Horizontal Concerns

Both Staples and Essendant source office supply products from a wide range of upstream trading partners, including small and large manufacturers alike. Proponents of the merger will claim that this will create "efficiencies" in the form of increased buyer power that reduces prices paid to suppliers. But is this an efficiency or a harm?

To start, efficiencies are far from a sure-fire defense to an anticompetitive merger.[2] Increased buyer power exerted by the combined firm against its upstream trading partners in this matter would not be an efficiency at all if it stems from an increase in market power on the buy side of the market.[3] Sycamore's expanded empire potentially allows it to squeeze its suppliers, in effect transferring income from those suppliers to the merged firm, with little or no resource savings.[4] In my view, the Commission's analysis did not adequately rule out the possibility of this type of harm from the merger.[5]

My colleagues voting for this settlement claim that the potential for this type of harm was ruled out after a thorough analysis and investigation. I disagree. If an independent fact-finder or a Court reviewed the same evidence, I think they would disagree too and find that there are many unanswered questions.

Manufacturers with market power and must-have brands may very well be able to protect themselves from an anticompetitive exercise of buyer power by the merged firm, but this is an area where we needed further analysis and investigation to reach a conclusion about potential monopsony power over a broad range of suppliers. Even if the wealth transfer from suppliers to Sycamore will translate into some cost savings for end-user purchasers, this is not necessarily an adequate legal justification.

Six months ago, this Commission ordered divestitures of blood plasma collection centers in the Grifols-Biotest merger, since the combined entity would be able to use its increased bargaining leverage to lower payments to suppliers of blood plasma.[6] The Commission rightfully did not

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[2] *See* Federal Trade Commission et al. v. Penn State Hershey Medical Center et al., 838 F.3d 327, 347 (3rd Cir. 2016), where Judge Michael Fisher, in a unanimous reversal siding with the Comm (a)1 (m)11.7 wirg( )-13.3MC /Span <</MCID 14 >>BD5 13 >>BDC 9 -0 0

seek to determine whether the reduced supply costs would be passed through to final consumers, since the reduction was caused by the merged firm's increased market power.[7]

Here, it is possible there will be some legitimate resource savings that are not merely the result of increased market power on the buy side of the market, such as supply chain improvements. However, it is unclear whether these are substantial or even merger-specific. Moreover, while benefits to downstream consumers might be weighed against harm to suppliers as a matter of prosecutorial discretion, it is not a bulletproof defense as a matter of law.[8]

Vertical Concerns

The record evidence and the buyer's track record suggest that Sycamore will have a strong incentive to rapidly increase margins to make a clear case to a potential future acquirer.[9] Absent this transaction, Essendant cannot easily raise prices or reduce service to its dealers, because Essendant would lose sales either because dealers would switch to another wholesaler, such as S.P. Richards, or because the dealers would pass on price increases to their B2B customers, some of whom would then switch to competing dealers, including Staples. After this transaction, however, Sycamore would capture revenue from B2B customers that switch to Staples in reaction to a price increase or reductions in customer service from Essendant. This strategy seems even more likely given Sycamore's actions to date since taking ownership of Staples.

The evidence in the record points to regional differences across markets in the country. The risk of steering to Staples will be particularly high in geographic markets where Essendant is the market leader.[10] Regional managers incentivized on sales and operating margin targets will be particularly susceptible to this type of conduct. This is not nefarious – this is just obvious.

The Commission has put great faith in its interpretation of the economic evidence to justify its conclusion. However, Commissioner Wilson rightfully notes in her statement that economic models are often more art than science. We must be humble about their predictive power, and this matter is a perfect illustration. The Commission's economic model predicts competitive harm, but largely ignored regional differences. I agree with Commissioner Slaughter that our prediction likely *underestimates* the harmful effects. How can the majority confidently reach an accurate conclusion on the vertical effects of this transaction without a closer look at specific geographic markets where effective switching would be particularly difficult?

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[7] This competitive harm is within the purview of the Clayton Act and is well recognized in the 2010 Horizontal Merger Guidelines. Horizontal Merger Guidelines, *supra* note 3, at § 12 ("Example 24: Merging Firms A and B are the only two buyers in the relevant geographic market for an agricultural product. Their merger will enhance buyer power and depress the price paid to farmers for this product, causing a transfer of wealth from farmers to the merged firm and inefficiently reducing supply. These effects can arise even if the merger will not lead to any increase in the price charged by the merged firm for its output."). *See* Sallet, *supra* note 3, at 84. *See also* Judge Millett's opinion in United States v. Anthem, Inc.: "[I]ncreased bargaining power is not a procompetitive efficiency when doing so 'simply transfers income from supplier to purchaser without any resource savings.'" United States v. Anthem, Inc. 855 F.3rd 345, 371(D.C. Cir. 2017).

[8] Case law supports the assertion that harm in one market cannot be offset by benefits in another. United States v. Philadelphia National Bank, 374 U.S. 321, 370-71 (1963); Department of Justice Buy-Side Memo, *supra* note 4, at 10 (citing *Philadelphia National Bank* for this conclusion).

[9] Private equity firms generally take controlling equity stakes in firms with the hope of realizing significant gains through sale to a buyer or an exit through public markets.

[10]

I am also less confident than the majority that Essendant-supplied dealers can easily switch to S.P. Richards to discipline any attempt by Sycamore to disadvantage Staples's

incentives and long-term market impact to inform how we can best exercise our prosecutorial discretion.

Abuse of Data