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IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SAN FRANCISCO DIVISION

MED VETS INC., and BAY MEDICAL SOLUTIONS, INC.,

Plaintiffs,

v.

VIP PETCARE HOLDINGS, INC., successor in interest to COMMUNITY VETERINARY CLINICS, LLC d/b/a VIP Petcare and PETIQ, INC.,

Defendants.

Case No. 3:18-CV-02054-MMC

PLAINTIFFS' OPPOSITION TO DEFENDANTS' MOTION TO DISMISS PLAINTIFFS' FIRST AMENDED COMPLAINT

Date: March 1, 2019
Time: 9 a.m.
Courtroom: Courtroom 7-19th Floor
Judge: Hon. Maxine M. Chesney

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I. INTRODUCTION

The relevant market alleged in this case is defined by the sources for traditionally "unmeasured" veterinary wellness and medication products purchased by retail stores.[1] Plaintiffs, Med Vets, Inc. ("Med Vets") and Bay Medical Solutions, Inc. ("Bay Medical") (collectively, "plaintiffs"), were participants in this market. They obtained these products from veterinarians, veterinary wholesalers, and veterinary pharmacy suppliers and sold them to retailers. As the First Amended Complaint ("FAC") alleges, "[t]he presence of unmeasured pet wellness and medication products on retailer's store shelves and in on-line fulfillment centers is due to historical reasons." FAC, ¶ 4. This group of unmeasured products exists, whose retail sales are not measured like other products, because "[a]nimal health manufacturers refused to sell their products to retailers directly." *Id.*

Plaintiffs challenge the acquisition of VIP by PetIQ because the combined entity will have the veterinary capacity and retailer relationships to monopolize the specialized supply of these unmeasured products.[2] The victims of the merger are and will be both retailers, which will have few if any other options for the supply of unmeasured veterinary medication and wellness products, and excluded market participants such as plaintiffs, which "are being foreclosed from the retail customer base and have been or may be forced to exit the market." FAC, ¶ 37 (giving examples of other foreclosed secondary distributors known to plaintiffs). The competitive injury resides in PetIQ's post-merger overwhelming dominance over a market that once was more competitive and populated by many secondary distributors. Pre-merger, price competition occurred due to a greater number of suppliers capable of meeting retailers' needs for unmeasured products. *See* FAC, ¶ 31 ("a robust mechanism emerged by which retailers could obtain supplies … through the secondary distribution system.").

All that changed with PetIQ's purchase of VIP. The merger removed VIP as a very large, independent veterinarian chain that had supplied the secondary distribution system and turned it into the

[1] Reference in this Memorandum to "retailers" does not include veterinarians and veterinary clinics that sell veterinary wellness and medication products to the public.

[2] Most of these products—such as chewable flea-and-tick preventative medications—require a veterinary prescription, with the notable exception of Merial's Frontline Plus, an unmeasured product whose distribution has been restricted to the secondary wholesale distribution system by its manufacturer.

exclusive supplier to PetIQ, a company led by a former animal health manufacturer executive. *See* FAC, ¶ 22 (alleging that PetIQ's president was formerly the head of Merial North America) and FAC, ¶ 23 (alleging "[m]anufacturers, such as Merial, stand to benefit from the creation of a single, dominant gateway for unmeasured products, giving them greater control over secondary distribution to retailers). Many of the smaller secondary distributors' customers turned *en masse* to PetIQ. Secondary distributors have been forced out. Prices are likely to rise and more conducive conditions for inter-brand coordination (price-fixing) are likely to emerge. FAC, ¶¶ 36, 38. These facts plausibly allege an illegal merger under Section 7 of the Clayton Act, 15 U.S.C. § 18.

Plaintiffs' allegations, taken as true, mean that the challenged transaction will upend the secondary distribution market and hand it to PetIQ. That likelihood is plausible, and such allegations are all that is required of plaintiffs at this stage. Although it is "'tough to make predictions especially about the future,'" plaintiffs' allegations adequately describe the anticompetitive tendencies that "'the amended § 7 was intended to arrest … in their incipiency.'" *St. Alphonsus Med. Ctr.-Nampa, Inc. v. St. Luke's Health Sys.*, 778 F.3d 775, 783 (9th Cir. 2015) (*quoting U.S. v. Phila. Nat'l Bank*, 374 U.S. 321, 362 (1963) and famed Yankee catcher Yogi Berra). In short, the facts allege a plausible scenario in which defendants' acquisition has allowed them to monopolize, or is an attempt to monopolize, a relevant market.

