a certain type of customer that needed to procure the output on national basis," said Bruce Sokler, antitrust chair for Mintz Levin Cohn Ferris Glovsky & Popeo PC. "Now they've gotten a pretty express judicial endorsement in the context ... of what I think is a well-reasoned and intellectually-respectable opinion."

Indeed, that conclusion that there is a national product market defined around certain subset customers is one of the "more novel" parts of what is generally a fairly traditional merger opinion, according to Hudes.

"If this was civil litigation, plenty of case law suggests judges should look skeptically on efforts to define markets based on a particular customer or particular group of customers," Hudes said. "There's also a developed group of case law that recognizes those markets as plausible, [and] the agencies are definitely using those kind of markets to their advantage."

And that could affect future deals, including the proposed merger between Staples Inc. and Office Depot Inc. currently pending before the FTC, according to Sokler. That's because in that case contracts to supply national businesses will likely be an issue.

### **Antitrust Remedies Must Restore Competition, Not the Number of Competitors**

The decision is also unusual because, unlike some of the other merger challenges that have gone through trial in recent years, the parties had proposed a remedy that the court could examine.

That kind of detail about what a court might find lacking in a prospective divestiture buyer — the judge worried about PFG's smaller geographic scope, number of distribution centers and purchasing volumes, among other things — is helpful, according to Murino.

"We now have a lot of guidance from a district court in the FTC's home jurisdiction about what kind of remedy will be sufficient and what won't," Murino said. "We also have some further guidance about what kind of potential remedy buyer you should be looking for."

The decision also emphasizes what the agencies have long said about the need to make up for the harm to competition, not just the number of players in the market, according to Sokler.

"The agency says that ... the divestiture needs to replace the lost competition and that is supposed to be virtually immediate," Sokler said. "What he was saying was he didn't think this necessarily would replace what US Foods was bringing to the table both in terms of geographic scope ... but also smaller volumes, smaller number of SKUs and it would have higher costs."

Still, Sokler said, at the end of the day companies crafting divestiture remedies should focus on pleasing the agencies, not the courts.

"It's more important to be able to convince the FTC staff," Sokler said. "It is difficult to go into court where the judge is first going to decide that there's a problem and then feels very, very out of his or her element in evaluating whether the solution solves the problem or not."

"If I draw a lesson out of it, it is do what you have to do to make the sale at the agency," Sokler added.

The case is Federal Trade Commission et al. v. Sysco Corp. et al., case number 1:15-cv-00256, in the U.S. District Court for the District of Columbia.

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