[Oral Argument Scheduled for April 23, 2008]
PUBLIC COPY – PROTECTED INFORMATION REDACTED
Case No. 07-5276

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

FEDERAL TRADE COMMISSION,
Appellant,

v.

WHOLE FOODS MARKET, INC.,
Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

CORRECTED BRIEF FOR APPELLEE WHOLE FOODS MARKET, INC.

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March 18, 2008

CERTIFICATE OF THE PARTIES, RULINGS, AND RELATED CASES

The Parties on Appeal

Appellant

Federal Trade Commission
600 Pennsylvania Ave., N.W.
Washington, D.C. 20580

*Appellees**

Whole Foods Market, Inc.
550 Bowie Street
Austin, Texas 78703

*Wild Oats Markets, Inc., 1821 30th Street, Boulder, Colorado 80301, an appellee when this appeal was filed, is now a wholly-owned subsidiary of appellee Whole Foods Market, Inc.

Amici on Appeal – Motion for Stay Pending Appeal

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The Parties in the District Court

Plaintiff

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Defendants

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Austin, Texas 78703

Wild Oats Markets, Inc.
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Intervenors in the District Court (regarding the Protective Order only)

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Purchase, NY 10577

H.E. Butt Grocery Company
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San Antonio, TX 78283-3999

Publix Super Markets, Inc.
P.O. Box 407
Lakeland, FL 33802-0407

Safeway Inc.
5918 Stoneridge Mall Rd.
Pleasanton, CA 94588-3229

Supervalu Inc.
11840 Valley View Road
Eden Prairie, Minnesota 55344

Target Corporation
1000 Nicollet Mall
Minneapolis, MN 55403

Delhaize America
Square Marie Curie 40
1070 Brussels, Belgium

Kroger Co.
1014 Vine Street
Cincinnati, Ohio 45202-1100

Trader Joe's Company
800 South Shamrock Ave.
Monrovia, CA 91016

Wal-Mart Stores, Inc.
Bentonville, Arkansas 72716-8611

Wegmans Food Markets, Inc.
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Amici in the District Court

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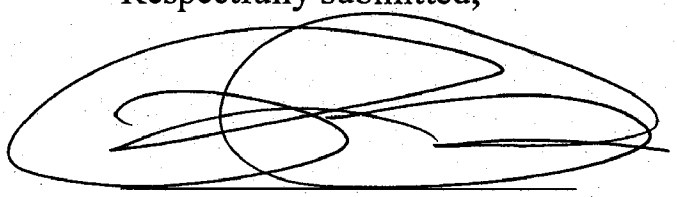
Ruling Under Review

The ruling under review is the August 16, 2007 decision of the District Court in *FTC v. Whole Foods Market, Inc., et al.*, No. 07-1021, denying the FTC's motion for a preliminary injunction, *published at* 502 F. Supp.2d 1 (D.D.C. 2007).

Related Cases

Appellees are not aware of any related cases before this or any other court.

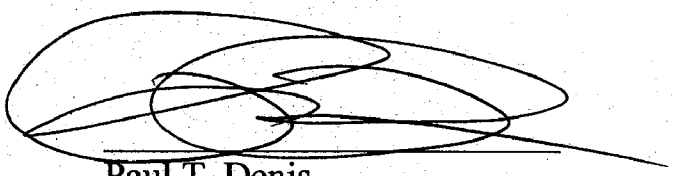
Respectfully submitted,



Paul T. Denis

CORPORATE DISCLOSURE STATEMENT PURSUANT TO FEDERAL RULE OF APPELLATE PROCEDURE 26.1 AND CIRCUIT RULE 26.1

Appellee Whole Foods Market, Inc., operates retail food stores nationwide. It has no parent company, and no publicly held company owns 10% or more of its stock. Former appellee Wild Oats Markets, Inc. is wholly owned by Whole Foods Market, Inc.



Paul T. Denis
Counsel for Whole Foods Market, Inc.

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OTHER SOURCES

GLOSSARY	
Term	*Definition or Full Citation*
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www.food-business-review.com	Cited material *available at* http://www.food-business-review.com/article_news.asp?guid=3698BF2F-86D0-4D05-96B0-1CD5E06E3AC7
www.freshandeasy.com	Cited material *available at* http://www.freshandeasy.com/home.aspx
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"Growth of Organics Continues Unabated"	AC Nielsen, in "Facts, Figures, and the Future" (June 2007), *available at* http://www.factsfiguresfuture.com/archive/june_2007.htm
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Reference Manual on Scientific Evidence	(2d ed. 2000), *available at* http://www.fjc.gov/public/pdf.nsf/lookup/sciman00.pdf/$file/sciman00.pdf
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INTRODUCTION

This appeal should be dismissed as moot because the only relief sought below – an injunction blocking the acquisition – is no longer available now that the acquisition has been consummated. In any event, subsequent events permitted by this Court preclude effective relief.

Were the appeal not moot, it would present no issue of law. The court below articulated and applied the same standard for evaluating a preliminary injunction motion under Section 13(b) of the FTC Act, 15 U.S.C. 53(b), that the FTC urges on appeal. What the FTC describes as the "gravamen of this appeal," FTC Br.26, lacks foundation.

The FTC's appeal, instead, is simply a disagreement with the district court over the weighing of the evidence. But the district court opinion on these issues of fact is unassailable, based as it is on a first-hand assessment of the credibility of the expert testimony and a thorough review of a detailed factual record compiled after an exhaustive FTC investigation. In short, the district court found, and the record supports, that the FTC would not be able to establish that "premium natural organic supermarkets" constituted a properly defined product market. This finding alone was dispositive but the court went on to find, again based on the credible record evidence, that regardless of the market definition, the FTC would not be able to prove that the effect of the proposed acquisition may be substantially to

lessen competition. The balance of the evidence was not close, much less in support of the FTC's claims.

The FTC's frustration with the court's conclusion reflects the wealth of real world evidence making clear that, no matter how "likelihood of success" is sliced, the FTC will not be able to establish a Section 7 violation here regardless of the additional time and resources it devotes to the attempt.

COUNTERSTATEMENT OF THE CASE

Whole Foods and Wild Oats filed the required pre-merger notification with the FTC on February 21, 2007. The FTC conducted a three-month administrative investigation – reviewing 16.5 million pages of documents and 2.4 gigabytes of data, interviewing the merging parties and other industry participants, and conducting 13 investigational hearings. It filed for a preliminary injunction on June 6.

The FTC agreed to a largely paper proceeding. JA1958-67.[1] The merging parties produced thousands of additional documents and an additional 68 gigabytes of data. The parties provided summaries of expected testimony, permitting full depositions of witnesses, and 26 depositions were taken. The parties agreed to the submission of declarations with each retaining the right to reopen a deposition of a witness whose declaration was submitted by the other. *Id.* The FTC did not seek

[1] JA cites refer to the JA filed under seal. Pagination in the public JA is not consistently identical.

to reopen the deposition of any declarant.

The FTC also agreed to a two-day hearing, with testimony from each party's economic experts on July 31, and lengthy closing arguments with documentary, video, and demonstrative exhibits on August 1. The district court actively questioned the expert witnesses and probed counsel as to the significance of the evidence. The district court's 93-page opinion issued on August 16, explaining why it denied a preliminary injunction. Despite copious citation to the record, the opinion captured only a portion of the evidence supporting its conclusions. The FTC sought a stay pending appeal before this Court. Emergency Motion, No. 07-5276 (Aug. 17, 2007). After reviewing two briefs from each side, and an *amicus* supporting the FTC, this Court denied the motion because the FTC had "failed to make a strong showing that it is likely to prevail on the merits of its appeal." 8/23/07 Order (quotations omitted).

COUNTERSTATEMENT OF THE FACTS

Whole Foods Market. Whole Foods is a small supermarket chain that grew from one small health food store to 194 supermarkets before the merger. It is a certified organic foods retailer. To attract a wider range of customers, it changed its product mix and became a full-line supermarket. Today, most items are not organic, including more than half of its produce and far more of its prepared foods, bakery and specialty items. JA2039-52; JA2754¶19, JA2756¶30; JA 2968¶17,

JA2971¶25.

Its growth has been fueled in part by acquiring and turning around floundering smaller chains. For example, it purchased Fresh Fields Markets – which had lost $35 million and never made a profit – in 1996 and earned profits without raising prices. It purchased Mrs. Gooch's in 1993, increasing its profits without raising prices. It turned around Bread & Circus (purchased 1992), Bread of Life (1997), Nature's Heartland (1998), Food for Thought (2000), Harry's (2001), and Wellspring (1991) in the same way – capitalizing on existing buildings and customer base, but providing better value. JA2827¶11; JA2828¶¶13-14; JA2918¶38; JA2945¶11. Whole Foods has also twice taken over abandoned Wild Oats' stores, Framingham MA in 2001 and Madison NJ in 2002. After renovations and price reductions under Whole Foods' management, both became profitable. JA2828-29¶15; JA2843-44¶¶7-8.

