IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

UNITED STATES OF AMERICA, Plaintiff, v. THE EARTHGRAINS COMPANY, SPECIALTY FOODS CORPORATION, and METZ HOLDINGS, INC., Defendants.	 Civil No: 00 C 1687 Filed: **4/10/00** Judge Bucklo Magistrate Judge Nolan

COMPETITIVE IMPACT STATEMENT

The United States, pursuant to Section 2(b) of the Antitrust Procedures and Penalties Act ("APPA"), 15 U.S.C. § 16(b)-(h), files this Competitive Impact Statement relating to the proposed Final Judgment submitted for entry in this civil antitrust proceeding.

I. NATURE AND PURPOSE OF THE PROCEEDING

On March 20, 2000, the United States filed a civil antitrust suit that alleges that an acquisition by The Earthgrains Company ("Earthgrains") of Metz Holdings, Inc. ("Metz") would violate Section 7 of the Clayton Act, 15 U.S.C. § 18. The Complaint alleges that in many markets in the Midwest, Earthgrains and Metz are two of only a few significant competitors in the production and sale of white pan bread, and that their combination would substantially lessen competition in these already highly concentrated markets, including Kansas City, Missouri; Omaha, Nebraska; Des Moines, Iowa; and many smaller communities in Illinois, Iowa, Kansas, Missouri, and Nebraska. According to the

Complaint, the loss of competition would likely result in retailers and consumers paying higher prices for white pan bread in these areas. The prayer for relief in the Complaint seeks: (1) a judgment that the proposed acquisition would violate Section 7 of the Clayton Act; and (2) a permanent injunction that would prevent Earthgrains from acquiring control of Metz or otherwise combining Metz's assets with its own business.

At the same time the Complaint was filed, the United States also filed a proposed settlement that would permit Earthgrains to complete its acquisition of Metz, yet preserve competition in the markets in which the transaction would otherwise raise significant competitive concerns. The settlement consists of a proposed Final Judgment and a Hold Separate Stipulation and Order. In essence, the Hold Separate Stipulation and Order would require Earthgrains to maintain certain bread brands, and associated production and distribution assets, as economically viable, ongoing concerns, operated independently of Earthgrains's other businesses until the divestitures mandated by the Final Judgment have been accomplished.

The proposed Final Judgment orders defendants to divest to one or more acquirers the Colonial and Taystee labels of white pan bread for use in each of the affected markets, including all of the cities and counties identified in the proposed Final Judgement. *See* Final Judgment, §II (H). Because an acquirer may require other assets in order to compete effectively and viably in the sale of white pan bread in the affected areas, under the Final Judgment the United States may, in its sole discretion, require the divestiture of additional assets, including (a) Earthgrains's Des Moines, IA bakery; (b) a license to produce buns, rolls, and any other bread under the Colonial and Taystee labels; (c) Earthgrains's and Metz's bread routes, trucks, and customer lists; and (d) other ancillary assets

currently used by Earthgrains and Metz in the production, distribution and sale of white pan bread under the Colonial or Taystee labels. Defendants must complete these divestitures within 90 days after filing of the Complaint,[1] or five days after entry of the Final Judgment, whichever is later. If they do not complete the divestitures within the prescribed time, the Court may appoint a trustee to sell the assets.

The United States and defendants have stipulated that the proposed Final Judgment may be entered after compliance with the APPA. Entry of the proposed Final Judgment would terminate this action, except that the Court would retain jurisdiction to construe, modify, or enforce the provisions of the proposed Final Judgment and to punish violations thereof.

II. DESCRIPTION OF THE EVENTS GIVING RISE TO THE ALLEGED VIOLATION

A. The Defendants and the Proposed Transaction

1. Earthgrains

Earthgrains, based in St. Louis, Missouri, is the nation's second largest wholesale commercial baker. It operates a total of 43 commercial bakeries throughout the United States, though its bread production and sales are concentrated primarily in the South and Midwest. In 1999, Earthgrains reported sales of $1.93 billion.[2]

2. Specialty Foods and Metz

Specialty Foods Corporation is a privately held concern that owns several baking operations, including Metz. Metz, based in Deerfield, Illinois, is one of the largest regional wholesale commercial

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[1] The Complaint was filed on March 20, 2000.