Defendants move to dismiss plaintiffs' FAC under Rule 12(b)(6) largely by alleging their own facts and interpretations of the facts. *See, e.g.*, Defendants' Motion to Dismiss Plaintiffs' First Amended Complaint ("DMem." or "Motion"), at 3 (purporting to show "participants and flow of goods"). They also misconstrue the alleged relevant market and mis-apply the "interchangeability" test. With those distortions firmly established, defendants argue that the "the relevant market offers puzzling and vague parameters." DMem., at 5. But the long-standing policy of all but one animal health manufacturer to sell only to veterinarians is a *fact*; the existence of a cohort of products subject to those policies is a *fact*; the emergence of a secondary distribution system to provide retailers with those products is a *fact*; the existence of a channel that flows through veterinarians to distributors specializing in supplying retailers with those products is a *fact*; and the existence of a product market defined by that channel through which these products flow to retailers is a *fact*. Defendants cannot use their own facts to render

"implausible" a coherently alleged product market delineated by the specialized nature of the sale of such products to retailers and rooted in accepted economic theory.

Defendants' contortion of the "interchangeability" test is likewise misplaced and does not make plaintiffs' alleged market definition implausible. Case law is clear that the interchangeability test has two prongs: functional substitutability and economic feasibility. Functional substitutability is only one piece of the puzzle. Plaintiffs' alleged product market is also defined by the only alternatives to which a retailer can turn without "undue expense or inconvenience," or the economic theory of cross-elasticity of demand. *FTC v. Sysco Corp.*, 113 F. Supp. 3d 1, 25-26 (D.D.C. 2015) ("*Sysco*"). Veterinarians, manufacturers, or pharmaceutical wholesalers are not viable options since they lack the capacity to meet the retailers' logistical and other needs. That capacity was possessed by plaintiffs as specialized secondary distributors, whose business, like PetIQ, was to meet the delivery and other requirements of large retail organizations. The product market definition alleged in the FAC is supported by the kind of market realities and economic theory that has been upheld in several merger cases. *See FTC v. Staples, Inc.*, 190 F. Supp. 3d 100 (D.D.C. 2016) ("*Staples II*") (product market of consumable office supplies sold to B-to-B customers); *Sysco*, 113 F. Supp. 3d at 25-33 (product market of broadline foodservice distribution sold to national customers); *FTC v. Staples*, 970 F. Supp. 1066 (D.D.C. 1997) ("*Staples I*") (product market of office supplies sold through office superstores).

Defendants' counter-interpretations of plaintiffs' factual allegations, discussion of other segments of the industry not relevant to this case, and piecemeal critique of plaintiffs' allegations viewed in isolation and out of context are not grounds to dismiss a complaint. The phantasmagorical world in which a veterinary clinic could simply enter the market, or a Costco or Wal-Mart could purchase supply from a veterinary clinic or directly from an animal health manufacturer simply does not exist. *See In re Lithium Ion Batteries Antitrust Litig.*, No. 13-MD-2420 YGR, 2014 U.S. Dist. LEXIS 141358, at *184 (N.D. Cal. Oct. 2, 2014) (competing explanations of plaintiffs' case are "not so strong as to dispel the plausibility" of the complaint for dismissal under Rule 12); *Newcal Indus. v. Ikon Office Solutions*, 513 F.3d 1038, 1045, 1051 (9th Cir. 2008) (the validity of the relevant market and exertion of market power are factual elements rather than legal elements that should "survive scrutiny under Rule 12(b)(6) subject to factual testing by summary judgment or trial"). Rule 12(b)(6) is intended to test the legal sufficiency

of the facts alleged in the FAC. But, defendants' Motion offers no legal basis for dismissal and defendants provide no legal authority suggesting otherwise. The motion should be denied.

II. FACTS ALLEGED IN THE FAC[3]

In the pet industry, the "unmeasured" products tend to include preventative medications such as prescription and non-prescription flea and tick treatment and heartworm medication, among others, produced by animal health pharmaceutical companies. FAC ¶ 2. In contrast, "measured" products are those that traditionally have been available at retail stores and through online commerce. *Id*. Retail sales in this much larger universe of pet products are conventionally tracked by data aggregators. The Nielson Company is one example of a data aggregator, but there are others. *Id*. This case is *not* about "measured" pet products, *i.e.*, those that flow through traditional sales channels with no veterinary or veterinary pharmacy intermediary.

Rather, the market in this case is the distribution market for unmeasured veterinary wellness and medication products that reach retail store shelves through a veterinary or veterinary pharmacy intermediary and a secondary wholesale distributor such as plaintiffs or defendants. FAC ¶¶ 24-26. This unique channel is a consequence of the policies of manufacturers such as Merial, Elanco Animal Health, Zoetis, Merck Animal Health, Pfizer and Novartis. *Id*. ¶¶4-5, 27-32. These policies motivated some veterinary clinics and practices to purchase excess product to supply retail stores through the secondary wholesale distribution channel. Retailers were able to charge lower prices than veterinarians and pet owners paid less for the unmeasured wellness and medication products. *Id*. Defendant's public filings recognize the secondary wholesale distribution channel for unmeasured products is a distinct line of commerce. *Id*. ¶¶ 33-34. PetIQ CEO McCord Christensen publicly explained that unmeasured accounts comprise approximately 64% of the company's sales. *Id*.