Whole Foods' ordinary-course-of-business documents demonstrate that Whole Foods tracked prices, products, openings, and remodels at all food retailers. These documents also show that Whole Foods' site-selection process included consideration of every supermarket in the area it evaluated for potential entry.

Wild Oats. The former Wild Oats had 69 stores under its own name. Only 35 of these stores were large enough to be competitive according to the FTC's expert. JA491¶26. It also had 35 stores operating under the Sun Harvest Markets

and Henry's Farmers Markets banners that Whole Foods planned from the outset to sell and did in fact sell. www.food-business-review.com (follow Sun Harvest). Wild Oats was not a certified organic foods retailer. JA2885-86¶29. The company lost tens of millions of dollars in recent years and closed 18 stores since 2003, of which only 5 were relocated. JA3019¶88. It had been unsuccessfully looking for a buyer since 2004. JA2146. Its average sales per square foot were half of those of Whole Foods. JA2882-83¶21; JA2975-76¶33.

In October 2006, its senior vice president of marketing and merchandising determined that Wild Oats' prices were [redacted] higher across-the-board than Whole Foods'. JA2133-35; JA2884-85¶27. His proposal to reduce prices to match Whole Foods was rejected by the CEO. *Id.* A more detailed proposal in February 2007, estimating the cost of matching Whole Foods at [redacted] million, was rejected by the Board of Directors as prohibitive. JA2120-32; JA2088-89; JA2722; JA2884-85¶¶27-28. Wild Oats tracked the prices and "competitive intrusions" of not only Whole Foods but also Trader Joe's, Kroger's King Soopers, Safeway and others not included by the FTC in its proposed market. JA2646; JA2668-69.

Industry trends. There are 34,000 supermarkets in the United States, and many more retail grocers and specialty food outlets. Dr. John Stanton, Professor of Food Marketing at St. Joseph's University and a leading industry expert, testified that Whole Foods and Wild Oats stores are supermarkets based on their size, depth

and breadth of product selection, and ability to offer one-stop shopping for a consumer's food and grocery needs. JA3753-54¶¶15-18. He also testified that supermarkets today, including Whole Foods, compete against each other by emphasizing one or two particular attributes to attract customers (e.g., service, low prices, high-quality produce, etc.) and that this differentiation does not mean that they do not compete with other supermarkets that emphasize other attributes, rather it is precisely *how* they compete with each other. JA3754-56¶¶20-26.

The primary method by which Whole Foods competes against other supermarkets – emphasizing natural and organic products – has significantly diminished in importance as other supermarkets have responded to the sharp increase in consumer demand for natural and organic products. JA3756-57¶¶30-34. Supermarket chains like Safeway, Wegmans, Supervalu (parent of Albertson's, Shaw's, Star, Jewel-Osco, Cub, and Acme), Kroger (parent of Kroger, Smith's, Fred Meyer, Dillon's, Ralph's and King Soopers), Publix, Giant Eagle, and Bashas' have repositioned themselves to carry a significant number of branded and private-label natural and organic products. JA3757-64¶¶35-65. Manufacturers are making natural and organic products readily available to all supermarkets. 3765-66¶¶72-75. Supermarkets also are providing "experiential" shopping experiences, and adding high-quality prepared and ready-to-cook foods. JA3755-57¶¶23-34; JA3760¶¶44-45.

Based on the huge growth in demand for natural and organic products, the increased availability of natural and organic products at retail, and the ongoing repositioning by supermarkets, Dr. Stanton concluded that Whole Foods will continue to face intense competition from other supermarkets after the acquisition. He testified that Whole Foods "will face robust competition [in] just about any major area that they go into" and that "other supermarkets will fight tooth and nail for those customers." JA3836-37 . This competition will include lower prices as other supermarkets increase their existing organic lines. *Id.*

Dr. Stanton testified that supermarkets can quickly and easily expand these offerings without significant investment, that such repositioning is commonplace, and that it is well underway. JA3766-67¶¶77-78. AC Nielsen reported that by year-end 2006, in addition to organic produce, there were 14,823 organic pre-packed and pre-weighed food UPCs sold in supermarkets and warehouse and drug stores. "Growth of Organics Continues Unabated," AC Nielsen.

Whole Foods' executives identified and discussed these trends in recent years. JA2076-80 (competitors are "opening lots of new stores and are remodeling existing stores on the East Coast. Every time they open a new store or remodel an existing one with better perishables and natural foods we see a hit"); JA2007-10 (Whole Foods facing "unprecedented competition" from supermarkets).

Delhaize's Hannaford stores and Supervalu's Bigg's – unlike Wild Oats –

are USDA certified organic foods retailers. JA1564-68; JA1599; [redacted]. Virtually all chains now offer USDA certified organic and natural private-label products: Delhaize (Hannaford, Sweetbay, Bloom) offers its Nature's Place line, JA1908; Kroger (King Soopers, City Market, Ralph's) offers its Naturally Preferred and newly announced "Preferred Organics" lines, Press Release (8/8/07), [redacted]; Supervalu (Albertsons, Shaw's, Bigg's) offers its Wild Harvest line, JA3760-61¶48; Giant Eagle offers its Nature's Basket line, www.gianteagle.com (follow brand); and Safeway (Genuardi's, Vons, Dominick's) offers its "O" organic line JA1544-63; JA1775, JA1801 [redacted]

Wegmans – which offers a huge variety of high-quality produce and other fresh products, prepared foods, and private-label organic products – has expanded. www.wegmans.com (follow history). Other chains have developed new formats, such as GreenWise from Publix – offering natural and organic foods, earth-friendly products, freshly prepared food, high-quality produce, dairy, etc., JA1681; Sweetbay and Bloom from Delhaize – offering premium goods, higher quality perishables, and special customer features, JA1872, JA1874; Central Market from

HEB, http://www.central market.com, JA2804¶23; and Ralph's Fresh Fare from Kroger, the nation's largest supermarket chain, *Knight Ridder Tribune Business News*. Supermarkets throughout the country have improved the quality of their perishables, adding artisanal bakeries, more prepared foods, nicer environments, and more. JA2007-10; JA2076-80; JA3757¶32.

[redacted]

Safeway, [redacted] is in the midst of a multi-billion nationwide program to improve its stores' perishables and ambience, calling them "Lifestyle" stores and broadly expanding their inventory of natural and organic products. JA3759¶40; JA1283-95. [redacted]

[redacted]

[redacted]

The changes have even been noted by the general press. *USA Today* reported on the widespread adoption of trends Whole Foods helped popularize:

> They look like Whole Foods. They smell like Whole Foods. They even taste like Whole Foods. But they're actually part of some of the oldest and most familiar chains in the supermarket industry: Mimicking Whole Foods might not be a bad idea.

USA Today; *see also Los Angeles Times*.

These major chains, however, have a couple of thousand, rather than a couple of hundred, stores. They are better capitalized, can negotiate bigger volume discounts, and have distribution and warehouse networks that often permit bypassing distributors to buy directly from manufacturers – making them formidable competitors. JA1838-39. [redacted]

[redacted]

[redacted]

Competition faced by Whole Foods. Market research, third-party, and ordinary-course evidence demonstrate that at least all supermarkets are in the market in which Whole Foods competes. Every study shows that virtually all Whole Foods customers also regularly grocery shop at other supermarkets. A 2007 Natural Marketing Institute study concluded that, on average, Whole Foods customers spend almost 80% of their grocery dollars at other stores – even core organic customers spend more than 70% elsewhere. JA1109; JA1118. A 2005 Nielsen study concluded that the average Whole Foods "shopper makes about 7 trips per year to Whole Foods," whereas shoppers average 2 trips *per week* to all grocery stores. JA867.

Market studies have consistently found that Whole Foods customers also purchase the same or similar products at other supermarkets. *See, e.g.,* JA754-71, "Trends," NMI (Oct. 2003); JA3038¶141 (85.4% of Whole Foods' customers said they also shopped for healthy and natural products in "traditional" grocery stores); JA3052¶172 (57% of the shoppers who buy Whole Foods private-label products also buy the same type of products at Trader Joe's, 46% also buy them at Safeway, and 38% also buy them at Krogers; 46% of shoppers who buy Whole Foods organic private-label products also buy the same type of products at Trader Joe's, 47% at Safeway and 40% at Krogers); JA1175, "Health & Wellness Trends

Database," NMI (Feb. 2007) (almost 2/3 of Whole Foods customers bought organic products at "traditional" groceries in 2006 and almost 20% had bought organic products most often in a "traditional" grocery).[2] A 2006 NMI study found that both gourmet and organic shoppers had increased their purchases from "traditional" grocery stores, that 67% of Whole Food shoppers purchased organic products at a "traditional" grocery in 2006 and that almost 20% of them purchased organic products most often in "traditional" groceries. JA1170-75.