[2] The Complaint inaccurately alleges that Earthgrains operates 28 commercial bakeries and reported sales of $1.6 billion in 1999. It, in fact, operated 43 commercial bakeries and reported $1.93 million in annual sales.

bakers. It produces and sells white pan bread throughout the Midwest, primarily in Colorado, Illinois, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Utah, and Wisconsin. In 1999, Metz's total revenues exceeded $600 million.

3. The proposed transaction

On November 15, 1999, Earthgrains agreed to acquire Metz from Specialty Foods for about $625 million. This proposed transaction, which would combine Earthgrains and Metz and substantially lessen competition in the sale of white pan bread in many areas of the Midwest, precipitated the government's antitrust suit.

B. The Bread Industry and the Competitive Effects of the Transaction

1. White pan bread

White pan bread describes the ubiquitous, white, sliced, soft loaf known to most consumers as "plain old white bread." An American household staple, typically used for sandwiches, white pan bread is sold in the commercial bread aisle of every grocery store, as well as many other retail stores. White pan bread differs significantly from other types of bread, such as variety bread (*e.g.*, wheat, rye or French) and freshly baked in-store breads, in taste, texture, uses, perceived nutritional value, keeping qualities, and appeal to various groups of consumers. Families with young children, for instance, strongly prefer to purchase white pan bread because children prefer this bread.

Because of its unique appeal and distinguishing attributes, a small but significant increase in the price of white pan bread by all producers would not cause a significant number of current purchasers to substitute any other type of breads, or for that matter, any other product. The sale of white pan bread

to consumers through retailers is, therefore, a relevant product market in which to assess the competitive effects of the acquisition.

White pan bread is mass produced on high-speed production lines by wholesale commercial bakers, who package and sell it to retailers under either their own brand or a private label (*i.e.*, a brand controlled by a grocery chain or buying cooperative). Though physically similar to private label bread, branded white pan bread is perceived by consumers as higher quality bread; consequently, consumers often pay a premium of twice as much or more for branded white pan bread.

The Complaint alleges that the provision of white pan bread through retail outlets takes place in highly localized geographic markets. The high transportation costs, short shelf life, and extensive bakery control over the sale of their branded white bread products all make it very expensive and difficult for retail stores and consumers to purchase white pan bread from bakers that are not local market incumbents.

2. Competition between Earthgrains and Metz in the sale of white pan bread

Earthgrains and Metz compete directly in producing, promoting, and selling both private label and branded white pan bread to grocery retailers, who in turn sell it to consumers. In the relevant areas alleged in the Complaint, Earthgrains sells two brands of white pan bread, either IronKids and Colonial or IronKids and Rainbo, and Metz sells two brands of white pan bread, either Pillsbury and Old Home or Pillsbury and Taystee.

Earthgrains and Metz recognize the keen rivalry between their bread products in the relevant geographic markets. To avoid losing sales to the other, each has engaged in extensive promotional and couponing campaigns that reduce the prices charged for their branded white pan breads to the benefit

of retailers and consumers. Each also competed against the other in pricing and in improving the quality and services offered in connection with both branded and private label white pan bread. Through these activities, Earthgrains and Metz have each operated as a significant competitive constraint on the other's prices for branded and private label white pan bread.

3. Anticompetitive consequences of the acquisition

The Complaint alleges that Earthgrains's acquisition of Metz would remove the competitive constraint each has had on the other, and create (or facilitate Earthgrains's exercise of) market power (*i.e.,* the ability to increase prices to consumers) in a number of relevant geographic markets throughout the Midwest, including the Kansas City, Missouri; Omaha, Nebraska; and Des Moines, Iowa metropolitan areas; and in many smaller communities in Illinois, Iowa, Kansas, Missouri and Nebraska.

Specifically, the Complaint alleges that in each of the markets, Earthgrains and Metz are two of only a few significant competitors. The acquisition would increase concentration significantly in these already highly concentrated, difficult-to-enter markets.[3] Post-acquisition, Earthgrains would dominate each market, accounting for at least 58 percent of all sales of white pan bread in the Omaha market, at least 52 percent in the Kansas City market, about 56 percent in the Des Moines market, and likely half or more of all sales of white pan bread in many smaller communities in Iowa, western Illinois, northeastern Kansas, northwestern Missouri, and eastern Nebraska. Moreover, after the merger,

[3] The Herfindahl-Hirschman Index ("HHI") is a widely-used measure of market concentration. Following the acquisition, the approximate post-merger HHIs, calculated from 1999 dollar sales, would be about 3800 with a change of 875 points for the Omaha area; 3400 with a change of 1378 points for the Kansas City area; and 3500 with a change of 1530 points for the Des Moines area. Under the *Merger Guidelines*, an acquisition that increases the HHI by 50 points or more in a market in which the post-merger HHI will exceed 1800 points may raise serious competitive concerns.