Until PetIQ and VIP merged, several secondary wholesale distributors such as plaintiffs, defendants and others supplied the retail channel, what the Court recognized to be the "consumer" in this case. FAC ¶¶ 1-5, 27-32; Dkt. No. 35 at 48-49. No single entity had control over "leaked" or "diverted" products to dominate this distribution channel or product market. *Id*. ¶¶ 1-5, 27-32.

[3] Defendants also requested that the Court take judicial notice of certain documents referenced in the FAC. Plaintiffs do not oppose that request. *See* Dkt. No. 52 at 1.

This changed when PetIQ acquired VIP. Pre-merger, VIP had supplied significant quantities of Merial's unmeasured products to multiple secondary wholesale distributors. FAC ¶¶ 10-11, 15-18, 22-23, 32-33. Merial is one of the leading pet wellness and medication products manufacturers. The merger removed VIP as a horizontal competitor for wholesale distribution. *Id*. ¶¶ 3, 9-14, 22-23, 32, 37. All of VIP's unmeasured products, including its Merial supply, are now being sent to PetIQ for distribution. *Id*. Defendants' relationship with Merial is further strengthened with the placement of Susan Sholtis, formerly the head of Merial's North American commercial operations as defendants' President and member of the Board. *Id*. at ¶ 22. Defendants boast that they now control 90% of direct purchasing from animal health suppliers (e.g., manufacturers). They are the "leading animal health partner to retailers." *Id*. ¶¶ 32-35.

III. APPLICABLE LEGAL STANDARD

A motion to dismiss tests the legal sufficiency of the complaint based on the allegations contained therein. *In re Animation Workers Antitrust Litig.*, 123 F. Supp. 3d 1175, 1192-93 (N.D. Cal. 2015). "[A]ll allegations of material fact are taken as true and construed in light most favorable to the nonmoving party." *In re Dynamic Random Access Memory (DRAM) Antitrust Litig.*, No. M 02-1486 PJH, 2008 U.S. Dist. LEXIS 86650, at *35-36 (N.D. Cal. Apr. 15, 2008). "There is no requirement that [the] elements of the antitrust claim be pled with specificity" (*Newcal*, 513 F.3d at 1045), and antitrust cases are not held to a heightened pleading standard. *See United Energy Trading v. Pac. Gas & Elec. Co.*, 200 F. Supp. 3d 1012, 1020 (N.D. Cal. 2016) (antitrust cases are "subject to Rule 8"); *In re Disposable Contact Lens Antitrust Litig.*, 215 F. Supp. 3d 1272, 1289 (M.D. Fla. 2016) (*Twombly* "declined to apply a heightened pleading standard to antitrust cases, instead holding that the facts alleged are subject to Rule 8(a)'s general requirement of a 'short and plain statement' of facts supporting a plausible claim"). Rather, antitrust plaintiffs only need to provide enough factual matter to "raise the right to relief above the speculative level." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007). *See also Ashcroft v. Iqbal*, 556 U.S. 662, 677-78 (2009). "'A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.'" *In re Animation Workers Antitrust Litig.*, 123 F. Supp. 3d at 1193 (*quoting Iqbal*, 556 U.S. at 678). That determination is "context-specific," requiring that the "non-conclusory

'factual content,' and reasonable inferences from that content, [] be plausible suggestive of a claim entitling the plaintiff to relief." *Toranto v. Jaffurs*, 297 F. Supp. 3d 1073, 1083-84 (S.D. Cal. 2018) (*quoting Iqbal*, 556 U.S. at 679).

The plausibility standard under Rule 8(a) "'*does not impose a probability requirement at the pleading stage*'; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence to support the allegations." *Starr v. Baca*, 652 F.3d 1202, 1217 (9th Cir. 2011) (*quoting Twombly*, 550 U.S. at 556) (emphasis in original). A given set of actions "may well be subject to diverging interpretations, each of which is plausible." *Anderson News, L.L.C. v. Am. Media, Inc.*, 680 F. 3d 162, 184 (2d Cir. 2012). "If there are two alternative explanations, one advanced by defendant and the other advanced by plaintiff, both of which are plausible, plaintiffs' complaint survives a motion to dismiss under Rule 12(b)(6)." *Starr*, 652 F. 3d at 1216. "The choice between two plausible inferences that may be drawn from factual allegations is not a choice to be made by the court on a Rule 12(b)(6) motion." *Anderson News*, 680 F.3d at 185. Even if the allegations' truth seems doubtful, "'Rule 12(b)(6) does not countenance … dismissals based on a judge's disbelief of a complaint's factual allegations.'" *Id.* (*quoting Twombly*, 550 U.S. at 555). A well-pleaded complaint should be allowed to proceed "'even if it strikes a savvy judge that actual proof of the facts alleged is improbable, and that a recovery is very remote and unlikely.'" *Id*.