The NMI's Trends Database reports that, in 2006, 53% of organic foods sold were purchased at "traditional" groceries. *Rocky Mountain News*. And most of Whole Foods' product selection is not even organic and can be found at many stores – Breyer's ice cream, Goya beans, French's mustard, Tropicana juice, non-organic produce, bakery and prepared foods, etc. JA3754¶18.

Third-party evidence also shows Whole Foods faces serious and increasing competition from many directions. [redacted]

[2] The "traditional" grocery category did not include Trader Joe's, warehouse or specialty stores. JA1175.

[redacted] Shaw's president announced its newly remodeled store "sounds like a Whole Foods, looks like a Whole Foods, but it's a Shaw's." JA2118-19.[3]

Supermarkets the FTC excludes in its proposed product market price-check against Whole Foods and Whole Foods price-checks against them. [redacted]

[3] Kroger's, Supervalu, Safeway, Wegmans, Publix, HEB, Trader Joe's and others intervened below to protect submissions arguing that Whole Foods is a competitor.

[redacted]

[redacted]

[redacted][4]

[4] The 2007 study by Tinderbox the FTC also cites as concluding that Whole Foods

Whole Foods' competition with Wild Oats. ***Pricing.*** Just as Whole Foods competes with other supermarkets, it competed with Wild Oats, on those rare occasions when Wild Oats acted competitively. Wild Oats' ordinary-course documents show that its prices were generally appreciably higher than Whole Foods'. A Wild Oats price check of 400 SKUs in September 2006 revealed that its pricing was approximately [redacted] above Whole Foods' in every geographic area checked. JA2133-35. Comparable Wild Oats products were priced as much as [redacted] above Whole Foods' private-label products. JA2310-43.

Whole Foods' documents and market research confirm Wild Oats' conclusions, and [redacted] *See, e.g.*, JA2053-56, JA796 (October 2004 NMI Institute conclusion that, based on shopping frequency and private-label usage, "Wild Oats seems to have little effect on [Whole Foods]").

Nonetheless, there were isolated occasions when Wild Oats lowered individual prices and Whole Foods went "toe-to-toe" with it just as it had with Wegmans, and so many others. [redacted]

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will not face significant competition from "Safeway, Wal-Mart, Costco etc." based that conclusion on interviews with 36 "core" customers – those spending 70% of their grocery dollars at Whole Foods – comparing three private-label products: tortilla chips, block cheese, pasta sauce. JA2756. The study did not consider the more than 90% of Whole Foods customers who do less than 70% of their shopping at Whole Foods and would be expected to switch more willingly; even, one-third of these most loyal customers chose the three Whole Foods products on the basis of lower price. JA2755.

[redacted]

There is no evidence that Whole Foods reduced prices more in anticipation of Wild Oats' announced – but never completed – Boulder headquarters store than it had in anticipation of Safeway's Boulder store. The FTC sought to introduce expert testimony to this effect for the first time at the hearing, but with no prior opportunity for the parties to review or test the conclusions this was denied.[6] The

[5] The Portland, Maine document the FTC cites is not similar. The "squashing" impact on Wild Oats anticipated from opening a Whole Foods store there assumed only Whole Foods' regular prices and quality. JA391-92.

[6] The FTC's assertion that its expert could not work with the pricing data until then is inconsistent with a study using that data he submitted earlier and his deposition testimony that he had been working with the data on another question. JA3901-02, JA3910-11.

report was never produced to Whole Foods. The record does show that there were three other Wild Oats stores within two miles of Whole Foods' Boulder store that were not alleged to have induced Whole Foods to reduce its prices, JA3351¶46; that the planned store was at the firm's corporate headquarters, and involved a higher investment and special features; and that the planned store was only four blocks from Whole Foods. JA2933¶49. Whole Foods later discovered that the planned store would not have been as competitive as anticipated because it was badly designed (*e.g.*, loading dock 30 yards from the store, pinch points where carts could not pass, insufficient storage and refrigeration). JA2867-69¶¶36-39; JA2886-88¶¶32-36.

Economic studies of Wild Oats/Whole Foods competition. Both economists attempted to determine whether Whole Foods charged higher prices where it did not compete with Wild Oats (purportedly "monopoly" markets) than in markets where it did (purportedly "competitive" markets). Neither found that Whole Foods behaved less competitively when there was no Wild Oats. Scheffman compared Whole Foods' prices in each and discovered that Whole Foods' prices in markets without a Wild Oats store were not systematically higher than in markets with one, and vice versa. JA3111-12¶314, JA3103¶292.[7]

[7] He used register data from June 9, 2007, which provided prices for all items whether or not sold that day and included all promotional prices except coupons, which Whole Foods rarely uses. Complete register data is not maintained long-

The FTC's expert studied the same type of question, but compared profit margins rather than prices.[8] His analysis showed that the presence of a competing Wild Oats store in the vicinity made no statistically significant difference in Whole Foods stores' profit margins. He conceded that what he found (0.7% higher where there was no Wild Oats store) was not statistically different from zero at the confidence level most commonly used in scientific studies and recognized by the Federal Judicial Center. Reference Manual on Scientific Evidence (194). That is, his analysis showed no reason to believe that margins at Whole Foods stores were anything other than the same, whether or not a Wild Oats store is nearby. JA507¶66.[9]

These findings were corroborated by additional economic studies from both sides analyzing entries by Whole Foods into markets that already included Wild Oats. Both found a decline in Wild Oats sales correlated with Whole Foods' entry, suggesting – at most – that Whole Foods is a competitor of Wild Oats, although

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term, so it was not available from prior years. JA3689.

[8] However, his figures were derived without adjusting for variables that cause total profit margins to vary even when prices remain the same. JA503¶55, JA44.

[9] Murphy also compared margins for individual departments, although the proposed product market was not any individual department and he did not address competition from other retailers for those product categories, such as greengrocers, farmers markets, seafood markets, etc., that might account for any differences. JA508¶67. Still, seven of the nine departments did not yield statistically significant differences and the other two were only barely above that level: seafood (1.7%) and produce (2.1%). *Id.;* JA52.

exactly how successful was not established because neither expert attempted to isolate which Wild Oats sales actually shifted to Whole Foods and which elsewhere. But Whole Foods' economics expert, Dr. David Scheffman, former director of the FTC's Bureau of Economics, showed that this shift was not critical to *Whole Foods'* success, because even if all sales Wild Oats lost went to Whole Foods, Whole Foods' overall sales overwhelmingly were attracted from stores outside the FTC's market definition, such that those stores imposed significant competitive restraints on Whole Foods.

Dr. David Scheffman studied Whole Foods entries affecting 13 Wild Oats stores for which there was pre-entry and post-entry sales data.[10] JA3014-15¶74. Looking at long-term results, he found an average 18% reduction in Wild Oats sales where the Wild Oats store remained opened following Whole Foods' entry. JA3019¶87. Sales reductions in the 13 affected Wild Oats stores ranged from 7.9% to, theoretically, 100% where the Wild Oats store eventually closed. JA3131. The FTC's expert Dr. Kevin Murphy reported on two of these – Ft. Collins CO and West Hartford CT, reporting shorter-term effects. JA504-05¶¶58-59. How much of Wild Oats' declines should be attributed to Whole Foods is unclear. Neither expert attempted to gauge the impact on Wild Oats of other entering stores or of competitive responses to Whole Foods by existing stores.

[10] No such data existed for the other four entries.

Other new stores entered at the same time Whole Foods did in both markets Murphy studied: King Soopers in Ft. Collins and Trader Joe's in West Hartford. JA3466-67¶51; JA3476¶87; JA3922-23; JA49.

Dr. Scheffman also determined the percentage of Whole Foods sales that came from Wild Oats versus other supermarkets not in the FTC's market by comparing Whole Foods' sales to Wild Oats' prior sales. He determined that, even assuming that every lost Wild Oats sale was won by Whole Foods (an unrealistic but conservative assumption), roughly 90% of Whole Foods' sales must have been attracted from other stores.[11] JA3131. That is, virtually all of Whole Foods' customers had been willing to make these purchases at supermarkets outside the FTC's proposed market – despite the availability of a Wild Oats – and presumably would be willing to resume making the same purchases at those other supermarkets if Whole Foods ever disappointed them in terms of either price or quality, or if those other supermarkets offered the same or better options.

Scheffman's findings are also consistent with market research studies, which conclude that Whole Foods' base has evolved into "a larger and more diverse, 'conventional' consumer base" and that its sustainability depends on continuing to attract this wide range of customers. JA1097.

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[11] As above, this figure reflects longer-term data that does not include markets where Wild Oats eventually closed. JA3016¶78. Considering all 13 markets, the median gain from other stores was 88%.