Earthgrains and only one or two other competitors would control more than 90 percent of annual sales revenues of white pan bread in these areas.

The Complaint alleges that Earthgrains's acquisition of Metz in each of these markets would cause a substantial reduction in competition either from an increased likelihood of coordinated pricing that would result from the elimination of a significant competitor, Metz, or from the likelihood that Earthgrains will acquire the power to unilaterally increase prices to consumers for branded white pan bread after the merger. In both instances, the merger is likely to lead to higher prices to consumers who purchase white pan bread through retail outlets in the relevant areas.

The Complaint alleges that entry by other wholesale commercial bakers into the sale of white pan bread in any of the adversely affected geographic markets is time-consuming, expensive and difficult, and hence, unlikely to soon counteract these anticompetitive effects.

III. EXPLANATION OF THE PROPOSED FINAL JUDGMENT

The proposed Final Judgment would preserve competition in the sale of white pan bread in each of the relevant geographic markets. Within 90 days after March 20th, the date the Complaint was filed, or five days after entry of the Final Judgment, whichever is later, defendants must divest two of their popular white pan bread brands, the Colonial and Taystee labels,[4] and such other production and

[4] As defined in the Final Judgment, a "label" "means all legal rights associated with a brand's trademarks, trade names, service names, service marks, intellectual property, copyrights, designs, and trade dress; the brand's trade secrets; the brand's technical information and production know-how, including, but not limited to, recipes and formulas used to produce bread currently sold under the brand, and any improvements to, or line extensions thereof; and packaging, marketing and distribution know-how and documentation, such as customer lists and route maps, associated with the brand." Final Judgment, §II (F). Divesting a label would require defendants to grant, at a minimum, "[a] perpetual, royalty-free, freely assignable and transferrable, and exclusive license to make, have made,

distribution assets that the United States determines may be necessary to create an economically viable competitor in the sale of white pan bread in each geographic market.[5] It may well be that the sale to an existing wholesale baker of exclusive rights to make and sell white pan bread under either the Colonial and Taystee labels is all that is required to accomplish this goal. Depending on the acquirer's requirements, however, effective divestiture may require the sale of other assets such as Earthgrains's Des Moines, IA bakery, which currently services the relevant areas; a license to sell buns, rolls, or other bread under the Colonial and Taystee labels; and the bread routes, trucks, thrift stores, depots, warehouses, customer contracts and lists used by Earthgrains and Metz in production, distribution, and sale of white pan bread under the Colonial and Taystee labels. Defendants must use their best efforts to accomplish the divestitures as expeditiously as possible. The proposed Final Judgment provides that the assets must be divested in such a way as to satisfy the United States, in its sole discretion, that the assets can and will be used by the acquirer as part of a viable, ongoing business or businesses engaged in the sale of white pan bread in the geographic areas covered by the Final Judgment.[6]

If defendants do not accomplish the ordered divestitures within the prescribed time period, the proposed Final Judgment provides that the Court will appoint a trustee to complete the divestitures. If a trustee is appointed, the proposed Final Judgment provides that defendants must pay all costs and

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use or sell white pan bread in the Relevant Territory under each of the Relevant Labels." *Id.*, §II (D)(1).

[5] These assets are defined in the Final Judgment as the "Additional Baking Assets." *See* Final Judgment, §II (E).

[6] These areas, listed in the "Relevant Territory" definition of the Final Judgment, §II (H), include a number of cities and counties in Illinois, Iowa, Kansas, Missouri and Nebraska.

expenses of the trustee. The trustee's commission will be structured so as to provide an incentive for the trustee based on the price obtained and the speed with which divestiture is accomplished. After his or her appointment becomes effective, the trustee will file periodic, biweekly reports with the parties and the Court, setting forth the trustee's efforts to accomplish the required divestiture. At the end of six months, if the divestiture has not been accomplished, then the trustee and the parties will make recommendations to the Court, which shall enter such orders as appropriate.

The relief in the Final Judgment has been tailored to ensure that the ordered divestitures maintain competition that would have been eliminated as a result of the merger and prevent the exercise of market power after the merger in each of the various markets alleged in the Complaint.