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IV. ARGUMENT

A. The FAC Alleges a Facially Sustainable Relevant Market

An antitrust complaint may not be dismissed based on challenges to the product market definition unless the defined market is "facially unsustainable" or suffers a fatal legal defect. *Newcal*, 513 F.3d at 1045. The "validity of the 'relevant market' is typically a factual element rather than a legal element [and] alleged markets may survive scrutiny under Rule 12(b)(6) subject to factual testing by summary judgment or trial" *Id*. (*citing High Technology Careers v. San Jose Mercury News*, 996 F.2d 987, 990 (9th Cir. 1993)). The Supreme Court in *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962), identified

several "practical indicia" to determine whether a relevant market such as the submarket advanced by plaintiffs exists. *Id.* at 325. *See also Staples I,* 970 F. Supp. at 1075. Several are present in this case, including: (1) defendants' public recognition of the secondary wholesale distribution market as a distinct product market; (2) the relevant market's peculiar characteristics as the only mechanism for providing certain unmeasured pet medication and wellness products to retailers; (3) distinct retail customers; (4) distinct prices to those customers; and (5) customers' sensitivities to price changes among distributors. *See also Brown Shoe*, 370 U.S. at 325 (listing practical indicia). These factors are "indicia' rather than requirements" and plaintiffs' product market is plausibly defined "even if only some of these factors are present." *Staples I,* 970 F. Supp. at 1075.

Defendants' emphasis of the use of the phrases "measured *accounts*" and "unmeasured *accounts*" in PetIQ's materials does not counter the identifiable presence of the cohort of products at issue in this case. It would be logical to categorize customers according to whether they purchase primarily measured or primarily unmeasured animal health products. And, the term "accounts" as opposed to "products" does not undermine the distribution channel and market participants delineated by the product market advanced here. Those semantics are issues for discovery. *See Anderson News*, 680 F. 3d at 185.

Defendants are also wrong to argue that the relevant product market cannot be as narrow or as broad as alleged by plaintiffs. DMem. at 9-14. The distribution product market here is defined by the alternatives available to retailers purchasing unmeasured veterinary wellness and medication products if defendants raise prices. These are the groups of producers "who have the actual or potential ability to deprive each other of significant levels of business." *Newcal*, 513 F. 3d at 1045 (citation omitted). Because retailers' only source of unmeasured veterinary wellness and medication product supply is the secondary distribution channel, the only alternatives to PetIQ available to retailers are plaintiffs and the other secondary wholesale distributors. Veterinary clinics do not sell these products directly to retailers and are appropriately excluded. As are manufacturers. Pet owners do not purchase these products directly from secondary wholesale distributors and are also appropriately excluded.[4] These facts

[4] The Court has already rejected defendants' argument for including pet owners in the relevant market, acknowledging that retailers are the appropriate "consumers" in this case. *See* Dkt. No. 35 at 48-49.

described above and contained in the FAC confirm that secondary wholesale distribution of unmeasured veterinary wellness and medication products is a relevant product market for purposes of evaluating defendants' merger.

Because plaintiffs' product market is defined by the specialized distributors to whom retailers would switch if faced with a small but significant and non-transitory increase in price ("SSNIP"), it satisfies the Hypothetical Monopolist Test, a commonly used method for defining product markets based on available substitutes and upheld by the Ninth Circuit. *See Theme Promotions, Inc. v. News Am. Mktg. FSI*, 546 F.3d 991, 1002 (9th Cir. 2008). Plaintiffs' allegations also invoke the theory of cross-elasticity of demand. *Sysco*, 113 F. Supp. 3d at 25. In attempting to distort plaintiffs' product market definition, defendants only consider functional interchangeability. DMem. at 9-14. But, under cross-elasticity of demand, products should not be included as substitutes unless a "switch can be accomplished without the consumer incurring undue expense or inconvenience." *Sysco*, 113 F. Supp. 3d at 26. "That is, 'a relevant product market cannot meaningfully encompass [an] infinite range [of products]. The circle must be drawn narrowly to exclude any other product to which, within reasonable variations in price, only a limited number of buyers will turn.'" *Id*. (*quoting Times-Picayne Publ'g Co. v. U.S.*, 345 U.S. 594, 612 n.31 (1953)). *See also H&R Block, Inc.*, 833 F. Supp. 2d 36, 58-60 (D.D.C. 2011) (explaining that "the relevant product market should ordinarily be defined as the smallest product market that will satisfy the hypothetical monopolist test"). Retailers cannot turn to veterinarians or manufacturers for unmeasured veterinary wellness and medication products, and those other forms of distribution are appropriately excluded from the product market circle drawn here.

Similarly, the presence of a measured "flea and tick" category in commercial retail sales is immaterial to whether the market alleged in the FAC is facially sustainable. Plaintiffs acknowledge the potential *functional* substitutability of a range of products available to pet owners, some of which are measured products. Such factual observations—even from materials judicially noticed—do not address the competition at the distribution level that threatens to be lost with the advent and continuation of the defendants' merger.