Murphy undertook several studies to determine whether Whole Foods faced substantial competitive pressure in the absence of Wild Oats. Contrary to the FTC's assertion that he discovered a far greater impact on Whole Foods from Wild Oats than from any other retailer, FTC Br.15, Murphy never studied whether Wild Oats imposed competitive pressure on Whole Foods. Wild Oats never entered a market with an existing Whole Foods store, JA506¶63, and he did not report on any other test of Wild Oats as a competitor, such as comparisons of pricing or quality or comparing Whole Foods' pricing before and after Wild Oats closed a nearby store. JA502¶52.

Instead, he looked at entries by a different firm in markets in which Wild Oats did not compete – North Carolina-based regional chain Earth Fare, one of only four chains included in the FTC's proposed product market – which had entered three North Carolina markets that already included a Whole Foods.[12] JA502¶52. The FTC reports Murphy's findings that Whole Foods' sales dropped almost [redacted]

[12] The FTC's characterization of Earth Fare entries as analogous to Wild Oats entries is unsupported by any evidence that they were equivalent competitors. FTC Br.17.

[redacted]

Murphy also purported to compare the impact of "conventional" supermarkets on Wild Oats and Whole Foods. JA500-02¶¶49-53. He did not, however, study the impact of any specific supermarket such as a Wegmans, Hannaford, or Safeway Lifestyle on either Wild Oats or Whole Foods, as he had with Earth Fare. Instead, he studied subcategories of supermarkets as groups. JA595-96. He considered a few banners separately, lumped "conventionals" together in one group, but excluded Wegmans and several others, which he lumped together in one group as gourmet supermarkets. *Id.* The impact on Whole Foods from the gourmet supermarket group was a [redacted] sales decrease. *Id.* Vitamin Cottage depressed sales at Whole Foods by [redacted], at Wild Oats by [redacted]; Sunflower depressed sales at Wild Oats by [redacted] Trader Joe's drove sales down at Wild Oats by [redacted] and at Whole Foods by [redacted]. *Id.*[13]

The record also includes evidence that the impact of Safeway's Lifestyle store in Boulder, for example, [redacted]

[13] Contrary to the FTC's claim that the district court "ignored" most of Dr. Murphy's work and alleged weaknesses in Dr. Scheffman's work that, it says, it explained to the court, FTC Br.21-22, the court asked dozens of questions about the two experts' work, addressing these to both the experts themselves and to counsel. JA43; JA44-45; JA47; JA48; JA57-58; JA58-59; JA78-JA80; JA92-JA93; JA101-02; JA103; JA112-13; JA104; JA107; JA180.

[redacted]

Anticipated impact of merger on competition. ***Wild Oats' value.*** The evidence demonstrates that the primary value of Wild Oats to Whole Foods is Whole Foods' ability to build on Wild Oats' existing construction and customer base. It is undisputed that Wild Oats achieved only half of Whole Foods' sales per square foot, and therefore considerable gains could be expected under Whole Foods management. It is also undisputed that Whole Foods increased sales at the eight other chains it acquired – making previously money-losing chains profitable – and that Whole Foods successfully turned around two failed Wild Oats stores. *See supra* at 4.

The evidence showed Whole Foods also expected to gain efficiencies: reducing Wild Oats' corporate costs by [redacted], increasing purchasing power, and improving distribution systems. JA2165-JA2222; JA2977-78¶37. In addition, Whole Foods anticipated value from selling Wild Oats' 35 Sun Harvest and Henry's stores at a profit to a third party. Whole Foods hired independent financial advisors to evaluate whether the 23% merger premium demanded by Wild Oats was financially reasonable; they concluded it was – without any post-merger price increases. JA2165-JA2222.

There was no evidence of real-life supracompetitive price increases by

Whole Foods where the FTC's product market definition would have predicted it – not in the four markets where Whole Foods continued to operate a store after Wild Oats exited;[14] not after Whole Foods acquired any of the other eight chains; and not after Whole Foods took over two failed Wild Oats stores. Instead, the evidence showed that Whole Foods operated acquired stores efficiently and successfully.

Whole Foods' internal documents show no intention to raise prices or lower quality. Rather, they confirm the opposite. Co-president Gallo explained to regional presidents that the merger presented an opportunity to advertise Whole Foods' "great prices":

> The concern in any merger is that prices may go up in acquired stores. In fact, we know that WOs prices are higher than ours and we will be bringing down quite a few prices. We could use this opportunity to shout out either on a local, regional or national basis our great prices.

JA2226-27.

Transfer estimates. Before the merger, Whole Foods considered closing some Wild Oats stores that were not competitive, initially 30 stores now reduced to 17, with other smaller stores repositioned to compete differently. JA353; JA690. Even the FTC's expert considered 34 of the 69 Wild Oats stores too small to be competitive as supermarkets and therefore irrelevant for antitrust purposes.

[14] The court noted the failure of the FTC to offer such evidence from Ft. Collins, JA251, although its expert had studied that data. JA3908-09. A Whole Foods' executive testified that its prices did not increase, JA480. Another testified that Whole Foods had never raised prices after a nearby Wild Oats closed. JA2934-35¶52.

JA482¶1n.2; JA484¶8n.3;JA491¶26; JA499¶48; JA3905.

If Whole Foods had expected that closing Wild Oats stores would create monopolies for Whole Foods, it would have estimated consistently that the transfer of the vast majority of Wild Oats' sales would shift to Whole Foods. Instead, its estimates predicted that more than half of Wild Oats' sales from the closed stores would go elsewhere. The estimates of retained sales varied significantly market-by-market – from [redacted] JA353. The average estimate of retained sales was less than [redacted], with Whole Foods expecting to win [redacted] of former Wild Oats' sales from only [redacted] of the 30 stores then considered for closure. JA2176; JA353.

Furthermore, the estimates were not higher where Whole Foods would become the only premium natural and organic supermarket than where it would face competition from stores within the FTC's putative product market. Indeed, the lowest estimates were for markets where Whole Foods would have been the only premium natural and organic supermarket remaining – [redacted] – and its highest estimate (that [redacted] of former Wild Oats sales would be diverted to Whole Foods [redacted]

[redacted]

The testimony the FTC cites to conclude that the estimates "correlated strongly" with prior experience, FTC Br. 44, actually states that the estimated gain from Wild Oats' closed store in Ft. Collins was only [redacted] of estimated Wild Oats sales [redacted]

Critical loss study. The FTC's own guidelines provide that the applicable test to determine the relevant product market is whether a hypothetical monopolist of the proposed market will be able profitably to impose a small but significant and non-transitory price increase. Guidelines §1.1. Dr. Scheffman applied this test by analyzing whether premium natural and organic supermarkets would lose enough sales from increasing prices even 1% that the result would be a net loss. He concluded that a hypothetical monopolist could not profitably undertake such a price increase and therefore that premium natural and organic supermarkets could

[15] The FTC mischaracterizes the district court as citing only the lowest estimates. The court considered the full range including the overall average, but noted the discrepancy between the FTC's theory and Whole Foods' low expected transfer estimates for markets where Whole Foods would become a monopolist according to the FTC. JA276.

not constitute a relevant product market.[16] JA3030¶121; JA3482¶¶104-05.

The analysis requires estimation of both critical loss (percentage of sales lost as a result of a price increase beyond which the increase would be unprofitable) and actual loss (percentage of sales lost that would actually occur in response to the price increase). Because actual loss is a prediction, it must be estimated. Scheffman considered factors affecting consumer behavior, from a wide range of record evidence, including 47 different market studies and many other documents produced in the ordinary course of business. They showed that: (1) Whole Foods and Wild Oats shoppers are price-sensitive, (2) such customers already are cross-shopping extensively at other supermarkets, (3) Whole Foods/Wild Oats customers already are shifting purchases to other supermarkets and can accelerate this shifting at no cost without changing their shopping patterns, (4) those other supermarkets are vigorously competing for these shoppers through repositioning and expanded product offerings, and (5) Whole Foods' recognition of this competitive threat is evidenced by, among other things, its extensive price-checking and monitoring of other supermarkets. Because these factors indicated significant demand elasticity, he concluded Whole Foods could not impose a significant unilateral post-merger price increase profitably.

No one had ever before even postulated a market for premium natural and

[16] The FTC has not even argued that Whole Foods could lower quality without driving its customers to other supermarkets.

organic supermarkets, so there were no data showing consumer response to relative price changes between these stores and other supermarkets or grocery retailers from which to estimate actual loss. Murphy's criticism of the critical loss study therefore could not rely on historical loss data either. Rather, he projected loss based on Whole Foods' hypothetical transfer estimates from closing particular Wild Oats stores. JA636-38¶32. He did not address the fact that, even as estimates, these assumed no price increases by any premium natural and organic supermarket. Instead, he simply assumed the transferring shoppers would stay with Whole Foods regardless. He also did not consider how many *existing* customers Whole Foods would lose if it raised prices. Thus, he did not estimate actual sales losses resulting from raised prices at all and therefore cannot and does not present an alternative conclusion as to whether a significant and non-transitory post-merger price increase would be profitable.

