UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES, Plaintiff,	)	
v.	)	No. 03 C 2528
UPM-KYMMENE OYJ, et al., Defendants.	)	Hon. John A. Nordberg

NOTICE OF FILING

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PLEASE TAKE NOTICE that on April 29, 2003, we filed with the Clerk of the United States District Court for the Northern District of Illinois, Eastern Division: Defendants' Initial Response to The Government's Motion for a Preliminary Injunction, a copy of which is herewith served upon you.

UPM-Kymmene Oyj and Raflatac, Inc.

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UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
Eastern Division

UNITED STATES, Plaintiff, v. UPM-KYMMENE OYJ, *et al.*, Defendants.	Civil Action No. 03 C 2528 Judge James B. Zagel Magistrate Judge Michael T. Mason

DEFENDANTS' INITIAL RESPONSE TO
THE GOVERNMENT'S MOTION FOR A PRELIMINARY INJUNCTION

In its Verified Complaint, the Government is compelled to concede that Raflatac has been a "particularly aggressive competitor" and that, as a result, "labelstock customers have enjoyed significantly lower prices and higher product and service quality than they would have otherwise received." Complaint ¶ 2. At the preliminary injunction hearing, Defendants will prove that the proposed merger of Raflatac and MACtac will bring even more competition and lower prices to the labelstock industry, to the substantial benefit of labelstock customers.

The Government misapprehends the competitive dynamics of the labelstock business. First, the Government posits two overly narrow product markets that artificially inflate the market shares of Raflatac and MACtac. In fact, there is no economically meaningful product market of "bulk VIP" or "bulk prime" paper labelstock. Such products compete with a whole host of reasonably interchangeable substitutes, such as film labelstock, wet-glue, direct print, in-mold and shrink-sleeve labels. Any properly defined product market will include numerous demand-side alternatives beyond the niches alleged by the Government. *See United States v.*

Continental Can Co., 378 U.S. 441, 455-56 (1964) (holding that government's proposed product market failed because end-users' changing preferences created "meaningful competition" between metal and glass containers); *W.H. Brady Co. v. Lem Products*, 659 F. Supp. 1355, 1370 (N.D. Ill. 1987) (rejecting narrow product market because "consumers actually use the products in a reasonably interchangeable manner"); *Federal Trade Commission v. Great Lakes Chemical Corp.*, 528 F. Supp. 84, 87 (N.D. Ill. 1981) (holding against government as "[b]rominated and non-brominated flame retardants must be included in a single market so as 'to recognize competition where, in fact, competition exists'"); *United States v. Gillette Co.*, 828 F. Supp. 78, 83 (D.D.C. 1993) (holding government's proposed product market "far too narrow," as according to consumer preferences, it should have encompassed "all premium writing instruments"); *Federal Trade Commission v. R.R. Donnelley & Sons Co.*, 1990-2 Trade Cas. (CCH) ¶ 69,239 at 64,854-55 (D.D.C. 1990) (holding that government's proposed product market was too narrow because offset and gravure printing were reasonably interchangeable); *Federal Trade Commission v. Owens-Illinois, Inc.*, 681 F. Supp. 27, 54-55 (D.D.C.) (holding government's proposed product market was too narrow because glass and other containers are functionally interchangeable), *vacated as moot*, 850 F.2d 694 (D.C. Cir. 1988).

Furthermore, there is almost complete substitutability between the different types of pressure-sensitive labels on the supply side. The same machines can manufacture all pressure-sensitive labels, be they paper, film, VIP or prime. Any anticompetitive effects are highly unlikely where "any attempt to restrict output in order to drive up price will be promptly nullified by new production." *Federal Trade Commission v. Elders Grain, Inc.*, 868 F.2d 901, 905 (7th Cir. 1989); *Blue Cross & Blue Shield United of Wisconsin v. Marshfield Clinic*, 65 F.3d 1406, 1410-11 (7th Cir. 1995) (holding that "[e]ven if two products are completely different from the

consumer's standpoint, if they are made by the same producers an increase in the price of one that is not cost-justified will induce producers to shift production from the other products to this one in order to increase their profits by selling at supracompetitive price"); *Ball Mem. Hosp., Inc. v. Mutual Hosp. Insur., Inc.*, 784 F.2d 1325, 1334-35 (7th Cir. 1986) (holding that firms lack market power where other firms "may be able to convert other productive capacity to the product in question").