Like the defendants in *Sysco* (and other merger cases), defendants argue for a broader product market because other market participants, such as veterinary clinics, sometimes choose to operate as a

distributor. DMem. 9-14. "But the fact that Defendants sometimes compete against other channels of distribution in the larger marketplace does not mean that those alternative channels belong in the relevant product market for purposes of merger analysis." *Sysco*, 113 F. Supp. 3d at 30-31. *See also FTC v. Whole Foods Market, Inc.*, 548 F.3d 1028, 1040-41 (D.C. Cir. 2008); *Staples I*, 970 F. Supp. at 1073-75. The *Sysco* court examined the *Whole Foods* and *Staples I* cases in which, as here, the defendants argued that the product markets were artificially narrowed. But the *Sysco* court found those cases support the narrower, rather than broader, product market advanced. *Sysco*, 113 F. Supp. 3d at 31. In *Whole Foods*, "just because customers were able to buy some categories of grocery store products from both outlets – similar to how broadline customers are able to purchase some products from other modes of distribution – did not mean that PNOS was in the same product market as grocery stores." *Id*. In *Staples I*, the unique combination of "size, selection, depth and breadth of inventory offered by the superstores distinguished them from other retailers" including giants such as Wal-Mart and, in *Staples II*, Amazon. *Id. See also Staples I*, 970 F. Supp. at 1073-75, 1079; *Staples II*, 190 F. Supp. 3d at 113-114, 134. That line of reasoning "appl[ies] with equal force" to the distribution market here. *Sysco*, 113 F. Supp. 3d at 31. The unique services and range of products secondary distributors provide retailers distinguishes them from other modes of distribution. For these same reasons, *Hicks v. PGA Tour, Inc.*, 897 F. 3d 1109 (9th Cir. 2018) is inapposite. *See* DMem. at 9. The caddies in that case did not consider all economic substitutes to advertising on their bibs when defining the product market. *Id*. at 1121-22. In contrast, plaintiffs' alleged product market here is defined by all alternative mechanisms for delivering certain unmeasured veterinary wellness and medication products to retailers - secondary wholesale distributors.

Defendants' other challenges to plaintiffs' advanced product market likewise fail. Specifically, defendants argue that "unmeasured" means something other than alleged and that the unmeasured product list fails to meet the interchangeability test. DMem. 9-14. First, defendants urge the Court to accept their own interpretation of plaintiffs' allegations, a mistake at this stage of the pleadings. A complaint may not be dismissed because two plausible inferences may be drawn from the factual allegations. *Anderson News*, 680 F. 3d at 185. Defendants' competing explanations for the term "unmeasured" and ultimate customer do not demonstrate that plaintiffs' product market and resulting foreclosure allegations are implausible. *In re Lithium Ion Batteries Antitrust Litig.*, 2014 U.S. Dist.

LEXIS 141358, at *184 (denying motion to dismiss antitrust complaint because the defendants' offered competing inferences were "not so strong as to dispel the plausibility" of their participation in the alleged conspiracy)) (*citing Starr*, 652 F. 3d at 1216; *Anderson News*, 680 F.3d at 189-90). Second, defendants' argument concerning pet medication interchangeability focuses on the medications distributed rather than the distribution channel product market advanced. When viewed with the appropriate lens considering the actual product market alleged and plaintiffs' allegations as a whole, the substitutability of one pet medication for another becomes irrelevant.[5] *See id*. Moreover, plaintiffs' allegations of actual anticompetitive effects from defendants' merger (to wit, foreclosure and exiting the market) "may more directly predict the competitive effects of a merger, reducing the role of inferences from market definition and market shares." Dep't of Justice & Fed. Trade Comm'n Horizontal Merger Guidelines (2010) ("Merger Guidelines") §4.

B. The Challenged Acquisition Will Harm Competition

Every facet of the secondary wholesale distribution channel for unmeasured products is being impacted by defendants' merger. Rival secondary distributors such as plaintiffs and competitors Southeastern Veterinary Exports, Lambert Vet Supply, Rainbow Vet Supply, Pet Vet Supply and others are unable to access unmeasured wellness and medication products. FAC ¶¶ 36-42. They are being foreclosed from the retail channel. *Id*. Some have already been forced out of the market. *Id*. Others are likely to follow. *Id*. Retailers are being deprived of wholesale distributor choice. With control over 90% of the supply, defendants have enough market power to unilaterally raise prices. *Id*. With no other access to the unmeasured veterinary wellness and medication products, retailers will have no choice but to pay. The Department of Justice and Federal Trade Commission recognize that this high degree of

[5] Even if pet medications were part of the product market inquiry, the fact that they are included together is of no moment. Each medication could be viewed as its own market for distribution but presented here as a "cluster market" for analytical convenience. *Staples II*, 190 F. Supp. 3d at 117. "The Supreme Court has made clear that '[w]e see no barrier to combining in a single market a number of different products or services where that combination reflects commercial realities.'" *Id*. (*quoting U.S. v. Grinnell Corp.*, 384 U.S. 563, 572 (1966)) (analyzing separate product markets for pens, file folders, Post-it notes, binder clips and paper for copiers and printers sold to B-to-B customers in single framework). Because distribution of each medication and wellness product would be impacted similarly by defendants' merger, it would be appropriate to consider them as a cluster market. *Id*.

concentration also increases the likelihood of inter-brand price-fixing and other coordinated effects. *See* Merger Guidelines §7. Defendants' merger must be halted.