Post-merger. Whole Foods consummated its acquisition of Wild Oats on August 30, two weeks after the district court ruled, almost a week after this Court denied the FTC's motion for an injunction pending appeal, and just barely before the binding merger and financing agreements expired on August 31. Whole Foods Press Release, "Whole Foods Market Closes Acquisition." The FTC's assertion that this occurred "as soon as the district court ruled," FTC Br.55, is untrue. Soon after, Whole Foods sold to Smart & Final 35 of Wild Oats' 109 stores operating

under the Sun Harvest and Henry banners per its long-disclosed contract to do so. Whole Foods Press Release, "Whole Foods Market Completes Sale." Smart & Final is not a party to this action.

Since the merger, Whole Foods has closed 10 additional Wild Oats stores, cancelled Wild Oats' supplier contracts, terminated leases, and largely dismantled Wild Oats' distribution system. Whole Foods has replaced these with its own product mix, its own suppliers of fish and seafood, meat, bakery goods, produce, cheese, prepared foods, grocery and personal care items, and introduced Whole Foods' holiday programs. Whole Foods is also renovating the remaining former Wild Oats stores' interiors, packaging, aprons, equipment, signage and displays to look like Whole Foods' stores; converting their operating systems to Whole Foods' systems; replacing store leadership; transferring many former Wild Oats employees and retraining remaining ones. The signs on the doors of the remaining stores Whole Foods acquired are being replaced, as they are transformed into stores Whole Foods is willing to put its name on. This process is scheduled to be nearly complete by the end of the year. JA689-90, JA692, JA696, JA701.

Sales at former Wild Oats stores began rising almost immediately, up 6.9% in the first seven weeks of FY2008 (October/November), and are projected to grow at 10% for the first year. JA691, JA697; 9/30/07 10-K. Prices at former Wild Oats stores, however, have been reduced throughout the stores to Whole Foods' levels,

while entry-level and other employees' wages and benefits have been raised to Whole Foods' levels. JA691, JA693.

COUNTERSTATEMENT OF STANDARD OF REVIEW

The applicable standard of review is abuse of discretion. *See, e.g., FTC v. H.J. Heinz Co.*, 246 F.3d 708, 713 (D.C. Cir. 2001) ("We review a district court order denying preliminary injunctive relief for abuse of discretion."); *see also* 15 U.S.C. §53(b) (injunction "may" be granted).

SUMMARY OF ARGUMENT

1. This appeal has become moot. Whole Foods' acquisition of Wild Oats rendered the only relief at issue unavailable. In addition, subsequent sales, closings, and transformations of Wild Oats' former stores preclude effective relief.

2. The district court performed the role Congress delegated, articulating and applying the standard of review this Court prescribed in *Heinz*. It did not insulate market definition from that standard. Rather, it carefully articulated that standard as the measure of the FTC's burden of proof under 13(b) and then evaluated whether the FTC had met it.

3. The district court's conclusion that, in light of all the evidence, the FTC had not raised serious, substantial questions making its proposed market definition fair ground for additional investigation by the FTC, and ultimately the Court of Appeals, is unassailable. The FTC was unable to offer the evidence that

would have been available if premium natural and organic supermarkets were, in fact, a distinct antitrust market. Overwhelming real-world and analytical evidence demonstrated that they are not.

4. The FTC also did not raise any separate serious or substantial questions as to whether Wild Oats' removal from the marketplace likely could have substantial adverse competitive effects. The evidence, including testimony from the FTC's expert, was consistent that Wild Oats did not impose any substantial competitive pressure on Whole Foods, in the form of prices, quality, or innovation, while exhaustive evidence demonstrated that the competitive constraints faced by Whole Foods come from other supermarkets.

5. Additional investigation in an FTC proceeding will not resolve the criticisms the FTC asserts afflict the record below or change the conclusion that this merger does not risk a substantial lessening of competition in any line of commerce.

ARGUMENT

I. THIS APPEAL IS MOOT.

By the FTC's own assurances to this Court, the only relief sought below and the only relief at issue on appeal is no longer available. The FTC moved for a preliminary injunction limited to "restraining the consummation of any acquisition by Whole Foods of Wild Oats." FTC TRO/PI Mot. 1. The FTC confirmed to this

Court that the district court's denial of that preliminary injunction "denied all relief sought by the Commission in the district court and resolved all issues before that court." FTC Br.1. It is undisputed that this relief is no longer available because Whole Foods has acquired Wild Oats. Thus, the only question before the Court is advisory.

The FTC's decision below not to seek any relief other than the injunction blocking the acquisition was no error in drafting. The FTC even represented to the district court that blocking the acquisition was necessary to "enable the Commission to order effective antitrust relief after an adjudication on the merits of the case." FTC TRO/PI Motion 2. If, as the FTC now argues, effective relief can be ordered even though the acquisition has been consummated, then the injunction was not necessary. The FTC cannot have it both ways and should be forced to live with its representations below. It is too late for the FTC to reverse field and now claim that it is entitled to relief that it chose not to seek below.

In any event, effective relief, which the FTC variously defines as "reconstituting Wild Oats" or "effective reconstruction of Wild Oats," FTC Br.57, is no longer available. The 35 Wild Oats stores operating under the Harvey's and Sun Harvest label, along with various distribution assets, were sold to Smart & Final, an entity that is not a party to this action. Other stores have been closed, and leases and other contracts (again with entities not party to this action) have been

terminated.

This Court has previously recognized that lawful consummation of a merger the FTC sought to enjoin moots the case. *See FTC v. Owens-Illinois, Inc.*, 850 F.2d 694 (D.C. Cir. 1988) (finding that an appeal "from an order of the district court denying [the FTC's] motion for a preliminary injunction, has become moot as a result of the consummation of the merger sought to be enjoined."). This appeal is in the identical procedural posture.

The fact that the FTC filed with this Court a suggestion of mootness in *Owens-Illinois*, but disagrees here, is irrelevant. Parties cannot moot an appeal by agreement. The FTC may voluntarily withdraw an appeal, but mootness is a question of constitutional law that a court must independently determine. Moreover, in *Owens-Illinois*, two glass container manufacturers with sizeable independent facilities had just merged. *Owens-Illinois* thus necessarily held that the FTC's appeal from denial of its request for a preliminary injunction was moot *regardless* of the Court's power to freeze Owens-Illinois' further integration of its acquisition.[17]

The FTC fails to cite, much less distinguish, *Owens-Illinois* and turns

[17] *See also FTC v. Beatrice Foods Co.*, 587 F.2d 1225, 1226 (Bazelon, J.) (abstaining from vote on the FTC's suggestion for rehearing *en banc*, given the "problems of legal mootness" after the merger had been consummated); *FTC v. Food Town Stores, Inc.*, 539 F.2d 1339, 1343 (4th Cir. 1976) (noting that, if the merger closes, "any [13(b)] proceeding . . . for a preliminary or permanent injunction will be rendered moot").

instead to inapposite cases. For example, *United States v. W.T. Grant Co.*, 345 U.S. 629 (1953), did not – as the FTC intimates – suggest that actions brought by government agencies cannot become moot. *W.T. Grant* merely explains that voluntary cessation of allegedly unlawful conduct does not moot an enforcement procedure that asks to enjoin future violations. *Id.* at 632. Other decisions it relies on merely found appeals not moot when the status quo ante *could* be restored – *Indus. Bank v. Tobriner*, 405 F.2d 1321 (D.C. Cir. 1968) (realty could be returned) – or when at least *some* of the relief requested could still be granted – *see, e.g., Byrd v. EPA*, 174 F.3d 239, 244 (D.C. Cir. 1999) (requested declaratory relief remained available and useful to Byrd); *Gull Airborne Instruments, Inc. v. Weinberger*, 694 F.2d 838 (D.C. Cir. 1982) (requested injunction against further performance might still be available to the disappointed bidder if the project had not been fully or satisfactorily completed) (remanding for inquiry into its status).

This Court's 1981 decision in *FTC v. Weyerhaeuser* also cannot help the FTC here. First, the question on appeal – whether the district court was empowered to issue a hold-separate order in a Section 13(b) proceeding – was fully preserved and presented on appeal because the validity of that order was what the FTC was challenging. 665 F.2d 1072 (D.C. Cir. 1981). In addition, the question was capable of repetition while evading review. In contrast, the only relief at issue in the instant appeal is the preliminary injunction the FTC requested

and the district court denied.

Second, *Weyerhaeuser* based its mootness decision on its determination that it *was* possible to "return to the status quo ante" in that case. *Id.* at 1077 (noting that all relevant parties were before the court). That is not true here. This Court does not have all the relevant participants before it and cannot restore all of the acquired assets because they are now in the hands of third parties. Without those assets, a reconstituted Wild Oats would have significantly less purchasing power, and thus be even less able to compete than the former Wild Oats.