IV. REMEDIES AVAILABLE TO POTENTIAL PRIVATE LITIGANTS

Section 4 of the Clayton Act, 15 U.S.C. § 15, provides that any person who has been injured as a result of conduct prohibited by the antitrust laws may bring suit in federal court to recover three times the damages the person has suffered, as well as costs and reasonable attorneys' fees. Entry of the proposed Final Judgment will neither impair nor assist the bringing of any private antitrust damage action. Under the provisions of Section 5(a) of the Clayton Act, 15 U.S.C. § 16(a), the proposed Final Judgment has no *prima facie* effect in any subsequent private lawsuit that may be brought against defendant.

V. PROCEDURES AVAILABLE FOR MODIFICATION OF THE PROPOSED FINAL JUDGMENT

The parties have stipulated that the proposed Final Judgment may be entered by the Court after compliance with the provisions of the APPA, provided that the United States has not withdrawn its

consent. The APPA conditions entry of the decree upon the Court's determination that the proposed Final Judgment is in the public interest.

The APPA provides a period of at least 60 days preceding the effective date of the proposed Final Judgment within which any person may submit to the United States written comments regarding the proposed Final Judgment. Any person who wishes to comment should do so within sixty (60) days of the date of publication of this Competitive Impact Statement in the Federal Register. The United States will evaluate and respond to the comments. All comments will be given due consideration by the Department of Justice, which remains free to withdraw its consent to the proposed Judgment at any time prior to entry. The comments and the response of the United States will be filed with the Court and published in the Federal Register. Written comments should be submitted to:

J. Robert Kramer II
Chief, Litigation II Section
Antitrust Division
United States Department of Justice
1401 H Street, NW, Suite 3000
Washington, D.C. 20530

The proposed Final Judgment provides that the Court retains jurisdiction over this action, and the parties may apply to the Court for any order necessary or appropriate for the modification, interpretation, or enforcement of the Final Judgment.

VI. ALTERNATIVES TO THE PROPOSED FINAL JUDGMENT

The United States considered, as an alternative to the proposed Final Judgment, a full trial on the merits against defendants Earthgrains, Specialty Foods and Metz. The United States could have continued the litigation to seek preliminary and permanent injunctions against Earthgrains's acquisition

of Metz. The United States is satisfied, however, that defendants' divestiture of the assets described in the proposed Final Judgment will establish, preserve and ensure a viable competitor in each of the relevant markets identified by the United States. To this end, the United States is convinced that the proposed relief, once implemented by the Court, will prevent Earthgrains's acquisition of Metz from having adverse competitive effects.

VII. STANDARD OF REVIEW UNDER THE APPA FOR PROPOSED FINAL JUDGMENT

The APPA requires that proposed consent judgments in antitrust cases brought by the United States be subject to a sixty-day comment period, after which the court shall determine whether entry of the proposed Final Judgment "is in the public interest." In making that determination, the court *may* consider--

> (1) the competitive impact of such judgment, including termination of alleged violations, provisions for enforcement and modification, duration or relief sought, anticipated effects of alternative remedies actually considered, and any other considerations bearing upon the adequacy of such judgment;
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> (2) the impact of entry of such judgment upon the public generally and individuals alleging specific injury from the violations set forth in the complaint including consideration of the public benefit, if any, to be derived from a determination of the issues at trial.

15 U.S.C. § 16(e) (emphasis added). As the Court of Appeals for the District of Columbia Circuit has held, the APPA permits a court to consider, among other things, the relationship between the remedy secured and the specific allegations set forth in the government's complaint, whether the decree is sufficiently clear, whether enforcement mechanisms are sufficient, and whether the decree may positively harm third parties. *See United States v. Microsoft Corp.*, 56 F.3d 1448, 1458-62 (D.C. Cir. 1995).

In conducting this inquiry, "the Court is nowhere compelled to go to trial or to engage in extended proceedings which might have the effect of vitiating the benefits of prompt and less costly settlement through the consent decree process."[7] Rather,

> absent a showing of corrupt failure of the government to discharge its duty, the Court, in making its public interest finding, should . . . carefully consider the explanations of the government in the competitive impact statement and its responses to comments in order to determine whether those explanations are reasonable under the circumstances.

United States v. Mid-America Dairymen, Inc., 1977-1 Trade Cas. (CCH) ¶ 61,508, at 71,980 (W.D. Mo. 1977).