C. Plaintiffs Plausibly Allege that Defendants' Merger Violates Section 7

Plaintiffs allege that defendants' merger may substantially lessen competition or tend to create a monopoly in the relevant market. The FAC details that the secondary wholesale distribution for unmeasured veterinary wellness and medication products is a distinct product market, as recognized by defendants. Defendants' merger eliminated a major supplier of those products to condense the vertical and eliminated a horizontal competitor at the wholesale level. Post-merger, by their own admission, defendants control 90% of the products supplied by animal health manufacturers, untouchable by any other secondary wholesale distributor. Competitors are being foreclosed from customers (retailers) and have either, already exited the market or will be soon. Prices to retailers are likely to rise. Inter-brand price fixing is likely. *See* Sections II, IV. A-B, *supra*. These allegations plausibly describe that defendants' acquisition creates an appreciable danger for future harm to competition, a Section 7 claim adjudicated under an incipient standard. *Boardman v. Pac. Seafood Grp.*, 822 F3d 1011, 1021 (9th Cir. 2016) ("To prove an unlawful merger claim under § 7 of the Clayton Act, a plaintiff must show that the effect of the challenged acquisition 'may be substantially to lessen competition, or to tend to create a monopoly'") (*quoting* 15 U.S.C. §18). Plaintiffs do not need to allege or otherwise demonstrate that the merger has already impacted the relevant market to state a plausible claim. *Id*. "All that is necessary is that the merger create an appreciable danger of such consequences in the future." *St. Alphonsus Med Ctr.-Nampa*, 778 F.3d at 788 (citation omitted). The Court's analysis is to focus on probabilities, not certainties; "this is what is meant when it is said that the amended §7 was intended to arrest anticompetitive tendencies in their incipiency." *Id*. at 783 (*quoting Phila. Nat'l Bank*, 374 U.S. at 362). Plaintiffs factual allegations described above meet that burden.

Defendants challenge plaintiffs' FAC primarily on product market grounds. They argue that the Court's concerns with the product market advanced have not been remedied. They further argue that market power and antitrust injury have not been plausibly alleged. Defendants are wrong. The product market advanced is facially sustainable, rooted in economic theory and defined by the group of substitutes capable of constraining defendants' pricing plans. *See* Section IV. A., *supra*. Defendants'

dominant market position plausibly describes their ability to exert market power post-merger. And, plaintiffs explain resulting harm to themselves, other distributors and retailers, the essence of antitrust injury. Much of defendants' attacks are impermissible competing explanations for plaintiffs' allegations. They also ignore or take allegations out of context and in isolation. They provide no legal grounds for dismissing plaintiffs' FAC at this stage.

1. Plaintiffs Plausibly Allege Market Power

Market power is the "ability to raise price profitably by restricting output"; when a party has sufficient market power to exclude competition or control prices, that party possesses monopoly power. *DocMagic, Inc. v. Ellie Mae, Inc.*, 745 F. Supp. 2d 1119, 1137 (N.D. Cal. 2010) (*quoting* IIB Phillip E. Areeda et al., *Antitrust Law* ¶ 501 (2007) and finding allegations of significant market share with high barriers to entry sufficient to plead market power). As the Supreme Court has explained:

> Market power is the power "to force a purchaser to do something that he would not do in a competitive market." [Citation]. It has been defined as "the ability of a single seller to raise price and restrict output." [Citation]. The existence of such power ordinarily is inferred from the seller's possession of a predominant share of the market.

Eastman Kodak Co. v. Image Tech, Servs., 504 U.S. 451, 464 (1992) (internal citations omitted). *See also U.S. v. Microsoft Corp.*, 253 F.3d 34, 51 (D.C. Cir. 2001) ("monopoly power" is the "'power to control prices or exclude competition'") (*quoting U.S. v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956)). Market power "need not be pled with specificity" (*United Energy Trading*, 200 F. Supp. 3d at 1020), particularly in Section 7 cases that require courts to use "prediction" about future market conditions to "arrest anticompetitive tendencies in their 'incipiency.'" *U.S. v. Penn-Olin Chem. Co.*, 378 U.S. 158, 171 (1964) (*quoting Phila. Nat'l Bank*, 374 U.S. at 362). Plaintiffs allege here that defendants control 95% of prescription medications in retail and 90% of "direct purchasing from animal health suppliers" to retailers. FAC ¶¶ 33, 37-41. With such a dominant market share, no other secondary distributor could serve as a constraint on defendants' ability to raise prices post-merger. *Id*. Defendants have wielded their market power to exclude competitors such as plaintiffs and other secondary distributors. *Id*. They will have the ability to raise prices post-merger. These facts plausibly describe defendants' post-merger ability to exclude competition and control prices to allege market power. *United*

Energy Trading, 200 F. Supp. 3d at 1020-21 (allegations of market share between 70% to 90% combined with entry barriers sufficient to allege market power).