In further contrast to *Weyerhaeuser*, the court below did not issue a hold separate order and Whole Foods has not held Wild Oats separate. Most of the remaining former Wild Oats are or will be completely transformed into Whole Foods stores by the time this appeal is resolved. The others are or will be closed, and leases to the properties terminated. The less visible infrastructure necessary to operate a supermarket chain – supplier contracts, distribution systems, operating systems – have already been dismantled. It will not be possible to reconstitute what Wild Oats offered to the public before the merger. Thus, effective relief is no longer available, even if the FTC *had* asked for it.

The FTC's own actions demonstrate its belief that meaningful relief cannot be granted so many months after this merger took place. If it had believed such relief could be obtained, it would have continued its own administrative action,

which could have provided the FTC itself with the power to order Whole Foods to stop further integration of Wild Oats if this was merited. *See* 15 U.S.C. §45 (FTC empowered to issue cease and desist orders if it finds a violation of the Clayton Act). Six months have already elapsed and further time will pass before this appeal is resolved.

The FTC apparently determined it could not obtain meaningful relief from an administrative action if the merger was consummated while the action was pending, and *sua sponte* stayed its own proceeding at the pleadings stage "as a matter of discretion." JA1968-69. The FTC has not reopened its proceeding, even after failing to obtain a preliminary injunction from the district court or this Court. The FTC's decision to stay its own administrative case could not reflect any expectation that this Court will provide partial relief much faster than the FTC itself could. The FTC has not even asked this Court to do so, even though expedited consideration is the norm for appeals in this type of merger case.

This Court should dismiss this appeal as moot because the only relief sought is no longer available, and effective relief could not be fashioned in any event.

II. THE COURT BELOW ARTICULATED AND APPLIED THE SAME STANDARD THE FTC ARGUES IS APPROPRIATE HERE.

Neither the statute nor this Court's decisions provide any basis for overturning the decision below based on the standard of review the court applied. Contrary to the FTC's intimations, Congress did not grant it authority in Section

13(b) of the FTC Act to obtain a preliminary injunction *in advance of finding unlawful conduct* simply because it seeks one. Congress placed the judiciary in the role of gatekeepers. Congress also imposed the burden of proof on the FTC and established a public interest standard that *requires* the court to consider the likelihood that the FTC will be able to establish a violation of the Clayton Act to its own satisfaction and that of the Court of Appeals on review.

The FTC's articulation of the appropriate standard of review bears an uncanny resemblance to the standard the district court itself articulated, at length, in its opinion. The FTC's allegation that the district court insulated the question of product market definition from that standard, in contrast, bears no resemblance to anything that court said or did.

A. The FTC Misconstrues the Role of the District Court.

The FTC appears to suggest that the primary adjudicative authority over whether a merger violates the Clayton Act that Congress conferred in Section 5(b) of the FTC Act automatically entitles it to a preliminary injunction to prevent a merger it has not yet found unlawful. Congress, however, expressly chose not to delegate that power to the FTC.

Section 5(b) permits the FTC to issue a cease and desist order only *after* it finds a violation. To obtain such an order in advance, the FTC must apply to a district court. 15 U.S.C. §53(b) (requiring the FTC to "bring suit in a district court

of the United States to enjoin any act" it suspects is unlawful). Congress further expressly placed the burden of making a "proper showing" that an injunction would be in the public interest on the FTC, and emphasized the court's role in "considering the Commission's likelihood of ultimate success." *Id.* Finally, Congress accorded the district court discretion in determining whether to grant the requested injunction if a proper showing is made. The district court's independent adjudicatory role is confirmed by the legislative history. The Conference Report on the bill that became section 13(b) states that the law "define[s] the duty of the courts to exercise independent judgment on the propriety of issuance of a temporary restraining order or a preliminary injunction" and "is intended to codify" decisional law establishing this principle. H.R. Rep. No. 624, 93d Cong., 1st Sess. 31 (1973), U.S. Code Cong. & Admin. News 1973, at 2533.

Heinz confirms that 13(b) compels the court to exercise its discretion to weigh all the evidence, not just the FTC's – even when the FTC's prima facie case is far stronger than what the agency presented here – before determining whether serious and substantial questions exist. 246 F.3d at 716. That is what the district court did here. JA308 ("Considering the voluminous factual record taken as a whole"). Indeed, in *Heinz* it was conceded that the FTC had established a prima facie case. The case involved a merger to duopoly in an undisputed market, where the district court found entry to be "difficult and improbable," and concentration so

high that anticompetitive harm was to be presumed "by a wide margin." 246 F.3d. at 716-17. This Court's reversal of the district court's denial of an injunction was not based on the strength of the FTC's prima facie case alone, but on a weighing of the entire record, using the *Baker Hughes* framework as the measure of what the FTC would ultimately have to show to prevail. *Id.* at 717 n.11 (*citing United States v. Baker Hughes Inc.*, 908 F.2d 981 (D.C.Cir. 1990). Thus, this Court has already rejected any suggestion that whether the FTC has met its burden of persuasion can be answered by reference to the FTC's evidence alone. This instead involves a weighing of all the record evidence.

It is unclear exactly what concerns the FTC about the district court's ending its review after finding "no likelihood" that the FTC could ultimately prove that the proposed merger may substantially lessen competition. FTC Br.33-34. The FTC's claim that this "flies in the face" of the statute is inconsistent with the statutory text, which requires courts to consider whether the FTC is likely to succeed. To the extent the FTC is hinting that the court should also have weighed the equities, there were no additional equities to weigh *in favor* of an injunction and no point in piling on by weighing equities asserted *against* an injunction, as the court recognized. JA308.

The only equity proffered by the FTC – its contention that the proposed merger may substantially lessen competition – collapsed when it failed to show

any serious likelihood that it would ultimately prove this is true. Surely, the FTC cannot be arguing that the public interest requires a preliminary injunction *regardless* of the likelihood that the challenged merger will be found to violate Section 7. Nothing in the statute even *authorizes* courts to issue preliminary injunctions on that basis. The statutory prerequisite is "a proper showing." §53(b)(2).

B. The Standard the FTC Urges Is Identical to the District Court's.

The FTC's quarrel with the legal standard the district court applied suffers from its inability to identify any standard the court should have adopted that it did not or any standard it adopted that it should not have.

The FTC's emphasis that a public interest standard applies, not the traditional equity standard, is in complete unison with the district court. JA221; JA308. (FTC request for injunction must be judged under a public interest standard, which "is broader than the traditional equity standard that is normally applicable to requests for injunctive relief").

The FTC's insistence that the court may not decide the merits of the antitrust question is, again, the same as the district court's. JA221 ("The district court is not authorized to determine whether the antitrust laws have been or are about to be violated.") (quotations omitted).

The FTC's further insistence that its burden is that set forth in *Heinz* – to

show questions on the merits so serious and substantial that they are fair ground for thorough investigation by the FTC in the first instance and ultimately by the Court of Appeals – is again the same standard the district court adopted. JA222 (FTC's burden is met if it meets *Heinz* standard); JA308.

Finally, the FTC's position that it need not show a mathematical probability of success or that the merger will in fact substantially lessen competition is, yet again, the same as the district court's. JA223 (FTC need only show it is likely to succeed in establishing that there is a reasonable probability the proposed merger will substantially lessen competition).

Thus, rather than arguing for a different standard of review, the FTC simply presents additional support for the standard the district court adopted.

C. The District Court Did Not Subject Product Market Definition to a Different Standard.

The FTC's efforts to tease out a standard articulated by the district court that is, in any way, different from the one articulated in *Heinz* is baseless. The district court's understanding that the FTC must meet "its burden to prove that 'premium natural and organic supermarkets' is the relevant product market," JA280, is no different than the statute's textual requirement that the FTC make "a proper showing" to obtain a preliminary injunction, 15 U.S.C. §53(b)(2). Indeed, in enacting the statute, Congress explained that the "proper showing" specified in the statute "relates to the standard of proof to be met by the Federal Trade

Commission." Conf. Rep. at 31.

What the FTC must prove is a separate question, but this is also settled law that the district court carefully followed. JA221, JA308 (adopting and applying the *Heinz* standard). The FTC must show likelihood of ultimate success. *Heinz* explains that the court's task is to evaluate "the Commission's showing of likelihood of success." 246 F.3d at 716. *Weyerhaeuser* also refers to the "FTC likelihood of success showing." 665 F.2d at 1082.

To evaluate the likelihood that the FTC will ultimately succeed on the merits in its administrative proceeding and on appeal, however, the district court needs to know what the FTC must establish to do so. The district court, quoting at length from *Heinz*, followed *Baker Hughes* in finding that the FTC would have to prove that the merged firm would have an undue share of a properly defined relevant market, that the merger would result in a significant increase in concentration in that market, and, if defendants submitted evidence of no anticompetitive effect, the FTC would have to counter with proof that the merger was likely to have anticompetitive effects. JA228. The FTC appears to have confused the court's discussion of what the FTC would ultimately have to establish – *i.e.*, the elements of a Section 7 violation, as set forth in *Baker Hughes* – with the standard the court held applicable to the preliminary injunction proceeding.