Even with its overly narrow and artificial "bulk" paper labelstock markets, the Government can merely assert that Raflatac and MACtac have a combined market share of "over 20%." Mem. at 1. *See also* Complaint ¶¶ 22-23. A Government challenge to a merger involving such low market shares is unprecedented in modern antitrust law and fails even to establish a *prima facie* case. *See, e.g., United States v. Long Island Jewish Medical Center*, 983 F. Supp. 121, 145 (E.D.N.Y. 1997) (holding that merging parties' market share of about 20% was insufficient to establish *prima facie* case under Section 7 of the Clayton Act). Courts often approve mergers with much higher market shares. *See, e.g., Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255, 274-77 (7th Cir. 1981) (upholding merger yielding 35.5% market share); *United States v. SunGard Data Systems, Inc.*, 172 F. Supp.2d 172, 192 (D.D.C. 2001) (refusing to enjoin merger with 70% market share); *United States v. Baker Hughes Inc.*, 908 F.2d 981, 987 (D.C. Cir. 1990) (affirming district court's finding of no Section 7 violation where post-acquisition market share exceeded 75%); *Federal Trade Commission v. Butterworth Health Corp.*, 1997-2 Trade Cas. (CCH) ¶ 71,863 (6th Cir. 1997) (affirming denial of injunction against merger resulting in postmerger market share of 47-65%); *United States v. Waste Mgmt., Inc.*, 743 F.2d 976, 982-83 (2d Cir. 1984) (reversing injunction against acquisition resulting in postmerger market share of 48.8%).

The Government also wrongly assesses the relative strengths of various sellers of labelstock. The Government elevates MACtac to leading status, while minimizing the significance of numerous other firms — including Green Bay, Technicote, Acucote, Ricoh, Spinnaker and Wausau Coated — as "fringe" producers. In reality, MACtac is competitively comparable to these competitors, and has been declining in competitiveness, as its parent, Bemis Company, has significantly decreased capital investment in MACtac in recent years. A merger with Raflatac is MACtac's best hope for obtaining the capital investment it needs to become a stronger competitive force. Meanwhile, the so-called "fringe" compete intensely and take business from Raflatac and MACtac on a regular basis within the Government's defined market.[1]

The merger would also make Raflatac a more formidable competitor. MACtac's business complements Raflatac geographically, and will permit Raflatac to offer customers a broader array of product choices.

The Government's speculation about post-merger price increases is wholly unfounded, as any attempt by the merged entity to raise prices would be quickly defeated. Various other competitors are poised to take sales from the merged entity through increased production or capacity additions, and new firms can easily and effectively enter and begin selling labelstock. Indeed, the ability of firms to introduce new production was among the reasons why the European Union approved this merger last fall. *UPM-Kymmene/Morgan Adhesives*, Case No. COMP/M.2867, Comm. Dec. on Oct. 16, 2002 at ¶27. *See Baker Hughes*, 908 F.2d at 988 (observing that "[i]f barriers to entry are insignificant, the threat of entry can stimulate competition in a concentrated market, regardless of whether entry ever occurs."). Furthermore,

[1] Oddly, during its investigation the Government obtained very little discovery from the competitors it now seeks to marginalize. This may explain why the Government does not understand the competitive significance of these firms.

many labelstock customers can manufacture their own labelstock, thereby eliminating their need to buy labelstock. *United States v. SunGard Data Systems, Inc.*, 172 F. Supp.2d 172, 182 (D.D.C. 2001) (holding that government's proposed relevant product market failed because it did not take into account the competition of customers' internal capabilities).