The Court declined to reach the issue of the defendants' market power previously because of its concerns with the product market definition. *See generally* Dkt. No. 35. Those concerns have been addressed with the revised product market alleged here, legally sustainable for reasons discussed above. *See* Section IV.A., *supra*. For these same reasons, defendants' arguments concerning market power allegations based on specious challenges to the relevant product market should be rejected. *See Toranto*, 297 F. Supp. 3d at 1092 (rejecting similar challenges to market power allegations because the plaintiffs' identified market was "facially sustainable, and [] clearly alleges Defendants have 100% of the market…").[6] And, to require plaintiffs to allege that defendants *already* possess and have exerted market power from a merger that closed shortly before this case was initiated and currently under the watchful eye of plaintiffs and the Court, while depriving plaintiffs the benefit of any discovery in this largely opaque industry, would vitiate the incipient standard (and dangerous probability element for attempted monopolization claims).

Defendants further challenge plaintiffs' market power allegations by offering competing explanations for the 95% and 90% figures included in the FAC. *See* DMem. at 14-15, FAC ¶ 33. Plaintiffs do not misquote the Jeffries Report as defendants suggest. Rather, defendants offer their own interpretation of the meaning of the words on the page. But, even if defendants' interpretation is correct, and the 90% figure refers to the percentage of defendants' supply obtained directly from animal health manufacturers, that would still be consistent with defendants' professed "95% share of Rx [prescription] in Retail," since nearly all of the unmeasured products flowing through the secondary distribution

[6] Defendants' reliance on *Rick-Mik-Enters., Inc. v. Equilon Enters. LLC*, 532 F.3d 963 (9th Cir. 2008) ("*Rick-Mik-Enters.*") and *Digital Sun v. The Toro Co.*, 2011 WL 1044502 (N.D. Cal. Mar. 22, 2011) is similarly misplaced. *See* DMem. at n.12. As with their last Motion to Dismiss (*see* Dkt. No. 25 at 21), those cases are inapposite to this one. In *Rick-Mik-Enters.*, the court was presented with a tying claim in which the plaintiff had failed to allege that the defendant possessed market power in the relevant tying market, an essential element in that claim. 532 F.3d at 973. In *Digital Sun*, the plaintiff brought a claim for attempted monopolization without alleging that the defendant is in danger of possessing power in the relevant market. 2011 WL 1044502 at *8-9.

channel are prescription veterinary medications and wellness products.[7] *See* FAC ¶¶ 2-5; 22-34. Notably, defendants do not dispute plaintiffs' interpretation of the 95% market share figure. *See* DMem. at 14-15. As discussed above, defendants' self-serving interpretations of their own documents are not grounds to dismiss plaintiffs' complaint. *In re Lithium Ion Batteries Antitrust Litig.*, *supra*, 2014 U.S. Dist. LEXIS 141358 at *184, (*citing Starr*, 652 F.3d at 1216; *Anderson News*, 680 F.3d at 189-90). Their argument that the Jeffries Report demonstrates that PetIQ has too small a percentage of the industry to have market power conflates the numbers and products. *See* DMem. at 15. The FTC report expects U.S. retail sales for all pet medications to grow to $10.2 billion, but this number does not measure the smaller segment of unmeasured pet wellness and medications sold through the secondary distribution channel. *See* FTC Report at 9. Plaintiffs allegations must be accepted as true at this stage of the pleadings (*DRAM*, *supra*, 2008 U.S. Dist. LEXIS 86650 at *35-36), and control over 90% of the relevant product market plausibly describes market power for Section 7 purposes. *See, e.g.*, *United Energy Trading*, *supra*, 200 F. Supp. 3d at 1020-21; Merger Guidelines §5 (discussing that high market share and market concentration reduce firms' incentives to act competitively).

2. Plaintiffs Have Alleged Antitrust Injury

The FAC sufficiently alleges antitrust injury for Rule 12 purposes through allegations that show harm to competition by eliminating suppliers to retailers and excluding plaintiffs and other market participants. FAC ¶¶ 36-42. *See also*, Sections IV.B-C, *supra*; *Amarel v. Connell*, 102 F.3d 1494, 1508-09 (9th Cir. 1996). "Standing is clear … when the plaintiff alleges that its rival engaged in an exclusionary practice designed to rid the market of the plaintiff … so that the defendant could maintain or create a monopoly." *Id*. (*citing* Phillip E. Areeda and Herbert Hovenkamp, 2 Antitrust Law ¶373d (revised ed. 1995)). Plaintiffs thus allege the exact type of injury the antitrust laws were designed to prevent. *See Blue Shield of Va. V. McCready*, 457 U.S. 465, 482 (1982) (antitrust injury should reflect "the type of loss that the claimed violations … would be likely to cause") (internal citations omitted).