The district court, however, was not similarly confused. It *never* determined

that the FTC's burden to prove the relevant product market is subject to a standard other than the *Heinz* "serious, substantial" standard. Rather, the court first spelled out the preliminary injunction standard in detail – the same standard the FTC urges – including making clear that the "'FTC is not required to *establish* that the proposed merger would in fact violate section 7 of the Clayton Act.'" JA221 (quoting *Heinz*). Then the court expressly moved on to a discussion of the FTC's future burden of succeeding on the merits under Section 7 – including proving the relevant product and geographic markets and likely anticompetitive effects – in order to assess the likelihood that the FTC would ultimately succeed in meeting it. JA224-28.[18] In doing so, the court was again following *Heinz*, which expressly noted: "Although *Baker Hughes* was decided at the merits stage as opposed to the preliminary injunctive relief stage, we can nonetheless use its analytical approach in evaluating the Commission's showing of likelihood of success." 246 F.3d at 716.

Most importantly, the district court applied the *Heinz* standard. Contrary to the FTC's assertions, the district court did not fail to assess whether there was "fair ground" for administrative adjudication and appellate review; it expressly concluded there was no "fair ground" because the FTC had not raised sufficiently

[18] The FTC does not, because it cannot, suggest that the district court misconstrued the elements of a Section 7 analysis. The court closely followed both agency guidelines and this Court's decisions.

serious and substantial questions going to the merits. JA308. The district court denied the requested preliminary injunction because it concluded: "There is no substantial likelihood that the FTC can prove its asserted product market and thus no likelihood that it can prove that the proposed merger may substantially lessen competition." *Id.* This *is* the standard articulated by *Heinz* and urged by the FTC – not a 50% or greater probability standard, or a Section 7 standard, or any other inapplicable standard.

III. THE FTC HAS SHOWN NO LIKELIHOOD OF ULTIMATELY ESTABLISHING ITS PROPOSED PRODUCT MARKET.

It is undisputed that the merger will not substantially lessen competition if the relevant market includes even other supermarkets, much less all food retailers. Post-merger Whole Foods owns fewer than 260 of the 34,000 supermarkets in the United States. Thus, a critical question is whether the relevant product market for analyzing this merger is the much smaller subset of all supermarkets invented by the FTC and dubbed "premium natural and organic supermarkets." The FTC, however, has not – and cannot – come close to showing a likelihood that it can ultimately establish its invention as a relevant market.

A. The FTC's Proposed Market Definition is Incapable of Application.

A fundamental problem with the FTC's market definition is that it cannot be applied. Not even the FTC could offer a consistent explanation of what

distinguishes premium natural and organic supermarkets from other supermarkets. Multiple unwieldy, amorphous multi-factor definitions were submitted by the FTC, including such attributes such as: focus on high-quality perishables, natural and organic products, emphasis on perishables rather than dry goods, higher levels of customer service, emphasis on authenticity, third place as an alternative to work or home, lifestyle brand, confidence in provision of products that are good for the consumer, unique environment, meets core values, and superior store experience. And even the FTC does not contend that each store of the only four chains it deems to be premium natural and organic supermarkets has each of these attributes or that excluded retailers lack them.

Moreover, none of the characteristics of an antitrust market as identified by Supreme Court precedent are present. The FTC could not show that these stores offered a unique inventory, both because most of their offerings are not organic and because they face substantial competition in natural and organic offerings from other supermarkets. The FTC could not show distinct customers because numerous market research studies make clear that virtually all of their customers regularly shop and spend most grocery dollars at stores outside the FTC's proposed market, and shop there for the same products purchased at Whole Foods. Finally, the FTC does not even contend that stores within its market compete like office superstores (e.g., Staples), by offering a dramatically larger and broader selection

of groceries in one place than other supermarkets. It is undisputed that both Whole Foods and Wild Oats are still playing catch-up in that area. *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962); *United States v. E.I. du Pont de Nemours & Co.*, 353 U.S. 586 (1961).

B. Market Research, Third-Party and Ordinary-Course Evidence Overwhelmingly Show There Is No Separate Market.

The very characteristics that the FTC uses to define its proposed market are among the most significant current trends for the entire supermarket and food retailing industry. It is not necessary to rely on any post-litigation declaration to reach this conclusion. It is evidenced by dozens of market research studies, industry expert testimony, documents and testimony from third-party food retailing executives and manufacturers. It is also confirmed by the ordinary-course documents of the parties.

Post-merger, Whole Foods is not alone in a market shared by only one regional and one local chain as the FTC asserts. Whole Foods faces competition from every direction. Having attracted almost 90% of its sales from shoppers who could have, but did not, choose to shop at a nearby Wild Oats, Whole Foods cannot survive now without continuing to attract them, a prospect inconsistent with supracompetitive price increases or reduced quality. This conclusion derives from real-world evidence – Whole Foods' entry into markets that already included Wild Oats – rather than estimates, though the estimates the FTC touts lead to the same

conclusion.

Market research studies show that Whole Foods customers are already shopping at food retailers not regarded as premium natural and organic supermarkets more often and more extensively than at Whole Foods, and that they purchase the same or similar items there that they purchase at Whole Foods. It is costless for customers to switch, and affordable for the other retailers to encourage them to skip Whole Foods altogether and buy what they want where they already are. Far from being able to raise prices and lower quality post-merger, Whole Foods has been lowering prices and investing in improvements both before and after the merger, and will need to continue to find ways to do so. Again, although the declaration testimony of Whole Foods and Wild Oats executives also support these conclusions, it is unnecessary to rely on them at all. The uncontroverted evidence of consumer behavior is sufficient.

The FTC's inferences reaching contrary positions do not withstand scrutiny. There is no basis for inferring from the evidence that Wild Oats exerted unique competitive pressure on Whole Foods. The FTC attempts to make much of the mundane fact that Whole Foods has, on occasion, actively competed with Wild Oats, while disregarding evidence that Whole Foods has regularly and continuously actively competed with Trader Joe's, Wegmans, Baker's, King Soopers, Byerly's, Giant Eagle, Harris Teeter, Albertsons, and others. That Whole

Foods occasionally competed hard against Wild Oats has no significance in a product market where Whole Foods competed and competes hard against so many others.

In addition, Whole Foods' history of successfully competing against Wild Oats reveals only that Whole Foods is a better competitor. Other retailers must have competed successfully against Wild Oats before Whole Foods entered the 13 Wild Oats markets it entered because Whole Foods won almost 90% of its sales from them, not from Wild Oats. And other retailers must have competed successfully with Wild Oats in the 56 markets Whole Foods never entered, or Wild Oats would have been printing money rather than losing it and unable to attract merger prospects.

The FTC's leap to assuming anticompetitive plans from Whole Foods' decision to meet Wild Oats' price even though the company was struggling is belied by Whole Foods' established history of turning around struggling companies and making them profitable, and by the based-on-undisputed-numbers opportunity here to double Wild Oats' sales while significantly cutting its costs. The FTC submitted no prior price increases by Whole Foods after its many prior acquisitions, after its subleasing two failed Wild Oats stores, or after Wild Oats closed a nearby store, because that is *not* why or how Whole Foods has survived.

IV. THE FTC HAS SHOWN NO LIKELIHOOD OF ESTABLISHING THE MERGER MAY SUBSTANTIALLY LESSEN COMPETITION.

If Wild Oats had imposed a substantial competitive constraint on Whole Foods, Whole Foods' prices and margins would have been significantly and systematically different where it did not face Wild Oats as a competitor than in markets where it did. Staples, for example, charged 13% more where it did not compete with another office superstore than where it competed with two others, and Office Depot – Staples' target – was found to charge "well over" 5% more in one-firm markets. *FTC v. Staples*, 970 F. Supp. 1066, 1075-76 (D.D.C. 1997).

The fact that neither side's experts found any meaningful differential here demonstrates that the presence or absence of Wild Oats did not alter the competitive landscape for Whole Foods. Given that Whole Foods' prices were not higher in so-called "monopolies," Wild Oats cannot have been a substantial presence in Whole Foods' competitive marketplace. The creation of additional "monopolies" through this merger cannot be expected to have any competitive effect.

Moreover, Wild Oats' prices were generally higher than Whole Foods' across the board. Wild Oats' own documents revealed a broad disparity – [redacted] on most items, [redacted] higher than comparable Whole Foods private-label products. JA2133-35. Although the FTC identified a few isolated, transitory instances where

Wild Oats attempted to compete by price, its own estimate that it would cost [redacted] million to bring its prices just into parity with Whole Foods' demonstrates how considerable and broad-based its competitive disadvantage was. JA2088-89. Independent market studies confirmed that – contrary to the FTC's expectation – Wild Oats had "little effect" on Whole Foods.