The Government has also ignored the pro-competitive aspects of the merger. The merger will lead directly to substantial synergies of $28 million per year. Customers will enjoy the benefits of these cost reductions.

Apparently recognizing that the merged entity's market share — even when artificially inflated by the Government's product-market gerrymandering — cannot support any theory of unilateral anticompetitive effects, the Government raises the specter that the merged entity might collude with Avery Dennison. This speculation is unfounded.

The Government darkly suggests that Raflatac is predisposed to coordinate with Avery, but this suggestion is refuted by the Government's own allegations. The Government's Verified Complaint alleges unequivocally that Raflatac has been a "particularly aggressive" and "vigorous" competitor at all relevant times. The Complaint acknowledges that Raflatac began importing labelstock in the 1980s, committed to expanding its North American position in 1999, and built a North Carolina production plant in 2001. Complaint ¶ 25; Mem. at 9. The Complaint further acknowledges that Raflatac has competed "aggressively" every step of the way right up until the present. Complaint ¶ 25; Mem. at 9-10. Despite these acknowledgements, the Government glibly asserts that the merger "likely would mark the end of [Raflatac's] aggressive pricing competition." Mem. at 10. Such uncabined crystal-ball gazing cannot support an alleged violation of Section 7 of the Clayton Act.

The Government seems to suggest that Raflatac is likely to coordinate with Avery because Avery is a customer of Raflatac's parent, UPM. This supplier-customer relationship appears to be the only basis for the Government's assertions regarding the likelihood of coordination. But, as the Government acknowledges, Raflatac has competed aggressively to date notwithstanding the fact that UPM sells to Avery. The Government tries to imply that UPM is beholden to Avery, stating that Avery is "UPM's largest customer of label papers." Complaint ¶ 11. The Government neglects to note that UPM sells many paper products, and that sales to Avery account for less than 1% of UPM's revenues.

In analyzing the likelihood of coordination, the Seventh Circuit has instructed that "the acquisition of a competitor has no economic significance in itself; the worry is that it may enable the acquiring firm to cooperate (or cooperate better) with the other leading competitors on reducing or limiting output, thereby pushing up the market price." *Hospital Corp. of America v Federal Trade Commission*, 807 F.2d 1381, 1386 (7th Cir. 1986). The Government never explains why the elimination of MACtac as an independent competitor would affect Raflatac's incentive or ability to coordinate in this market. The answer is that it will not. Bemis has significantly reduced its investment in MACtac and MACtac's withered effectiveness is evidenced by the fact that Bemis is now willing to accept from Raflatac less than half the price for MACtac that it rejected just two years ago.

In fact, the merger would reduce any incentives to coordinate between Avery and UPM. After the merger, UPM would have a larger captive buyer of label papers (i.e., the MACtac business) and its sales to Avery would be even less important. The Government itself candidly acknowledges that it is unable to allege any anticompetitive effects stemming from UPM's sales to Avery. Complaint ¶ 3.

Moreover, the conditions of the labelstock industry make coordination highly unlikely. There are many competitors, many of them have excess capacity, the products are extremely heterogeneous, there is frequent churning of customers, and information about prices and sales is difficult to determine. The Government never articulates how coordination could occur in this industry, most likely because it is impossible to fathom coordination in light of these structural impediments.

* * * *

At the preliminary injunction hearing, Defendants will present evidence from numerous marketplace sources — competitors, customers, and end-users alike — to prove that a merger between Raflatac and MACtac will bring even more competition to an already competitive industry. In the process, Defendants will also prove that the Government's challenge to the merger is premised upon misunderstandings of commercial realities and unwarranted speculation.

Dated: April 28, 2003

Respectfully submitted,

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