[7] Merial's Frontline Plus does not require a veterinary prescription but is still an unmeasured product that, by virtue of Merial's sales policies, is available to retailers only through the secondary distribution system. The product is now distributed exclusively through defendant, PetIQ, a company led by a former Merial executive, and contributes significantly to defendants' dominance over the relevant market alleged in the FAC.

Defendants argue that plaintiffs "only" allegation of injury is that they "have been 'foreclosed from customers.'" DMem. at 16-17. Not so, as the allegations described above and in the FAC demonstrate. These allegations "more than merely recite bare legal conclusions" and are sufficient to "raise a reasonable expectation that discovery will reveal evidence of an injury to competition." *Toranto*, 297 F. Supp. 3d at 1090 (citation omitted). *See also Amarel*, 102 F.3d at 1509 (collecting cases conferring antitrust standing to a competitor of an alleged attempted monopolist, "where it was either driven out of business or suffered reduced profits because of the alleged anticompetitive acts of the attempted monopolist"). Moreover, defendants' attacks take plaintiffs' allegations out of context and in isolation. But the inquiry is whether plaintiffs' allegations as a whole satisfy the antitrust injury analysis. *See, e.g., In re Lithium Ion Batteries Antitrust Litig.*, 2014 U.S. Dist. LEXIS 141358, at *184. Here, they do.

D. Plaintiffs Plausibly Allege Monopolization and Attempted Monopolization

Monopolization claims are properly pled through allegations that the defendants (1) possess monopoly power in the relevant markets; (2) have willfully acquired or maintained that power; and (3) their conduct has caused antitrust injury. *Cost Mgmt. Servs. v. Wash. Nat. Gas Co.*, 99 F.3d 937, 949-50 (9th Cir. 1996). Attempted monopolization requires allegations of Defendants' (1) specific intent to control prices or destroy competition; (2) anti-competitive conduct to accomplish the monopolization; (3) dangerous probability of success; and (4) causal antitrust injury. *Id*. At this stage, plaintiffs "need only allege sufficient facts from which the court can discern the elements of an injury resulting from an act forbidden by the antitrust laws." *Id*. (citation omitted) *See also Covad Communs. Co. v. Pac. Bell*, No. C 98-1887 SI, 1999 U.S. Dist. LEXIS 22789, *30-33 (N.D. Cal. Dec. 14, 1999) (allegations that the defendant imposed costly and unnecessary conditions to access its network survived motion to dismiss).

Plaintiffs have pled both claims with sufficient factual detail. Specifically, plaintiffs allege that defendants (1) control 90% of the supply in the relevant market; (2) acquired that dominant position through the VIP acquisition; and (3) have foreclosed plaintiffs and other market participants from access to customers with the likelihood of increasing prices. *See* Sections II, IV.A-C, *supra*. For attempted monopolization, plaintiffs further allege that defendants specifically intend to remove competitors and raise prices and have a dangerous probability of success in doing so based on their dominant market

position. *Id*. Moreover, the FTC report makes it clear and defendants agree that the secondary wholesale market is a creature of anticompetitive restraints imposed by manufacturers. Those restraints combined with the manufacturers' cooperation and intersection with defendants constitutes a threat to the continued flow of unmeasured pet wellness and medication products through the secondary distribution system. These factual allegations are not "conclusory" as defendants suggest (DMem. at 18-19), but plausibly describe efforts to monopolize and attempt to monopolize the relevant markets. *See Cost Management Servs.*, 99 F.3d at 950-51.

E. Plaintiffs Have Standing to Seek Injunctive Relief

Section 16 of the Clayton Act, 15 U.S.C. § 26, provides in pertinent part that "any person … shall be entitled to sue for and have injunctive relief … against threatened loss or damage by a violation of the antitrust laws … under the same conditions and principles as injunctive relief against threatened conduct that will cause loss or damage is granted by courts of equity." Under those principles, injunctive relief based on likely injuries is sustainable.

Defendants again argue plaintiffs do not have standing for injunctive relief, repackaging arguments advanced in their first Motion to Dismiss. DMem. at 19-20. Those arguments fail for the same reasons as before. This case is brought by two related entities, one of which has *already* lost its business because of defendants' merger. The other is being threatened with a similar fate. These injuries cannot be remediated in a suit for damages.

Defendants' arguments here ask this Court to assess the evidence entitling plaintiffs to relief rather than an evaluation of whether the allegations of the FAC state plausibly antitrust violations. The cases cited still shed little light on whether the FAC adequately places defendants on notice of the nature of plaintiffs' claims. Defendants have failed to raise legitimate grounds to deny plaintiffs standing to seek injunctive relief at this early stage of the litigation.

V. CONCLUSION

Plaintiffs respectfully submit that the Defendants' Motion to Dismiss the FAC should be denied in its entirely, or, alternatively, that plaintiffs be granted leave to amend.

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