Accordingly, with respect to the adequacy of the relief secured by the decree, a court may not "engage in an unrestricted evaluation of what relief would best serve the public." *United States v. BNS, Inc.*, 858 F.2d 456, 462 (9th Cir. 1988), quoting *United States v. Bechtel Corp.*, 648 F.2d 660, 666 (9th Cir.), *cert. denied*, 454 U.S. 1083 (1981); *see also Microsoft*, 56 F.3d 1448 (D.C. Cir. 1995). Precedent requires that

> the balancing of competing social and political interests affected by a proposed antitrust consent decree must be left, in the first instance, to the discretion of the Attorney General. The court's role in protecting the public interest is one of insuring that the government has not breached its duty to the public in consenting to the decree. The court is required to determine not whether a particular decree is the one that will best serve society, but whether the settlement is "*within the reaches of the public*

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[7] 119 Cong. Rec. 24598 (1973). *See United States v. Gillette Co.*, 406 F. Supp. 713, 715 (D. Mass. 1975). A "public interest" determination can be made properly on the basis of the Competitive Impact Statement and Response to Comments filed pursuant to the APPA. Although the APPA authorizes the use of additional procedures, 15 U.S.C. § 16(f), those procedures are discretionary. A court need not invoke any of them unless it believes that the comments have raised significant issues and that further proceedings would aid the court in resolving those issues. *See* H.R. 93-1463, 93rd Cong. 2d Sess. 8-9, *reprinted in* (1974) U.S.C.C. A.N. 6535, 6538.

interest." More elaborate requirements might undermine the effectiveness of antitrust enforcement by consent decree.[8]

The proposed Final Judgment, therefore, should not be reviewed under a standard of whether it is certain to eliminate every anticompetitive effect of a particular practice or whether it mandates certainty of free competition in the future. Court approval of a final judgment requires a standard more flexible and less strict than the standard required for a finding of liability. "[A] proposed decree must be approved even if it falls short of the remedy the court would impose on its own, as long as it falls within the range of acceptability or is 'within the reaches of public interest' (citations omitted)."[9]

Moreover, the court's role under the Tunney Act is limited to reviewing the remedy in relationship to the violations that the United States has alleged in its complaint, and does not authorize the Court to "construct [its] own hypothetical case and then evaluate the decree against that case," *Microsoft*, 56 F.3d at 1459. Since "[t]he court's authority to review the decree depends entirely on the government's exercising its prosecutorial discretion by bringing a case in the first place," it follows that the court "is only authorized to review the decree itself," and not to "effectively redraft the complaint" to inquire into other matters that the United States might have but did not pursue. *Id.*

VIII. DETERMINATIVE DOCUMENTS

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[8] *United States v. Bechtel Corp.*, 648 F.2d at 666 (citations omitted) (emphasis added); *see United States v. BNS, Inc.*, 858 F.2d at 463; *United States v. National Broadcasting Co.*, 449 F. Supp. 1127, 1143 (C.D. Cal. 1978); *United States v. Gillette Co.*, 406 F. Supp. at 716. *See also United States v. American Cyanamid Co.*, 719 F.2d 558, 565 (2d Cir. 1983), *cert. denied*, 465 U.S. 1101 (1984).

[9] *United States v. American Tel. and Tel. Co.*, 552 F. Supp. 131, 150 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983) *quoting United States v. Gillette Co., supra*, 406 F. Supp. at 716; *United States v. Alcan Aluminum, Ltd.*, 605 F. Supp. 619, 622 (W.D. Ky. 1985).

There is a single determinative document within the meaning of the APPA that was considered by the United States in formulating the proposed Final Judgment. That document, a letter dated March 17, 2000 from Kim Murphy, an attorney at Interstate Brands Corporation ("IBC"), to David Groce, General Counsel of Earthgrains, is attached to the Final Judgment as Appendix A. (A copy of this letter is reproduced in the attached Appendix.) Although defendants proposed licensing the Taystee label as a step toward alleviating the competitive harm, Metz's license rights to that label were subject to the approval of the original licensee, IBC. Defendants subsequently secured assurances from IBC that it would permit the Taystee label to be licensed to an acquirer acceptable to the United States under the terms of the Final Judgment. Divestiture of the Taystee label became acceptable to the United States only after it had received that written assurance.

Dated: April 7, 2000.

Respectfully submitted,

/s/

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