The FTC's allegation that removing Wild Oats risks substantially lessening competition is thus necessarily wrong. The studies show that Whole Foods sustained no appreciable competitive impact from Wild Oats in the past. And removal of a higher-priced competitor does not reduce the competitive pressures on surviving firms.

Finally, the real world dynamic of repositioning by supermarket rivals eager to compete more effectively with Whole Foods precludes any adverse competitive effect from this transaction. The FTC contention that repositioning could not be counted on as a likely response to hypothetical supracompetitive pricing by Whole Foods post-merger was conclusively rebutted by documents and testimony from other supermarkets (not included in the FTC's proposed market), that showed that repositioning was already occurring and having an appreciable effect on Whole Foods. *See supra* at pp. 6-12.

V. THE FTC'S CRITICISMS CANNOT BE RESOLVED WITH FURTHER STUDY.

Additional investigation in an FTC administrative proceeding will not help

the FTC solve the problems it asserts afflict the record or the assessment below. No amount of time and resources will change the market realties of consumer behavior and rival repositioning that underlie the district court's findings on product market and competitive effects, two points on which the FTC offered no evidence. Direct evidence of market realities outweighs whatever inferences might be gleaned from the isolated generalities by Whole Foods and Wild Oats executives in some documents.

No amount of time or resources will render statistically significant the margin differentials Dr. Murphy attempted to show between so-called "monopoly" and "competitive" markets. The fact that Wild Oats' prices were substantially higher than those of Whole Foods, and the absence of any meaningful difference in Whole Foods' prices and margins where Wild Oats was present and where it was not cannot change. These facts present an insurmountable hurdle for any future effort at proving that Wild Oats' continued existence would make a competitive difference.

Nor will additional time and resources enable the FTC and its expert to repair their failed critique of Dr. Scheffman's critical loss analysis. There are no natural experiments from which the FTC could study the effect of changes in relative price between what they contend to be premium natural and organic supermarkets and the other supermarkets that comprise over 99% of the industry,

and the FTC does not contend otherwise. Dr. Scheffman's analysis of actual consumer behavior remains the best available evidence.

Likewise, no additional time and resources will change the fact that the so-called diversion estimates undercut rather than support the FTC's case. If the FTC's proposed market definition were correct, substantially all the dollars formerly spent at a closed Wild Oats would be spent at Whole Foods or another premium natural and organic supermarket or would not be spent at all. Moreover, sales transfers would be lowest in markets where former Wild Oats customers could shop at a different premium natural and organic supermarkets and highest where Whole Foods was their only remaining premium natural and organic supermarket option.

But the estimates – if even remotely accurate – wholly undermine the FTC's theory. Whole Foods did not predict a transfer of all Wild Oats customers in *any* of the markets in which it was alleged that it would become a premium natural and organic supermarket monopolist. Indeed, the lowest estimated transfers – [redacted] – were in markets supposedly post-merger monopolies. And, the highest estimated transfer – [redacted]

The FTC's objections to "post-litigation" declarations also fail to afford a

basis for further investigation. First, the declarations themselves are largely vehicles for the introduction of ordinary-course documents that predate the merger. Second, remaining evidence in the record, including the documents introduced by the declarations, fully supports the district court's conclusions, and therefore setting the declarations aside entirely could not affect the result. Third, the declarations were not inconsistent with other evidence. The FTC's combing the record to find conflicts unearthed only two alleged instances that are not, in fact, inconsistencies. FTC Br.14, 49.

One – the non-existent inconsistency between declarations that Wild Oats' prices are generally higher than Whole Foods' and the few transitory instances of price competition between them – is discussed above, at pp. 19-20. Moreover, the general conclusion that the Court drew from the declarations – that Wild Oats prices are *generally* higher than Whole Foods' – is entirely consistent with pre-litigation documents from Whole Foods, Wild Oats, and market research.

The other alleged instance – declarations about Safeway – are also not contradicted by the pre-litigation documents cited by the FTC. The declarations note that Safeway's launching private-label organics and Lifestyle format stores imposes competitive pressure on Whole Foods, and acknowledge Whole Foods' initially losing [redacted] sales per week to Safeway's Boulder Lifestyle store but that sales [redacted]. The pre-

litigation documents confirm the new format, [redacted] The Boulder comparison between Safeway's actual and Wild Oats' planned store the FTC attributes to these pre-litigation documents appears nowhere. And dozens of other pre-litigation documents confirm Whole Foods' view of Safeway as competition and attest to Whole Foods' [redacted] and recognizing the continuing competitive pressure imposed by Safeway's repositioning.

Rather than help the FTC establish the validity of its highly restrictive proposed market, additional investigation would show instead that Whole Foods competes for sales with a much broader variety of food retailers than were taken into account in reaching the decision below. The district court adopted the narrowest view of the relevant antitrust market the evidence could support: "at least all supermarkets." JA247; JA277. Considerable evidence from market research studies, third parties and ordinary-course documents showed that Whole Foods also competes with other food retailers who are capable of, and have, imposed considerable competitive pressure. Additional investigation would make even clearer that Whole Foods competes with smaller grocers such as Trader Joe's – which the district court decided did not have a sufficiently broad selection to be

counted as a supermarket – [redacted] It would show that Whole Foods competes with warehouse stores like Costco and with limited purpose outlets like farmers markets, greengrocers, gourmet food stores, specialty seafood and meat markets, and Asian, Latin and other ethnic markets.

Additional investigation, however, will not make the aggressive comments by CEO John Mackey or other executives, which raised the FTC's suspicions, any more probative.[19] These statements did not go to the issue of the likely effect of the merger on prices and no additional investigation will change that fact. Indeed, Mackey made the same type of aggressive comments about Wegmans, Trader Joe's and others but the FTC has chosen to credit such comments only when they concern Wild Oats.

In any event, the hostile *intent* Mr. Mackey displays toward competitors does not put him in a position to substantially lessen the competition Whole Foods continues to face. *See Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1973 & n.13 (2007) (disregarding statement of intent in light of additional statements and real-world evidence); *A.A. Poultry Farms, Inc. v. Rose Acre Farms, Inc.*, 881 F.2d

[19] Despite the FTC's claims that the district court overlooked statements by Mr. Mackey, FTC Br.13, the judge suggested to counsel during oral argument that he harbored doubts about some Mackey remarks. JA103. Counsel did not pursue this point.

1396, 1402 (7th Cir. 1989) ("Stripping intent away brings the real economic questions to the fore"); P. Areeda & H. Hovenkamp Antitrust Law § 1506 (2d ed. 2003).

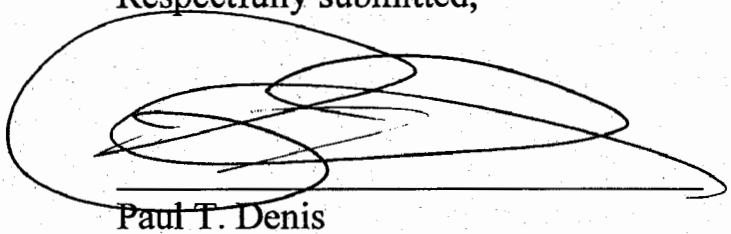
Additional investigation will also not add credence to the self-justifying boasts of former Wild Oats CEO Perry Odak, whose contract Wild Oats had chosen not to renew, and whose self-congratulations are contradicted by the same real-world evidence and by pre-litigation documents from Wild Oats itself.

The FTC began the proceeding below with only suspicions. It has pursued it with only those same suspicions – disregarding studies and evidence that demonstrate that its proposed product market cannot be correct and disregarding evidence from third-party competitors and manufacturers that the real world is very different from what it supposed. But the FTC cannot and has "not nudged [its] claims across the line from conceivable to plausible," *Twombly*, 127 S.Ct. at 1974, much less into serious and substantial questions. Thus, the FTC has not met the *Heinz* standard, and its request for a preliminary injunction was properly denied.

CONCLUSION

For the foregoing reasons, this Court should either dismiss this appeal as moot or affirm the decision below.

Respectfully submitted,



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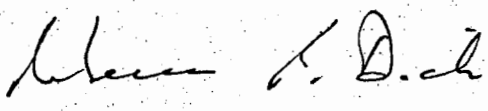
CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

This Brief of Appellee Whole Foods Market, Inc., complies with the type-volume limitations of Federal Rules of Appellate Procedure 32(a)(5), 32(a)(6), and 32(a)(7)(B). The brief contains 13,580 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). The brief has been prepared in a proportionally spaced typeface using Word 2003 in 14-point Times New Roman font.



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CERTIFICATE OF SERVICE

I hereby certify that, on this 18th day of March, 2008, I caused a true and correct copy of the foregoing Request to Supplement the Joint Appendix to be served by hand and e-mail on the following counsel for Appellant Federal Trade Commission:

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