Judge Grants Preliminary Injunction, Staples-Office Depot Call Off $6.3 Billion Deal

Skadden

05/12/16

If you have any questions regarding the matters discussed in this memorandum, please contact the following attorneys or call your regular Skadden contact.

Matthew P. Hendrickson
New York
212.735.2066
matthew.hendrickson@skadden.com

Clifford H. Aronson
New York
212.735.2644
clifford.aronson@skadden.com

Steven C. Sunshine
Washington, D.C.
202.371.7860
steve.sunshine@skadden.com

Maria Raptis
212.735.2425
New York
maria.raptis@skadden.com

Kenneth B. Schwartz
New York
212.735.2731
ken.schwartz@skadden.com

Four Times Square
New York, NY 10036
212.735.3000

skadden.com

On May 10, 2016, Judge Emmet G. Sullivan of the U.S. District Court for the District of Columbia released his highly anticipated decision in the matter of Staples' acquisition of Office Depot, granting the Federal Trade Commission's (FTC) request for a preliminary injunction and effectively bringing the $6.3 billion deal to an end. Both parties to the transaction announced their intention to abandon the deal shortly after the ruling was issued.

Judge Sullivan's decision (the opinion has not yet been released to the public) marks the latest chapter of an 18-year standoff between the FTC and the office supply superstores (OSS). Staples first sought to acquire Office Depot for $4 billion in 1996. Although the two companies only accounted for roughly 5.5 percent of all U.S. sales of office supplies at the time, the FTC successfully argued in federal court that the deal would cause unilateral price effects in the relevant product market of "consumable office supplies sold through office supply superstores." By proving a narrow market definition, the FTC convinced Judge Thomas F. Hogan of the D.C. district court in 1997 that Staples and Office Depot were two of only three major retailers in the OSS space (with Office Max as the third); as a result, Judge Hogan enjoined the transaction.

Fast forward to 2013, when Office Depot sought to acquire Office Max for $1.2 billion. Again, the key antitrust question was the definition of the relevant market — and the participants in that market. In stark contrast to its position in 1996, the FTC cleared the transaction based on the conclusion that the market for the retail sale of consumable office supplies had broadened to include competition from big-box stores and online retailers. In its closing statement concerning the proposed merger, the commission specifically noted that the parties had "shown that the market for the sale of consumable office supplies has changed significantly in the intervening years," and that as a result, office supply superstores "today face significant competition [such that] the proposed merger is unlikely to substantially lessen competition in the retail sale of consumable office supplies."

Perhaps seeing renewed opportunity given the shifting industry dynamics and the FTC's conclusion in Office Depot-Office Max, Staples and Office Depot decided to attempt another merger in February 2015. Although the competition from non-OSS players cited by the FTC in 2013 had only increased in strength and intensity, the FTC again sued to block the deal. This time however, the FTC's complaint rested on concern for the "business-to-business" segment, an alleged relevant product market distinct from the retail consumer market that was at issue in the past. "Business-to-business" customers (also known as "B-to-B" customers) are large customers who buy consumable office supplies in large quantities and under long-term contracts that also include services such as nationwide delivery, dedicated customer service, customized online catalogs, procurement system integration and utilization reports. Specifically, the complaint alleged that "Staples and Office Depot are the only two office supply vendors that can provide on their own the low prices, nationwide distribution, and combination of services and features that many large B-to-B customers require," and that entry or expansion into the market by other vendors, manufacturers, wholesalers or online retailers of office supplies would not be timely, likely or sufficient to counteract the anti-competitive effects of the merger.

The FTC made its case over the course of a two-week trial, presenting evidence and witnesses. During that time, the FTC staff encountered several stumbling blocks, including the exclusion of some expert testimony from its economist (Carl Shapiro) regarding Amazon's nascent B-to-B business unit's future projections and ability to compete. Judge Sullivan also appeared at times to be highly skeptical of the case. In addition, when the OSS retailers offered a mid-trial settlement, which included the promise of a three-year price freeze for B-to-B customers, the judge encouraged the agency to seriously consider the offer.

After the conclusion of the FTC's case, in a decision sure to be second-guessed by Monday morning quarterbacks, counsel for Staples and Office Depot elected not to call any witnesses or present any evidence, rather arguing that the FTC had not met the legal burden of proof required for a preliminary injunction. Judge Sullivan ultimately disagreed with Staples counsel, concluding that it was likely that the deal would "substantially impair competition in the sale and distribution of consumable office supplies to large business-to-business customers." Although the details underlying Judge Sullivan's conclusion remain under seal pending a public version, this case provides further evidence in the wake of *US Foods-Sysco* and *GE-Electrolux* (also decided by Judge Sullivan) that protecting discrete customer segments is an enforcement priority and such segments should not be overlooked in antitrust risk assessments of potential transactions.

Additional Contacts

Simon Baxter
Brussels
32.2.639.0310
simon.baxter@skadden.com

C. Benjamin Crisman, Jr.
Washington, D.C.
202.371.7330
benjamin.crisman@skadden.com

Frederic Depoortere
Brussels
32.2.639.0334
frederic.depoortere@skadden.com

Paul M. Eckles
New York
212.735.2578
paul.eckles@skadden.com

Shepard Goldfein
New York
212.735.3610
shepard.goldfein@skadden.com

Peter E. Greene
New York
212.735.3620
peter.greene@skadden.com

James A. Keyte
New York
212.735.2583
james.keyte@skadden.com

Karen Hoffman Lent
New York
212.735.3276
karen.lent@skadden.com

John H. Lyons
Washington, D.C.
202.371.7333
john.h.lyons@skadden.com

Matthew M. Martino
New york
212.735.2402
matthew.martino@skadden.com

Jeffrey A. Mishkin
New York
212.735.3230
jeffrey.mishkin@skadden.com

John M. Nannes
Washington, D.C.
202.371.7500
john.nannes@skadden.com

Neal R. Stoll
New York
212.735.3660
neal.stoll@skadden.com

Ingrid Vandenborre
Brussels
32.2.639.0336
ingrid.vandenborre@skadden.com

James S. Venit
Brussels
32.2.639.0300
james.venit@skadden.com